Product Liability and Product Safety in Europe: Harmonization or Differentiation?

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I. INTRODUCTION

In Europe it is known for a long time that the domains of product safety and product liability are, already for many years now, not longer only subjected to national legislation. Europe has on the one hand issued many Directives harmonising product safety standards. In addition there is the Council Directive 85/374/EEC of 25 July 1985 on the approximation of the laws, regulations and administrative provisions of the Member States concerning liability for defective products.

The question that will be addressed in this paper is whether there are economic reasons for a harmonisation of product safety standards and product liability. The effect that product safety standards have, to a large extent, been harmonised, can at first blush easily be understood as an important instrument to facilitate interstate trade. However, it is less clear why a harmonisation of product liability law was also needed. This harmonisation of product liability is all the more remarkable since Europe has so far taken in fact only one initiative with respect to tort law, which is precisely the domain of product liability. Other attempts, e. g., to harmonise the liability for services, have failed.

The European product liability Directive entered into force when there was not yet any talk about a subsidiarity principle. According to this principle, which was introduced by the single European Act for environmental matters and enlarged to a general principle of community policy by the Maastricht treaty, the ‘community shall take action if and only in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member States and can, therefore, by reason of the scale or effects of the proposed action, be better achieved by the community’¹.

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¹ Art. 3 B (2) EC treaty. This formulation has not been changed by the Treaty of Amsterdam.
The issue, which will therefore be addressed in this paper, fits, from a legal perspective in the discussion concerning the interpretation of the subsidiarity principle. This subsidiarity principle indeed allows for a new and probably more critical approach concerning the proper role of Europe with respect to product liability. The question indeed arises what reasons can be advanced for a full harmonisation of product liability law. To answer this question, attention will be paid to the economic literature on the optimal level of regulation within federal systems.

It is, moreover, not only academically interesting to address the optimal level of regulation of product liability in Europe. The European Commission itself has also established that the product liability Directive in its current version is not able to reach the goal of harmonising marketing conditions, which it is, according to the preamble, supposed to achieve. Therefore, on 28 July 1999 a green paper on liability for defective products was launched in which the Commission addresses several features of the product liability Directive which may be reconsidered. One of these issues, although this is only briefly addressed in the green paper, may be the question on the proper division of tasks between Europe and the Member States concerning the regulation of product liability².

The paper is set up as follows: after this introduction (Section I) the European product liability and product safety Directives will be briefly introduced (Section II), to turn immediately to the corpus of the paper, being the criteria for centralisation of product liability and product safety (Section III). In the light of these criteria the question will be asked whether the product liability Directive could effectively reach the goals set and can be considered to promote economic efficiency (Section IV). A public choice perspective is presented to explain some of the ‘defects’ of the product liability Directive (Section V). Finally, a few recent developments will be discussed (Section VI) and a few concluding remarks are formulated (Section VII).

II. EUROPEAN PRODUCT LIABILITY AND PRODUCT SAFETY

1. Product Liability


A first draft was presented in 1974 but this was already modified in 1975³. The first official Proposal for a Directive was presented by the Commission of the

² Com (1999, p. 396 final).
³ See Reich (1986, p. 137).
PRODUCT LIABILITY AND PRODUCT SAFETY IN EUROPE

EEC on September 9, 1976. This Proposal was debated in the Economic and Social Council and in the European Parliament, which both suggested important changes to the initial proposal, e.g., with respect to the problem of development risks. Following these discussions, the Commission published a revised proposal in 1979. It was only more than five years later that the Council finally passed the Directive on July 25, 1985.

Reading the Considerations, which precede the Directive, it is apparent that the purpose of the Directive was the approximation of the laws of the Member States. It was argued that this approximation was necessary, because the existing divergences between liability rules in the different Member States could distort competition. The various approaches to product liability in the Member States had lead to different liability rules and safety standards. If product liability claims and investments in safety become an important factor in production costs, the different product liability rules might indeed result in different marketing conditions and could distort competition. For the same reasons, it is also held that differing levels of product liability might affect the free movement of goods within the common market.

The goal of approximating the laws of the Member States could be achieved through (the old) art. 100 of the EEC Treaty, which allowed harmonization through Directives of the EEC council in all cases where the functioning and establishment of the common market were directly concerned. Since ‘harmonization-article’ 100 was the legal basis for EEC jurisdiction in this matter, it is relevant to examine whether the Directive under discussion did indeed realize this harmonization objective. This point will be addressed below.

It is interesting to note that the considerations preceding the Directive refer not only to the possible distortion of competition and the endangering of the free movement of goods as justifying the need for harmonization, but also to the consumer protection argument. Indeed, the argument is advanced that the existing divergences in the product liability rules of the Member States might ‘entail a differing degree of protection of the consumer property’. This harmonization of the level of consumer protection seems to have become an important goal of the Directive too. Consumer protection will not only be harmonized, as the first consideration suggests, but the level of con-

10. See also Reich (1986, p. 135).
sumer protection will also be increased. This becomes clear when reading the other considerations preceding the Directive, where the notion ‘protection of the consumer’ is mentioned as much as twelve times. So, this would indicate that the goal of the product liability Directive, is not just to harmonize existing laws, but to harmonize them at a higher level of consumer protection. However, in this respect some authors suggest that the primary motive for the EEC intervention is to create uniform marketing standards through harmonized liability rules and not the promotion of consumer interests. They argue that one of the reasons for EEC harmonization was a fear that the American ‘product liability explosion’ might start in Europe too. In that respect the Directive would only be intended to stifle excessive Member States’ initiatives based upon the U. S. Model11.

2. Main Principles of the Product Liability Directive

It is, within the scope of this paper, obviously not possible to provide a detailed overview of the contents of the product liability Directive; therefore a brief overview of the main points will be provided.

The first article of the Directive gives the key rule for product liability, stating that the producer shall be liable for damage caused by a defect in his product. The following articles develop what is meant by the different notions which are used in article 1. The considerations preceding the Directive make clear that this concerns a liability without fault. A product according to article 2 means all movables, which have been industrially produced. The Directive was not applicable to primary agricultural products and game. These are the products of the soil, of stock-farming and fisheries12. The producer according to the Directive is only the manufacturer of a finished product, the producer of any raw material or the manufacturer of a component part. Also those, who, by putting their name, trademark or other distinguishing feature on the product, present themselves as producer, are considered producers. The same is true for all importers of products into the community. Suppliers are, as a general rule, not liable under the Directive.

A product is considered to be defective under the Directive when it does not provide the safety, which a person is entitled to expect. The considerations make clear that the defectiveness of the product should be determined by ref-

12. This has, however recently been changed. This will be discussed in Section VI which deals with recent developments.
reference to the lack of safety which the public at large is entitled to expect. An
element to be taken into account is the use to which it could reasonably be ex-
pected that the product would be put as well as ‘the time when the product was
put into circulation’. The burden of proof lays according to article 4 on the vic-
tim, who has to prove the damage, the defect and the causal relationship be-
tween the defect and the damage.

Non liability clauses are unvalid according to article 12 of the Directive.
There are, however, certain exclusion grounds for the producer. E. g., article 7
(b) excludes liability if the producer can prove that, having regard to the cir-
cumstances, it is probable that the defect which caused the damage did not exist
at the time when the product was put into circulation by him or that this defect
came into being afterwards.

Article 10 of the Directive states that a limitation period of three years shall
apply to proceedings for the recovery of damages. In addition article 11 pro-
vides that the rights of the victim pursuant to the Directive shall be extin-
guished upon the expiry of a period of 10 years.

Finally, article 16 of the Directive introduces the option for the Member
States to limit the producers liability to an amount which may not be less than
70 million ECU if the damage resulted from death or personal injury and if it
was caused by identical items with the same defect (so called serial damage).

The green paper on liability for defective products makes clear that the goal
of the Directive was to provide a balanced approach providing on the one hand
a protection to victims, but avoiding on the other hand a crushing liability, e. g.,
by requiring the victim to prove the defective nature of the product and by pro-
viding limitations in time13.

2. Product Safety

1. Goals and Purpose

In addition to the product liability Directive the Commission has also issued a
variety of Directives providing harmonised safety standards for specific items,
such as, e. g., for machines. Moreover, on 29 June 1992 a council Directive 92/
59 on general product safety was issued. This Directive clearly aimed at remov-
ing differences in safety standards, since the Commission considered that those

13. See the section in the green paper on maintaining the balance (pp. 18–19), where the Commis-
sion especially underlines its fear that Europe should not follow the American example of an
expanding product liability.
differences might endanger the establishment of the internal market. The goals of this Directive are probably best understood by citing the considerations:

‘Whereas it is important to adopt measures with the aim of progressively establishing the internal market over a period expiring on 31 December 1992; whereas the internal market is to compromise an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured; whereas some Member States have adopted horizontal legislation on product safety, imposing in particular, a general obligation on economic operators to market only safe products; whereas those legislations differ in the level of protection afforded to persons; whereas such disparities and the absence of horizontal legislation in other Member States are liable to create barriers to trade and distortions of competition within the internal market’.

