

2 Background to the reference

2.1. This is the third report by the Monopolies and Mergers Commission (MMC) that has been concerned with aspects of the supply of car parts.

2.2. The first such reference, made by the Director General of Fair Trading (DGFT) in November 1980, and on which the MMC reported in May 1982,¹ concerned the practices of certain car manufacturers and importers in requiring their franchised car dealers to obtain car parts exclusively from them or from sources approved by them.

2.3. The MMC found that certain car manufacturers and importers (which together supplied at least one-quarter of the car parts supplied in the United Kingdom) imposed requirements of this sort and that this complex monopoly situation operated against the public interest. The adverse effects identified by the MMC were limitation of the extent to which component manufacturers could compete with one another and with car manufacturers and importers; restriction of price competition; less speedy delivery of parts to franchised dealers in some cases; and limitation of the extent to which parts factors could compete with each other and with car manufacturers and importers.

2.4. The MMC recommended that car manufacturers and importers should be required to exclude from their franchise agreements any clause having the effect of requiring franchised dealers to buy car parts exclusively from them or from sources approved by them, and to cease enforcing any such clauses in current franchise agreements. In making this recommendation the MMC recognised that even in the absence of any formal requirement to buy parts exclusively from car manufacturers and importers it was virtually certain that franchised dealers would continue to buy mainly from them. Nevertheless the MMC had been told by the component manufacturers and parts factors that if the formal restrictions were removed they were confident that they would gradually be able to penetrate the franchised sector of the market to a significant extent.

2.5. In making their recommendations the MMC noted that it would be possible, even after the abandonment of exclusive purchasing requirements, for car suppliers to ensure by other methods that their franchised dealers bought car parts only from them. This reflected views that had been expressed to the MMC on a number of practices, in addition to exclusive purchasing requirements, which it was alleged were used by car manufacturers and importers to restrict the freedom of their franchised dealers. These practices included imposing minimum stocking requirements, stock control systems, sales or purchase targets, and discounts and bonus schemes. The MMC did not conclude that any of these practices were at that time being operated in such a way as to ensure that franchised dealers bought parts exclusively from their franchisors. The MMC recognised, however, that the practices could be operated in this way and that if exclusivity clauses were to be removed from franchise agreements any of the practices separately, or all of them together, might be used as other means of achieving exclusivity. The MMC thought that these practices might then be the subject of inquiry under the Competition Act or Fair Trading Act, but that they had no relevance to the practice (of exclusive purchasing requirements) that was the subject of the reference.

2.6. Following the MMC's report the recommendation relating to exclusive purchasing clauses in dealer agreements was implemented by the Restriction on Agreements (Manufacturers and Importers of Motor

¹ *Car Parts: A Report on the matter of the existence or the possible existence of a complex monopoly situation in relation to the wholesale supply of motor car parts in the United Kingdom*, HC 318, May 1982.

Cars) Order 1982.¹ Under this order such clauses were made unlawful except when relating to the acquisition of parts by a franchised dealer for warranty repair or replacement or for recall campaign purposes.

2.7. In May 1984 the DGFT referred to the MMC the policy and practice of the Ford Motor Company Ltd of not granting licences to persons wishing to manufacture or sell in the United Kingdom certain replacement body parts for Ford vehicles. The MMC's report was published in February 1985.

2.8. Ford had claimed that it was entitled to refuse such licences because of the copyright protection subsisting in drawings or design of body parts. At that time it was pursuing legal action, claiming infringement of Ford's copyright, against some independent manufacturers and suppliers of body panels that were supplying replacement body parts for Ford vehicles. Ford could not be compelled to grant any licences or could ask for any royalty it chose.

