International developments

Visit by Geraint Howells

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European product liability

1. Background

One of the most enjoyable aspects of my visit to Australia last Easter was the enthusiasm I found for discussing product liability matters, both during my visits to the ACCC offices in Canberra and Sydney and in discussion with other practitioners and university colleagues at the University of Sydney where I had kindly been invited as a Parsons scholar. Whilst products scholars in the US are in constant demand, in Europe we seemed to have had our hey-day in the wake of the enactment of the European Community (EC) product liability directive 1985 and its subsequent implementation in the member states (although France has still not implemented it, despite a deadline of 1988!).

More than 10 years after the directive's enactment, there has been little case law and the legal community's willingness to contemplate the subtleties of legal analysis of the directive's provisions has waned. Thus it was nice to be able to return to discussions which are familiar to me, particularly the central issues of: What is the meaning of defectiveness? What is the impact of the development risks defence? How far have the substantive rights of consumers been improved? What will be the practical impact of the reforms?

However, the depressing feature of my visit to Australia was the lack of assistance I could provide to my Australian colleagues as to how these questions have been answered in Europe. There have been few reported cases relying on the directive, and the important challenge by the European Commission to the United Kingdom's wording of the development risks defence is still pending (see next section). So we are still left with posing questions and suggesting possible interpretations, but have few additional clues as to the outcome.

The EC product liability directive of 25 July 1985 (OJ 1985 L 210/29) is outlined in the next section, in a way that provides a guide to the directive's structure. Readers will soon realise how similar it is to the provisions in Part VA of the Trade Practices Act. (A fuller paper comparing EC/UK law with the Australian provisions is to appear in a forthcoming edition of the *Competition and Consumer Law Review*). The third section of this paper looks at two key elements of the provisions — the defectiveness standard and the development risks defence. The fourth section assesses the impact the directive has had on the law and practice of the member states. The final section comments on the interchangeability of product liability experiences between nations.

2. The EC product liability directive

Product

The directive applies to movables, even those incorporated into another movable or an

immovable. Electricity is expressly included. Member states have the option of including primary agricultural products and game, but only Finland, Greece, Luxembourg and Sweden have opted to include them.

Defendants

Liability is imposed on producers. This includes manufacturers of the finished product and component parts, producers of the raw materials of the product, and those who present themselves as producers by putting their name, trade mark or other distinguishing marks on the product (i.e. own-branders). Importers into the EC are also liable (note that liability falls on the first importer into the EC, not the importer into individual states). Suppliers may be liable if the producer cannot be identified and they fail to inform the injured person, within a reasonable time, of their supplier or the producer (in the case of imported products, the importer).

Basis of liability

The plaintiff must prove damage, defect and the causal relationship between the defect and damage. This liability cannot be limited or excluded. Thus, in theory at least, the requirement to prove negligence has been removed, but the need to establish damage, defect and causation remains. The defectiveness standard is considered in the following section. Causation continues to be based on traditional national rules. In the UK this means there is no move towards proportionate or market share liability nor acceptance of lost chance claim. Readers may care to note that the Dutch Hoge Raad has imposed joint and several liability on the producers of dethylstilbestrol (DES)(see note by Hondius [1994] Consum LJ 40).

Damage

This includes damage caused by death and personal injury, although non-material damages are left to national laws. The directive gives member states the option of limiting a producer's total liability for death and personal injury caused by identical items with the same defect to a minimum of 70m ECU. Claims can also be made for damage to, or destruction of, any item of property other than the defective product itself, subject to a lower threshold of 500 ECU (this has been treated as an excess in most states, but in the UK claims above 500 ECU are met in full). The property damaged must have been of a type ordinarily intended for private use or consumption and actually used by the injured person for those purposes.

Defences

Several defences are available to the producer. The burden is placed on producers to establish:

- they did not put the product into circulation;
- it is probable that the defect did not exist when they put the product into circulation;
- the product was neither manufactured by them for sale or distribution for any economic purpose nor distributed in the course of their business;
- the defect was due to compliance with mandatory regulations issued by public authorities;
- the development risks defence (considered below);
- in the case of a component part, that the defect was attributable to the design of the product into which it was fitted or to instructions given by the manufacturer.

It is also a defence that the product was put into circulation before the directive came (or possibly in some circumstances should have come) into force. There is a three-year limitation period from the time the the producer became, or reasonably should have become, aware of the damage, the defect and the identity of the producer. There is also a long stop limitation period of 10 years from the time of marketing the actual product causing the damage.