This Directive therefore had as goal to remove trade barriers, which could result from differing product safety standards, within the framework of the internal market program.

According to Silva and Cavaliere European regulation of product safety has always been concerned with two main aims: 1. To guarantee a minimum level of safety to all European consumers and 2. To harmonize the different national legislation in order to prevent the erection of non-tariff barriers to free trade among European countries.

2. Main Principles

The Directive contains, inter alia, in article 3 a general obligation on producers to place only safe products on the market. Producers are also expected to provide consumers with the relevant information to enable them to assess the risks inherent in a product throughout the normal or reasonably foreseeable period of its use.

However, article 4 of the Directive provides that

‘where there are no specific Community provisions governing the safety of the products in question, a product shall be deemed safe when it conforms to the specific rules of national law of the Member State in whose territory the product is in circulation, such rules being drawn up in conformity with the Treaty, and in particular Articles 30 and 36 thereof and laying down the health and safety requirements which the product must satisfy in order to be marketed’.

In other words: this general product safety Directive functions as a stop gap for issues not covered by other Directives fixing harmonised safety standards. In the absence of specific community provisions the conformity of a product to the general safety requirement shall be assessed having regards to voluntary na-

tional standards giving effect to a European standard or, where they exist, to community technical specifications or, failing these to standards drawn up in the Member State in which the product is in circulation, or to the code of good practice in respect of health and safety in the sector concerned.

The considerations preceding the Directive and article 13 of this general product safety Directive specify that this Directive does not affect victims’ rights with respect to the product liability Directive. In other words: it is not because a product is considered safe, because it corresponds with a code of good practice, that this would mean that the product can no longer be considered defective within the meaning of the product liability Directive.

The Directive moreover provides for specific obligations on the Member States to make regulations in such a way that products placed on the market are safe and it contains a duty to notify the Commission of the measures taken under the general product safety Directive.

III. CRITERIA FOR (DE)CENTRALISATION

1. Starting Point: ‘Bottom up Federalism’

The question whether regulation should be promulgated at central (European or federal) level or at a more decentralised level (or, to put it in a more balanced way, what kind of regulations should be set at which level) has been addressed in the economics of federalism. The starting point for the analysis is usually the theory of Tiebout (1956) about the optimal provision of local public goods15. Tiebout argued that when people with the same preferences cluster together in communities, competition between local authorities will, under certain restrictive conditions, lead to allocative efficiency. If there are, e. g., in one community citizens with a high preference for sporting facilities and in another one a majority of citizens with a preference for opera, the first community will probably construct sporting facilities, whereas the second will probably provide an opera house. If someone living in the second community would prefer sporting facilities instead of the opera house, he could then move to the first community, which apparently provides services that better suits his preferences. The idea is that well-informed citizens will move to the community that provides the local services that are best adapted to their personal preferences. Through this so-called ‘voting with the feet’ competition between local authorities will lead cit-

15. For a discussion of this theory, see Rose-Ackerman (1992a, pp. 169–170).
izens to cluster together in communities according to their preferences. In practice one can notice that different communities do indeed offer a variety of different services. The idea is that the citizen can influence this provision of local public goods either by influencing the decision-making (vote) or by moving (exit).

This basic idea applies not only to community services, but also, e.g., to fiscal decisions\textsuperscript{16} and environmental choices\textsuperscript{17}. In addition, this idea of citizens moving to the community that provides services which best correspond with their preferences, can also be applied with respect to legal rules. Thus, it has been argued by Van den Bergh (1994) that a competition between legislators will lead to legal systems competing each other, to provide legislation that corresponds best to the preferences of citizens. Also Ogus (1999) argued that the various lawmakers in the nation-states would create competitive markets for the supply of law. The idea therefore is that in an optimal world, citizens will cluster together in states that provide legal rules that correspond to their preferences. Well-informed citizens, who may be dissatisfied with the legislation provided, could move (voting with the feet) to the community that provides legislation that corresponds best to their preferences. This idea, assuming that those different legal systems offer different legal rules thus explains the variety and differences between the legal systems (Van den Bergh 1998). Moreover, it also shows that differences between the various legal rules of different countries should not necessarily be judged as negative, as is often the case in Europe today. The idea of competing legal systems can probably best be seen ‘in action’ in international private law where actors can choose the legal system that best suits their needs in a choice of law regime\textsuperscript{18}. Frey and Eichenberger (1996a, 1996b) have proposed an extreme form of this competition between legal orders by suggesting the emergence of Functional Overlapping Competing Jurisdictions (FOCJ), whereby citizens could choose different governmental unities for different functions of government.

Obviously, this system, assuming that a competition between legal orders leads to allocative efficiency in the provision of legal rules, works only if certain conditions are met. One condition is that citizens have adequate information on the contents of the legal rules provided by the various legislators, in or-


\textsuperscript{17} So Oates and Schwab (1988, pp. 333–354).

\textsuperscript{18} Although the choice for a particular legal regime may not always be related to the quality of the legal system but, e.g., to the quality of the court or arbitration system. The latter explains, according to Ogus (1999, p. 408) the popularity of English law in choice of law clauses in contracts.
order to be able to make an informed choice. In addition, exit is often costly, so people may stay even if the (legal) regime does not suit their needs optimally\(^\text{19}\). Moreover, a location decision is obviously made under the influence of a set of criteria, whereby the legal regime may not be decisive\(^\text{20}\). Usually the job location and residence are that important that in reality there is often little left for people to choose\(^\text{21}\). Finally, as we will discuss below, this system of competition between legal orders works only if the decisions in one legal order have no external effects on others.

In economic literature, this Tiebout model is used to argue that, from an economic point of view, decentralisation should be the starting point, since competition between legislators will lead to allocative efficiency. Van den Bergh (1994) uses this theory as well to provide criteria for centralisation/decentralisation within the European Union. Taking Tiebout as a starting point and assuming that competition between decentralised legislators will lead to an optimal provision of legal rules, the central question is: why centralise? Van den Bergh therefore criticises a part of the current discussion in the European legal literature which seems to focus on the question why there should be decentralisation (referred to by Van den Bergh as ‘top down federalisation’). According to economic theory, that is the wrong question. Starting from Tiebout’s model, there is reason to believe in what Van den Bergh calls a ‘bottom up federalisation’, assuming that in principle the local level is optimal, since the local level has the best information on local problems and on the preferences of citizens. Only when there is a good reason, should decision making be moved to a higher level. Economic theory has indeed suggested that there may be a variety of reasons why the local level is not best suited to take decisions and where central decision making can lead to more efficient results.

These criteria for centralisation will now be applied to product liability and product safety.

2. Transboundary Character of the Externality

The Tiebout argument in favour of competition between local communities obviously works only if the problem to be regulated is indeed merely local. Once

\(^{19}\) As Ogus (1999, p. 407) states, there should be no barriers to the freedom of establishment and to the movement of capital.

\(^{20}\) That is one of the reasons why Frey and Eichenberger (1996) argue in favour of FOCJ: the choice for one legal or institutional regime should not be exclusive; there may be ‘overlapping’ jurisdictions depending upon the different functions.

\(^{21}\) Rose-Ackerman (1992a, p. 169).
it is established that the problem to be regulated has a transboundary character, there may be an economics of scale argument to shift powers to a higher legal order that has competence to deal with the externality over a larger territory. This corresponds with the basic insight that if the problem to regulate crosses the borders of competence of the regulatory authority, the decision making power should be shifted to a higher regulatory level, preferably to an authority which has jurisdiction over a territory large enough to adequately deal with the problem.22

'Economic theory provides a straightforward but unrealistic answer to regional pollution problems: draw ‘optimal’ jurisdictional boundaries’ 23.

This externality argument in favour of centralisation plays traditionally an important role with respect to environmental problems.24. The question, however, arises how this ‘transboundary externality’ argument relates to product liability. One can certainly argue that the product liability area is a totally different one than the traditional tort as far as the potential of affecting international trade is concerned. The chance that a ‘normal’ tort might have an interstate effect is, with a few exceptions (like the transboundary pollution case) relatively small, whereas, given mass production, products nowadays are seldomly just meant for the national market. Indeed, as Schwartz (1996) argued in the American context, the imperatives of mass production require a manufacturer to sell the same product throughout the nation, so that the need for uniformity in product liability law seems huge. For the same reason Ackerman (1996) argues that product liability is in principle a good candidate for national law. These arguments, however, mainly amount to the point that uniformity in product liability law would come in ‘handy’ in the American context25, they do not explain why the mere fact that products cross national borders would constitute the risk that states would be able to shift external costs to others.

