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AUTOMOTIVE & MOBILITY 2023

Contributing editors

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A once-in-a-century transition complicated by geopolitics

A change in technology: from ICE to EVs and software

Many have long anticipated a once-in-a-century transition of the automotive industry oriented around a change in technology.

Most industry analysts expected significant challenges with the transition away from the internal combustion engine (ICE) towards electric vehicles (EVs). Further complexity was expected with the fundamental shift in the driving experience and new sources of revenue enabled by connectivity, sensors and software.

That technological transition, long in process, is accelerating into the mainstream. The share of EVs in the market, while still relatively small, is growing and moving beyond early adopters. Advanced driving technology is becoming ever more prevalent as technology becomes both more robust and less expensive.

Government policy: geopolitics, climate change and energy security

Taking a profound shift in technology into the mainstream is always a complex undertaking, but it is particularly so for the automotive and mobility industry. The industry is massive, operates on a global scale and is economically important in all major markets. The industry's size is not, however, in itself the challenge.

Global scale and economic importance mean the industry is the focus of government policy and of activists. The industry does not have the luxury of focusing solely on commercial issues by 'merely' working to modulate technological change and consumer acceptance in a way that reasonably ensures profitability. Instead, government policy is an increasingly significant factor for the industry. The automotive and mobility industry has always been highly regulated, but geopolitical factors are now increasingly important in government policy, impacting the industry's core operating parameters.

Geopolitics: the United States and the global west versus China and Russia

Geopolitical competition between the United States and China – the world's two largest economies and auto markets – has increased over the past several years. That competition accelerated dramatically as covid-19 laid bare the vulnerability of supply chains. That competition exploded with Russia's war on Ukraine and China's 'unlimited' partnership with Russia.

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These events also expanded the range of governments on the 'front lines' of this geopolitical competition. Increasingly, the United States and the global west (ie, North America, Europe and allies in Asia) are in tension with China (the origin of so many supply chains) and Russia (a major producer of energy and raw materials).

While geopolitical tensions have grown in significance for all major industries, commercial ties remain robust. Cross-border trade between the United States and China again broke records in 2022.

The automotive and mobility industry and its supply chains are strategically valuable

These political and commercial realities are ever more in tension for the automotive and mobility industry because the industry, its core technologies and its supply chains are strategically significant.

Electric vehicles are seen as the future of mobility. Nothing is more critical to an EV than the battery. Battery technology is thus now seen as a strategically significant industry, essential to future economic success.

China is, by volume, the dominant producer of batteries for EVs. China also dominates the supply lines of critical minerals and metals essential to EV production. Many policymakers in the global west have begun to worry that dependence on China for battery supply and critical materials could be more strategically challenging than the world's reliance on OPEC for petroleum resources, particularly if tensions build and commercial relationships are deeply fractured.

China has long recognised the strategic potential of EVs to ease their energy security concerns and allow the nation to capture a strategically significant industry. China's industrial policy has assiduously built this capacity through a particularly deep interconnection between government and industry.

The United States is now responding with its own entry into industrial policy. The Inflation Reduction Act (IRA) and other legislation passed in the United States in 2022 will invest dramatic sums into critical infrastructure, the production of semiconductors and new energy technologies. Batteries for EVs and their supply lines of critical minerals and metals are a particular focus of the IRA.

This industrial policy initiative seeks to bring production to the United States and North America. The considerable subsidies involved around EVs and batteries have concerned allies in Europe and Asia. Those concerns are easing somewhat as the United States has sought to accommodate some concerns while also encouraging those governments to enact their own policies to rapidly increase capacity beyond China.

Batteries are not the only focus of this competition. Advanced vehicles are at the forefront of integrating sensors, artificial intelligence and software to offer rapidly advancing driver assistance and connectivity-related functions. The production of semiconductors and the development of artificial intelligence are also areas of growing geopolitical competition, and thus governmental engagement with the market. Again, the United States feels China's

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industrial policy has given it an edge that US policy seeks to respond to and overcome by leveraging US leadership in technology development.

In past years, we have noted geopolitical concerns impacting policy and forecast their growing importance, but this year those concerns have accelerated to a magnitude of prominence that requires significant attention. As commercial enterprises that operate on a global scale, geopolitical issues are increasingly challenging for all major players in the automotive and mobility industry. This challenge is perhaps most simply evident when one notes that China is now the largest single auto market and the origin of many supply chains, while the United States and the global west summed are an even bigger market and a more open one, but one that relies on Chinese supply for many components. If government policy forces choices, they will be difficult because they will be economically and operationally consequential.

Rapid EV transition: climate change, energy security and economic security

The transition to EVs has long been seen as critical to combating climate change. While EVs take more greenhouse gases (GHGs) to produce than a traditional vehicle with an internal combustion engine, over time the climate impact of EVs is less. The GHG imbalance favouring EVs is expected to become greater over time as battery production becomes more sustainable and energy transition advances to more sustainable generation of electricity.

Concerns about climate change have, particularly in Europe, motivated government policy to require a very rapid transition to EVs.

In China, energy security has been the dominant factor in policies that have advantaged EV production and consumer adoption.

In the United States, concerns about climate change have impacted emissions policy more sporadically and less aggressively than in Europe. Under the Biden Administration, climate and geopolitical concerns have combined to stimulate proposed emissions rules that will force a much more rapid shift to EVs than previously contemplated.

Advanced driving capacity but not robo-taxis

Some envisioned a rapid transition to (fully) autonomous vehicles (AVs) with mobility services provided by 'robo-taxis'. Technical issues were seen as soluble in the very near future and this capacity would pull along consumer acceptance and regulatory development.

This extreme optimism has, in many circles, shifted to extreme pessimism as many assume AV investments are a lost cause.

We have long argued that as to autonomous drive technology, the issue is not so much when as where. Robo-taxis will not in the near-to-medium term be a widely available mobility solution. Yet this reality does not mean that autonomous driving technology is not developing and having a significant impact.

AV technology is advancing in off-road application in agriculture and industry. This capacity will further transform as sensors and artificial intelligence increase capacity.

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Driver assistance technology continues to advance, and its applications are increasingly both more robust and more widespread within new vehicles. This technological revolution is neither as rapid nor occurring where some had expected, but that does not mean it is not continuing to both develop and transform the on-road driving experience.

Cybersecurity and privacy

As advanced driving features expand and connectivity becomes even more robust, vehicles generate ever more massive amounts of data that is economically valuable.

As the value of data expands, so does concern about privacy. Again, government policy is a critical factor. Europe's rules are more rigorous and are expected to remain so. China's rules optimise for national security with little real concern for individual privacy. Rules in the United States are less aggressive than in Europe but evolving.

With connectivity comes concern about cybersecurity, both to protect sensitive data and to ensure the safe operation of the vehicle. In this area, government policy is again key but has been reasonably stable over recent years.

ESG and activism: the 'new' political risk

Environmental, social and governance (ESG) concerns are of increasing importance to every business. ESG disclosures initially were exclusively voluntary and largely seen as a branding function, but such disclosures are increasingly compelled by government action in the United States and Europe.

Sustainability, labour practices, governance rules, data protection, privacy and other issues have long been regulated by governments. ESG concerns add more force and depth to those regulatory efforts. Again, because the automotive and mobility industry is massive in scale and economic significance, it is greatly impacted by these efforts as the industry is a target for activism and governmental action.

Activism over ESG issues is particularly important for the industry. All major companies report on ESG factors. These reports are increasingly the focus of activist groups that use research and social media to advance their cause through publicity that impacts brand value. This research and publicity can also stimulate litigation. Publicity and litigation can also foster government action.

This 'new' political risk is of increasing importance to the automotive and mobility industry. The challenges here will grow as geopolitical factors advance. For example, in the global west, concerns about labour practices in China have received recent attention. This attention poses branding issues for the industry and raises concerns about compliance with current regulations and the development of more stringent rules in the future.

In China, activists have used social media on occasion to generate consumer action against companies that are perceived, either by themselves or by the governments where they are headquartered, to have inappropriately addressed China's concerns. These actions are often paired with governmental action by China to create a powerful dynamic designed to force corporate action.

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Given the increasing geopolitical tensions, it is not surprising that activist activities in China and the global west are sometimes in tension. Appeasing one group can create further issues in another jurisdiction.

Tension between the demands of activists is far from limited to the geopolitical realm. Often enough, there is significant tension between the goals of competing activists even within a single economy. Addressing the concerns of activists is both of increasing importance and complexity.

Choices and trade-offs but marvellous transformation, too

Aggressive technological change in the context of increasingly challenging geopolitical and climate concerns, all while activism becomes more aggressive, means a time of challenging choices and trade-offs for all in the automotive and mobility industry.

We do not want to minimise those challenges. So much of our work is directed at identifying those issues and trends so we can help those in the industry make informed choices to meet their goals.

Focusing on these challenges, however, obscures the marvellous evolution taking place in the automotive and mobility industry that is positively transforming the future, because transportation is critical to economic, social and personal development. We have expressed this optimism in other forums by discussing what we have termed 'Living Mobility' – a mobility environment that is more inclusive, objective, unifying and sustainable.



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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

The automotive industry is one of Canada's largest manufacturing sectors and accounts for 11 per cent of North American vehicle production (1.9 million vehicles per year). The sector

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supports nearly 500,000 employees and contributes C\$16 billion annually to Canada's gross domestic product.

For foreign investors in this sector, Canada offers a strategic location in the heart of one of the world's largest and most lucrative automotive markets. There are 37 high-volume assembly plants within a 500km radius of the Windsor–Detroit border. These plants have produced up to 7.4 million vehicles in one year.

Canada has one of the lowest cost structures among advanced economies, with the lowest cost structure among G7 countries and an overall cost advantage of 8.2 per cent over the US in the automotive sector. According to a KPMG study, automotive parts operations based in Canada typically enjoy an 11.2 per cent labour cost advantage compared to their US-based counterparts.

Most of the OEM assembly plants and parts manufacturing facilities are located in Southwestern Ontario where 92 per cent of shipments are made. Ontario is the only jurisdiction in North America to be home to five major automakers, including Ford, Toyota, Honda, General Motors and Stellantis. Ontario is home to many of the world's leading parts suppliers including large Tier 1 manufacturers, such as Magna, Linamar, Stackpole and Martinrea. Ontario's automotive supply chain is comprised of over 700 parts companies, over 500 tool, die and mould makers, and over 300 connected and autonomous companies.

The Ontario region also includes a growing technology hub (second only to California) in close proximity to Toronto and the University of Waterloo. The cluster of fast-growing technology companies are within easy driving distance to 37 light vehicle assembly plants producing 6.1 million vehicles on both sides of the Canada–US border. This collocation is important, as communications technology plays an increasingly key role in the development of connected and autonomous vehicles. There are 24 colleges and 11 universities in Ontario offering auto-related research initiatives and training programmes. Further, over 200 companies, including GM, Ford, Google, Uber, Apple and BlackBerry QNX, are developing connected and autonomous vehicles technologies in Ontario.

The most significant investment in the industry relates to the rapid shift away from combustion engines to battery electric vehicles. This investment is centred on the supply of batteries and battery materials and in retooling plants to build electric vehicles and components. Since 2020, global automakers and suppliers of electric vehicles, batteries and battery materials have invested over C\$17 billion into the Ontario economy.

COMMERCIAL OPERATIONS

Regulation

- 2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

Federal and provincial levels of government share the responsibility for motor vehicle safety oversight. The federal government is responsible for the safety standards for new

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and imported vehicles of prescribed classes, tyres and equipment for use in the restraint of children and disabled persons. The provinces are responsible for driver licensing, vehicle registration and operational use.

Federal

The Minister of Transport (Transport Canada) has the responsibility for the administration and enforcement of the Motor Vehicle Safety Act (MVSA). The MVSA applies to companies that manufacture regulated vehicles or vehicle equipment in Canada, companies that distribute vehicles or equipment obtained from those manufacturers to other persons for the purpose of resale, importers of regulated vehicles or equipment into Canada for the purpose of sale, and persons who import regulated vehicles previously sold at the retail level in the United States. The MVSA also regulates the temporary importation of non-compliant vehicles and equipment.

Provincial

Each provincial government oversees various aspects of transportation in its respective province, including the establishment and maintenance of the provincial highway system, the licensing and training of vehicles and drivers and the policing of provincial roads. For example, in Ontario, the Ministry of Transportation has the responsibility for the administration and enforcement of the Highway Traffic Act, which regulates the licensing of vehicles, classification of traffic offences, administration of loads, classification of vehicles and other transport-related issues. The provinces also regulate automobile insurance.

Development, manufacture and supply

- 3** | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

OEMs and supply chain

OEMs operating in Canada use terms and conditions for contracting with parts suppliers. These terms and conditions are generally based on each OEM's global standards. The OEMs resist any variance from their standard terms and conditions.

The supply chain is segregated into distinct tiers. For example, in a three-tier supply chain, the Tier 1 supplier sells a finished assembly product directly to an OEM. The Tier 2 supplier, however, sells its parts, which would reflect some value-added labour and minor sub assembly, to the Tier 1 supplier for use in the production of its components. The Tier 3 supplier sells engineered raw materials, such as rolls of sheet steel, to the Tier 2 supplier. It is not uncommon for suppliers to straddle more than one tier. For example, a supplier may be a Tier 1 and Tier 2 supplier, selling some parts directly to an OEM and other parts to other Tier 1 suppliers.

In the Canadian automotive industry, just-in-time inventory and purchase orders containing little or no long-term purchase obligations are common.

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Distribution and retail

Automotive companies typically contract with distributors and dealers to sell their vehicles, parts and accessories. The substantial majority of these distributors and dealerships are independently owned and the relationship with the distributor or dealer is governed by a written contract.

Automobiles are subject to various consumer protections. There is no 'cooling-off period' in Canada for motor vehicle contracts, so the consumer must be sure of his or her decision before signing the contract. In most cases, the contract will be binding. When a consumer buys a vehicle, the dealer must provide the most accurate information available about the vehicle's history and key features. If the dealer omits certain information, the buyer will have 90 days to cancel the contract. Additional consumer protections apply when the purchase of the vehicle is financed, which is often the case.

The Canadian Motor Vehicle Arbitration Plan is a free arbitration programme from participating manufacturers. Vehicle dealers must let the buyer know if the car being purchased qualifies for this programme. If it does, the programme can assist the consumer in dealing with disputes about manufacturing defects.

Distribution

- 4 | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

Agents and distributors

A foreign automotive company may wish to offer its products or services in Canada by means of an independent agent or distributor. An agent will usually be given limited authority to solicit orders for acceptance at the foreign head office, and will not normally take title to the goods or provide services to the customer. A distributor, on the other hand, usually takes title to the goods and offers them for resale, either directly to the customer or through dealers or retailers.

The relationship with an agent or distributor should be established by contract. Although provincial law does not generally prohibit the termination of an agent or distributor, the courts will require reasonable notice to be given, or damages in place of notice, in the absence of an agreed contractual term for the relationship. The nature of the relationship determines whether the arrangements are subject to franchise legislation.

Distribution and dealers

Distributors and dealerships, which are most often independently owned, are the most common intermediaries between automotive companies and the retail consumer and fleet markets. Dealerships primarily deal parts and accessories to retail consumers while authorised parts distributors primarily distribute parts and accessories to retailers. All provincial governments have some form of legislation regulating motor vehicle dealers. The nature of

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this legislation varies from province to province, as do its scope and comprehensiveness. The general aim of legislation concerning motor vehicle dealers is to regulate the trade in a valuable and dangerous commodity that is susceptible to theft and raises consumer protection issues, and to provide a compensation system in the event of a motor vehicle dealer's misconduct.

Importers

With certain exceptions, all types of vehicles that Canadians import that are designed to be driven on public roads, and those designed for off-road use, must comply with the MVSA. Once modified (other than having general repairs or routine maintenance), the vehicle no longer maintains its original factory-issued certification. This certification is required for importation into Canada. Importing an electric or hybrid vehicle is no different from importing any other type of vehicle. The MVSA does not regulate shipments of individual parts, with the exception of tyres, child car seats and booster seats.

Franchising

Franchising is not as heavily regulated in Canada as it is in some other jurisdictions. In Canada, franchising is a purely provincial matter. About half of the provinces currently have franchise legislation in effect. While there are slight differences in the legislation and regulatory requirements of each province, they are all derived ultimately from the US model of mandated disclosure by a franchisor to prospective franchisees, coupled with a duty of good faith and fair dealing owed by each party to the other, and a right of franchisees to associate freely among themselves.

Mergers, acquisitions and joint ventures

- 5 | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

M&A

As in any other industry, a threshold question in an automotive acquisition is whether to purchase shares or assets. In addition to the usual considerations, a purchaser and vendor of an OEM or parts manufacturer may want to proceed by way of share purchase to avoid the right of members of the dealer network to consent to the assignment of the dealership agreements.