3. Key concepts

Defectiveness

The directive provides a definition of defectiveness which is similar to that found in

s. 75AC of the Trade Practices Act, although the Australian standard is more detailed and specific. The directive states that:

> A product is defective when it does not provide the safety which a person is entitled to expect, taking all the circumstances into account, including:
>
> (a) the presentation of the product;
>
> (b) the use to which it could reasonably be expected that the product would be put;
>
> (c) the time when the product was put into circulation.
>
> A product shall not be considered defective for the sole reason that a better product is subsequently put into circulation.

The choice of this consumer expectation standard was surprising given that US jurisprudence had highlighted the weaknesses of this formulation of the defectiveness standard. It is problematic when dealing with patent defects which consumers could not expect to be safe and because of the problem of having to rely on consumer expectations which may not be very sophisticated. US courts have tended to prefer a more objective risk:benefit analysis or a dual consumer expectation and/or risk:benefit analysis. The choice of the European legislators was therefore somewhat disappointing.

However, when assessing how novel a departure from negligence the new regime of alleged strict liability is, two benchmark questions need to be answered. To what extent does the new regime base liability on the condition of the product rather than the behaviour of the producer? To what extent does it judge the product with the benefit of hindsight knowledge acquired after marketing?

In theory, the focus of the new liability regime is on the condition of the product rather than producer behaviour. Negligence no longer has to be proven. The only question should be: Was the product defective? However, the defectiveness concept impacts differentially on the various categories of defect. For a manufacturing defect, all that is required is a comparison of the alleged defective product with a perfect model, and if there is a flaw then a defect will be established. For design and defectiveness claims based on a failure to warn or improper instructions the matter is not so simple. The liability regime does not require products to be perfectly safe, merely that they are as safe as people are entitled to expect. We can expect products always to be properly manufactured, but when considering the safety of the design or the adequacy of the accompanying warnings and instructions one is forced to make various trade-offs between, for instance, safety and price and availability. It would be unrealistic to require all cars to incorporate every safety feature available, otherwise few of us would be able to afford them! Equally, drugs should normally be marketed after proper, but not excessive, testing. Although side-effects of some drugs may have long latency periods, many people would suffer if drugs were held back until testing had been carried out over a 20- or 30-year period.

When these types of questions are at stake, simply looking at the final product is of little assistance. The danger may even be acknowledged by all. The question of defectiveness will then turn on one's view of whether the producer was right not to include an expensive safety feature, or whether the producer had adequately researched the possible risks. For design and failure to warn of defects, the focus therefore remains firmly on the reasonableness of the producer's conduct rather than the condition of the final product.

If the new regime is to be a major advance over the negligence standard with regard to design defects, the change must be found in the point of time from which the producer's decisions are assessed. In fact this issue has two dimensions. First, it is necessary to determine against which set of safety expectations the product is to be judged: those which pertained when the product was marketed or those which pertained when it caused the damage. The latter will generally be higher because of the development of safer alternatives. The definition of defect seems to settle for judging the product by the safety expectation at the time of marketing. It provides that the time when the product was put into circulation should be taken into account, and also states that a defect should not be inferred merely because a better product had been marketed subsequently.

Although in parenthesis, it should be noted that the subsequent marketing of a better product might be led as evidence that such a product could easily have been produced at the time the defective product had been marketed. Thus the definition of defectiveness contains what I label a 'state of the art' defence. This is to be contrasted with the development risks defence which assists a producer when a product did not comply with safety expectations at the time of marketing but the reason for this was a danger of which the producer was unaware.

Development risks defence

The directive provides a producer with a defence if the producer proves:

> the scientific and technical knowledge at the time when he put the product into circulation was not such as to enable the existence of the defect to be discovered.

The directive gives member states the option of excluding the defence, but only Finland and Luxembourg have chosen to do so. This is not perhaps surprising, but it is certainly unfortunate. This defence has the potential to leave victims of a thalidomide-type disaster uncompensated, since at that time it was arguable that the pharmaceutical industry was not aware that drugs ingested by a pregnant woman could harm their baby *in uterus*. This is ironic, for the plight of those unfortunate children who were born deformed was one of the significant motivations behind product liability law reform in Europe.

A similar defence is to be found in s. 75AK(c) of the Trade Practices Act. The wording differs slightly in that it refers to scientific *or* technical knowledge rather than scientific *and* technical knowledge. This would, however, appear to be of no moment. How the defence is interpreted in Europe may therefore be of interest to Australian lawyers. In fact, I have only heard of one decision on the defence. A German court has held that the defence does not apply to manufacturing defects. Although it is true that most manufacturing defects would seem to fall outside the defence, one might think the defence should retain some relevance where a producer claims that, for instance, there were no quality control systems good enough to detect a hairline fracture.