Indeed, the starting point for the analysis remains as Van den Bergh (1998, pp. 133–134) rightly points out, that different communities in the Member States may have different preferences concerning both the level of product safety and product liability law. The fact that these differing preferences lead to differing legal solutions should in principle, as be discussed above, be considered as a benefit instead of a problem. He therefore argues that a problem only

25. And might therefore fit into the transaction cost argument, to be discussed below.
arises if, e.g., a producer in the Netherlands would produce products which comply with the Dutch (supposedly low) product liability and product safety standards and would largely export products to, say, Belgium and France, where (again supposedly) the required level of product safety would be much higher. In this hypothesis a ‘transboundary externality’ problem would only arise if the consumers in Belgium and France would not have the possibility to file a lawsuit against the Dutch manufacturer. This problem is, however, not very realistic since the victims will in this case be the French and Belgian citizens which presumably have a higher product liability standard which would then also be applied on the Dutch manufacturer. In other words, manufacturers of defective products are generally liable in damages for harm suffered in export markets (Van den Bergh 1998, p. 141).

Of course, the fact that, in the example given, the manufacturer is located in the Netherlands and the products are marketed in Belgium and France and the harm is suffered equally in those countries may lead to a few practical problems for victims, but these do not necessarily immediately justify central regulation, with the corresponding loss of differentiated regulation according to preferences. First of all, choice of law regimes may be used to guarantee, e.g., that the French and the Belgians can have their (supposedly higher standard) product safety and product liability law applied. This, however, is criticised by Schwartz who points at the fact that in this example the court in say, France, will apply high standard French law on the Dutch manufacturer. The effect therefore is that the Dutch manufacturer will be confronted with the higher standard French law. From this Schwartz (1996) implies that a regime of state product liability law is hence inconvenient as a means for expressing state values. In the view of Schwartz France would express its sovereignty by subordinating the sovereignty of the Netherlands through the application of French law. Still, it can hardly be seen how this argument can justify central regulation. The effect of the choice of law regime is precisely that the Dutch manufacturer will not be able to externalise harm by shifting this only to export markets. Of course this presumes that a system is in place which allows the Belgian and French victims to sue the Dutch manufacturer. But this is, in the European context, precisely given through the (recently revised) European Convention with respect to the jurisdiction and execution of judgements of 1968. Of course one should be aware that even with this convention it might still remain difficult for victims to recover losses in another state (so Kirstein and Neunzig 1999). This practical problem can, however, not be remedied by harmonization. There are indeed no differences in legal rules that cause difficulties in the transboundary enforcement of claims, but different rules of civil procedure in the member states.
In sum, the mere fact that different states would hold different preferences with respect to product liability and product safety and that therefore different regimes would exist, can as such hardly be considered as an argument for centralisation as long as states are not capable of externalising harm to victims in third countries. A problem might in that respect merely exist, so Van den Bergh has argued, if the rules of the import country do not allow a full internalisation because the injurer may escape the payment of damages. Van den Bergh gives the example of a situation where a state would not allow recovery in tort in case of causal uncertainty, meaning that the manufacturer would not be held liable unless the victim can prove ‘beyond reasonable doubt’ that the particular manufacturer caused his loss. A problem could according to Van den Bergh (1998, p. 142) also arise if a legal system would not allow recovery of non-pecuniary losses. In those cases there would be inefficiencies in national product liability law of the importing state which would indeed allow exporting manufacturers to externalise harm. This, however, assumes that, e. g., the decision not to compensate non-pecuniary losses would be inefficient and would not be a reflection of national values and preferences of citizens.

3. Race for the Bottom

There may be an economic argument for a regulation of product safety problems, in that there is a risk that a ‘race for the bottom’ between countries would emerge to attract foreign investments. As a result of this, prisoners’ dilemmas could arise, whereby countries would fail to enact or enforce efficient legislation. Centralisation can be advanced as a remedy for these prisoners’ dilemmas. This ‘race for the bottom’ argument could, according to Van den Bergh (1998, pp. 136–139) in theory play a role in the case of product safety as well. It would mean that local governments would compete with lenient product safety regulation to attract industry. The result would be an overall reduction of product safety below efficient levels. This should correspond with the traditional game theoretical result that prisoners’ dilemmas create inefficiencies.

The basic idea behind this argument applied to product liability, is that product liability law may impose costs on industry. If governments would highly fear these costs and would prefer to favour national industry they could do so by lowering product standards. If lowering product standards would be a way to attract industry distortions could occur which would justify centralised decision making.

There are, however, some weaknesses in the application of this argument on the area of product safety. First of all product liability and product safety law may effectively create costs for manufacturing industry but these costs can often be passed on to the purchasers of the product. Second, it is as far as the liability of a producer in the sense of the product liability Directive (being the manufacturer) is concerned, also difficult for states to incur in a ‘race to the bottom’ for the simple reason that the harm may well occur in another state. Imagine, again, that France would like to attract industry with a lenient product liability regime. In doing so it can hardly attract manufacturing industries that largely depend upon the export market. Their exposure to product liability will indeed depend upon the legislation applicable in the state where the harm will occur. It is therefore, especially as far as the liability of manufacturers is concerned, unlikely that states would engage in a race to the bottom to attract industry.

This shows that the theoretical basis for a race to the bottom risk in case of product liability is relatively weak. This argument would only justify centralisation if it could be proven that without centralisation a risk of destructive competition would indeed emerge. There is no proof of such a destructive competition towards lower product liability standards and this risk is, moreover, not very realistic. Indeed, one can doubt that the law of tort and more particularly product liability, plays a significant role in attracting or repulsing businesses to or from a given state. Other elements, such as labour conditions, the amount of direct government regulation and taxes may be far more important than the level of product liability in location decisions of business. Moreover, if product liability were to have any effect as far as a race for the bottom is concerned, it is even more likely that states would wish to protect accident victims instead of corporate interest. Consumer advocates may call this a ‘race for the top’, although a system whereby foreign manufacturers are penalised with overprotective product liability law may well be considered inefficient and in that (reverse) sense a race towards the bottom.

30. In the words of Rose-Ackerman: “If state and local laws seem designed to protect local business rather than reflect genuine differences in tastes across jurisdiction, the federal government should take a hard look to determine the possible interference with interstate commerce” (1992a, p. 173).
4. Harmonising Marketing Conditions

In the European debate the question of centralisation has never focused on the 'race to the bottom'. In Europe a different, somewhat related argument has been used to harmonise legislation of the Member States in a variety of areas. This has been the legal argument that the creation of harmonised conditions of competition is necessary to avoid trade distortions. Simply stated, the argument runs that complying with legislation imposes costs on industry. If legislation is different these costs would differ as well and conditions of competition within the common market would not be equal. This argument apparently assumes that total equality of conditions of competition is necessary for the functioning of the common market. This argument, also referred to as 'levelling the playing field for European industry' is obviously closely related to the desire to create a common European market. This 'harmonisation of conditions of competition' argument is different than the economic 'race for the bottom'-argument and more linked to the European political idea of the creation of the common market. It is the traditional argument that uniformed rules in Europe are necessary to guarantee free movement of goods within the EC 33. What can be said about this argument?

Probably a difference should be made in this respect between product safety standards on the one hand and product liability rules on the other hand. It could be argued that differences in product safety standards may indeed endanger interstate trade. Therefore rules with respect to – inter alia – a free flow of products and services may certainly contribute to the European goal of market integration. Where the preamble to the Directive of 29 June 1992 on general product safety states that disparities and the absence of horizontal legislation in other Member States are liable to create barriers to trade and distortions of competition within the internal market, this is probably true. However, the question arises whether this goal of market integration can only be achieved via this far reaching instrument of total harmonisation and more particularly the question arises whether this may justify a harmonisation of rules of private law, such as product liability. Indeed, the political goal of market integration may justify the need for some rules aiming at the reduction of trade restrictions (think about the case law of the European court of justice with respect to the free movement of goods) and may justify a minimum harmonisation of product standards in the framework of the single market initiative. In that respect the Directive on general product safety in fact only pro-

vides for a general obligation to place only safe products on the market, but safety standards may still be drawn up in the Member State in which the product is in circulation or they may rely on codes of good practice, which need not necessarily be European\textsuperscript{34}.

Ogus (1994, pp. 177–179) is relatively enthusiastic on these product safety directives, precisely because the harmonization is limited to ‘essential safety requirements’. To meet these requirements the member states can still use their national standards, whereby voluntary standards, set by expert committees will allow for an easy mutual recognition. The approach chosen in the product safety directives therefore even promotes competition between different national and European standard systems, so Ogus.

The goal of ‘levelling the playing field’ is much more apparent in the product liability Directive. That Directive is clearly justified on the ground that differing liability rules in the Member States would hamper the conditions of competition. The considerations preceding the Directive read:

‘Whereas approximation of the laws of the Member States concerning the liability of the producer for damage caused by the defectiveness of his products is necessary because the existing divergences may distort competition and affect the movement of goods within the common market’.