In the case of an acquisition of a large OEM or parts manufacturer, regulatory considerations are important, particularly potential pre-clearance under the Competition Act and the Investment Canada Act (ICA). In addition to such regulatory approvals, third-party consents from dealers, suppliers, landlords, equipment owners, creditors and shareholders are typical. Under most Canadian corporate statutes, if a sale involves the disposition of all or substantially all of a corporation's assets, shareholders must approve the transaction by special resolution.

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Joint venture structuring

As is sometimes done in the Canadian automotive industry, two or more parties may engage in a joint venture or syndicate where they collaborate in a business venture. There is no specific statutory definition or regulatory scheme for joint ventures, at either the provincial or federal level, although they are not uncommon. A well-known Canadian example of a joint venture is a large OEM assembly plant, Canadian Automotive Manufacturing Inc (CAMI). CAMI is now owned by General Motors but commenced as a joint venture with Suzuki.

Incentives and barriers to entry

- 6** | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

Incentives for investment

Canadian automotive manufacturers are recognised for their strong capacity in launching complex and advanced automotive manufacturing projects due to their world-class plant and labour quality. Canadian assembly plants have won one-third of all JD Power plant quality awards in North America. The industry is highly concentrated in Ontario, with manufacturing centres also located in Quebec, Manitoba and British Columbia.

Foreign investors rely on strong supplier and research capabilities in lightweight metals, biomaterials and composites, advanced safety systems, software and connected cars, alternative powertrains (electric vehicles, fuel cells, natural gas and biofuels) and vehicle safety and testing. Manufacturers that do research and development in Canada take advantage of Canada's Scientific Research and Experimental Development Tax Incentive Program.

The province of Ontario recently created the Ontario Vehicle Innovation Network (OVIN), which is intended to build on the already created Autonomous Vehicle Innovation Network. Ontario mandates OVIN to accelerate the development of next-generation electric, connected and autonomous vehicles and mobility technologies, as well as support the province's role as the manufacturing hub of Canada. OVIN is charged with encouraging innovation and collaboration through partnerships with small and medium-sized enterprises, academia, the automotive industry and the battery sector, with the goal of continuing to lead on electric and autonomous vehicle research and technologies.

Other programmes are in place at the retail level in some Canadian jurisdictions to incentivise the adoption of new technology.

Barriers to entry and new entrants

The ICA is a federal statute of broad application regulating investments in Canadian businesses by non-Canadians. Investments by non-Canadians to acquire control over existing Canadian businesses or to establish new ones are either reviewable or notifiable under the ICA. The rules relating to an acquisition of control and whether an investor is 'Canadian' are complex and comprehensive.

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Subject to certain exceptions, an acquisition of a Canadian business by a non-Canadian investor controlled by persons who are residents of World Trade Organization member countries (WTO investors) is reviewable where the enterprise value is C\$1.287 billion or more. There are additional restrictions in place in respect of certain prescribed circumstances, such as investments by non-WTO investors or by state-owned enterprises, and investments that may pose a national security risk.

PRODUCT SAFETY AND LIABILITY

Safety and environmental

- 7** | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

Product compliance and safety

The Motor Vehicle Safety Act (MVSA) was recently amended to introduce broad powers for Transport Canada to order manufacturers to submit a notice of defect or noncompliance when Transport Canada considers it would be in the interest of safety. According to guidelines on compliance issued by Transport Canada, the Motor Vehicle Regulations Enforcement Branch is empowered to conduct 'post-market surveillance and oversight of the regulated community through programs of compliance inspection, testing, corporate audits and the investigation of alleged safety-related defects and recall monitoring'.

National Safety Marks (NSMs) are used to indicate the compliance of a vehicle or equipment with the MVSA and the related regulations and safety standards. Transport Canada authorises their use and any company that intends to use an NSM must apply to Transport Canada to obtain this authorisation.

The Canada Motor Vehicle Safety Standards (CMVSS) prescribe the minimum performance levels that vehicles and equipment must meet. Each CMVSS standard includes performance requirements against which regulated vehicles and equipment are measured and compliance is determined. These standards may include Transport Canada approved Motor Vehicle Safety Test Methods, Technical Standards Documents or third-party published test methodologies.

The Defect Investigations and Recalls Division has a mandate under the MVSA to investigate complaints relating to alleged manufacturing safety defects. At times, these investigations may lead to safety recall campaigns or safety advisory publications.

Environmental regulations

Vehicular greenhouse gas emissions (GHG) in respect of light-duty vehicles are regulated under the Canadian Environmental Protection Act. In May 2018, the federal government introduced new regulations under that Act establishing more stringent greenhouse gas emission standards for heavy-duty vehicles and engines.

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In 2017, a federal government agency, Environment and Climate Change Canada, released a regulatory framework outlining the proposed design of Canada's Clean Fuel Standard, which is aimed at assisting in meeting Canada's goal of lowering GHG to a target of 30 per cent below 2005 levels by 2030 as part of Canada's participation in the Paris Agreement. The Clean Fuel Standard will include reductions in the carbon footprint of transportation fuels and will require increases in renewable fuel content or the purchase of credits that can be generated through the deployment of energy sources that offset fossil fuels, such as electric vehicles.

Product liability and recall

- 8** Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

Product liability

There are three key categories of claims typically made in the nature of product liability claims:

- claims against manufacturers alleging negligence in the design or manufacture of vehicles;
- claims against manufacturers and dealers alleging the breach of express or implied warranties of fitness and quality; and
- claims against manufacturers and dealers seeking consumer protection remedies based on unfair business practice provisions of consumer protection legislation or breach of the misleading advertising provisions in the federal Competition Act.

In negligence, a plaintiff may recover for bodily injury or property damage (and in some specific circumstances, economic loss) if the plaintiff can establish a duty of care, a breach of the applicable standard of care and damages caused by the alleged breach. These claims typically assert negligence in design, manufacture or failure to warn potential users of the product's inherent dangers.

A party to a purchase or supply contract is entitled to sue for damages for breach of contract or breach of an express warranty, or both, if the product does not comply with express contractual or warranty terms. In some jurisdictions, legislation imposes implied warranties regarding the fitness and quality of the automotive products sold. This legislation commonly prohibits exclusion of the statutory warranties and conditions from contracts for the sale of products to consumers. In some jurisdictions, legislation implies statutory warranties in favour of consumers by manufacturers and others in the distribution chain in certain circumstances, even in the absence of contractual privity.

The federal Competition Act provides a civil right of action for damages caused by misleading advertising in specific circumstances.

Some provincial jurisdictions provide remedies to consumers against automotive dealers, manufacturers or distributors for 'unfair practices', including the making of false, misleading

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or deceptive representations. Provincial consumer protection legislation may provide consumers with relaxed criteria for recovery.

Class actions

It is not uncommon for a class action alleging negligence and breach of express or implied warranties to follow a product recall. Class actions seeking consumer protection remedies are also common. To date, many class actions have been certified but relatively few class actions have proceeded to trial in Canada (outside Quebec), though this number has increased in recent years. It remains to be seen whether the availability of class actions will result in larger punitive damage awards or other changes in substantive laws.

DISPUTES

Competition enforcement

9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

Participants in the automotive industry must ensure compliance with Canada's Competition Act, the key legislation in Canada that regulates competition. The Competition Act includes provisions that regulate civil practices (such as mergers, refusals to deal, price maintenance, exclusive dealing, tied selling, abuse of dominance, competitor collaborations and deceptive marketing practices) and those that prohibit criminal conduct (including conspiracies, bid rigging and criminal misleading advertising practices).

Over the past few years, one of the key issues for the automotive industry has been the enforcement activity of antitrust regulators in the automotive parts sector. Specifically, numerous investigations have been launched by antitrust regulators around the world concerning alleged conspiracies and bid-rigging arrangements entered into among various suppliers for the sale and supply of automotive parts. These investigations have resulted in convictions and fines, including in Canada. To date, the Canadian Competition Bureau's investigations have resulted in multiple guilty pleas and over C\$80 million in fines imposed by courts.

The investigations in Canada, and around the world, have led to significant follow-on civil litigation. Section 36 of the Competition Act provides that any person who has suffered loss or damage arising out of conduct that contravenes the criminal provisions of the Competition Act has the right to commence a private right of action to recover the damages suffered, plus legal costs. Class actions alleging conspiracies and bid-rigging arrangements relating to approximately 40 different automotive parts have been launched in British Columbia, Saskatchewan, Manitoba, Ontario and Quebec. These actions seek millions of dollars in damages from the defendants (automotive parts suppliers) on behalf of both direct purchasers of the alleged cartelised products, such as OEMs, and indirect purchasers, such as consumers who purchased automobiles during the proposed class period.

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Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

Disputes in the automotive industry generally arise in three contexts: vehicle owner or lessee claims against manufacturers, distributors and dealers; claims between OEMs and their dealer networks; and claims involving OEMs and their suppliers.

Vehicle owner and lessee claims

In Canada, automotive owner or lessee claims take many forms including class action civil suits by one or more plaintiffs seeking to represent a class of owners or lessees of vehicles. These representative plaintiffs commence a civil action alleging a class-wide product defect in the manufacture or design of a vehicle model or some specific part of a vehicle or alleging breaches of consumer protection legislation provisions implying warranties or prohibiting 'false', 'misleading' or 'deceptive' practices. These claims seek compensation or other relief against manufacturers or distributors, or both, on behalf of the entire class. In Canada, product liability class actions will often be commenced in concert with similar proceedings in the US and, increasingly, recalls of vehicles in the industry will lead to class action proceedings where a plaintiff is seeking additional economic loss damages that extend beyond the repairs called for in the recall notice.

In addition, the courts deal with many individual personal injury or property damage civil suits alleging that a product defect caused damage, usually personal injury or property damage. Another source of litigation is individual warranty claims in which vehicle owners or lessees allege defects in the manufacture of a vehicle that are not adequately repaired by a manufacturer under warranty. For these disputes, owners or lessees may seek binding arbitration under the Canadian Motor Vehicle Arbitration Plan, an arbitral process set up by participating Canadian manufacturers, which is available at no charge to consumers and can be accessed by consumers in all provinces and territories in Canada.

OEM versus dealer claims

In provinces where franchise laws apply, duties of good faith and fair dealing are imposed by statute on the OEM and the dealer. Some disputes between manufacturers and dealers in the automotive industry are determined in the courts, but most are not because roughly 90 per cent of Canada's automobile dealers have agreed to participate with their manufacturers in a nationwide mediation and arbitration plan called the National Automobile Dealer Arbitration Program.

OEM versus supplier claims

Disputes between OEMs and their suppliers can be determined in court proceedings in Canada, but most supplier agreements will include mandatory mediation and arbitration clauses that require that disputes be determined by way of private alternative dispute mechanisms. The exception is when suppliers are added as third parties to ongoing court proceedings involving product liability and product quality claims made by consumers

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against OEMs. Increasingly, manufacturers are pursuing suppliers in claims for contribution and indemnity in the context of product liability and product quality class action proceedings as well as other civil product liability proceedings.

Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

The statute of choice for the restructuring of an insolvent company of any size or complexity is the Companies' Creditors Arrangement Act (CCAA). The CCAA is federal legislation and the functional equivalent to Chapter 11 of the US Bankruptcy Code, although there are some important technical differences. Generally, to qualify as an applicant under the CCAA, a debtor company (or the corporate group of which it is a part) must be insolvent and have in excess of C\$5 million in debt. The CCAA allows for wide judicial discretion and relief can largely be tailored to fit the specific needs of a particular case.

A supplier subject to CCAA protection can seek to either sell its assets and business through a court-approved process or restructure its business and affairs through a plan of compromise and arrangement. If the court is satisfied that certain commercially reasonable steps have been taken to obtain the highest and best price for a supplier business and assets, the court can approve a sale free and clear of any liens and encumbrances, without any creditor vote. If the distressed wishes to pursue a plan to, for example, rationalise its balance sheet, the plan must be passed by each class of creditors to whom the plan is made, by a majority of voting creditors representing two-thirds of voting claims, in each affected class.

Generally, a Canadian court cannot order a supplier to a debtor company to advance 'further credit' following the CCAA filing. Suppliers are entitled to payment on delivery. Also, if a party is not under a continuing legal obligation to supply or provide services, it cannot be compelled to supply the debtor following the filing, even if the debtor is prepared to pay on a cash-on-delivery basis. Thus, in certain circumstances, the court may authorise the payment of 'prefiling debt' to critical vendors to induce them to continue the provision of goods or services to the debtor during the restructuring. One exception to this rule is if a supplier is deemed to be a critical supplier. If certain criteria are met, the court can order the critical supplier to continue to supply on credit, provided the supplier is granted a charge on the assets of the debtor company to secure payment.

In the case of an insolvency of an automotive parts supplier, a large proportion of these critical supplier payments are made to tooling vendors. The Tier 1 and Tier 2 suppliers will often act as a general contractor for building tools and outsource construction to specialised tool builders. As a result, critical supplier payments could be required to induce the contractor to finish or release the tools. This is of greater significance if the tools are needed for an upcoming product launch.

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Intellectual property disputes

- 12** | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

Automotive companies generally own their own licences to use numerous patents, copyrights and trademarks on a global basis. Automotive companies often have policies to protect their competitive position by, among other methods, filing international patent applications to protect technology and improvements that the companies consider important to the development of their businesses, including the filing of patents under the Canadian Patent Act.

Non-practising entities, more commonly referred to as ‘patent trolls’, are a large issue in Canada. This is increasingly so in the automotive industry given the proliferation of communications technology in automobiles. Patent trolls typically acquire patent rights that are perceived to be infringed by the industry at large. Since the cost of patent litigation can be millions of dollars, patent trolls often propose a quick settlement that is less than the potential cost of litigation. A sophisticated intellectual property strategy – namely, having strong intellectual property protections in place – can minimise the effect of patent trolls.

EMPLOYMENT ISSUES

Trade unions and work councils

- 13** | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

With certain notable exceptions, most hourly workers in the Canadian automotive manufacturing sector are unionised. Unionised workers are covered by collective bargaining agreements, which are negotiated by the original equipment manufacturer and parts manufacturers periodically with various unions. Many automotive manufacturing workers are members of large unions such as Unifor (resulting from the 2013 merger of the Canadian Auto Workers union and the Communications, Energy and Paperworkers Union of Canada, currently with over 300,000 members).

Collective bargaining agreements grant guaranteed wage and benefit levels and provide members with a significant level of job security. Unions have often negotiated with automotive companies in Canada for defined benefit pension plans and other benefits and perquisites that have significant employer costs. Unionisation and the terms of collective bargaining agreements may restrict the ability of automotive companies to close plants, divest businesses and outsource functions. Employment of unionised employees generally transfers automatically on the sale of a business, as the purchaser remains bound by the terms of the collective bargaining agreement in place at the time of the sale.

Aside from unionisation of automotive workers, Canadian employment law is unique. Unlike in some other jurisdictions, there is no at-will employment in Canada. Absent valid contractual provisions limiting the employee’s termination entitlements to minimum statutory amounts,

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non-union employees are entitled to 'reasonable notice' of termination or payment in lieu of such notice. Termination entitlements for employees tend to be much higher in Canada than in other jurisdictions. Also, on an asset transaction, the employment of non-unionised employees does not transfer automatically, other than in the province of Quebec. Employees must be offered and accept employment with the purchaser. The defined benefit and contribution pension plans that are maintained by many Canadian employers to supplement the federal Canada Pension Plan may be subject to various federal and provincial legislation. Relevant to the acquisition of a Canadian automotive business, these rules govern such things as recognition of an employee's past service and transfers of plan assets.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

Driving and safety are regulated in Canada by the provincial governments. Automated vehicles (AVs) equipped with Society of Automotive Engineers' (SAE) international driving automation Level 3 may now be legally driven on roadways in Canada's two most populous provinces, Ontario and Quebec. In addition, both provinces have pilot projects in place to permit limited use of SAE international automation Level 4 and Level 5 AVs. Other provinces, such as British Columbia, Alberta, Saskatchewan, Manitoba and Nova Scotia have some legislation at the provincial or municipal level allowing for the driving of some AVs.

Ontario also has a separate pilot programme for cooperative truck platooning. A cooperative truck platoon means two or more commercial motor vehicles that use an advanced driver assistance system and vehicle-to-vehicle communication system to travel in a convoy where the vehicles steer, accelerate and brake cooperatively and synchronously.

At the federal level, Transport Canada is engaged in several initiatives relating to the safety and testing of automated and connected vehicles, and published the following two documents in February 2019: Canada's Safety Framework for Automated and Connected Vehicles; and Safety Assessment for Automated Driving Systems in Canada. These new reports complement work outlined in two other recently published documents: Automated and Connected Vehicles Policy Framework for Canada (released in January 2019 by the Council of Ministers Responsible for Transportation and Highway Safety); and Testing Highly Automated Vehicles in Canada: Guidelines for Trial Organizations (released in June 2018 by Transport Canada).