Of crucial significance is a case pending before the European Court of Justice. The European Commission believes the United Kingdom has provided producers with too generous a defence. Section 4(1)(e) of the United Kingdom's Consumer Protection Act 1987 provides producers with a defence if they can prove that:

> The state of scientific and technical knowledge at the relevant time was not such that a producer of products of the same description as the product in question might be expected to have discovered the defect if it had existed in his products while they were under his control.

The United Kingdom version of the defence seems to replace a test of discoverability by one of expectation of discoverability and to judge producers by the standard of their fellow producers in that sector rather than by the highest standard possible. The danger with the United Kingdom version lies in the fact that it would permit producers a defence where they admit that a danger was known or discoverable, but argue that they could not have been expected to go to the trouble of discovering it because the effort and costs involved would be beyond the budget and/or capabilities of a firm in their sector. Such a defence has actually been pleaded in the United Kingdom by yoghurt manufacturers who are arguing that they were not equipped to undertake the test which would have revealed the presence of a toxin and that such testing was not routinely available to producers of their product.

The importance of the European Commission's challenge to the United Kingdom's wording of the defence for Australia lies in the fact that the United Kingdom will doubtless seek to justify their wording by arguing that not only was their wording permissible, but that in fact the defence has to be interpreted in this manner. Thus, by implication, it could be argued that the Australian defence must be interpreted in accordance with the wording to be found in the United Kingdom Act. The United Kingdom argument is unlikely to be restricted to a textual analysis of the directive, but rather it is likely to suggest that it only makes sense to have a defence with which the defendant has a chance of complying. There is no point in judging the producer against knowledge to be found in some exotic academic work. Rather, producers

should be judged by the knowledge they can realistically be expected to have.

In truth, the development risks defence does not sit easily in a strict liability regime. But one hopes that the European Court of Justice will view it as a rather narrow and arbitrary exception to the strict liability principle. Indeed the directive contains mechanisms for the defence to be reviewed with a mind to the possibility of its eventual repeal. Although the European Commission has not yet proposed repeal, one must hope that it does so in the not too distant future and that in the meantime the defence is viewed as a narrow concession based on political compromise (the Commission never favoured the defence, which was included at the insistence of some member states) rather than as an integral part of a principled piece of law reform which must therefore fit into a cogently thought-out legal framework.

If construed strictly, the development risks defence will be difficult for producers to invoke. If construed generously, it almost brings us back full circle to a negligence standard. Some argue that, even if the defence is generously interpreted, there has still been an advance in that the burden is placed on producers to show that the state of scientific and technical knowledge had not been such as to allow them to discover the defect. Personally I see this as more of a theoretical than practical advantage; for, once producers lead some evidence to support their version of what the level of knowledge was, the burden will then revert to the injured party to disprove this.

4. Impact on law and practice in member states

How much stricter, if at all, the new European product liability regime is than a negligence standard is difficult to gauge until we have experience of how the defectiveness standard is to be applied and the scope of the development risks defence, in those states where it is available. Moreover, it should be remembered that the negligence concept had been applied fairly strictly to products in many member states. Thus in the United Kingdom there was almost automatic liability for manufacturing defects and manufacturers were held to quite demanding standards of research. In Germany the burden of proof was frequently reversed in negligence claims, and in France strict liability was in practice imposed on producers on the basis that they retained control of the product design.

Also, the role of contract law should not be underestimated. Even after implementation of the directive, British consumers may find it easier to bring a claim for lack of satisfactory (formerly merchantable) quality against their seller. In France the placing of a defective product on the market is held to be an act of bad faith, with the result that clauses excluding liability for hidden defects (*vice cachée*) are invalid and consequential damages are available. Also, an *action directe* can be made against higher links in the production and distribution chain, thereby circumventing problems of privity. (For deeper analysis of the existing laws of the member states see my work, *Comparative product liability*, Dartmouth, 1991).

Perhaps the most significant impact of the directive will be seen to be the extended range of possible defendants it affords injured parties. Certainly importers into the EC and own-branders are subject to far more onerous obligations since the adoption of the directive.

Litigation in the EC is not becoming simpler. The new regime is not seen as the sole source of rights in product liability claims, but rather tends to be used as an additional head of liability to any contractual, negligence or other tortious claims. Incidentally, a partial reason for the delay in implementing the directive in France was the proposal that the law implementing the directive should be the sole basis for product liability claims. This would have in fact represented a reduction in the level of consumer protection in France, particularly if the development risks defence was permitted. The present draft law no longer seeks to make the new law the exclusive source of remedies in product liability cases. In Germany the pre-existing laws will continue to have great relevance since non-pecuniary damages are not recoverable under the new strict liability regime.