The weakness of this argument is that it assumes that differences in marketing conditions are always and necessarily a problem for the creation of a common market. Conditions of competition are obviously never equal, as the ‘levelling the playing field’-argument assumes. In the ideal case of totally equal marketing conditions, there would also be no trade. This political goal of market integration may moreover be questioned on economic grounds\textsuperscript{35}. In addition one should realise that even if product liability law were totally harmonised in Europe, this would still not create a level playing field, since differences in, e.g., energy sources, access to raw materials and atmospheric conditions will still lead to diverting marketing conditions\textsuperscript{36}.

There is, in addition, a strong counter-argument, in that there are many examples showing that economic market integration is possible (without the distortions predicted by the race for the bottom argument) with differentiated legal orders. Public choice scholars, such as Frey (1994), have often advanced the Swiss federal model as an example where economic market integration goes hand in hand with differentiated legal systems. It is apparently possible to cre-

\textsuperscript{34} See article 4 (2) of the Directive 92/59 of 29 June 1992 on general product safety.
\textsuperscript{35} See for a critical analysis Van den Bergh (1999).
\textsuperscript{36} So Van den Bergh (1999, p. 6).
ate a common market without a total harmonisation of all legal rules and standards.37

Finally, ‘the proof of the pudding is in the eating’. The question can therefore be asked whether the European product liability Directive, as it has been drafted, can indeed achieve a total harmonisation of marketing conditions. This question will be addressed in the next Section.

5. Transaction Costs

There may, however, be one final economic argument in favour of harmonisation, based on transaction costs reduction. This argument is often advanced by European legal scholars pleading for harmonisation of private law in Europe, and is based on the argument that differences in legal systems are very complex and only serve Brussels law firms. This argument cannot be examined in detail here. It is obviously too simple to state that a harmonised legal system is always more efficient than differentiated legal rules because of the transaction costs savings inherent in harmonised rules. This argument neglects the fact that there are substantial benefits from differentiation whereby legislation can be adapted to the preferences of individuals. Moreover, given the differences between the legal systems (and legal cultures) in Europe the costs of harmonisation may be huge – if not prohibitive – as well. The crucial question therefore is whether the possible transaction costs savings of harmonisation outweigh the benefits of differentiated legal rules. There is little empirical evidence to support the statement that transaction costs savings could justify a European harmonisation of all kinds of legal rules. Moreover, the transaction cost savings are likely to be relatively small.

However, the transaction costs argument may play an important role to justify, again, a coordination of product safety standards to prevent states to hinder a free flow of products and services.

38. A somewhat related but different argument relates to economics and diseconomies of scale in administration, see Rose-Ackerman (1992a, pp. 165–166).
39. This is one of the arguments made by the Danish scholar Lando in favour of harmonized private law. Lando (1993, pp. 473–474).
40. It is further developed and criticized by Van den Bergh (1998, pp. 129–152).
41. Compare Rose-Ackerman (1992a, p. 172), who argues that uniform federal regulation may reduce search costs and tends to produce a more stable and predictable jurisprudence.
42. See, for the environmental cases: Mendelsohn (1986, p. 301).
43. That point has especially been made by Legrand (1997, p. 111).
Indeed, some co-operation between states seems necessary to avoid that if a product is mass produced and internationally distributed, interstate trade would be hampered as a result of varying national product safety standards. Indeed, also in international trade law it is well-known that diverging health, safety and related regulatory standards between countries of origin and countries of destination, especially in cases where these standards are more stringent in countries of destination, provide a source of allegations by countries of origin that they are subject to discrimination in countries of destination. This might result in a violation of the GATT and regulatory harmonisation will therefore occur to minimise product incompatibilities to allow producers to maximise access to export markets. Harmonisation is therefore certainly useful to avoid pointless incompatibilities which do not reflect different preferences. These transaction costs arguments do therefore apply in the field of economic regulation and product safety. Indeed, the information required to formulate these rules may be useful for the whole of Europe and the formulation of uniform rules in these cases may save on information costs and can hence, promote interstate trade. Therefore, once more, the Directive on general product safety, taken in the framework of the 1992 program to establish the internal market may well be considered as an instrument which saves on transaction costs.

The question, however, arises whether these transaction costs saving as a result of harmonised rules can also be expected for product liability. One could argue that a manufacturer who markets his products Europeanwide would, in the absence of harmonisation, need specialised legal counsel in every state and their insurance-underwriters would have to calculate the liability exposure separately in accordance with each state's product liability law. This argument, however, as mentioned above, neglects the fact that there is a benefit in differentiated liability rules, which reflect varying preferences. Moreover, the costs of harmonisation in the field of private law (which is so rooted in legal culture) may be huge and the alleged transaction costs savings may be less than expected. Indeed, even in case of a harmonised legal rule, manufacturers still would need local counsels to try cases. Accordingly, scale economies under a harmonised rule would likely be insignificant. Here again ‘the proof of the pudding is in the eating’, so that the question arises whether the European prod-

47. So Trebilcock and Howse (1998, pp. 21 and 30).
uct liability Directive has been able to create the legal certainty required, reduc-
ing transaction costs for manufacturers51. One may conclude so far that there are a few arguments in favour of harmonised product safety standards, the most important one being the facilitating of interstate trade via uniformity and reduced transaction costs. There are, however, fewer arguments at first sight in favour of harmonised product liability rules.

6. Balance

There would be arguments in favour of centralised European rule making if 1. there would be inefficiencies in national product liability law which would allow manufacturers to externalise damage caused by product defects or 2. if it would be established that states could attract industry with lenient product safety standards. The latter is, however, unlikely since states would to the contrary enact legislation to protect victims of product accidents within their own jurisdiction with high standard product liability legislation. There may be transaction costs savings of uniform product liability law if a Directive would be able to create legal certainty and achieve a full harmonisation, which needs to be examined below. The answer to that question is also relevant to verify the justification given by the European Commission for the European product liability Directive, being that it would harmonise marketing conditions in Europe. The question therefore arises whether the European product liability Directive has been able to achieve those goals.

IV. EFFECTIVENESS OF THE PRODUCT LIABILITY DIRECTIVE OF 1985


As we have stated above (see Section II.1.) the European products liability Directive had two goals: first, it aimed at creating equal marketing conditions to

51. Van den Bergh rightly points at lots of interpretation problems in the European product liability Directive (which we will discuss below) which backs up the conclusion that the transaction costs savings may be small, simply because a full harmonisation of rules of private law is apparently difficult to achieve (Van den Bergh 1998, pp. 146–147).
PRODUCT LIABILITY AND PRODUCT SAFETY IN EUROPE

‘avoid distortions of competition’. Second, it wished to achieve a high level of consumer protection. Both goals can, within the focus of this paper, be rephrased in economic terms. The question whether the product liability Directive actually leads to harmonisation is obviously useful to judge the desirability of a European action in the first place. If the Directive would have been able to create full harmonisation of product liability, it might have created transactions costs savings to such an extent that they may have outweighed the advantages of differing product liability laws. The question whether the contents of the Directive leads to an increased consumer protection may simply be rephrased by asking whether the product liability regime chosen in the Directive promotes economic efficiency.

2. Harmonisation?

A first question which had to be asked is whether the justification given in the considerations preceding the Directive, being that the existing divergences before the product liability Directive may distort competition and affect the movement of goods within the common market is actually correct. It is undoubtedly true to argue that before 1985 there were different product liability regimes in the Member States, but the question arises whether these differences were that important that they ‘may distort competition and affect the movement of goods within the common market’, as the product liability Directive argues. A Dutch author, Van Wassenaer van Catwijck (1986, p. 81), has indicated that although the product liability regimes did indeed differ, insurance premiums for the coverage of the product liability risk were not substantially different. If that is true, the differences in marketing conditions where probably not as large as the Commission holds. More important is obviously the question whether the Directive in the 1985 version could at all reach the harmonisation goal. It is in fact very unlikely that this is the case.

Indeed: according to article 13 all the different, already existing, product liability laws remain in effect, which means that already existing differences will remain unchanged. In addition at many points the Directive itself refers to national legislation, e. g., with respect to the rights of contribution or recourse (article 5 and 8,1), with respect to non-material damage (article 9), the suspension or interruption of the limitation period (article 10,2) and with respect to nuclear accidents (article 14). It should also be mentioned that in three cases the Directive expressly allowed the Member States to derogate from the provisions of the Directive, – namely liability for primary agricultural products, liability for development risks and the introduction of a financial limit on liability. Moreover,
the Directive cannot of course bring any harmonisation for all the product accidents to which it does not apply, because of limitations in the definitions of ‘product’, ‘producer’ and ‘damage’. Many notions in the Directive are also unclear and can give rise to interpretation problems\textsuperscript{52}. These problems might lead to different interpretations of the provisions of the Directive by the legislator and courts of the different Member States. These interpretation problems can be solved by the European Court of Justice in Luxembourg. But it often takes a long time before an interpretation problem is brought before the Court and as long as there is no definitive solution, these interpretation problems of unclear notions in the Directive might again endanger the harmonisation objective. Interpretational problems are all the more likely in practice since even the language differences of the various translations of the Directive can lead to different interpretations of the same provision\textsuperscript{53}.