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UPDATE AND TRENDS

Trends and new legislation

- 15 | Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

Cybersecurity protection has been a major area of concern for the automotive sector. The threat is particularly meaningful to the manufacturers of autonomous vehicles as the sensors in those vehicles collect vast amounts of sensitive data about the vehicles and the people in them. It is recommended that companies have an information technology security policy, data governance framework and cybersecurity incident response policy in place, that employees receive appropriate training and that insurance coverage is obtained.



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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

China is one of the world's largest automotive markets and vehicle manufacturing countries. The total vehicle output and sales volume of China in 2022, respectively, reached 27.02 million and 26.86 million units. Involving over 100 sub-industry sectors, the automotive sector has been a pillar industry with economic and strategic significance in China given its contribution to the GDP growth.

Since its accession to the World Trade Organization in 2001, China has experienced unprecedented growth in the automotive industry and market. Despite multiple headwinds faced by the sector in recent years, including the resurgence of covid-19, shortage or high price of certain components or raw materials and a reshuffling of global supply chain, the year-on-year growth did not falter. With steady improvements in product quality, Chinese automotive brands have continued to grow and have tapped into the international market. They have also gained an increasing edge in segmented markets, especially in the field of new energy vehicles (NEVs). In 2022 in China, 5.366 million purely electric vehicles and 1.518 million plug-in hybrid vehicles were sold, with a year-on-year growth of 81.6 per cent and 151.6 per cent, respectively. Several Chinese brands are among the main players in this sector. NEV output in China totalled 7.058 million units in 2022, an increase of 96.9 per cent year-on-year, while sales of NEVs rose by 93.4 per cent to reach 6.887 million units; from January to March 2023, NEV output in China totalled 1.65 million units, an increase of 27.7 per cent year-on-year, while sales of NEVs rose by 26.2 per cent to reach 1.586 million units. There is little doubt that China's automotive market has matured, but it has not necessarily levelled out. Market demand will continue to outpace other consumer markets, especially for NEVs, given the Chinese government's policy of having 40 per cent of vehicles powered by new energy by 2030 and taking petrol cars off the market gradually, potentially from 2030. It is expected that NEVs will become mainstream in the automotive market by 2035, accounting for more than 50 per cent of total sales. China aims to peak national emissions by 2030 and achieve carbon neutrality by 2060.

The following trends have been observed based on consumer behaviour and are likely to indicate the future direction of the automotive industry in China.

- It is generally believed that China will sustain a continuous economic growth in the mid-length term. The decline in production and sales since the outbreak of covid-19 has been contained and the market has rebounded with the help of economic stimuli, especially after the zero-covid policy of China was lifted in December 2022. For 2023, economic growth in China is forecast at around 5 per cent despite domestic and international uncertainties, according to the annual sessions of the National People's Congress and the National Committee of the Chinese People's Political Consultative Conference held on 5 March 2023. However, considering the rise in global economic uncertainties, whether such forecast will be realised is to be seen.
- Rapid urbanisation, rising family incomes, desire for vehicle ownership, consumption upgrading and increased mileage capacity and accessibility of recharging infrastructures

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for electric vehicles will all contribute to the industry's growth, as well as the preferences of new buyers. Chinese consumers will have a bigger appetite for luxury, roomier and greener models.

- Chinese consumers are paying more attention to vehicle safety, accessories and value-added functions, and fuel economy (in the case of fossil fuel cars) or mileage capacity (in the case of NEVs). Affordability at the cost of the above will be much lower than the norm for automotive manufacturers.
- Consumption of NEVs continues to grow quicker than other major markets due to various causes. Carbon emissions and the environmental crisis have been under the spotlight and the Chinese government has committed to achieving carbon neutrality by 2060, as mentioned above. China's crude oil import has also been skyrocketing for decades. In an effort to reduce carbon emissions and dependence on fossil fuels, the Chinese government has put forward a series of stimuli to promote the production and consumption of NEVs, such as providing subsidies for NEV manufacturers, offering tax exemptions for the purchase of NEVs by consumers (these tax exemptions will expire by the end of 2023, but may be extended) and setting up 'green channels' for the application of licence plates for NEVs in certain major cities where issuance of licence plates is managed under a rigid quota system.

COMMERCIAL OPERATIONS

Regulation

2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

China's automotive manufacturing sector is, in general, heavily regulated. Nevertheless, the Chinese government has in recent years put some efforts into streamlining its various administrative approval procedures for foreign investment in this sector. One example is that, since the promulgation by the National Development and Reform Commission (NDRC) of the new Provisions on Administration of Investment in Automotive Industry, which entered into force on 10 January 2019, building a new automotive manufacturing plant no longer needs the approval of the NDRC or the State Council, but only requires record filing with the NDRC's local or provincial counterpart. Another example is that after the Foreign Investment Law came into effect on 1 January 2020, foreign direct investments in all industry sectors (except for prohibited sectors) no longer need to be either filed with or approved by the Ministry of Commerce (MOFCOM). Subsequently, foreign direct investment in the automotive manufacturing sector does not require approval by MOFCOM (but is still subject to all other applicable approvals and procedures), which could add several months to the overall timeline for establishing a foreign invested automotive manufacturing business.

Once the automotive manufacturing plant has been established, the manufacturing process is subject to a special 'access permit for automotive manufacturers and their products' according to the Regulations on Automotive Vehicle Manufacturing Enterprises and Product Access Management (the Management Regulations), issued by the Ministry of Industry and

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Information Technology (MIIT) on 27 November 2018, effective from 1 June 2019. To qualify for a manufacturing permit, an automotive manufacturer must meet all the requirements set out by MIIT, including obtaining the site, capital and personnel necessary for carrying out manufacturing operations, as well as demonstrating capabilities on product design and development, facility, consistency and quality control, and product sale and post-sale services. MIIT periodically publishes a list of manufacturers and products for which permits have been granted. We have seen a draft amendment to the Management Regulations published by MIIT on 28 October 2022, soliciting public opinions and incorporating provisions regulating intelligent networked vehicles and the protection of data security and personal information.

Each vehicle model produced by manufacturers with the above-mentioned access permit must also:

- meet the relevant standards (as set out in Items and Underlying Standards for Compulsory Standards Inspection of Automotive Products promulgated by MIIT);
- obtain the China Compulsory Certification (CCC); and
- pass an inspection performed by a qualified inspection institution.

The production of automotive parts, on the other hand, follows a different licensing regime. First, for many types of automotive parts, a production licence issued by the State Administration for Market Regulation (SAMR) is required. Second, the automotive parts must be manufactured in accordance with the compulsory standards (known as Guobiao or GB), formulated by the Standardization Administration of China (affiliated to SAMR since 2018). In addition, certain automotive parts being subject to CCC must also undergo a specific accreditation process.

As to distribution, suppliers and distributors must register with the national automobile distribution information management system administered and maintained by MOFCOM within 90 days of the issuance of their business licence.

Furthermore, vehicles for sale must be registered in accordance with the National Environmental Protection Catalogue and, where applicable, the local Environmental Protection Catalogue, which might set a higher standard for registration. The issuance of on-road permits (vehicle registration licence) and licence plates is administered by the vehicle administration office under the local Public Security Bureau (PSB) based on the automobile register and CCC. In addition, all vehicle owners must purchase mandatory liability insurance for transportation accidents before their vehicles can be registered with the PSB and legally allowed on the road. The base insurance premium rate and the insurance terms are uniformly set by the China Banking and Insurance Regulatory Commission. Vehicle owners are free to decide whether to purchase additional commercial property and liability insurance.

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Development, manufacture and supply

3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

Foreign automotive companies must establish foreign-invested enterprises (for example, in the form of a limited liability company) in China to operate their businesses, and cannot operate without a permanently established business presence.

There used to be restrictions on the shareholding of foreign investors in a Chinese automotive manufacturing enterprise, such as a shareholding threshold of 50 per cent and the prohibition of investing in more than two automotive manufacturing enterprises of the same type. These restrictions have been progressively lifted since 2018 and, according to the latest version of the Special Administrative Measures (Negative List) for Foreign Investment Access issued by MOFCOM in 2021, as of 1 January 2022 all such restrictions are lifted. There is now no restriction over foreign shareholding in automotive manufacturing companies. There is also no restriction on foreign investors holding equity interests in automotive part manufacturers.

Due to the aforesaid historical restrictions on shareholding, traditionally overseas automotive manufacturers have partnered with large state-owned or privately owned automotive groups to establish Chinese-foreign joint venture companies. Under this model, overseas automotive manufacturers – mainly from the United States, Europe, Japan and South Korea – localise their brands and share in the profits with their joint venture partners.

Foreign automotive companies also establish wholly owned subsidiaries without a Chinese partner. This model is traditionally possible only for automotive parts manufacturers and import and sales companies, but is now permitted for all types of automotive manufacturers. One of the advantages of setting up a wholly owned subsidiary is that the foreign automotive company has full autonomy in deciding on all strategic and operational matters in relation to the subsidiary. However, lacking a Chinese partner with an inside track can limit the wholly owned subsidiary's ability to tap into the local market and in many cases supply to the local government, which itself is a highly sought-after customer base.

There are two sources of supplies: imported and local. In the automotive parts market, foreign companies, as well as localised foreign-invested enterprises, are key players in technology-heavy areas such as electronic components including power steering, electronic braking, suspension systems and engine management systems, while local suppliers have a clearer advantage in less technology-driven areas, such as vehicle windows. Branded automotive manufacturers may impose certain constraints on small-scale automotive parts suppliers. Historically, for example, they were able to require suppliers to sell parts only to their branded vehicles. Except for large automotive parts suppliers, many local suppliers used to make and sell their products to automotive manufacturers under an exclusive OEM arrangement. However, under the Administrative Measures for Automobile Sales enacted by MOFCOM on 1 July 2017 (the Automobile Sales Measures), this practice is no longer permitted, as the Automobile Sales Measures generally prohibit automotive manufacturers from restricting or preventing automotive parts makers and importers from supplying their products to others.

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Distribution

- 4** | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

Prior to the enactment of the Automobile Sales Measures and with the exception of parallel imports, car sales in China were primarily made through a branded sales and service system under the Implementation Measures on Management of Automobile Brand Sale, issued in 2005. Under the branded sales and service system, an automotive manufacturer may establish a branded sales and service network, or authorise a sole distributor to do so, by using a unified shop name, logo or trademark. While a domestic automotive manufacturer may sell cars by itself, an overseas automotive manufacturer must establish a local presence or authorise a domestic entity to act as its sole distributor to sell cars in China. The sole distributor may further authorise several sub-dealers to engage in automobile sales and service activities. In other words, a dealer must be authorised by either the automotive manufacturer or the sole distributor to sell cars and car parts. Within this traditional regulatory framework, automotive manufacturers and their sole distributors gain more leverage in negotiating their contractual arrangements with dealers.

The introduction of the Automobile Sales Measures in July 2017 has reshaped the automobile sales and post-sales service market in China by granting distributors more freedom and leverage in the market. Under the Automobile Sales Measures, for the first time it is possible for dealers to distribute automobiles without pre-authorisation from automotive manufacturers in certain circumstances. It also allows dealers to purchase cars from other authorised dealers for resale and sell imported vehicles through a parallel import scheme. In addition, the Automobile Sales Measures permit the establishment of automobile post-sales service providers without in-house sales functions, which reportedly have a higher profit margin than those with an in-house automobile sales function. It was widely expected that, alongside the traditional dominant single-brand 4S (sales, spare parts, service and survey) store networks, additional automobile distribution and post-sales service channels that are relatively independent from automotive manufacturers and their sole distributors would emerge, especially in rural areas where the profit margin is typically lower and too costly for 4S store networks to cover. Nevertheless, it seems that the traditional single-brand 4S stores still play a dominant role in automobile sales. It may take longer to see the changes brought about by the Automobile Sales Measures.

Mergers, acquisitions and joint ventures

- 5** | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

Mergers, acquisitions and consolidations in the automotive industry are generally encouraged by the Chinese government to the extent that they enhance overall competitiveness in the automotive industry. As the Special Administrative Measures (Negative List) for Foreign Investment Access (2021 version) removes the final restrictions on foreign shareholding in

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automotive manufacturing companies, more acquisitions and restructurings occur to allow foreign car manufacturers gain increased shareholding in Chinese companies.

Merger control (antitrust) filing could still be a major concern, since many of the players in the market are global automotive makers and might have significant market share in a specific segment. Another major issue is how to protect a foreign brand or trademark in China. Licensing of such brands requires careful consideration and strategy.

Incentives and barriers to entry

6 | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

The Chinese government has been providing substantial incentives to the NEV sector for the past few years, ranging from manufacturing and purchasing subsidies and tax breaks to legislation and policy stimuli. Since the end of 2022, purchasing subsidies are no longer provided for NEVs. But according to the Circular on Continuing Tax Exemptions on Purchases of New Energy Vehicles jointly issued by the Ministry of Finance, State Taxation Administration and MIIT on 18 September 2022, NEVs are eligible for vehicle purchase tax exemptions until the end of 2023. The validity period of this tax exemption has been extended several times and may be further extended. Other incentives include the preferential enterprise income tax rate – if an automotive manufacturer qualifies as a High and New Technology Enterprise in China, it will be granted a preferential enterprise income tax rate of 15 per cent (reduced from the regular 25 per cent) and certain R&D expenditure may be deducted from its pre-tax revenue. Also, the Amendment to the Regulations on Management of New Energy Vehicle Production Enterprises and Product Access (which came into effect on 1 September 2020) has further lowered the entry thresholds into the NEV market by, among others, removing design and development capacity requirements for NEV manufacturers. Moreover, there are no longer any restrictions on foreign capital investor shareholding in automotive manufacturers; Tesla's wholly owned Shanghai Gigafactory, completed in October 2019, is a good example of this.

However, there are still barriers to entry into the market. On 4 June 2017, NDRC and MIIT jointly issued the Opinions on Accomplishing the Administration of Automotive Investment Project, which provided that, as a general principle, the Chinese government will not approve the establishment of any new traditional petrol and diesel vehicle manufacturer. Also, capital requirements do apply to both foreign and domestic investors, subject to the type of automotive product manufactured. For example, the total investment amount for establishing a new commercial vehicle manufacturer must be no less than 2 billion yuan, of which 800 million yuan must come from the investor's self-possessed funds. Nevertheless, high-quality, environmentally friendly and innovative products will still find their opportunities. We have seen successful cases in non-first tier local cities in China particularly, which we understand may be associated with a greater willingness of local governments to attract foreign investment. For example, in Sichuan Province, the commercial vehicle manufacturer Sichuan Hyundai Motor Co completed its conversion from a 50:50 Chinese-foreign joint venture to a wholly owned subsidiary of Hyundai Motor in January 2020, aiming to develop the hydrogen commercial vehicle market. In Anhui Province, Volkswagen took over the majority stake (75 per cent) of its joint venture with Chinese partner Anhui Jianghuai

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Automobile (JAC) in December 2020, planning to establish an e-mobility hub, as Anhui is known as a hotspot for NEV manufacturing. It must be noted, however, that the Provisions on Administration of Investment in Automobile Industry, promulgated by NDRC and in effect since 10 January 2019, have set forth requirements and restrictions for the establishment of NEV manufacturers. The requirements pertain to design and R&D capacity, production and post-sales services, and a new NEV factory can only be set up in a province where all existing NEV factories in that province have commenced operations with the approved production capacity, and the overall automotive production capacity in that province must be at a utilisation rate higher than other local industries in the two years before the establishment of the new factory.

PRODUCT SAFETY AND LIABILITY

Safety and environmental

7 | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

Automobiles and automotive-related products are among the most highly regulated in the product quality and liability regime of China. A China Compulsory Certification (CCC) must be secured before whole vehicles and applicable automotive parts (either domestically manufactured or imported) can be sold in the Chinese market. Under the current version of the CCC Catalogue, promulgated by the Certification and Accreditation Administration of the People's Republic of China (CNCA) on 22 April 2020, whole vehicles including passenger cars, trucks, trailers and motorcycles, and components including tyres, vehicle windows, rear-view mirrors, safety belts, seats and door locks, all require CCCs prior to sale in China. CCC-related regulations are actively enforced by CNCA. Manufacturers must apply CCC marks to their products (including applicable modifications) and are subject to routine CNCA inspections once a year.