2.9. The MMC concluded that Ford's course of conduct in refusing the granting of licences constituted an anti-competitive practice which operated against the public interest by tending to keep the prices of body panels higher than they would otherwise be. The MMC also concluded that a satisfactory remedy could be achieved only by a change in the law. (Under the then existing law the granting of licences by Ford to other manufacturers to supply replacement body parts for Ford vehicles would have been insufficient to overcome the anti-competitive conduct if Ford attached very high royalties to the granting of licences). The MMC therefore recommended changes in the law as it related to body panels in order to reduce the period of protection given to designs under the Registered Designs Act 1949 and the Copyright Act 1956. The MMC also commented on the desirability of a more general reform in the law in order to remove the protection of artistic copyright from purely functional designs or from industrial designs generally.

2.10. Following the MMC recommendations, the Copyright, Designs and Patents Act 1988 introduced a 'design right' to replace the existing copyright protection for industrial designs. The protection given to designs under this design right excluded protection for any design features enabling an article to be functionally fitted to, or aesthetically matched with, another. These exceptions to the right- called, for convenience, the 'must-fit' and 'must-match' exceptions-were intended to ensure that competing designs for spare parts were not kept out of the market; competitors could not be prevented from copying any feature which was required to enable an article of their design to be connected to or matched with existing equipment designed by someone else. The Act also gave the Secretary of State power, consequent upon an appropriate finding in an MMC report, to cancel or modify conditions attached to licences by copyright owners and also to require that such licences should be available as of right.

2.11. The legal relationship of the vehicle manufacturer to the component manufacturer that wishes to produce RE parts was considered by the House of Lords in *British Leyland Motor Corporation Ltd v Armstrong Patents Co Ltd* [1986] 1 AC 577 where it was decided that a component manufacturer that copies the shape and dimensions of an original car part is not in breach of the vehicle manufacturer's copyright in the original drawings. The reason given was that car owners have an inherent right to repair their cars in the most economical way possible and for that purpose must have access to a free market in spare parts. It is also clear under EC law that manufacturers of cars, which are to be regarded as dominant in respect of their own products for the purposes of Article 86 of the Treaty of Rome, must not unreasonably restrict the availability of spare parts. This emerged from the cases of *Volvo v Veng* [1988] ECR 6211 and *Maxicar v Renault* [1988] ECR 6039, decided by the European Court of Justice in October 1988 on Article 177 references from the United Kingdom and Italian courts respectively. In both cases the plaintiff had claimed that the relevant car manufacturer, by refusing to grant a licence for the independent manufacture of front wing panels and ornamental body panels respectively, had committed a breach of Article 86. The Court rejected these claims on the ground that the mere securing of the protection of an exclusive right to manufacture by virtue of intellectual property rights was not abusive, but it went on to make clear that the exercise of such an exclusive right to manufacture nevertheless could become an abuse if it led to certain results including:

¹SI No 1146.

²*Ford Motor Company Limited: A report on the policy and practice of the Ford Motor Company Limited of not granting licences to manufacture or sell in the United Kingdom certain replacement body parts for Ford vehicles*, Cmnd 9437, February 1985.

- (a) an arbitrary refusal to supply spare parts to independent repairers;
- (b) the fixing of prices for spare parts at an unfair level; or
- (c) a decision to stop producing spare parts for a particular model.

2.12. In December 1984 the EC Commission promulgated EC Regulation 123/85 laying down conditions to which supply agreements between car suppliers and their dealers must conform if the benefits of block exemption were to be enjoyed. The relevant provisions of this Regulation are considered in Chapter 4.

2.13. In May 1990 the DGFT made a third reference to the MMC on the supply of parts (see Appendix 1.1). This report deals with that reference. Concurrently the DGFT also referred to the MMC the existence or possible existence of a monopoly situation in relation to the supply of new motor cars within the United Kingdom by manufacturers or importers of such cars. The MMC reported on that reference on 31 October 1991. There was ground common to both inquiries, since most suppliers of new cars also supply car parts, and, under the selective and exclusive distribution (SED) system, their franchised dealers sell both cars and parts.