It was just mentioned that the product liability Directive gave several options to the Member States, concerning the including of primary agricultural products, the liability for development risks and the possibility to introduce a financial limit on liability. This has obviously also caused differences, as we just indicated. These differences as far as the transposition of the Directive in domestic law is concerned are shown in the annex 1 to the green paper on liability for defective products which is included in the Appendix to this paper.

Since it is clear that this product liability Directive cannot reach an approximation of the Member States Legislation, it has been suggested that this was only used as an argument to give the EC competence in this matter\textsuperscript{54}.

There are other inconsistencies that are worth mentioning in an effectiveness evaluation of the Directive. Both the introduction of the 10 year extinguishing period and the optional introduction of a financial limit on liability have been defended by referring to the introduction of liability for development risks. In the final version the producer is in principle not liable for development risks, but nevertheless the extinguishing period as well as the optional financial limit remained, although the reason given has disappeared. In addition one notices that the Directive is said to introduce a ‘liability without fault’, but nevertheless

\textsuperscript{52} One can, e. g., think about the defect notion in article 6, which might lead to different interpretations.

\textsuperscript{53} See for instance the different meaning of the ‘lower threshold’ of article 9 in the french and the dutch version. Another example is that in the english text the producer’s liability is called a ‘liability without fault’ whereas in the dutch version it is just mentioned ‘liability’. For other examples see Faure and Vanbuggenhout (1987–1988).

\textsuperscript{54} Article 100 of the EEC treaty indeed gave legislative competence to the community in order to harmonize the different legislations of the Member States. It was, however, heavily debated whether this article 100 was an appropriate basis to ground the legislative power of the EC with respect to product liability (see Krämer 1986).
the conduct of the producer will still be important, e. g., when the defectiveness of a product is assessed and with respect to the defect notion. So, in fact the fault notion still plays a role in establishing whether there is liability under the Directive.

For all these reasons some authors qualify the Directive itself as a defective product.55

3. Efficiency and Consumer Protection

The Directive also claims to provide an increased consumer protection. The question arises whether the Directive is indeed aiming at the protection of consumers. Moreover, this question can also be rephrased by asking whether the Directive promotes economic efficiency.

1. Consumer Protection?

As far as the ‘protection of the consumer’ is concerned one can argue that in comparison with existing product liability schemes in some Member States, e. g., Germany and France, the Directive did not add a lot as far as consumer protection is concerned.56

Indeed: damage caused by primary agricultural products was excluded from the scope of the Directive. For material damage there is a lower threshold. There are short limitation and extinguishing periods. The Member States can even introduce a financial limit on liability. One could oppose to these remarks that for some countries, which had no product liability system at all the Directive substantially improves the situation of the victim of a defective product. One could say the same for countries which already had a product liability system since according to article 13 the liability system of the Directive is only added to the already existing system, so that the victim is always better off. This is however, only true on a short-term basis. Most authors hold that the Member States are not allowed to introduce after July, 30th, 1985 a product liability system which would give more rights to the victim than does the Directive.58 This interpretation is also followed in the green paper. If this were true, then the Di-

55. This is the title of the article by Storm (1985).
56. For a comparison between the European products liability Directive and German/French law see Van Wassenaer van Catwijck (1986, pp. 80–81).
57. Which basically means that the victim had a tort based action in which he had to prove a fault of the producer.
58. See Duintjer Tebbens (1986, p. 373) and Van Wassenaer van Catwijck (1986, p. 81).
receptive does limit the right of Member States and also limits the ‘protection of the consumer’ in the future. It is therefore unclear even whether the Directive does indeed provide ‘consumer protection’, certainly when one regards this on a long-term basis.

A detail which should also be mentioned, is that the notion ‘consumer protection’, which is so often used in the considerations preceding the Directive, is in fact misleading. A ‘consumer’ is a purchaser, who buys a product. The Directive is, of course, not at all limited to a protection of the buyer of the product. Also third parties that suffer harm from a defective product can benefit from the protection of the Directive. Indeed, for many Member States the main improvement of the Directive is that also third – parties now benefit from the strict liability of the producer. The damage suffered by someone who stood in a contractual relationship with the producer (the ‘consumer’), was often already subjected to strict liability of the producer. In addition, the damage caused to a victim ‘as consumer’ being the damage caused to the purchased product itself, is excluded by article 9 (b) of the Directive. For these reasons it appears that the term ‘consumer protection’ which is so often used with respect to the Directive, is not that well chosen. What is meant is the protection of the victim, whether this is a consumer or not.

2. Some Economic Effects of the EC Directive

Apparently the drafters of the EC Directive judged that the best way to realise the ‘protection of the consumer’, of which they spoke so much, was to implement a generalised strict liability rule for harm caused by a product defect. It is striking that when one compares this rule with the economic theory of product liability, the Directive advances one single rule to deal with all product accidents, whereas the economic theory is much more balanced and detailed. Depending upon whether or not the victim is a consumer, whether the latter has information on the product risk, what the influence of insurance is etc., economic theory would only hold that a strict liability rule is efficient in some cases, but certainly not in all (Silva and Cavaliere 2000).

59. This is of course more painful for Member States which had no product liability law on July, 30th, 1985 than for Member States which already had an elaborated product liability system on that date.
60. Also Cornelis (1987–1988, pp. 1158–1159) notices that in comparison with previously existing Belgian Product Liability Law, the victim is worse off under the applicability of the Directive.
At the policy level it is, using all the relevant criteria, almost impossible to give advice to the legislator to use one single rule for all product accidents. There is even a question as to whether the legislator would have to define such a rule. An obvious alternative would be to let the judge decide what type of liability rule should govern the product accident (Epstein 1988). Thus case law could take into account all the relevant criteria and the application of the strict liability rule could be limited to certain product accidents. The Directive, which introduces one strict liability rule for all product accidents, disregards all the various factual situations, which make different liability rules efficient. Thus, by using one single rule inefficiencies will unavoidably be created since the strict liability rule will also be applied where this would be inefficient taking into account the economic criteria. It is also doubtful whether the savings in administrative costs by using one legal rule outweigh the inefficiencies. The costs of applying the economic criteria for strict liability should not be that high either. Especially if they can easily be recognised (e.g., whether the victim was a consumer or a third party) an individualised product liability system, where strict liability will only be applied in some cases, could be used by the judge at relatively low costs.

One of the criteria was also applied for a long time in legal practice. Indeed: in most legal systems product accidents whereby the victim stood in a contractual relationship with the producer were treated differently from those where the victim is a complete stranger to the producer. One of the reasons for introducing the generalised strict liability in the Directive was that this different treatment was considered ‘unjust’. However, this distinction is quite sound from an economic point of view. If the victim stands in a contractual relationship with the producer a coasean solution (Coase 1960) is in principle possible if the consumer is well informed on the accident risk (Buchanan 1970 and Oi 1973). Such a solution is of course always excluded in the event that the victim is a third party because of the prohibitive transaction costs. For that reason Goldberg (1974) critized the idea of applying the Coase theorem on product liability. So there is a good economic reason for treating both situations differently.

Of course the EC Directive does not introduce a general strict liability rule for all damage caused by a product. The producer will only be liable when the damage was caused through a defect in the product. It looks like this is more a fault liability since a product is often defective because the producer did not take efficient care. However, liability is indeed strict since the producer will always incur liability when harm was caused by a defect in his product even if he can prove to have taken due care. The producer only escapes liability when the harm was not caused by a defect of the product. Given the broad defect notio
in the Directive a product is almost already considered defective by the mere fact of having caused the harm. Therefore, there is not, from an economic point of view, a substantial difference between a strict liability for all damage caused by a product and strict liability for damage caused by a defect in the product as in the Directive.

It was mentioned above that the general strict liability rule for all activities, which is used in the Directive, might create inefficiencies since it will also be applied in cases where a fault rule would be preferable from an efficiency-view-point. It should not be forgotten, however, that the purpose of the Directive was the harmonisation of product liability law in Europe. If this should succeed it could create benefits which could easily outweigh the disadvantages of the generalised strict liability rule discussed above. Indeed, if a single product liability rule were to be created in all Member States this could contribute to the creation of equal marketing conditions and thus to the realisation of the internal market. This could bring substantial savings which could easily outweigh the inefficiency of the use of a single rule. This, however, will not be the case in practice since it was shown in the previous subsection that the Directive can never bring a harmonisation of product liability law in Europe. So the inefficiencies remain without any compensating benefit for the realisation of the internal market.