For whole vehicles, however, CCC is only the first regulatory step before entering into the market. For consumers to be able to actually drive the cars on the road, they must receive emissions type approvals according to the standards set by the Ministry of Ecology and Environment (MEE) as well as its local and regional counterparts. As vehicle emissions are regarded to have a major impact on air quality, China has recently taken action to strengthen its vehicle emissions standards. From 1 July 2021, all types of motor vehicles (including heavy-duty vehicles) imported into and distributed and registered in China must comply with the Stage VI emission standard (Stage VI), replacing the previous Stage V emission standard implemented in 2018. The 2021 date is the national standard, and local governments have discretion to move it forward. Several cities, such as Shanghai, Chengdu, Guangzhou and Shenzhen enforced Stage VI in 2019.

Apart from the above, manufacturers, sellers and other parties in the distribution chain – such as those that provide transportation, warehouse services and repair and maintenance – are subject to various post-sale product quality and safety monitoring and reporting obligations pursuant to the Product Quality Law, the Consumers' Interests and Rights Protection Law and the Civil Code. If a product is found to contain a defect, the laws require primarily

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that manufacturers, or their domestic importers if the car is foreign-made, conduct a public recall, pursuant to guidelines and procedures set up in the Regulation on the Administration of Recall of Defective Auto Products (the Recall Regulation) effective as of 1 January 2013 and the implementing rules of the Recall Regulation effective as of 1 January 2016. The Recall Regulation covers both motor vehicles and trailers and applies to automobiles produced or sold within China. The requirement to recall is triggered when automotive products are determined to pose unreasonable risks to personal and property safety, or when products fail to comply with mandatory national or industrial standards that safeguard personal and property safety. Under the Recall Regulation, manufacturers are also required to promptly evaluate and investigate potential defects when they become aware of them, and the State Administration for Market Regulation (SAMR) will also notify the manufacturers about potential defects when they come to its notice through reports or its own investigation. Manufacturers and operators in the distribution chain who refuse to cooperate with SAMR during the defects investigation and recall process will be subject to penalties, and automotive manufacturing permits may be revoked in serious circumstances. Moreover, Provisions on the Administration of Motor Vehicle Emissions Recalls, promulgated by SAMR and MEE, effective as of 1 July 2021, have expanded the scope of product recalls to include emissions recalls. Hence, motor vehicles with substandard exhaust emissions must be recalled.

Moreover, around 15 March each year (World Consumer Rights Day), SAMR publishes a report on product recall due to safety and environmental issues. It appears that the safety of new energy vehicles (NEVs) has been a major focus for SAMR in recent years. According to the 2022 report, published on 10 March 2023, SAMR intends to continue to develop innovative product safety supervision systems, enhance the supervision of auto product recalls, improve the technical support system for auto product recalls and optimise the recall and quality improvement mechanism by cooperating with the industry association and relevant enterprises.

Product liability and recall

- 8** Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

The Part III Contract and the Part VII Tort Liabilities of the Civil Code, Product Quality Law and Consumers' Interests and Rights Protection Law are the primary legislation setting out the bases for product liability in civil law cases, which generally are divided into contract actions and tort actions. A potential breach of contract claim exists between the customer and the party that directly sells the automotive product to the customer. In comparison, a cause of action under torts can be asserted by anyone who has allegedly been injured by a defective product against a party in the distribution chain that allegedly caused the damage. In extremely serious product liability cases, the government may also pursue criminal charges pursuant to the Criminal Law.

The civil procedures of China recognise joint or representative actions, but this is substantially different from a class action under other common law jurisdictions, such as the US. A joint action is for claimants who share the same legal relationship against the defendant or defendants. The court's decisions in such cases apply only to parties acknowledging the

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proceedings. We are not aware of any large-scale joint or representative action ever being brought in consumer or product liability claims.

The 2013 amendments to Civil Procedure Law also allow qualified parties, such as national or provincial-level consumer interests and rights protection organisations, to represent groups of consumers in public interest litigations against defendants of product defect claims. In practice, neither joint actions nor public interest actions are common in cases involving automotive product defects. Claims involving numerous consumers are primarily settled through public recall actions under the supervision of the Chinese government, or filed against manufacturers and sellers on a case-by-case basis.

DISPUTES

Competition enforcement

9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

The State Administration for Market Regulation (SAMR) is empowered to exercise the anti-trust-related functions that were previously exercised by the competent divisions under the National Development and Reform Commission (NDRC), the State Administration of Industry and Commerce and the Ministry of Commerce.

The automotive industry has long been a major target of the competition enforcement. On 4 January 2019, SAMR promulgated Antitrust Guidelines for the automotive industry, which grabbed the attention of potential investors for various reasons. For instance, the Antitrust Guidelines offer some clarification about the demarcation of relevant markets. Compared to the 2016 draft published by NDRC, the Antitrust Guidelines provide more specific explanations on how to define a relevant market according to various components in sales and aftersales services. With respect to anticompetitive agreements, they establish a 'prohibition plus exemption' framework, meaning agreements that substantially hinder competition are prohibited, but exemptions are granted if they satisfy the conditions set forth in the Antitrust Law. Moreover, they stipulate a list of common types and thresholds applicable to presumed exemptions, which could have significant implications for vertical anticompetitive agreements that have been crucial but also tricky for major economic entities across the world. It is also worth noting that Antitrust Guidelines make it clear that suppliers can be considered dominant in aftersales markets even if they are not dominant in sales markets, and any conduct that falls within the three categories of abuse of a dominant position is prohibited.

According to the 2021 Annual Report on Antitrust Enforcement published by SAMR on 8 June 2022, antitrust enforcement efforts in the automotive industry in 2021 were mainly against the illegal concentration of undertakings, including failures to file mergers with SAMR for antitrust review or failures to do so in a timely manner. That said, the then applicable Antitrust Law provided that monetary penalties for an illegal concentration of undertakings must not be higher than 500,000 yuan. This situation has changed since the Amendment to the Antitrust Law took effect on 1 August 2022, the first time China has

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amended the Antitrust Law since it came into force in 2008. The amended Antitrust Law increased the maximum fines on the illegal concentration of undertakings from the previous 500,000 yuan to:

- 10 per cent of the sales amount of the preceding year on top of other corrective measures, where the concentration has the effect of eliminating or restricting competition; or
- 5 million yuan, where the concentration has no eliminating or restricting impacts.

Moreover, the amended Antitrust Law increased the maximum fines for monopoly agreements and failure to cooperate with antitrust investigations. Where the violation is extremely severe, its impact is extremely high and the consequence is especially serious, SAMR can multiply the fine amount by a factor between two and five. The greatly increased penalties are expected to make M&A dealmakers in the automotive industry more conscious of antitrust reviews. Other major changes in the Antitrust Law include prohibiting the use of certain technologies that lead to anticompetitive behaviour, enabling SAMR to review non-threshold transactions, introducing the stop-the-clock system and safe harbours for vertical monopoly agreements, and abandoning per se treatment for resale price maintenance. With the updated Antitrust Law, we anticipate that enforcement actions will continue to reflect the antitrust authority's active initiative and hard stance against monopolistic practices. The automotive industry is likely to remain a major target under stringent scrutiny.

Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

The majority of disputes in the automotive industry arise as a result of product liability and contractual issues, such as supply chain disruptions or commercial disputes. The parties involved usually include automotive manufacturers, suppliers, dealers, service providers, consumers and any other third party that suffers injuries or losses. Employment issues and intellectual property issues are also commonplace.

These disputes will be resolved through litigation or arbitration. In some major cities in China, there are arbitration or mediation centres specifically chosen by state-run industry associations or quality inspection institutions to settle automotive-related disputes, such as automotive industry consumer arbitration centres in Shanghai, Hangzhou, Wuhan, Nanjing, Harbin and Changchun. The government also provides personnel, contract templates and expert opinions to those who need help in this area.

The 2013 amendments to the Civil Procedure Law introduced pretrial preliminary injunctions, allowing the party who claims damages to receive injunctive relief before a judgment is rendered.

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Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

There is no specific formula for dealing with distressed suppliers in the automotive industry in China. Some of the steps that can be taken are as follows:

- negotiating and documenting a security agreement with the distressed supplier; and
- negotiating new supply agreements with prospective purchasers of the troubled supplier's business.

When suppliers are likely to become bankrupt, before the court officially accepts the bankruptcy application, the manufacturer (if unsecured) can initiate an action against the supplier for debt repayment and apply for preservation measures. In practice, the court often asks the applicant to provide security for its application for preservation measures.

Intellectual property disputes

12 | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

Along with the rapid expansion of China's automotive industry, the number of intellectual property (IP) disputes has also been on the rise. Both domestic and international automotive companies have acted as claimants in intellectual property disputes in past years.

China has a well-established IP protection legal framework and IP rights owners should familiarise themselves with how the system operates. IP rights owners need to identify and register IP rights where they can to reinforce their IP portfolios in China and ensure the future enforceability of such rights. Indeed, the China aspect should form a part of any international filing strategy. Trade secrets are another asset in the automotive industry and both contractual and physical protective measures should be adopted. Periodical training of employees and suppliers plays a key role in pre-empting leakage of confidential information.

China has undergone a series of judicial reforms in the IP disputes area in the past few years. In particular, China has established specialist IP courts in Beijing, Shanghai and Guangzhou, and an IP court of the Supreme People's Court to hear technical cases, such as disputes over patent rights and trade secrets. Since 1 January 2019, appealing certain patent-related judgments made by Higher People's Courts, IP courts and intermediate courts nationwide have been subject to the jurisdiction of the Supreme People's Court's IP court. In addition, while specific performance and injunctions have generally been difficult to ascertain as legal remedies, Chinese courts have become more willing to grant preliminary injunctions, exercise their discretionary powers and order defendants to substantiate their denials in some cases. The reform has resulted in greater consistency and increased predictability of case outcomes, as well as improved court efficiency.

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EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

Unlike some countries, China does not recognise independently run trade unions, but rather unions that are formed under the auspices of the All-China Federation of Trade Unions, a central quasi-governmental body. A union formed within an enterprise or company is, therefore, part of the All-China Federation of Trade Unions. Union formation is more on a top-down, as opposed to grassroots, basis. This has important implications for automotive companies operating in China and their relationships with the enterprise union. While the enterprise union's goal is to advance and protect the rights of employees, it can also serve as a mediator in employee disputes and act as a conduit between management and staff. Chinese unions tend to be less confrontational than trade unions in the automotive industries of other jurisdictions.

It is not possible to terminate an employee at will. Employers in China may unilaterally terminate an employment contract only under certain statutory grounds. Some of these grounds allow the employer to terminate immediately without the need to pay severance. These grounds include, but are not limited to, where the employee is in serious breach of the labour rules and regulations of the employer, or the employee commits a serious dereliction in the performance of his or her duties or commits graft causing severe damages to the employer. Other grounds allow the employer to terminate upon 30 days' notice (or 30 days' pay in lieu of notice) with the obligation to pay severance. These include circumstances where the employee is unable to fulfil his or her job obligations even after receiving training or being transferred to another position or, due to non-work-related illness or injury, the employee is unable to perform his or her original work or other tasks assigned by the employer after the expiry of the statutory medical treatment period.

While the law enumerates the grounds under which an employer may terminate an employee, defending such terminations before a labour arbitration tribunal can be rather challenging. This is largely because of the pro-employee atmosphere in China.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

In the race towards innovation in automated driving, the Chinese government has invested heavily over the years in driverless car technology, and developing automated driving vehicles (legally classified as intelligent networked vehicles or INVs) is a key focus in the Chinese government's automotive industrial development plan. In 2015, the Chinese government inaugurated the Made in China 2025 initiative to transform the country into an innovation hub.

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Under Medium and Long-Term Development Plan for the Automotive Industry jointly issued by the Ministry of Industry and Information Technology (MIIT), the National Development and Reform Commission (NDRC) and the Ministry of Science and Technology on 6 April 2017, it is stipulated that by the end of 2025 at least 80 per cent of new automobiles in China will be equipped with a driver assistance system, partial driving automation system or conditional driving automation system; and vehicles equipped with high driving automation and full driving automation systems will be launched in the market. This plan is also echoed in the Smart Car Innovation and Development Strategy issued by NDRC, to join forces with other key Chinese government agencies on 10 February 2020, which sets specific goals in smart automobile development to be achieved by 2025.

On 27 July 2021, MIIT, the Ministry of Public Security (MPS) and the Ministry of Transport (MOT) jointly issued the Management Specifications for Road Testing and Demonstration Application of Intelligent Networked Vehicles (for Trial Implementation) (INV Road Test Specification), which came into effect on 1 September 2021, replacing an older version issued in 2018. In addition to providing the qualifications and rules for road tests and demonstration application of INVs, the INV Road Test Specification expands the testing and demonstration area to designated public roads, which can include highways and urban roads.

Apart from road test rules for INVs, rules regulating market access and usage of INVs are being developed in some cities. The Regulations on the Administration of Intelligent Networked Vehicles in the Shenzhen Special Economic Zone (the Shenzhen INV Regulations) were adopted by Shenzhen Municipal People's Congress on 23 June 2022 and took effect from 1 August 2022. The Shenzhen INV Regulations cover many aspects of the INVs including road testing and demonstration, market access, registration, usage, cooperative infrastructure, cybersecurity and data protection, accident disposal and legal liability. Notably, they urge INV companies to create data security management systems and prepare privacy protection plans, to take measures to prevent data leakage, loss and damage, and to locate data storage servers within the territory of China. Following the example of Shenzhen, on 23 November 2022, Provisions of Shanghai Pudong New Area on Promoting Innovative Application of Driverless Intelligent Networked Vehicles were adopted by the Standing Committee of the Shanghai People's Congress, coming into effect on 1 February 2023 and providing a regulatory basis for the operation of driverless INVs in Shanghai. It is expected that these regulations will serve as models for other cities in China to promulgate similar provisions and accelerate the promotion of INVs.

In addition to INVs, new energy vehicles (NEVs) remain at the top of the Chinese government's agenda, judging from the State Council's Circular on the New-Energy Vehicle Industry Development Plan for 2021–2035 (the Development Plan) promulgated on 20 October 2020 and the 14th Five-Year Plan of the Chinese government promulgated on 11 March 2021. In recent years, the central government has established a comprehensive policy framework to support the NEV sector, ranging from policies on research, technology innovation, finance and tax incentives to infrastructure. For instance, the Development Plan encourages an integrated intelligent transport service, tapping into cloud computing and data collection and realising highly efficient coordination between 'people, cars, roads and clouds'. According to the Development Plan, the penetration rate of NEVs in China will increase from the current 4 per cent to 20 per cent by 2025. On 27 September 2017, MIIT, the Ministry of Commerce (MOFCOM), the Ministry of Finance, the General Administration of Customs of China and the General Administration of Quality Supervision, Inspection and Quarantine of China

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(AQSIQ) (now merged with SAMR) jointly issued Measures for the Parallel Administration of the Average Fuel Consumption and New Energy Vehicle Credits of Passenger Vehicle Enterprises (the Parallel Credits Measures), which came into effect on 1 April 2018, and was amended on 15 June 2020. Under the Parallel Credit Measures, if a passenger vehicle enterprise manufactures or imports more than 30,000 (inclusive) traditional-energy-powered (eg, gasoline-powered) passenger vehicles annually, it will be assigned an annual NEV credit target. This target can be met by a passenger vehicle enterprise through manufacturing NEVs to obtain credits or through purchasing NEV credits generated by other enterprises under a quota trading scheme. In the meantime, traditional energy powered vehicle manufacturers and large-scale importers will be assigned an annual average fuel consumption credit target. Automotive manufacturers and importers are required to meet that target in terms of the average volume of fuel consumption generated by the traditional energy powered vehicles they manufacture and import into China. With a view to incentivising auto makers and importers to shift their focus onto NEVs, the aforesaid NEV credits can be used to offset actual average fuel consumption credits, to help the relevant enterprises to achieve their average fuel consumption credit targets. The Parallel Credits Measures are expected to be further amended in 2023 to adapt to the changes in the market. With the positive and negative incentives provided under the Parallel Credit Measures, it is predicted that the NEV industry in China will continue to evolve.

Car-sharing businesses experienced explosive growth in China from 2012 to 2017 and have enjoyed steady growth in recent years. To regulate these businesses, MOT, MIIT, MOFCOM, the former AQSIQ, MPS, SAMR and the Cyberspace Administration of China (CAC) jointly issued the interim Measures for the Administration of Online Taxi Booking Business Operations and Services (the Online Taxi Measures) on 27 July 2016 (amended on 28 December 2019 and 30 November 2022). The Online Taxi Measures set out the licensing requirements for online taxi-booking business platforms and vehicles and drivers engaging in car-sharing businesses. The Online Taxi Measures also provide that the local transport authority in each city may impose additional criteria when issuing licences to vehicles and drivers engaging in car-sharing businesses. For example, in Shenzhen, starting from 2021, the use of traditional petrol cars in car-sharing businesses is no longer allowed. Other cities such as Dalian, Zhengzhou and Hainan intend to follow this trend. Moreover, MIIT and seven other governmental authorities issued the Notice on Organising and Carrying Out the Pilot Work of Pioneering Zones for Comprehensive Electrification of Public Sector Vehicles on 30 January 2023, which proposes to increase the proportion of NEVs used in public sectors to 80 per cent.