The impact of the directive on the substantive law of the member states is debatable. What cannot be doubted, however, at least in the

United Kingdom, is the changed safety culture and litigation environment. Defendant lawyers and risk assessors were keen to promote product liability to their industrial clients. The new EC law may not have a dramatic impact on claims, but it might! Businesses, especially if they had some experience, even second-hand, of the US situation could easily be persuaded that the new law was something they should be informed about and take steps to be protected from. Plaintiff lawyers have also become more pro-active in a legal practice environment which allows lawyers to advertise and to offer (on a modest basis) contingent fees. How much of this plaintiff lawyers' activity is ascribable to the product liability directive is unclear. In the area of service safety, where the EC has lamentably failed to enact even a directive simply reversing the burden of proof, there has also been a considerable increase in the amount of litigation activity, particularly in the wake of a string of disasters.

Nevertheless the new product liability laws have helped raise the profile of litigation possibilities. One is tempted to conclude that the main benefits of the law reforms have derived not so much from the substantive improvements, but rather from the publicity which has surrounded them and which has caused businesses to become more aware of their responsibilities and has heightened the awareness of consumers and their advisers as to the possibility of redress.

However, the lack of legal decisions in this area is a problem, given the opaqueness of the central legal principles. In this respect Europe might learn from the Australian law. Section 75AQ of the Trade Practices Act gives the ACCC the right to bring actions. Judicious use of this power could ensure that the courts are able to adjudicate on key issues of principle, but doubtless there will remain a tension between securing an acceptable settlement for the injured party and forcing the matter to formal adjudication, with the risk that the injured party recovers nothing.

5. Interchangeability of experiences

Now that Europe and Australia, as well as many other Asia-Pacific countries (see J. Kellam (ed.), *Product liability in the Asia-Pacific*, Legal Books, Australia, 1995), share a product liability law with many common concepts, it is interesting to speculate whether the experiences in all these countries will be interchangeable. In other words, do Australian lawyers need to be interested in the case law from Europe and other Asia-Pacific countries?

A similar matter is currently preoccupying European product liability lawyers. Now that the law has been formally harmonised throughout the EC (France excepted?), is that the end of the matter or will/should the application of the rules vary according to local circumstances? In other words, is it a strength or weakness of the new regime if its norms are so open-textured that they allow the local culture to be reflected in their application? Similarly it could be argued that Australian consumer expectations are unique to Australia so that overseas experiences of the application of a test with reference to the expectations of their local consumers is of only marginal interest to the Australian lawyer.

However, nowadays, advertising and marketing is increasingly organised on a global basis and consumers in Europe and Australia have similar values, so the types of questions being addressed in litigation and the answers adopted are likely to be of relevance to lawyers in the other jurisdictions. English negligence law has indeed been influenced by Australian cases, like *Sutherland Shire Council v Heyman* (1985) 60 ALR 1.

Certainly there is more common ground between Europe and Australia in the products field than there is between Europe/Australia and the United States. In the United States, products litigation plays quite a different role as surrogate for a welfare state, so its results cannot always easily be transplanted into other systems. European experience to date suggests that litigation will be so sparse that the product liability specialist will be desperate to find inspiration from any source. Australia is likely to be a good source of inspiration.

It will be interesting to see whether the European Court of Justice will take cognisance of common law jurisdictions outside the European Union. It should, for there is a rich tradition of intellectual exchanges within the common law world from which European law

could benefit. Equally, common lawyers in Australia, like their counterparts in the United Kingdom, may have to come to terms with civil law traditions if they are to fully comprehend the future development of product liability law. The world is indeed becoming a smaller place.

From New Zealand

The following item was extracted from the August–September 1996 issue of the New Zealand Commerce Commission's newsletter Fair's Fair.

The Commerce Commission enforces both the Commerce Act 1986, which contains restrictive trade practices provisions, and the Fair Trading Act 1986, which deals with consumer protection matters.

New Zealand electricity market

In a draft determination, the Commerce Commission has said its preliminary view is that it would not oppose rules proposed for the New Zealand Electricity Market (NZEM).

It is proposed that, from 1 October 1996, NZEM will provide a market for the wholesaling of electricity, and a market for short-term financial hedges for electricity traders.

The administrator of NZEM, the Electricity Market Company, is seeking authorisation of some of its rules — the pricing mechanisms, prudential provisions and metering standards.

Commission Chairman, Dr Alan Bollard, said that, at this stage, the Commission's view is that it:

- would authorise the pricing mechanisms on public benefit grounds;
- would not authorise the prudential provisions because they do not lessen competition; and
- would not authorise the metering standards because they are already in place.

The Commission has called for further submissions and will call a conference of interested parties to assist it to reach a final determination.