3. Distributional Effects

One could go one step further and argue that the Directive does not only create several inefficiencies, but that it is also problematic from a distributive point of view. Many lawyers favour the introduction of strict liability since it would protect the consumer. It is even argued that strict liability would be necessary to restore the broken balance between producers and consumers. The Coase-theorem teaches that in product liability from a distributive point of view there will be no difference between a fault rule and a strict liability rule. Fully informed consumers will only take into account the full price of the product (cost price + expected accident costs) and will base their purchase decision upon this full price. Even if the legislator would like to protect the consumer by introducing a strict liability rule, the producer will still add the expected accident costs.

62. One could argue that as soon as a product causes serious injuries it does not provide the safety which a person is entitled to expect and is therefore defective according to article 6 of the Directive.

to the cost price. The consumer will again pay the full price since the expected accident costs are passed on to him, which is reflected in a higher market price. Since producers and consumers are bound through the price mechanism, every shift of liability to the producer will be passed on to the consumer. In this setting a legal intervention to redistribute wealth to the consumer by introducing a strict liability rule seems therefore useless.\(^6\)

When consumer groups are heterogeneous, the introduction of strict liability will even have adverse distributional effects. Indeed: the most important part of damages is lost income. The expected damages are therefore of course higher for high-income consumers than for low-income consumers. The producer will, however, take into account an average expected damage and will add this to his cost price to get one single market price for all consumers. The effect is that when low-income consumers still buy the product, they ‘pay’ for the expected damages of the high-income consumers. Therefore Adams (1987) holds that strict liability in a product liability setting creates a redistribution from poor to rich consumers. For the same reason Priest (1987) argued that the product liability explosion in the US hurts especially the low-income groups.

This effect will be stronger still when the strict liability rule does not only apply on harm suffered by consumers, but is extended to damage caused to third parties, as the EC Directive does. In that case the market price will again be higher since the producer will also have to pay for damage caused to third parties. The increased expected damages will again be passed on to the consumer who pays a higher market price for the damage a product he bought can cause to third parties. The consumer has no possibility to pass on this increased price and therefore he, in effect, pays for the protection of third parties.

So the expansion of strict liability to damage caused to third parties redistributes wealth from consumers (of the product) to third parties. Consumers will indeed have to pay for the protection of third parties. This again increases the adverse redistributive effect of poor consumers paying higher prices for the expected damages of third parties. Since lost income is an important part of the damage, again the high-income groups do indeed benefit from the redistribution.

This shows that the generalised strict liability which has been introduced by the EC Directive will not only create inefficiencies, but is also based on wrong ideas concerning the protection of consumers.

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4. Curing Externalities?

So far, in our analysis of the European product liability Directive, we argued that the Directive can hardly lead to a harmonisation of marketing conditions or to a lowering of transaction costs (given all uncertainties and information problems). Another point, made by Van den Bergh (1998, p. 145), is that the product liability Directive can also not be considered to cure the risk of externalising damage caused by defective products since the Directive does not address the issue where such a risk of externalisation may occur. First of all Van den Bergh refers to the fact that such an externalisation may occur in case non-pecuniary losses are insufficiently compensated under national law, which may lead to underdeterrence. Another problem may arise if full scientific proof of a causal link with a certain product defect is required and, e.g., proportionate liability is not accepted. The Directive does not cure these problems, since it does not touch upon the issue of causation, nor upon the compensation of non-pecuniary loss, which is explicitly left to the national Member States. Moreover, the Directive allows for a financial limit on compensation which is generally considered inefficient, especially in case of strict liability. Therefore the Directive in fact increases the risk of cross border externalities, so Van den Bergh (1998) argues. Finally there is a problem since the Directive, as we indicated above, does not apply to retailers. Above it was indicated that a state can not attract industry with lenient product liability legislation for manufacturers, but it could attract retailers by doing so. The EC Directive does not cure that risk since it does in principle not apply to retailers.

4. Test

After this analysis of the effectiveness of the European product liability Directive, it seems that the way the product liability Directive is structured makes the case for European harmonisation in fact even weaker. If we compare the analysis of the effectiveness of the Directive presented in this Section with the criteria for centralisation discussed in the previous Section we can conclude as follows:

1. The EC product liability Directive is not able to cure the risk of interstate externalities caused by product damage, if there were already such a risk.

PRODUCT LIABILITY AND PRODUCT SAFETY IN EUROPE

2. There is no empirical evidence of a risk that states could attract manufacturers with lenient product liability legislation (the Directive only applying to manufacturers). On the contrary, there might be a risk of a ‘race for the top’, protecting national victims of product related accidents.

3. The product liability Directive can, given its high reliance on national law, never lead to a ‘levelling of the playing field’ or a ‘harmonisation of marketing conditions’.

4. The product liability Directive, which in fact adds an additional layer of complexity to the labyrinth of conflicting standards of liability does not lead to uniformity or a lowering of transaction costs.\(^68\)

Obviously many of these weaknesses are well known to the European Commission itself. Precisely for that reason the product liability Directive provided for a review every five years

‘in fact to proceed towards greater harmonisation with a view to establishing a regulatory framework which is as comprehensive, coherent, balanced and effective as possible for protecting victims and ensuring legal certainty for producers’.\(^69\)

V. PUBLIC CHOICE CONSIDERATIONS

A question which can obviously not be avoided is whether some of the inefficiencies found with respect to the product liability Directive can be explained on the basis of public choice theory, which pays a lot of attention to the role of interest groups in legislation.\(^70\) Many scholars have written about the lack of transparency at the European level and the strong lobbying activities in Europe. Several aspects of the European product liability Directive can undoubtedly be considered the result of lobbying.

Interest group considerations might explain why at all a product liability Directive came into being. Since it can not achieve a ‘harmonisation of marketing conditions’ the Directive might have another reason than the formally stated goal. One important reason might have been the fear of producers in Europe for an American type product liability crisis. As we indicated above (at Section II.1.1.) one motive for the Directive was to avoid that some Member States would go too far in their wish to protect ‘consumers’. The Directive aims at a

69. Green paper on liability for defective products, p. 11.
balanced approach, so it is stressed many times in the green paper. For that reason the manufacturers are also ‘protected’ with, e.g., some defences, thresholds, relatively short statutes of limitations and the option to impose a financial cap on liability. Since the Directive is clearly mandatory for the areas it covers (meaning that Member States are not allowed to go further in protecting victims in the areas which the Directive covers), the Directive could at least avoid that some Member States might introduce too far reaching product liability regimes. But the Directive may also be considered ‘defective’ in reaching that goal since the areas which could precisely have given rise to an increase in liability exposure, e.g., the non-pecuniary losses, are not dealt with by the Directive.

Public choice explanations might also have influenced specific features of the Directive. This is obviously the case for the initial exclusion of primary agricultural products from the scope of the Directive. Some authors held that indeed the increased protection of strict liability is only necessary against the increasing risks of modern industrial production. Strict liability for agricultural products would unnecessarily increase the insurance burden71. This explanation, however, is not convincing. Even if agricultural products were produced industrially, they were still excluded from the scope of the Directive. This means that a consumer will not be able to claim damages against a breeder of veal who has employed artificial hormones or against a grain producer who used dangerous pesticides72. It is not at all clear why strict liability would not be necessary for those cases. The real reason for the exclusion of primary agricultural products was in fact that European farmers engaged in successful lobbying and convinced the politicians that the Directive’s strict liability should not be applicable to them73.

Another example constitutes the proposal which was made during the discussion preceding the EC product liability Directive to set up a compensation fund as alternative to product liability. This, however, stood no chance as a result of lobbying by the insurance industry who feared losing business74. Therefore Van den Bergh (1998, p. 151) argues that the European product liability Directive is to a large extent to be considered as the result of rent seeking by industry instead of an instrument to increase economic welfare.

The same can be said, moreover, for the general justification for many European Directives, being the ‘harmonisation of conditions of competition’. This argument is often used by industry in Member States where already strict

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national regulation applies. In those cases the European harmonisation has the main effect that artificial barriers to entry are erected. This might also have played a role in the context of the European product liability Directive and it merits even careful analysis whether this has not played a role as well with respect to the general product safety Directive. One may not forget that in some Member States, especially in the North, such as Germany, the Netherlands and Belgium, a relatively high and elaborated level of product safety existed. If this were the case, industry in those Member States would have an interest to lobby for stringent safety standards at the European level, for the simple reason that they already have to comply with the safety standards nationally. By making their stringent national standards the European norm they can impose these stringent norms also upon the southern competitors. Indeed, as Ogus (1994, p. 198) holds: producers will favour stringent specification standards if they result in protection against domestic and foreign competitors. One should, therefore, always be careful with the ‘harmonisation of conditions of competition’-argument, as it is presented in European rhetoric, since it may be in the interest of particular interest groups that ‘conditions of competition’ are harmonised.

Moreover, one should also be careful with respect to the European product safety Directive in so far as this refers to technical specification standards or codes of good practice. Indeed, these standards may, once more, function effectively as barriers to entry. This is a point that certainly merits further empirical investigation.