We have seen a strong regulatory trend for improving data protection in the automotive industry in 2022. Along with the Data Security Law (effective from 1 September 2021) and the Personal Information Protection Law (effective from 1 November 2021), NDRC, MIIT, MPS, MOT and CAC jointly promulgated the Several Provisions on the Management of Automotive Data Security (for Trial Implementation) (the Auto Data Provisions), the first data protection regulation targeted at the automotive industry, which came into effect on 1 October 2021. To implement the Auto Data Provisions, local counterparts of CAC require automotive manufacturers to submit annual reports to specify their automotive data security management. In terms of surveying and mapping, the Notice on Promoting the Development of INV and Maintaining the Security of Surveying, Mapping and Geoinformation was issued by the Ministry of Natural Resources on 25 August 2022. According to the Notice, if an INV is equipped with certain sensors to collect, store, transfer and process surveying, mapping and

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geoinformation and data, its usage falls into the scope of surveying and mapping activities and will be subject to a licence requirement. Foreign-invested automotive manufacturers must entrust qualified map partners to carry out such activities. The national standard information security technology – Security Requirements for Processing of Motor Vehicle Data (published on 12 October 2022 and effective from 1 May 2023) – outlines more detailed requirements for processing automotive data and is an important reference for automotive manufacturers. We expect these regulations and standards, together with the Data Security Law and the Personal Information Protection Law, will pose a compliance challenge for companies operating in automotive and transport industries in China, especially as regards the data localisation and cross-border data transfer and sharing that foreign car manufacturers will usually encounter and need to deal with on their daily operations.

UPDATE AND TRENDS

Trends and new legislation

15 Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

The promotion of intelligent networked vehicles (INVs) and the enhancement of data and personal information protection seem to be emerging trends in the automotive industry in China.

On 28 October 2022, the Ministry of Industry and Information Technology (MIIT) published a draft amendment to the Regulations on Automotive Vehicle Manufacturing Enterprises and Product Access Management (the Management Regulations), soliciting public opinions. The Management Regulations form a substantial part of the fundamental rules regulating the manufacture and sales of whole vehicles, which were issued by the MIIT on 27 November 2018, effective from 1 June 2019. This draft amendment mainly incorporates new provisions regulating INVs and the protection of data security and personal information.

Since the Shenzhen Municipal People's Congress first issued the Regulations on the Administration of Intelligent Networked Vehicles in the Shenzhen Special Economic Zone on 23 June 2022, effective as of 1 August 2022, it appears that efforts are also being made at a national level to further promote INVs. The Equipment Industry Development I of MIIT published a draft of Notice on the Pilot Programme of the Access and Road Test for Intelligent Networked Vehicles on 2 November 2022, soliciting public opinion. According to this draft, some qualified auto manufacturers and INV products equipped with autonomous driving capabilities may carry out road tests in a broader range of selected cities. It is expected that road tests for INVs will be carried out more commonly in China, and the INV industry will advance a step closer towards full commercialisation.

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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

France is a major automotive market. OEMs and the entire automotive and mobility industry play a significant role in the French economy due to the impact of intermediate consumption, distribution and car-related services and production along the supply chain. Nearly

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4,000 industrial companies make up the French automotive sector, with over 400,000 direct employees and 2.3 million people employed in related activities, making France the first European destination for job-creating foreign industrial investment in this sector. Estimates of the sector's global turnover are in the region of €155 billion.

For several years before the covid-19 breakout, French automotive manufacturers achieved growth and a substantial increase in production volumes. Production levels in 2017 exceeded by nearly 30 per cent that of 2007. In 2019, the number of registrations of passenger vehicles rose by 1.9 per cent, reaching 2.2 million new passenger vehicles. Around 80 per cent of the production of French manufacturers is sold abroad.

The covid-19 pandemic and the conflict in Ukraine have very seriously affected the French automotive market. Sales and registrations of new vehicles in France have dropped since the beginning of 2020 (eg, a decrease of more than 25 per cent for new registrations of passenger vehicles compared to 2019). However, since the beginning of 2023, sales have recovered slightly with an 8 per cent increase in January 2023 compared to January 2022.

Nowadays, diesel vehicles face a long-lasting downward trend in France. In January 2022, the registrations of diesel vehicles represented only 15.6 per cent of newly registered passenger vehicles versus 70.8 per cent in 2010, 57 per cent in 2015 and 31 per cent in 2020. Conversely, the registration of electric passenger vehicles has seen a significant rise in the past three years, from 42,764 vehicles in 2019 to 1 million by 2022 in total. Electric and hybrid passenger vehicles represented more than 21 per cent of all registrations of passenger vehicles in 2020 (compared with less than 8 per cent in 2019).

The French automotive industry is constantly making efforts to increase competitiveness, in particular through high pressure to mitigate costs at every level, as well as strong investment in research and development (with spending in excess of €5 billion on a yearly basis).

COMMERCIAL OPERATIONS

Regulation

- 2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

The regulatory framework applicable in France is based on European legislation.

Approval legal and regulatory framework

Vehicle approval is regulated by [Regulation \(EU\) 2018/858 of 30 May 2018](#), establishing a framework for the approval of motor vehicles and their trailers, and of systems, components and separate technical units intended for such vehicles, which entered into force in September 2020. The majority of the provisions of the Regulation were implemented into French law by a Decree dated 30 April 2009, according to [Directive 2007/46/EC of 5 September 2007](#), now replaced by Regulation (EU) 2018/858.

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The Regulation contains administrative provisions and general technical requirements for the approval of all new vehicles falling under its scope, and of the systems, components and separate technical units intended for those new vehicles, with a view to facilitating their registration, sale and entry into service within the European Union.

Article 13 of the Regulation provides that it is the car manufacturer's responsibility to ensure compliance with the type-approval process, as well as to ensure the conformity of production of the vehicle. This is the case whether or not the manufacturer has produced all the technical components of the vehicle. This Regulation is 'implemented' under French regulatory framework by [Decree No. 2009-497 of 30 April 2009](#) as amended and several ministerial orders, in particular [Ministerial Order of 18 February 2022](#) amending [Ministerial Order of 11 January 2021](#) on approval of motor vehicles and their trailers and systems and equipment for these vehicles within the scope of the Regulation. Vehicles for which (1) type approval is not mandatory or harmonised under Regulation (EU) 2018/858 of 30 May 2018, [Regulation \(EU\) 167/2013](#) on agricultural or forestry tractors or [Regulation \(EU\) 168/2013](#) on quadricycles, or (2) do not fall into any of the internationally recognised categories, must comply with the [Ministerial Order dated 19 July 1954](#). In any case, the scope of the French approval framework does not specifically differentiate between testing and normal-use scenarios.

[European Regulation \(EC\) 715/2007](#) as amended by Regulation (EU) 2018/858 and [Regulation \(EU\) 2017/1151](#) on type approval of motor vehicles with respect to emissions from light passenger and commercial vehicles (Euro 5 and Euro 6) further establishes harmonised requirements for the type-approval process in terms of emissions. The Regulation also establishes rules for in-service conformity, durability of emission control devices, onboard diagnostic systems and measurement of fuel consumption.

The manufacturer has the obligation, pursuant to article 4 of the Regulation (EC) 715/2007, to prove that all vehicles placed on the European market are type approved in compliance with the said Regulation. Notably, car manufacturers must demonstrate that they meet all emission limits as set out in Annex I.

[European Regulation \(EU\) 2019/2144](#) concerning type-approval requirements for the general safety of motor vehicles, their trailers and systems, components and separate technical units intended therefor, on the other hand, entered into force on 6 July 2022 and aims to ensure a high level of road safety throughout the EU. This Regulation introduces advanced safety systems offering new possibilities to reduce casualties, repealing [Regulation \(EC\) 661/2009](#) on road safety.

Pursuant to article 4 of the Regulation, car manufacturers must ensure that their vehicles are manufactured 'to minimise the risk of injury to vehicle occupants and other road users'.

The above-mentioned Regulations further provide that the national authorities of EU member states can grant the EC type approval once the concerned vehicles comply with the applicable Regulations. In France, it is the Ministry of Transport, pursuant to [article R 321-9 of the French Highway Code](#), that grants type approvals to vehicles that comply with the above-mentioned European Regulations.

The [Commission Implementing Regulation \(EU\) 2021/535](#) under the General Safety Regulation of 21 March 2021, lays down rules for the application of Regulation (EU)

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2019/2144 as regards uniform procedures and technical specifications for the type approval of vehicles, and of systems, components and separate technical units intended for such vehicles, as regards their general construction characteristics and safety. This Regulation provides for uniform procedures and technical specifications for EU type approval of vehicles of categories M, N and O, as well as of systems, components and separate technical units in accordance with articles 4(7), 8(3) and 10(3) of Regulation (EU) 2019/2144.

Registration requirements

The registration of a vehicle is an obligation for all owners of motor vehicles pursuant to articles [R 322-1 et seq of the French Highway Code](#).

However, pursuant to article R 321-11 of the French Highway Code, the registration of the vehicle can only succeed if the vehicle has been type approved by the authorities.

Publicity requirement

According to the [Climate and Resilience Act of 22 August 2021](#), manufacturers are required to include in their vehicle advertisements the level of carbon dioxide emissions of the models promoted via a CO₂ label on a gradient of seven classes (ranging from A to G).

In addition, under article 75 of [the Law on Orientation of Mobilities \(LOM\)](#) dated December 2019, manufacturers have the obligation promote active mobility, carpooling and public transport via statements to be inserted systematically in their advertisements, defined by the [Ministerial Order of 28 December 2021](#).

A penalty system is applicable from 1 June 2022 in case of non-compliance with the above requirements.

Insurance requirements

European Directive 2009/103/EC of 16 September 2009 relating to insurance against civil liability in the use of motor vehicles, and the enforcement of the obligation to insure against such liability, repealed and consolidated the five previous Directives on this matter: Directive 72/166/EEC, Directive 84/5/EEC, Directive 90/232/EEC, Directive 2000/26/EC and Directive 2005/14/EC.

European Directive 2021/2118 is to be implemented into national regulation by 23 December 2023 at the latest. Order No. 2023-171 of 9 March 2023, including several provisions for adjusting to European Union law in the fields of economy, health, labour, transport and agriculture, was published in the official journal of the French Republic on 10 March 2023. The Order gives the French government the faculty to implement the provisions of European Directive 2021/2118 into French law by means of an ordinance.

The provisions of European Directive 2009/103/EC had been transposed into the French Insurance Code under articles L 211-1 et seq and R 211-2 et seq. Pursuant to these provisions, car owners have an obligation to insure their vehicles. These provisions are subject to future provisions of European Directive 2021/2118 to be implemented into national law in the near future.

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Insuring motor vehicles is not an obligation devolved on manufacturers but on the owners of vehicles.

Development, manufacture and supply

3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

Design is usually done internally, except for some niche vehicles where manufacturers use freelance designers. In very rare cases, the development – including vehicle design, manufacture and supply – can be entirely outsourced.

Development of collaboration agreements for connected and automated vehicles is bringing new contractual structures to the market, which go beyond the usual licensing and joint development agreements. Ownership of data, data-sharing agreements and value-added supervision and support agreements for these vehicles are adding a further layer of complexity to the development, manufacture and supply arrangements in this sector – for instance, for the manufacture of sensors (eg, LiDAR), deployment of AI platforms and communication systems.

As for manufacturing, 80 per cent of the vehicle value is produced by the manufacturer's subcontractors through OEM partnerships. Internal manufacturer rules require the issuing of calls for tender between the manufacturer's major partners for compliance purposes and to optimise commercial deals. Specific tooling is usually provided by the manufacturer to its OEM.

Manufacturers can also share plants or in some rare cases use local plants through cost-plus agreements.

The assembly of a vehicle is typically done internally by the manufacturer or in a joint venture abroad.

Supply logistics for vehicle spare parts is often managed by the manufacturer using carrier services, while transport of vehicles is done by the manufacturer's internal services.

Distribution

4 | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

New vehicles are distributed by dealers, dealer networks and agents under different contractual arrangements (eg, manufacturer's subsidiary or independent owner; exclusivity or non-exclusivity). Second-hand vehicle markets are generally not under manufacturers' control. In large or major cities, manufacturers sometimes provide financial support to distributors to compensate for the high costs of rent. Importers are often referred to as independent dealers abroad in countries where manufacturers have no subsidiary.

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Commercial policy is under the manufacturer's control: product, price, promotion and place.

Until 2010, vehicle distribution was excluded from the general regulation on vertical restraints and solely governed by specific exemption regulations (eg, Regulation (EC) 1400/2002). Therefore, some contracts concluded before this date still contain provisions complying with these specific regulations.

Considering that the Commission's consultation and analysis conducted in 2008 in the vehicle distribution sector did not reveal any major competition issues, the application of a distinct regime to this sector was deemed no longer justified; it was therefore decided to align, as of June 2013, rules applicable to this sector with those applicable to vertical agreements in general, which are laid down in Regulation (EU) 330/2010 (the Vertical Block Exemption Regulation or VBER).

A specific regime was, however, maintained as regards vertical agreements related to the purchase, sale, resale of spare parts and repair and maintenance services for motor vehicles, which are governed by Regulation (EU) 461/2010 applicable since 1 June 2010 (Motor Vehicle Block Exemption Regulation or MVBER). Pursuant to the latter, agreements containing the following three hardcore restrictions cannot benefit from the exemption:

- restrictions on the sales of spare parts for motor vehicles by members of a selective distribution system to independent repairers;
- restrictions, agreed upon between a supplier of spare parts, repair tools or diagnostic tools or other equipment and a manufacturer of motor vehicles, on the supplier's ability to sell those goods to authorised or independent distributors or to authorised or independent repairers or end users; and
- restrictions agreed upon between a manufacturer of motor vehicles that uses components for the initial assembly of motor vehicles and the supplier of such components, on the supplier's ability to place its trademark or logo effectively and in an easily visible manner on the components supplied or on spare parts.

The MVBER is supplemented by Guidelines on vertical restraints in agreements for the sale and repair of motor vehicles and for the distribution of spare parts for motor vehicles (2010/C 138/05). The MVBER has been under review since December 2018; between 6 July and 30 September 2022, a public consultation was run by the European Commission, during which all interested parties were invited to comment on its draft Regulation extending the validity of the existing MVBER for five years (ie, until 31 May 2028) and a draft Communication introducing targeted updates to the Guidelines (in particular on the way the Commission will assess access to data generated by the cars' sensors when assessing vertical agreements between vehicle manufacturers and their authorised networks under article 101 Treaty on the Functioning of the European Union). Likewise, since 1 June 2022, [VBER](#) has been replaced by [Regulation \(EU\) 2022/720](#).

The automotive market is also governed by non-mandatory rules implemented by manufacturer associations' codes of good practice (the European Automobile Manufacturers' Association at the EU level and French Automobile Manufacturers Committee at the state level).

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Agreements with distributors are usually terminated at the end of the fixed term or freely in a non-fixed-term relationship. Regulation (EC) No. 1400/2002, applicable to contracts concluded between 1 June 2010 and 31 May 2013, sets out a notice period of one to two years depending on the definite or indefinite term of the contract. Codes of good practice provide for a notice period of two years.

Compliance with legal or contractual notice periods is not always sufficient to end a relationship, especially in the case of an established relationship. To estimate the length of the notice period, other criteria must be taken into account (eg, length of the relationship, percentage of turnover, retail revenue and economic dependency).

Mergers, acquisitions and joint ventures

5 | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

There are no particularities other than the control of the European Commission and the Competition Authority over concentrations.

Attention should be paid to the range of products sold by the target. Indeed, should some of these products have a dual use (including military vehicles) that would trigger the need for prior authorisation by the French Ministry of the Economy and Finance (quite similar to the US Committee on Foreign Investment in the United States); this approval, if required, will become a condition to closing. It generally takes between two and three months, bearing in mind that the legislation in this area has been significantly strengthened in France as from 1 April 2020 pursuant to [Decree of 31 December 2019](#), and further enhanced controls applied until 31 December 2022 (in particular with respect to listed companies). In addition, should the seller want to go through a locked-box transaction, possible variation of inventories and cash between the date of the binding offer and the date of the contemplated closing should be carefully examined by the buyer, in particular in light of major variations in valuations in the context of the covid-19 pandemic and subsequent semiconductor shortages, and more recently the Ukraine crisis. The war has caused major disruption for both carmakers and suppliers who have been forced to adjust their activities in both Ukraine and Russia due to component shortages. Economic sanctions imposed on Russia will also impact trade. Going forward, the legal risks that come with doing business with Russia will weigh heavily on automotive companies, especially regarding the import of aluminium, palladium and steel.