Finally in the context of a public choice analysis, one should obviously also point at the interests of the European bureaucracy itself. Until 1985 Europe had done relatively little as far as the harmonisation of private law is concerned (for obvious reasons of differing legal cultures). It is possible that a European product liability Directive, although it did not fulfill the economic criteria for centralisation, might have served the interests of the Brussels bureaucracy. The Directive allowed them to show that Europe could bring about a piece of legislation in an area which is considered important by many lawyers, touches upon manufacturers interests and is moreover very sensitive in the public opinion. Hence, the fact that the Commission wanted a European product liability Directive may to some extent also simply have been due to the prestige that this Directive would, as one of the first in the area of private law, provide the European Commission.
VI. RECENT DEVELOPMENTS

1. Including Primary Agricultural Products

There was increasing criticism on the exclusion of primary agricultural products after the BSE-crisis. An effect of the exclusion of primary agricultural products from the scope of liability under the Directive was obviously that the liability will in fact be passed on to the industrial processor or producer. If, e.g., baby food has been derived from veal which has been treated with hormones, this will not lay a strict liability on the farmer, but on the producer of the finished product. Of course the cattle breeder might be liable under a fault rule, according to his national tort law.

For these reasons the product liability Directive was amended by Directive 1999/34/EC of 10 May 1999. The goal of this Directive is to amend the product liability Directive to include defective agricultural products as well. Again, the functioning of the internal market is given as the most important justification:

'It is necessary and appropriate in order to achieve the fundamental objectives of increased protection for all consumers and the proper functioning of the internal market to include agricultural products within the scope of Directive 85/374/EEC.'

The idea is that including primary agricultural products within the scope of the product liability Directive would help to restore consumer confidence in the safety of agricultural products. This Directive, including the agricultural products simply changed the definition of ‘product’ in the product liability Directive of 1985 and enters into force on the day of its publication in the Official Journal, which was 4 June 1999.

One could argue that with this new Directive, forcing the Member States to apply the product liability regime mandatorily also on agricultural products, (whereas before this was optional) one of the criticisms on the Directive (protecting the farmers as a result of lobbying) has disappeared. However, this quick action of the Commission shows probably more that the sensitivity to the European public opinion and the decreasing influence of the agricultural lobby are more important reasons for action by the European Commission than the concerns to promote economic welfare.

2. Green Paper on Liability for Defective Products

1. Objectives of the Green Paper

The product liability Directive of 1985 had called for a five year review to analyse the working of the Directive. This five year review has resulted in a green paper of the Commission which was launched on 28 July 1999. It is addressed to the larger European business and consumer community with two aims:

1. It allows to seek information which will serve to assess its application in the field in view of the experience of those concerned (in particular industry and consumers) and to establish definitely whether it is achieving its objectives;
2. It serves to ‘gauge’ reaction to a possible revision as regards the most sensitive points of this legislation.

The Commission wishes to promote the reflection and debate and therefore invites replies provided on facts. Obviously the Commission has indicated guidelines for discussion concerning all of the important topics in the product liability area, such as the existence of financial limits, the 10 year deadline, the burden of proof, the assessment of the insurability of risks, the suppliers’ liability and the type of goods and damage covered. Although the green paper clearly states that it does not prejudge the Commission’s position on these area the fact that a lot of topics which were previously highly criticised are now put on the agenda for possible reform is interesting in the light of the analysis provided in this paper.

2. Inefficiencies Revisited?

First, a number of features of the product liability Directive which could be criticised from an economic perspective are now openly put on the agenda for possible review (which will obviously not necessarily mean that such a review will take place). Interesting in that respect are inter alia:

– The fact that the financial limit on liability is put on the agenda for possible reform. There has been debate to increase the option for a ceiling to EUR 140 million, but the question is equally asked whether the existence of financial limits is strictly justified.

78. See article 21 of the product liability Directive which states ‘Every five years the Commission shall present a report to the Council on the application of this Directive, and, if necessary, shall submit appropriate proposals to it’.
79. See green paper on liability for defective products, p. 2.
– The Commission is also asking the question whether there would be a need to require producers to have insurance cover for risks linked to production. Currently the product liability Directive does not require producers to have any kind of financial cover. Economic analysis indicated that strict liability with insolvency may create inefficiencies, so that this question certainly merits attention.

– The question is also addressed whether the product liability under the Directive should be extended to suppliers. So far, the product liability Directive, with a few extensions, only applied to manufacturers. In that respect the criticism was formulated in the literature that if retailers are excluded from the product liability regime, the Directive can also not be considered as an appropriate means to cure a ‘race for the bottom risk’ discussed above.

It is interesting that some of the issues which were criticised from an economic perspective are now open to possible review. From a normative perspective it can of course be hoped that the European Commission takes the lessons from economic analysis into account.

3. More Transparency?

Second, there seems to be a trend towards more transparency in the (European) decision-making process, at least on paper. One of the criticisms which could be made on the way that the product liability Directive of 1985 came into being was that apparently lots of interest have played a role, but that it is not easy to find out what the precise results of the lobbying activities were. The Commission now invites comments on the green paper in the widest possible spirit of transparency:

'It was the Commission’s intention that the assessment process should be governed by transparency and that producers, consumers, insurers, practitioners and any other sectors concerned should be able to make known their experience and views on implementation and the subsequent development of producers’ liability. In this spirit of transparency, the replies will not be confidential and can be made public unless the participants in the consultation process explicitly request otherwise’.

Transparency is also an issue as far as the contents of the Directive is concerned. The Commission regrets that today there is no provision in the Directive for any means of making its implementation more transparent. There is, e.g., no obligation on producers to keep records of claims against them. The Commission therefore asks whether it would be useful to increase the transpar-

ency of the way in which operators apply the rules, especially by identifying the cases involving defective products that are still on the market.82

This increasing attention for the transparency issue seems of course nice on paper and corresponds with a general concern in Brussels to react to the criticisms concerning the lack of transparency. If the review procedure concerning the Directive would indeed be truly transparent, this would obviously make lobbying efforts for industry far more costly and might indeed increase the chances that the Directive would be reviewed in a way which corresponds more with public interest.

However, the green paper clearly still is very much concerned with the evolutions of product liability law in the US. Differences between European product liability law and US product liability are extensively discussed in the green paper, among others the issue of punitive damages. The Commission concludes:

‘Seen in this light, the European producer is better off, as the European Directive establishes a uniform and coherent framework of liability, without the most criticised elements of the American system (the role of juries, punitive damages, etc.)’83.

The central goal for a possible revision of the product liability Directive should therefore, in the words of the Commission be ‘maintaining the balance’. The Commission holds that apparently the European system of product liability constitutes a conciliatory approach, balancing interests of both producers and consumers. The Commission sets as a guideline that this internal balance of the European product liability Directive should be maintained.84

Therefore one can not escape the impression that already this green paper on liability for defective products has largely been issued because of the still growing concern concerning the expanding American product liability regime and the corresponding need to protect European business. This concern to maintain the position of European business in ‘the global context’ appears clearly from the questions in this respect, which the Commission puts as follows:

‘Do you think that the Directive weakens the position of European businesses vis-à-vis their foreign competitors because of the conditions governing liability for defective products?’

What are the main reasons for this, and how can it be avoided?87

What is the impact of European businesses of exporting products to markets with stricter legislation (or legal practice) such as the United States (in terms of costs, production methods, insurance, level of litigation etc.)?88

4. Subsidiarity?

Third, an interesting question obviously arises how the Commission considers the task of Europe now that it has (differently than in 1985) to take into account the subsidiarity principle. Does it accept the consequence of ‘less Europe’ for product liability? The Commission has on the one hand, as we just indicated, a lot of attention for the effects of European product liability on the global position of European business, but on the other hand also for the effects of the Directive on intra community trade. The Commission repeats that the internal market was the goal for the coming in the being of the product liability Directive:

‘The existence of harmonised legal conditions is intended to make trade easier, since the producer is in the same legal position no matter where his products are distributed’\(^86\).

The Commission, however, agrees that the system of harmonisation which is provided in the Directive is ‘both incomplete and complementary to any other national producer liability scheme’, as we have equally indicated above. However, the Commission argues that the Directive of 1985 should only be seen as an initial step towards establishing a genuine producer liability policy at community level and that the process of reviewing the Directive is in fact to proceed towards greater harmonisation. The Commission acknowledges that the objective of a total harmonisation can only be reached by upholding the present position that no Member State can adopt stricter rules under the Directive. Without spending a lot of words on this, the Commission nevertheless asks the question whether it would be useful to allow each Member State to adopt stricter liability rules, therefore introducing a ‘minimum’ clause in the Directive\(^87\).

Although formulated most cautiously, the Commission obviously acknowledges that the Directive in its current form can never reach the goal of total harmonisation and therefore at least opens the discussion whether Member States should be allowed to adopt stricter rules. The question whether, in the light of subsidiarity, even more powers to the Member States in this area would be justified, is however not discussed by the Commission.

3. White Paper on Environmental Liability

Very recently the Commission also launched a white paper on environmental liability\(^88\). It is interesting to take a brief look at this white paper on environ-

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86. Green paper on liability for defective products, p. 10.
87. See green paper on liability for defective products, pp. 11–12.
mental liability to see how the Commission deals with the subsidiarity issue in yet another area of private law. The Commission's approach seems to be far more careful in this area than with respect to product liability where a 'total harmonisation' is apparently the policy goal. The Commission proposes a strict liability for dangerous activities which are regulated by EC environment related law for traditional damage (health and property) contaminated sites and damage to bio diversity. For non-dangerous activities there will be a fault based liability for damage to bio diversity. Here, the Commission apparently does not propose a European-wide similar environmental liability regime, but links the EC liability regime with existing EC environmental legislation. The idea is that by using liability law, the implementation of EC environmental legislation can be promoted. Obviously, the argument that a community regime for environmental liability should be drafted 'to create a level playing field' in the internal market is again mentioned, but at the same time the Commission states that the existence of any problem of competition in the internal market caused by differences in Member States’ environmental liability approaches is still unclear. The Commission specifically focuses its environmental liability regime on damage to bio diversity since most existing Member States environmental liability regimes do not cover this type of damage. The approach seems therefore to be rather balanced in that it focuses merely on those areas where Member States have apparently not enacted legislation and limits itself largely to liability resulting from activities regulated under EC environment related law.

Moreover, the subsidiarity issue is explicitly addressed, stating that the Commission in fact only intervenes to guarantee that the goal of article 174 (1) of the EC treaty (which requires the community policy on the environment to contribute to preserving, protecting and improving the quality of the environment, and to protecting human health) can be achieved. Interestingly enough the Commission also discusses the possibility to install a European regime for transboundary damage only. In the literature it has been suggested that if inter-state externalities are a reason for centralisation, the European Directive should not necessarily cover both local and community-wide pollution. This idea of a ‘transboundary only’ regime was rejected, since this could lead to inequalities in treatment of victims in Member States depending on whether they were vic-

89. White paper on environmental liability, p. 12.
91. White paper on environmental liability, p. 27.
92. Van den Bergh suggested that a distinction should be made between regional and interstate pollution (Van den Bergh 1999, p. 10).
tim of a transboundary or a local pollution. Nevertheless this white paper on environmental liability shows that the Commission recently (the white paper was issued on 9 February 2000) seems at least to be aware of the arguments advanced in economic literature in favour of (de)centralisation and at least discusses them.

VII. CONCLUDING REMARKS

In this paper I looked at the question whether product liability and product safety in Europe should be regulated in a decentralised or centralised manner. After a description of the main features of the product liability and product safety Directives, the economic literature was examined to look at the question whether product safety and product liability should be centralised or decentralised. Europe has traditionally justified harmonisation in all kind of areas, also for product liability, by referring to the traditional argument that conditions of competition should be harmonised ‘to create a level playing field’. This argument seems, however, far too general to fit into the economic criteria for centralisation. These provide for more balanced answers with respect to the types of subject matters which should be regulated at the centralised or at the decentralised level. These economic criteria were confronted with the way mainly the product liability Directive of 1985 is shaped. The conclusion was that this product liability Directive shows on the one hand many inefficiencies and defects. It also seems unable to reach its goal of ‘harmonisation of marketing conditions’. This objective as such has also been criticised on economic grounds since it does not necessarily correspond with economic efficiency.

The main economic argument in favour of centralisation, a reduction of transaction costs, may work for product safety, but is far less convincing for instruments of private law, such as product liability. But also as far as product safety is concerned one should not accept a harmonisation of product standards without any critical analysis. If product safety harmonisation merely aims at removing useless incompatibilities, such a harmonisation seems a useful tool to facilitate international trade. So far, the product safety directives often limited the harmonization to ‘essential safety requirements’ and thus provided room for competition between various standard systems (Ogus 1994). However, the danger always exists that in fact high safety standards are introduced at the European level as mandatory safety regulations to create barriers to entry. Also the

various European safety regulation Directives therefore certainly merit further research.

Given the fact that the product liability Directive in its current form can not reach the objectives it has set and shows various defects and inefficiencies, it may to some extent be explained as the result of lobbying by interest groups. Industrial interest groups probably wished a European product liability Directive which balanced the interests of producers and consumers in order to avoid an ‘American’ product liability crisis. Moreover, even the Commission argued (in the green paper on liability for defective products) that the product liability Directive was only a first step towards harmonisation. The own interests of the European bureaucracy of the Commission probably also explained the willingness of the Commission to issue a Directive in the area of liability law, although it should have been clear for the Commission as well that this Directive could never meet the goal of harmonisation of marketing conditions.

Product liability in Europe has come to a crucial point now, since the Commission has invited all interested parties via a green paper to comment on the future of the product liability Directive. On paper the Commission calls for more transparency, which may reduce the influence of interest groups. In addition there seems to be, although limited, scope for taking the subsidiarity principles serious, also with respect to product liability. The Commission advanced the option of merely having a basic European product liability regime and giving powers to the Member States to adopt stricter rules (which is not allowed under the product liability Directive today). It would be desirable that at the occasion of this debate on the revision of the Directive the Commission not only looks at the possibility of minor revisions of the Directive, but re-examines critically the basic question why there needs to be a regulation of product liability at the European level in the first place. Economic literature can, as we have tried to show, provide useful and balanced insights to structure a fundamental debate concerning that question.
### Directive on Liability for Defective Products: Transposition in Domestic Law

#### Member State  Adoption  Entry into force  Liability for defective agricultural products (art. 15.1.a)*  Liability for development risks (art. 15.1.b)  Financial Ceiling (art. 16)

<table>
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<tr>
<th>Member State</th>
<th>Adoption</th>
<th>Entry into force</th>
<th>Liability for defective agricultural products (art. 15.1.a)*</th>
<th>Liability for development risks (art. 15.1.b)</th>
<th>Financial Ceiling (art. 16)</th>
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* Following the adoption of Directive 99/34/EC, the Member States are obliged to extend Directive 85/374/EEC to primary agricultural products.

Source: green paper on liability for defective products, p. 35–36.
PRODUCT LIABILITY AND PRODUCT SAFETY IN EUROPE

REFERENCES


The paper examines whether there are economic reasons for a harmonisation of product safety and product liability. Europe has traditionally justified harmonisation of product liability and product safety by referring to the argument that conditions of competitions should be harmonised ‘to create a level playing field’. The paper argues that this argument seems far too general to fit into the economic criteria for centralisation. On the basis of the economic criteria an analysis is given of the areas which may be centralised at the European level. It is argued that there are arguments in favour of centralised European rule making if there would be inefficiencies in national product liability law which would allow manufacturers to externalise damage caused by product defects or if it would be established that states could attract industry with lenient product safety standards. However, the paper claims, analysing the effectiveness of the European product liability directive, that this directive is not able to cure the risk of interstate externalities and that there is no empirical evidence of a risk that states could attract manufacturers with lenient product liability legislation. Moreover, since the product liability directive adds an additional layer of complexity to the labyrinth of conflicting standards of liability, it does not create a uniformity or a lowering of transaction costs.

There are, however, more reasons for centralisation of product safety standards, since product safety harmonisation seems a useful tool to facilitate international trade, in so far as this harmonisation merely aims at removing useless incompatibilities. However, the danger always remains that in fact high safety standards are introduced at the European level as mandatory safety regulations to create barriers to entry.

ZUSAMMENFASSUNG

RÉSUMÉ
L’article examine si une harmonisation de la sécurité et de la product liability peut être fondée sur des critères économiques. La raison donnée pour cette harmonisation en Europe a été celle de vouloir créer des conditions de compétition égales pour tous. Cependant, cet argument paraît un peu trop général. Sur la base de critères économiques, cet article analyse quels domaines pourraient être centralisés au niveau européen, et à quelles conditions. Ces conditions sont d’une part des inefficacités dans les lois sur la product liability au niveau national, qui permettraient aux producteurs d’externaliser
MICHAEL G. FAURE

les dommages causés par des produits défectueux, et d’autre part des standards de responsabilité for-
tement réduits par un État afin d’attirer des industries. Analysant l’efficacité des directives euro-
péennes sur la product liability, l’article conclut que cette directive n’est pas en mesure d’exclure le
risque d’externalités à l’intérieur d’un État, et qu’il n’y a aucune évidence pour l’attractivité de rè-
glements trop libéraux. De plus, cette directive ajoute à la complexité et l’incohérence existantes et
ne pourrait ni créer une uniformité ni baisser les coûts de transaction.
Il y a cependant d’autres raisons pour une centralisation des standards de sécurité des produits:
en abolissant des incompatibilités inutiles, elle facilite le commerce international. Il persiste pourtant
le danger que des standards de sécurité élevés soient introduits en Europe dans le seul but d’en faire
des barrières d’entrée.