If the seller or the target has benefited from French government support to get through the covid-19 crisis, there could be important restrictions imposed on the seller or the target of the assets concerned. Close attention should be drawn to any impact on the right of the seller to transfer the target or the assets or on the way the purchaser may operate the business post-closing as a result.

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Incentives and barriers to entry

6 | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

There are no specific tax incentives for investment in the automotive market. General tax incentives for investors include:

- R&D tax credit (CIR), which applies to French companies incurring R&D expenses, regardless of their activity or size. This tax credit is assessed on eligible R&D expenses (including notably salaries, social security contributions, operating costs and so on). The CIR is equal to 1) 30 per cent for the portion of R&D expenses up to €100 million; and 2) 5 per cent of R&D expenses in excess of that threshold. It can be offset against French corporate income tax due for the year during which the R&D expenses are incurred (or refunded, subject to certain requirements);
- a new tax credit mechanism for collaborative research (CICo), available since 1 January 2022, which allows companies to benefit from a tax credit on outsourced R&D expenses, equal to 40 to 50 per cent (depending on the size of the enterprise). The CICo is subject to the following conditions in particular: 1) the service provider must be a specific research organisation; and 2) a collaboration agreement must be concluded between the two parties before the work begins;
- the innovation tax credit (CII), which applies to French small and medium-sized innovative enterprises, is assessed on certain innovation expenses (up to €400,000 per year) at a rate of 30 per cent;
- the young innovative company status (JEI), which applies to R&D small and medium-sized enterprises that meet certain criteria (eg, less than eight or 11 years old). JEI can notably benefit from an exemption on 1) certain social security charges on remunerations paid to R&D staff; and 2) French corporate income tax (full exemption on the first profitable fiscal year and 50 per cent exemption on the second profitable fiscal year); and
- companies located in certain areas and eligible for regional aid, which are usually companies carrying out new industrial, commercial activities, may be fully exempt from French corporate income tax during their first two fiscal years and then partially exempt from French corporate income tax for the next three fiscal years.

Specific green automotive incentives are available to French customers:

- an environmental bonus for any purchaser of a new passenger vehicle with an emission rate lower than 20g of CO₂ per kilometre, for an amount of up to €5,000 for individuals and €3,000 for companies, depending on the purchase price (€6,000 and €4,000 for vans, respectively); and
- in addition, the destruction of certain old vehicles entitles the holder to a conversion bonus of up to €6,000 (€10,000 for vans) for the purchase of an electric vehicle. The amount of the bonus depends on the income of the purchaser, the vehicle to be destroyed and the new vehicle purchased.

Certain automotive taxes and fees that are applicable to customers (individuals or companies) may be viewed as barriers to entry into the market:

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- a registration tax levied at the time the car registration certificate is issued, which notably includes:
 - a local regional tax (from which electric and hydrogen powered vehicles are exempt);
 - an environmental penalty if the CO₂ emissions exceed a certain threshold (the maximum amount being set at €50,000 for vehicles emitting over 225g of CO₂ per kilometre. The penalty is limited to 50 per cent of the vehicle acquisition price (including VAT) and certain exemptions may be available;
 - an additional weight tax, on vehicles over 1.8 tons (from which electric vehicles are exempt). Its rate is set at €10 per excess kilo. However, the sum of the environmental and weight penalties is capped at the maximum amount of the environmental penalty (€50,000 in 2023); and
- as of 1 January 2022, several existing car taxes (eg, the tax on company vehicles) have been repealed. Instead, three new taxes have been introduced on vehicles used for the purpose of carrying out an economic activity: 1) for passenger vehicles, two annual taxes on CO₂ emissions and atmospheric pollutant emissions; and 2) for heavy vehicles, an annual axle tax.

PRODUCT SAFETY AND LIABILITY

Safety and environmental

7 | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

The most relevant regulations regarding product safety and environmental issues are European Regulation (EU) 2018/858, Regulation (EU) 2019/2144, Regulation (EC) No. 715/2007 and Regulation (EU) 2017/1151.

Former Directive 2007/46/EC (repealed by Regulation (EU) 2018/858) had been implemented in the French Highway Code, which still provides that:

- if the French Ministry of Transport considers that, even if compliant with the type-approval Regulation, a vehicle presents a serious risk to road safety or seriously harms the environment or public health, the EC type approval may be refused (article R 321-9 of the French Highway Code);
- if, after the French Ministry of Transport granted EC type approval, new tests show non-compliant results, the ministry may take all necessary actions, including withdrawal of the type approval (article R 321-10 of the French Highway Code); and
- more generally, manufacturers must recall all vehicles already sold, registered or put into service if the model in question presents a serious risk to road safety, public health or the environment. In addition, they have to immediately inform the authority that issued the type approval thereof (article R 321-14-1 of the French Highway Code). The General Product Safety Directive 2001/95/EC provides general guidelines through the Commission Implementing Decision 2019/417 that apply to recall of type-approval vehicles.

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Since June 2020, a new entity named the Vehicles and Engines Market Surveillance Department (SSMVM) was created whose mission is to check that vehicles and engines placed on the French market comply with the technical requirements laid down by European and national regulations on safety, health and environment.

Governmental Ordinance No. 2020-701 dated 10 June 2020, Decree No. 2020-703 dated 10 June 2020 and an Order of the same day detail the powers and missions entrusted with this new entity. The SSMVM carries out documentary checks, tests and trials on its own initiative or following complaints. The Order of 7 February 2022 requires economic operators to immediately notify the SSMVM where a vehicle, system, component, part or equipment placed on the French market presents a risk to safety, health or the environment, or a non-conformity, and must explain the subsequent recall process conducted. The specific form of the notification to be sent to the SSMVM is available online on the [website of the French Ministry of Ecological Transition](#). The SSMVM will transmit the information received to the European Commission through the online platform called Rapid Exchange of Information System (RAPEX) or Safety Gate.

The SSMVM is expected to publish annual reports summarising its activities. The first report was issued for the 2018–2021 period summarising notably that:

- among the 85 economic operators inspected, 33 per cent of vehicles were considered non-compliant;
- 86 complaints were filed (40 per cent by users, 25 per cent by administration, 18 per cent by denouncing operators, 5 per cent resulting from self-referrals) mainly concerning passenger vehicles; and
- 43 vehicles were seized for inspection, from which three were found non-compliant on pollution emissions tests and one on braking system tests.

No statement was made on the potential warnings, sanctions or penalties that might be issued by the SSMVM against economic operators. The 2022 report has not been published yet.

In the event of a finding of non-conformities, the SSMVM may order administrative fines of a maximum of €1 million per product and can decide to make public the sanctions ordered against the manufacturer. The SSMVM can also order other administrative measures such as recalls, suspension of marketing or destruction of the products.

Criminal penalties may also be ordered in the case of non-compliance. Article L 329-49 of the French Highway Code notably provides that if the products have created a danger to health, safety or the environment, a criminal fine may be ordered of a maximum of 10 per cent of the average annual turnover of the manufacturer.

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Product liability and recall

- 8** Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

Product laws are very significant for the automotive sector: defective cars (or parts) are a source of particularly serious risks, which can potentially lead to road accidents, severe bodily injuries and significant material losses, plus the reputational loss for car manufacturers and their brands.

Under French product liability law, claimants bear the burden of proof to assess the product defectiveness and causation with the damage. There is, however, a trend in French (and EU) case law making the burden of proof easier to meet for claimants by making use of presumptions.

The automotive industry is one of the areas where product recalls and maintenance campaigns are very frequent. In 2022, more than a 100 recalls related to motor vehicles originating from France were registered on RAPEX. This includes recalls associated with defects and environmental issues.

Many questions are currently being debated concerning potential reforms of product laws. At European level, the Commission has taken a step towards a revision of the Product Liability Directive 85/374/EEC with an initiative entitled 'Adapting liability rules to the digital age and circular economy', which started with the issuance of an Inception Impact Assessment, and the launching of a large and public consultation process with key stakeholders ending in January 2022. The Commission's two main objectives are to modernise and adapt strict liability rules to the digital age and circular economy, and reduce obstacles to getting compensation in general and with respect to innovative products. On 28 September 2022, the European Commission adopted [two new proposals](#) that aim at adapting liability rules to the digital age with a focus on artificial intelligence. The first proposal, a revised Product Liability Directive, builds on known rules such as the strict liability of manufacturers for unsafe products, while modernising their scope to encompass digital products, circular economy business models and global supply chains. The second proposal, a first of its kind, is the AI Liability Directive and targets harmonisation of non-contractual liability rules for AI-enabled products and services, by notably introducing a presumption of causality applicable under cumulative conditions and a right of access to evidence in cases where high-risk AI is involved. This would impact the automotive sector, and in particular autonomous vehicles and their software. The Commission's proposals now need to be adopted by the European Parliament and the Council.

Class actions are a growing risk for automotive manufacturers in France. This procedural option was introduced into French law by the Hamon Law of 17 March 2014, which came into force on 1 October 2014 and is available to consumers who are placed in a similar situation and have suffered a financial loss resulting from material damage caused by a professional. Only a limited number of registered associations can bring class actions, where consumers can opt to join after a general judgment on the defendant's liability has been made. This system cannot be used to obtain compensation for bodily injuries. Since October 2014, a

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limited number of class actions have been launched in France. According to publicly available information, only a few of these class actions relate to the automotive sector. Various French consumer associations have launched class actions (at least three) against major car manufacturers as a consequence of emission issues. No information on the status of these proceedings has been made publicly available. On 15 December 2022, a new bill was filed before the French National Assembly introducing a single and unified legal regime for all class actions in civil matters. This bill aims to simplify the class action procedure, ensuring better compensation for the consumers concerned and shortening the time within which a judgment is issued, to better encourage the launching of French class actions. At this stage, the bill is not yet final and will be discussed between the MPs during public sessions. It will also allow France to consider the transposition of Directive (EU) 2020/1828 on representative actions.

DISPUTES

Competition enforcement

9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

The European Commission has fined 14 price-fixing cartels in the automotive industry for a total amount exceeding €5 billion over the past 10 years. All these cases were initiated by leniency applications filed by suppliers (which were not fined as a result), revealing the existence of the cartel and providing supporting evidence.

In 2016 and 2017, the European Commission imposed record fines of €3.7 billion on six European truck manufacturers, including a €1 billion fine, which is the highest fine ever imposed on a single company in a cartel case. Over a period of 14 years, truck manufacturers colluded on prices and on passing on the costs of compliance with stricter emission rules imposed by an EU regulation.

The European Commission punished 13 other cartels that involved car parts manufacturers for coordinating price increases to be passed on to car manufacturers, bid rigging, allocating customers and exchanging sensitive commercial information. These practices concerned 13 categories of products: wire harnesses; alternators and starters; parking heaters; automotive bearings; thermal systems; refrigerants; braking systems; spark plugs; lighting systems; occupant safety systems; flexible foam used in vehicle seats; door modules and window regulators; and latches and strikers.

In July 2021, the European Commission imposed fines totalling €875 million on Daimler and the Volkswagen Group after Daimler revealed that the companies had been colluding to limit their ambitions in reducing pollution from diesel cars.

The European Commission's decisions gave rise to numerous follow-on damages claims, in particular, in the truck manufacturers' case. The implementation in March 2017 of Directive 2014/104/EU on actions for damages under antitrust issues into French law can only encourage the development of such actions in France. In the trucks cartel case, the Court

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of Justice of the European Union ruled in October 2021 that victims of an antitrust violation may seek compensation from the subsidiary of the infringing parent company.

The French Competition Authority also showed interest in automotive spare parts. It issued a detailed opinion in 2012, pointing out that spare part prices were higher in France than in Germany or in the UK and making recommendations to stimulate price competition between manufacturers and suppliers for the supply of car parts. In this respect, France adopted in August 2021 Law No. 2021-1104, opening competition to the manufacture and distribution of visible spare parts (bumpers, lights, mirrors and so on) in the automotive sector.

The French Competition Authority dismissed (in May 2019) a claim by three repair companies against a car manufacturer after the latter refused to approve them. The repair companies claimed that this denial was discriminatory and would favour the manufacturer's authorised resellers. The French Competition Authority held that the manufacturer's decisions to refuse approval have been made on objective criteria and that the repair companies had not proven that the refusal was part of a general anticompetitive scheme implemented by the manufacturer.

In February 2023, the French Competition Authority launched a public consultation on the electric vehicle charging infrastructure sector; it is expected to issue an opinion (potentially including recommendations) on the competitive functioning of this sector in the first half of 2024.

Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

Apart from competition or antitrust and intellectual property issues, most disputes in the automotive industry relate to consumer matters, supply chain issues and criminal liability allegations.

There are several grounds in French consumer law enabling a consumer to sue an automotive manufacturer, such as defective product rules (article 1245 et seq of the French Civil Code), hidden defects (article 1641 et seq of the French Civil Code), non-conformity (article L 217-3 et seq and L 411-1 of the French Consumer Code) and general safety obligations (article L 421-1 et seq of the French Consumer Code).

In most cases, consumer disputes are resolved in court and settlement agreements are less frequent.

In the past, commercial disputes along the supply chain remained limited. This has changed quite drastically in recent years. In a context of shrinking margins, fiercer competition, increased likelihood of defective technology and growing remediation costs, pressure is strong on all actors, resulting in more frequent litigation to share the costs or recover them from another party. The causes of such issues may also lie in insolvency or bankruptcy cases.

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As a result, we see more and more frequently tensions between suppliers and OEMs or Tier 1 companies, even leading sometimes to threats to stop supplying or to terminate the business relationship. In certain circumstances, the dependency of an OEM in a single-source situation enables suppliers to exert higher prices for the remainder of the supply cooperation.

The covid-19 pandemic has generated a surge in supply chain litigation, with some companies trying to rely on force majeure doctrines to mitigate the consequences of the pandemic.

In addition, the current shortage of components and raw materials, as well as the substantial rise in energy prices aggravated by the ongoing Ukraine war, have had a strong impact on commercial relations and led to ever-increasing tensions on the market. This results, in particular, in forced renegotiations of contractual terms and prices, often in a contentious context, as well as commercial disputes related to injunction to supply or abrupt termination of business relationships. While French courts seem reluctant to apply the ground of hardship to modify or terminate a contract between parties, they tend to be more inclined to acknowledge this approach in light of the current circumstances. In this respect, the Paris Court of Appeal notably acknowledged by its decision of 25 November 2022 (Docket No. 22/00326) that the increase in a raw material price, linked to the increase in gas prices, constituted an unforeseeable circumstance affecting the initial agreed sales price, which could have grounded the request for the anticipated termination of the contract on the basis of hardship under article 1195 of the French Civil Code. However, the court considered that the excessive cost incurred in the performance of the contract was not proven in the case at hand and that the evidence could not be deduced from the mere price increase itself or from the variations in prices recorded on the wholesale gas markets. Failing to provide accounting and financial elements, the court dismissed the plaintiff's claim. In contrast, a first-instance judgment handed down by the Paris Commercial Court ordered the anticipated termination of a contract on the basis of hardship in light of the rise in electricity and packaging costs amplified by Russia's invasion of Ukraine, the impact of which on the plaintiff's financial situation was proven by the loss in its operating result (Docket No. 2022033136).

To restore the contractual balance between the parties, three new French bills to reform commercial relations between car manufacturers and distributors were filed before the National Assembly on 29 November 2022, 17 January 2023 and 14 February 2023. They aim at:

- specifying that the investments required of vehicle distributors must be reasonable in the light of economic prospects;
- giving vehicle distributors the freedom to sell their businesses by granting manufacturers or importers a preferential right, with the option of substitution if necessary, enabling them to retain control of their network; and
- providing for compensation in the event of termination of the contract, taking into account the investments made by the distributors and the customers they have attached to the brand locally.

These bills are not yet final and were referred to the Committee on Economic Affairs. They will be discussed by the MPs during public sessions.

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Summary proceedings are available in obtaining court injunctions either in cases of urgency or when the claim cannot be seriously challenged. Interim payments can also be sought through this type of proceeding.

Both automotive companies and their legal representatives have potential criminal liability exposure in the case of bodily injuries caused by their products (on grounds of involuntary bodily harm, manslaughter or placing someone under an immediate risk of injury or death). Corporations and legal persons may be prosecuted where the company financially benefited from the offence committed by one of its employees or representatives. Legal representatives can be prosecuted when there is either a manifest and deliberate violation of a specific safety rule, or in the case of gross negligence causing serious danger.

Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

Typically, distressed suppliers do their best to avoid pre-insolvency and insolvency proceedings, and may seek to obtain price increases, sometimes exerting pressure by threatening to stop or actually stopping deliveries. The customer can seek court orders in summary proceedings in an attempt to force the supplier to resume the supply and comply with orders regularly placed. Courts can also acknowledge settlement agreements, where some commercial provisions may be included regarding timing and organisation of the deliveries. Such acknowledgment increases the chances of the agreement being enforced by the distressed supplier, as well as facilitating the enforcement of the agreement in the case of failure to comply.

If the supplier is cash-flow insolvent, it must file for insolvency proceedings with the local commercial court. An administrator is appointed by the court and typically assists the management (but does not replace them save in specific circumstances). The administrator often asks customers to provide support by funding the insolvency period until an investor can be found or at least to give the supplier a chance of finding an investor. The administrator cannot force this manner of support, but customers do not have much choice if they do not have other supply options. This financial support often takes the form of price increases, limited in time, or in raw materials pre-payment, tooling financing and so on. All customers are usually asked to participate in the effort in proportion to their share in the volumes.

Distressed suppliers can also seek preventive proceedings. These are not insolvency proceedings with publicity, but rather confidential proceedings led by a court-appointed mediator who will assist the company in its discussions with its main stakeholders. In the automotive sector, it is often OEMs, shareholders and creditors (all bound by confidentiality) who try to reach a solution to avoid formal insolvency. This tool is commonly used for financial or industrial restructurings in the automotive sector. In practice, preventive proceedings are often used before insolvency proceedings (eg, in view of preparing the insolvency proceeding beforehand), but can also be conducted on a stand-alone basis.

Public authorities are often involved in distressed supplier issues through various channels. In significant cases that involve more than 400 employees, the department of the Ministry

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of the Economy and Finance dedicated to industrial restructurings will oversee the negotiations and request customers to participate in the discussions. In smaller situations, which are still important locally, local representatives of the state can be involved. Dedicated funds to support distressed suppliers in the automotive sector have been created since 2008 by French public authorities, together with French OEMs and major Tier 1 suppliers. The state-owned bank Bpifrance is also regularly called in to support major suppliers in the automotive sector.

The process, therefore, depends on how distressed the supplier is and how politically sensitive the issue is (ie, how many jobs are at stake).

The current crisis faced by the automotive sector that started with technological evolutions, and was then accelerated by the covid-19 pandemic and the war in Ukraine, has already generated multiple insolvency proceedings for companies at every stage of the supply chain, despite the massive economy recovery plan implemented by the French government for the automotive sector in 2020.

Intellectual property disputes

12 Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

There are a fair number of intellectual property disputes in France. These usually do not involve car manufacturers but rather OEMs and suppliers. The intellectual property rights most commonly relied upon in the automotive industry are patents, designs and trademarks.

Intellectual property rights in France are effectively protected. French law on intellectual property rights is the result of national statutory and regulatory provisions, statutory provisions implementing international and multilateral agreements and European regulations having direct effect in France as a member state of the European Union. The implementation of these international rules is codified by the national substantive law in the French Intellectual Property Code.

Among other things, French law includes provisions regarding patents, trademarks, designs, trade secrets, authors' rights and database producer rights. Since 1 January 2023, the scope of protection of registered designs over spare parts has significantly reduced. Pursuant to article L 513-6-4 of the French intellectual property Code, 'acts intended to restore a motor vehicle or trailer to its original appearance [...] and which: a) concern parts relating to glazing; b) or are carried out by the equipment manufacturer who produced the original part' will no longer be considered as design infringement. This means that design rights over glazing parts can no longer be enforced. The duration of the protection for other spare parts designated in article L 513-6-4 is reduced to 10 years (instead of a maximum period of 25 years). The upcoming EU design Directive and Regulation notably aim to harmonise rules regarding spare parts, and their impact on French law will be monitored.

Also from 1 January 2023, copyright is no longer enforceable against the sale, use and reproduction of spare parts intended to restore a motor vehicle or trailer to its original appearance, pursuant to article L 122-5(12) of the French Intellectual Property Code.

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Car manufacturers and OEMs have traditionally been among the top filers of patents in France, and they extensively use registered design rights to protect vehicle body parts. As for trademark, in the 2022 Interbrand ranking, four trademarks designating car manufacturers were ranked among the top 20 brands worldwide (all sectors combined).

Intellectual property enforcement in France is for courts to ascertain. As regards patents and EU trademarks and designs, the Paris Civil Court (where decisions are issued within 18 to 24 months depending on the complexity of the matter) has exclusive jurisdiction. This allows for harmonisation of case law beginning at first-instance level. Decisions can be appealed before the Paris Court of Appeal, and a further appeal on legal issues is possible before the Court of Cassation.

Intellectual property law in France provides for a specific means of obtaining evidence: the infringement seizure. The infringement seizure is a highly effective evidence-gathering procedure whereby an intellectual property rights holder, suspecting an infringement of its rights, applies *ex parte* for an order of the presiding judge of the Civil Court authorising a bailiff and possibly an independent person knowledgeable in the art to enter any premises (including those of competitors or suppliers) where evidence of the infringement may be found, to seize samples of the allegedly infringing product or to describe it. Following the infringement seizure, the claimant must follow a strict timeline (ie, 20 working days or 31 calendar days) to serve the defendant with a writ of summons.

On the merits, intellectual property rights holders mainly seek a permanent injunction and compensatory damages. Intellectual property rights holders may choose to apply for a preliminary injunction in summary *prima facie* cases before or while an infringement case is pending on the merits.

Similar evidence gathering means and remedies have been available for trade secrets since July 2018, when Directive (EU) 2016/943 on the protection of undisclosed know-how and business information against their unlawful acquisition, use and disclosure was implemented in France. Alternative dispute resolution is also available in intellectual property rights infringement issues. *Ad hoc* mediation enables the parties to reach a settlement. Additionally, French intellectual property law now clearly states that the exclusive jurisdiction of the Paris Civil Court 'does not preclude the use of arbitration'.

EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

There are some specific employment issues or trends that the automotive industry (OEMs and car manufacturers) must be aware of.

Owing to the tense and complicated employment law climate in France, cost pressures and reduction in production, many automotive companies in the country had to negotiate forced or voluntary mass redundancy plans.

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This happened to most of the OEMs' French sites, which faced a significant decrease in importance in the European market over the past 10 years.

Instead of negotiating strict mass redundancy plans, the cost of which is extremely high in France and could give rise to important disputes with terminated employees, Stellantis and Renault negotiated various voluntary departure plans with unions to cut job positions and to reach agreements with unions to restore competitiveness.

Agreements on the restoration of competitiveness have also been entered into and involve significant and tough negotiations with major French unions (CFDT, FO, CGT, CFTC and CFE-CGC) and works councils to agree on:

- voluntary departures;
- salary freezes;
- increases in working time; and
- increases in working time flexibility.

In a context of increased tension within the automotive market (due to the covid-19 crisis, Ukraine war, shortage of components and decrease in raw materials) stoppages of production have become more frequent since 2020. Long-term furlough schemes have been negotiated at the level of the industry, but also at level of car manufacturers themselves (such as Stellantis and Renault) to increase flexibility and the adaptability of employee activities to market constraints.

This strategy has been widely endorsed by successive French governments that recognise the role of French car manufacturers in promoting the country's international development, while preserving to a certain extent local employment and using a concerted strategy with regional authorities, unions, manufacturers, suppliers, subcontractors, distributors, service providers and research institutes to maintain excellence and research and development centres in France.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

The development of autonomous vehicles and Mobility as a Service (MaaS) is certainly the biggest source of legal questioning.

Automated and autonomous driving

At the international level, during its 81st session in Geneva from 21 to 25 September 2020, the Global Forum for Road Traffic Safety (WP.1) voted an amendment to the Vienna Convention on road traffic to favour the development of automated vehicles. On 14 January 2022, 53 United Nations member states, including France, adopted an amendment to article 34, governing autonomous vehicles, as well as a new article 34-bis to the Vienna Convention

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paving the way to the development of Level 3 autonomous vehicles. The amendment to the Vienna Convention was integrated into the French legal system with Decree No. 2022-1034 of 21 July 2022. Also, on 22 January 2021, the United Nations Economic Commission for Europe's (UNECE) [Regulation No. 157](#) entered into force. This regulation provides for the technical requirements to be complied with by Level 3 automated vehicles. In particular, the Regulation prescribes that automated vehicles may not exceed a speed of 60km per hour and should only operate on roads where pedestrians and cyclists are prohibited and which, by design, are equipped with a physical separation that divides the traffic moving in opposite directions. An [amendment](#) to UNECE Regulation No. 157 was adopted on 22 June 2022 and will increase the maximum authorised speed of Level 3 automated vehicles from 60km per hour to 130km per hour.

At the EU level, Regulation (EU) 2018/858 and European Regulation (EU) 2019/2144 were modified by [Commission Delegated Regulation \(EU\) 2022/1398](#) of 8 June 2022, [Commission Delegated Regulation \(EU\) 2022/2236](#) of 20 June 2022 and [Commission Implementing Regulation \(EU\) 2022/1426](#) of 5 August 2022. These Regulations adopted the technical type-approval rules to be complied with by Level 3 and Level 4 automated vehicles.

At the national level, on 3 August 2016, an [Ordinance](#) was issued authorising manufacturers to conduct tests with automated vehicles on French roads. This was a first step towards the arrival of autonomous vehicles on the French market. Since then, a [Decree](#) was issued in March 2018 to set out the authorisation regime for the testing of automated driving vehicles on public roads.

The authorisation regime is made up of two levels: a test that can cover one or several vehicles involved, and a specific registration for each vehicle. Testing must relate to either:

- technical and development assessments;
- evaluation of the performance in a situation where the automated vehicle is intended to be used; or
- public demonstration, notably during events.

Authorisations will be granted for a maximum of two years but can be renewed. The testing framework is not adapted to SAE Level 5, as the presence of a driver who can operate the vehicle and take control of the vehicle at any time is required. However, the driver can be outside the vehicle. The authorisation holder must provide all the information to prove that when a driver is outside the vehicle, he or she will be ready to take control over the vehicle at all times and be able to do so.

Finally, a [Decree](#) modifying the testing regime of delegated driving vehicles was adopted in December 2020 to allow, as part of a testing framework, delegated vehicles platooning and the circulation of rolling machines on certain pavements and sidewalks for the purpose of goods delivery.

In December 2020, the French government also issued an [updated strategy](#) for the development of automated road mobility 2020–2022. Under this strategy, France planned to finalise the legislative and regulatory framework, by Q1 2022, for the operation of automated vehicles resulting from article 31 of the Law on orientation of mobilities (LOM) dated December 2019,

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for vehicles with a driver on board and for those (including without a driver on board) used as part of an organised transport of passengers on a predefined route or zone.

In this respect, the French government adopted on 14 April 2021, an [Ordinance](#) setting forth the rules regarding the criminal liability in case of circulation of delegated driving vehicles and automated road transport systems. Regarding the conditions of use of automated driving systems, the Ordinance provides that such conditions of use are defined by the vehicle manufacturer and must be provided to the consumer before the purchase or lease of the vehicle. The decision to activate the automated driving system is made by the driver and, when the automated driving system's conditions of use are no longer met, the automated driving system must alert the driver and request the driver to take back control and engage and perform a minimal risk manoeuvre in the case of lack of response from the driver or serious failure.

An [implementing decree](#) of the Ordinance was adopted on 1 July 2021. This Decree provides, in particular, for the definition of a delegated driving vehicle and sets out the specific features that automated driving systems may be equipped with. It also defines the interaction between the human driver and the automated driving system, as well as the manoeuvres that the system may perform automatically. It specifies the level of attention expected from the driver on his or her driving environment when an automated driving system is activated. The government adopted an [Order](#) on 8 December 2022 setting forth the content and means of provision of mandatory information to consumers regarding the conditions of use of the automated driving system. The implementing decree also prescribes the conditions of use of automated road transport systems, which can only operate on pre-defined routes or areas.

In conclusion, since 1 September 2022, the French legal framework authorises the operation of Level 3 automated vehicles for passenger cars and Level 4 automated vehicles for road transport systems.

Focus on automated vehicle liability aspects

On 28 September 2022, the European Commission published a proposal Directive No. 2022/0303, the AI Liability Directive, adapting non-contractual civil liability rules to artificial intelligence. The AI Liability Directive aims at improving the functioning of the internal market by laying down uniform rules for certain aspects of non-contractual civil liability for damage caused with the involvement of AI systems. In this respect, article 4 notably provides for a rebuttable presumption of a causal link in the case of fault, when specific conditions are met. Article 3 also provides that a court may order the disclosure of relevant evidence about specific high-risk AI systems that are suspected of having caused damage, and introduces a presumption of non-compliance with a duty of care. This proposal Directive is not yet final and will be discussed by the European Parliament.

France has not yet implemented a specific civil liability regime that would be applicable to a series deployment of automated vehicles. As a matter of principle, civil liability is incurred under French law if there is 1) wrongdoing or negligence (including putting on the market or selling a product deemed defective or unsafe); 2) damage; and 3) if causation between the two is established.

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The LOM enabled the government to adopt rules to amend French legislation (notably the French Highway Code) to take into account the circulation of automated vehicles and to define the liability regime applicable to automated driving. The LOM enabled the government to regulate both 'partially or fully' automatic vehicles. This regulation was adopted by an Ordinance on 14 April 2021, which sets new criminal liability rules for both manufacturers and drivers within the French Traffic Code.

As a general principle, these regulations provide that the driver of 'a vehicle whose driving functions are delegated to an automated driving system' should not be held criminally liable for the offences committed when the automated driving system holds the dynamic control of the vehicle at the time of the incident. This general principle suffers a few exceptions, notably when the driver does not regain control of the vehicle after being requested to do so by the system, or when the driver does not comply with injunctions given by law enforcement authorities. It is also provided that the driver must constantly be in a position to respond to a request to take control of the automated driving system.

Outside these exceptions, the regulations provide for the liability of the car manufacturers in the case of manslaughter or bodily injuries when the vehicle operates according to conditions of use, if it is established that the manufacturer committed a criminal fault. The manufacturer will also be financially liable for petty offences resulting from breaches of driving rules.

A series of rules is set to ensure that the law enforcement authorities and the holder of the registration certificate of the vehicle access to the relevant data of the driving system in the case of traffic accidents, roadside checks and petty offences to driving rules. The manufacturer must guarantee the integrity of the data.

In addition, the provisions of the French Traffic Code and the French Transport Code were amended by a Decree of 29 June 2021 to allow for the circulation on French roads of autonomous vehicles and automated road transport systems on predefined routes or zones as of September 2022.

Specific criminal liability rules are also provided for the deployment of automated road transport systems. These rules notably state that persons authorised to carry out remote intervention on a vehicle operated as part of an automated road transport system will be liable for the offences resulting from their intervention or lack of intervention on the vehicle. These rules are an important step towards the implementation of a special liability regime applicable to autonomous driving in France, even though a number of questions (notably with regard adjustments of civil liability and product liability regimes to autonomous driving) remain open even after the enactment of the above rules.

One of the outstanding questions will be whether Law No. 85-677 of 5 July 1985 improving the situation of victims of traffic accidents will need to be amended, because this law imposes a specific regime of liability for drivers and vehicle custodians that is designed to ensure the compensation of victims of traffic accidents. Indeed, even if this law does not directly impact product liability, it could impact the liability of car manufacturers or software developers if they were to be considered drivers or custodians of automated vehicles in an accident. The 1985 law notably does not precisely define who must be considered the driver of the vehicle. Also, this law imposes that any person that can be held liable for damages

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suffered resulting from a traffic accident must be insured accordingly. It is yet to be determined how this obligation could transpose to Level 4 automated vehicles.

With regard to product liability *stricto sensu* and putting aside the recent rules applicable to criminal liability, the main question will be to assess, in the case of an accident, from which equipment or service it originated and which operator or person should be held liable (ie, car manufacturer, software developer, other components suppliers, custodians or authorities who must put in place infrastructures for the automated vehicle to operate safely). In this respect, data recorders will have a significant impact on determining the origins of the accident involving automated vehicles. This question impacts all potential defendants and their cross-claims against each other depending on the nature of the issue.

In this respect, France has passed an ordinance on access to vehicle data providing detail on the data to be collected and the conditions of access to such data in the event of a road accident.

Connected vehicle data

One of the key principles of European and French data protection laws is transparency. Data subjects (ie, drivers) must be informed by the data controller (ie, car manufacturer) of how their personal data will be used. Therefore, the French Data Protection Authority (CNIL) published in October 2017 [guidelines](#) on the use of personal data collected by connected vehicles through vehicles' sensors, telematics devices or mobile applications. Such guidelines provide guidance to OEMs on how to integrate data protection by design and by default requirements into the production pipeline. Also, the European Data Protection Board adopted [guidelines](#) on processing personal data in the context of connected vehicles and mobility-related applications on 9 March 2021. The main changes between the draft guidelines (released in February 2020) and this final version are the increased requirement of consent as legal basis to process personal data from connected vehicles, the classification of speed data combined with geolocation data as potential offence-related data and further clarifications on the obligation that vehicles provide clear and easy privacy settings to allow the user to control the data collected and transmitted from the vehicle. At the beginning of March 2023, CNIL announced the set-up of a [compliance club](#) dedicated to connected vehicles and mobility players. The creation of this club is carried out in line with its 2017 compliance pack and aims to establish a dialogue between the sector's players in order to update the recommendations on personal data protection and integrate new use cases. This initiative will result in new standards for data protection in connected vehicles.

The [Ordinance](#) resulting from article 32 of the Mobility Law was adopted on 14 April 2021. It sets out the legal framework on access to the data of connected or autonomous vehicles by law enforcement authorities, infrastructure managers, emergency services, transport organising authorities and insurance undertakings for various purposes such as accident prevention, knowledge of the road infrastructure and traffic conditions, or in the case of accidents, for insurance compensation or analysis of accidents. It enables vehicle manufacturers to correct by telematic means flaws and defects of vehicle systems or components affecting a series of vehicles and threatening the vital interests of individuals in a serious and imminent manner. The Ordinance finally includes new cybersecurity obligations upon vehicle manufacturers or vehicle equipment manufacturers in the case of electronic attacks.

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On 23 February 2022, the European Commission presented a [proposal for a regulation to frame transfers of non-personal user or business data generated by the internet of things](#), including by connected vehicles. The objective of the Data Act is to establish a clear and pro-competitive set of rules for services based on access to connected vehicles data. This regulation will have a direct impact on automotive suppliers with regards to access to in-vehicle data and resources, where vehicle manufacturers currently have complete control over the data flow to and from connected vehicles. The European Commission's approach is to put users at the centre of the system, by giving them the power to decide if and how vehicle generated data is shared. However, when sharing the data with third parties, the data holder and the user may agree on measures to preserve the confidentiality of the data and trade secrets. The shared data provided may not be used to develop products that would compete with the product the data originates from, but allows third parties to use the data to provide competing services. The Data Act is currently being discussed at the EU Council.

In addition, [DG GROW's proposal](#) launched a public consultation on 'Access to vehicle, functions and resources' from 29 March to 21 June 2022, to set the conditions for access and use to generated data. The proposal will help in clarifying EU regulations and enable favourable competition in the automotive and mobility industry (ie, competition for services based on access to vehicle data). The commission lists several of these services:

- repairs and maintenance;
- vehicle sharing;
- mobility as a service; and
- insurance.

This consultation could put the entire industry on an equal footing by promoting competition and innovation. However, the legislation, which has been awaited for several years, was not studied as planned on February 2023 by the regulatory scrutiny committee and therefore creates a new delay in the process.

Finally, on 10 February 2023, Roland Lescure, Minister Delegate for Industry, Jean-Noël Barrot, Minister Delegate for Digital Transition and Telecommunications and Clément Beaune, Minister Delegate for Transport, announced the four priority actions intended, from 2023 to 2025, to support the deployment of automated and connected road mobility services in the territories. Among these four actions, the first consists of prioritising and coordinating the implementation of connectivity and data exchange systems.

Indeed, connectivity systems allow supervision and remote interventions and improve the safety and quality of service of automated vehicles. The development of connectivity systems can be a factor in accelerating the development of the autonomous vehicle. In addition, the first action, which targets data exchanges, makes it possible to create value through the development of mobility-related services, while respecting the personal data protection framework and cybersecurity requirements.

Shared transportation services

The LOM and the EU Regulation 2017/1926 impose on 'on-demand transport service providers' and 'sharing service providers' a series of obligations relating to data sharing. Also, a National Access Point for transport open data was created by the LOM with the aim

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of gathering data on the entire mobility system on a national basis. The Data Governance Act, entered into force on 23 June 2022, will also apply from 24 September 2023. This regulation is part of the European strategy on data. It provides the reuse and share of personal and non-personal data via data pools. As stated by the Commission, this sharing is useful in different areas such as health and agriculture, but also in the automotive sector. Sharing data should facilitate and encourage research in automotive and especially for connected and autonomous vehicles, and smart road systems. For example, it can be very useful for real-time navigation systems that will be crucial in future smart cities.

UPDATE AND TRENDS

Trends and new legislation

15 | Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

Since the beginning of 2020, because of the covid-19 pandemic and the conflict in Ukraine, the automotive sector in France has faced one of the worst crises in history: registrations of passenger vehicles decreased by 18 per cent in 2021 compared to the previous year, and by more than 35 per cent compared to 2019.

One growing concern in the past year has been the supply chain problem (shortage of semiconductors, plastic and steel) that directly impacts OEMs and car manufacturers in France. Eighty-four per cent of the French automotive equipment manufacturers would be impacted by these shortages and some car manufacturer plants have had to stop due to supply problems.

In May 2020, the French president presented a massive recovery plan for the automotive sector, valued at nearly €8 billion. The French president notably announced that grants for the purchase of vehicles will be raised with a view to promoting greener vehicles, as well as the creation of an investment fund of €1 billion to help companies in the sector modernise and digitise production chains, and to foster the environmentally friendly transformation of the automotive industry.

The [Climate and Resilience Act](#), adopted on 21 August 2021, provides for new measures to support the ecological transition in the transport industry.

The text amends article 73 of the [Law on Orientation of Mobilities](#), which introduced the objective of ending the sale of new passenger vehicles and light commercial vehicles using fossil fuels by 2040, by adding two additional objectives. It first sets the end of the sale of new passenger vehicles emitting more than 95g of CO₂ per kilometre on 1 January 2030, with the exception of certain special purpose vehicles (eg, off-road vehicles for professional use or in mountain areas) without these derogations being allowed to exceed 5 per cent of total annual sales of new passenger vehicles. The second objective is the end of the sale of new heavy-duty vehicles used to transport people or goods and using mostly fossil fuels by 2040.

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These developments come with support for the acquisition of greener vehicles as well as a funding for the conversion of thermal-engine vehicles into electric motors or the installation of technical equipment to improve safety. For example, [Implementing Decree of 29 December 2021](#) strengthened the green bonus and conversion premium to support the development of very low-emission light commercial vehicles.

Lastly, the [Decree](#) amending the French Environmental Code regarding the greening of vehicles used by delivery platforms was published on 5 April 2022. Introduced by article 114 of the Climate and Resilience Law, the decree requires delivery platforms with more than 50 workers to respect a minimum share, increasing over time, of very low emission vehicles and bicycles.



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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

If you click on 'About us' on the website of the German Association of the Automotive Industry (VDA), the first sentence reads as follows: 'Germany is where the automobile was invented.'

Despite all the disruptions of the past few years, the automotive industry in Germany is obviously one of the most important drivers of the German economy in general. Of all the industrial sectors, it is by far the strongest in terms of turnover, research and exports, generating prosperity, growth and employment in numerous other sectors as well. Automotive manufacturers (OEMs) such as Audi, BMW, Daimler, Porsche and Volkswagen, as well as the world's largest and leading automotive suppliers such as Bosch, Continental and ZF, are headquartered in Germany with global operations and among the leading automotive companies worldwide. Foreign automotive companies such as Ford, Hyundai, Kia and Opel have their European headquarters in Germany as well.

It is expected that the German automotive industry will continue to be one of the most important drivers globally, even as disruptions continue to take place, such as supply bottlenecks caused by covid-19 or Russia's war on Ukraine, and new entrants become part of 'the future of mobility'. This is mainly for two reasons. First, by redefining their strategies, German automotive companies are relentlessly trying to adapt and transform to the radically changing new automotive world. This includes developments in the four main areas called ACES: autonomous, connected, electric and shared vehicles. Second, Germany has a strong technology focus, which should allow it to play a substantial role and maybe also lead the development of such vehicles. The automotive industry is by far the most research-intensive sector in Germany.

COMMERCIAL OPERATIONS

Regulation

- 2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

Type approval

Type approval is a prerequisite for the registration, sale and entry into service of vehicles and vehicle parts in Germany. Type approval is granted and monitored by the German Federal Motor Transport Authority (KBA) and can be generally obtained under three different

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regulatory frameworks: the United Nations Economic Commission for Europe (UNECE), the EU and the German type-approval framework.

The UNECE framework is based on an international agreement dated 20 March 1958 (the 1958 Agreement) concerning the adoption of uniform technical prescriptions for wheeled vehicles, equipment and parts that can be fitted or used on wheeled vehicles and the conditions for reciprocal recognition of approvals granted based on these prescriptions. This agreement currently comprises 165 technical regulations on safety and environmental subjects (the UN Regulations), but not all signatory states apply all technical regulations. Therefore, the applicability of the UN Regulations must be determined on a case-by-case basis. The objective is to harmonise the UNECE type-approval framework and the EU type-approval framework. This process is still ongoing and not yet completed.

Within the European Union, type-approval regulations are harmonised and mutually recognised under the EU type-approval framework. The German type-approval framework is therefore only applicable if no EU harmonisation is in place. Thus, in practice, the most relevant regulatory framework in Germany is the EU type-approval framework.

Under the EU type-approval framework, Regulation (EU) 2018/858, which repealed Directive 2007/46/EC and has been directly applicable in all member states since 1 September 2020, establishes a framework for the approval and market surveillance of motor vehicles and their trailers, and of systems, components and separate technical units intended for such vehicles. Regulation (EU) 2018/858 provides for administrative provisions and general technical requirements for the type approval of vehicles and their parts, with a view to facilitating their registration, sale and entry into service within the European Union.

Several separate EU directives and regulations lay down more specific technical requirements concerning the construction and functioning of vehicles and their parts. Annex II to Regulation (EU) 2018/858 provides for an exhaustive list of all regulatory acts applicable to type approval. Examples of these regulatory acts are Regulation (EC) 715/2007 on type approval of motor vehicles with respect to emissions from light passenger and commercial vehicles (Euro 5 and Euro 6) and Regulation (EC) 661/2009 concerning type approval requirements for the general safety of motor vehicles, their trailers and systems, components and separate technical units intended therefor. On 6 July 2022, Regulation (EC) 661/2009 was repealed and replaced by Regulation (EU) 2019/2144 (the new General Safety Regulation), which aims to further improve the safety performance of vehicles, in particular by introducing new advanced vehicle safety systems (eg, warning of driver drowsiness and distraction, intelligent speed assistance and data recorder) as standard vehicle equipment and establishing, for the first time, mandatory EU-wide cybersecurity requirements for vehicles. The new General Safety Regulation establishes final phase-in dates for new type approvals that range from 6 July 2022 to 7 January 2026.

Also, applicable regulatory acts may include specific requirements for electric vehicles.

Manufacturers are generally responsible for ensuring compliance with the type-approval process and conformity of production of vehicles and their parts, regardless of whether the manufacturer is directly involved in all stages of construction. In addition, manufacturer's representatives, importers and distributors also have certain responsibilities under Regulation (EU) 2018/858.

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Regulation (EU) 2018/858 also contains provisions on market surveillance of vehicles and their parts already placed on the market and specifies, among other things, the rights and obligations of the national market surveillance authorities or the European Commission as well as the responsibilities of the economic operators in the supply chain.

Development, manufacture and supply

3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

The automotive companies' supply is usually organised in the form of a purchase order business with a contract structure that is typically implemented by automotive original equipment manufacturers (OEMs) and similarly flows down the supply chain (ie, by Tier 1 suppliers to Tier 2 suppliers and so on). This contract structure is characterised by a stepwise increase and concretisation of supply obligations. There are generally only limited purchase obligations as the automotive business is traditionally very much a customer demand-driven business, though this eventually depends on the contractual arrangements. For example, obligations to purchase a certain share of demand, which is typically forecast, are quite common. However, recent developments resulting in increasing pressure on supply chains have significantly strengthened the negotiation power of suppliers of critical raw materials and components. In certain areas, automotive customers have thus been more and more forced to commit to mid- or long-term purchase obligations (eg, 'take or pay') and other supplier-dictated terms that would not have been accepted in past times.

The traditional stepwise structure may typically begin with a non-binding tender or offer, followed by a formal or informal supplier validation and nomination of certain components for specified vehicle platforms or ranges. The nomination or admission letter may include an initial development phase for the supplier to adapt to the customer's requirements and specifications, and ultimately aims to establish a supply relationship that lasts until the end of the series production of the relevant vehicle range. Within the framework of the nomination more specific purchase agreements are then concluded, which set out prices as well as volumes linked to demand – the latter usually being specified as the supplier's expected percentage share in the customer's overall demand within a given production period (eg, annually). Finally, the actual delivery of definite volumes is based on forecasts and short-range purchase orders that often provide for just-in-time delivery.

Usually, no comprehensive written framework agreements with negotiated legal terms are in place, but rather supply relationships are largely based on the application of the OEM's or higher-tier supplier's general purchasing terms. These terms, especially those of German OEMs, are to a large extent (ie, with only minor deviations) based on the general purchasing terms of the German Association of the Automotive Industry. OEMs usually have rather extensive additional standardised contractual documents in place, such as a warranty, quality assurance, logistics and other side agreements. More detailed individual agreements are concluded, though, where the supply relationship includes joint development efforts or otherwise is of particular strategic importance (eg, joint ventures and cooperations, in particular regarding strategically important technologies such as autonomous, connected, electric and shared vehicles).

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With new entrants such as technology companies coming into the automotive market, concluding strategic cooperations has become a trend in the automotive industry. Also, traditional automotive rules are currently being challenged and redefined. For example, an obligation to supply spare parts for 15 years is something that technology companies can hardly accept.

Recent developments such as the covid-19 pandemic and international political instabilities have significantly increased the pressure on global supply chains and raised sensitivities about security of supply regarding critical raw materials and components, most notably in the automotive industry relating to semiconductors and scarce raw materials required for high-voltage batteries for electric vehicles. Particularly, the covid-19 pandemic and related lockdown and ramp-up issues as well as the recent semiconductor shortage crisis resulted in automotive production downtimes and major disruptions of supply chains also in Germany, and – at least temporarily – decline in vehicle sales. This immediately raised contractual issues for OEMs and suppliers regarding the extent of binding purchase and supply obligations under existing contracts as well as questions of force majeure and hardship. The experience of recent disruptions are driving OEMs to strategically adjust their supply chain arrangements, with a tendency to increase their direct arrangements with suppliers further down the supply chain (Tier 2, Tier 3 and so on) to be able to better control and manage security of supply issues. As such, new structures may interfere with the traditional concept of flowing down rights and obligations along the supply chain, the implementation regularly triggers new contractual and commercial aspects.

Distribution

4 | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

The marketing of new vehicles usually takes place through a two-level distribution system. On the first level, the OEM (or its national importer) establishes a network of authorised dealers that – on the second level – market and sell the vehicles in their own name and for their own account to end customers. Recently, several OEMs have moved from a two-level dealership model to a (genuine or non-genuine) agency concept, with agents engaging in customer-facing marketing activities and brokering sales on behalf of the OEM. Alternatively, some OEMs have set up a three-level structure with an additional intermediary acting on the third level towards end customers, usually in the form of an agency model. The contractual arrangements within the distribution chain vary (eg, regarding exclusivity, non-compete obligations, marketing obligations and branding requirements) and to that effect the degree of integration of the intermediaries in the OEM's distribution system also vary.

Alternatively, or in addition to the above, some OEMs maintain a network of own-retail branches that sell directly to end customers without involving any third-party distribution intermediary. In other cases, it is common for OEMs to reserve the right to make direct sales to high-volume or special customers, such as fleet customers. As a general trend, direct end-customer relationships are becoming increasingly important for OEMs, in particular in the provision of connectivity and mobility services to end customers as well as offering vehicles via direct online sales. Simultaneously with focusing on direct online sales, some OEMs

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are developing new showroom concepts to offer point-of-sale customer experience (with showrooms either operated by the OEMs themselves or by third-party operators). Several OEMs have increasingly also started trialling or rolling out new innovative subscription models that aim to respond to evolving customer demands in terms of flexible and hassle-free full-service mobility offers. As a basic concept of such models, the customer pays a flat rate subscription fee and is provided with a car, similar to a longer-term rental contract, but in addition is offered a range of car-related services as well as the option to change car models at frequent intervals or on demand.

Under German contract and distribution law, some special rules and principles may apply to distribution relationships, with certain particularities in the automotive industry. Some of these rules are mandatory (ie, they cannot be deviated from by contractual arrangement). The rules and principles are largely based on case law, and there are many court decisions that deal with and specifically take into account the customary distribution structures and other particularities in the automotive industry. The most important examples of special rules under German contract and distribution law are as follows.

- Mandatory minimum notice periods usually apply where the principal intends to terminate a distributorship. The length of the notice period depends on the circumstances of the specific case, taking into account, among other things, the distributor's economic dependency on the terminated business, the duration of the distribution agreement, the extent of exclusivity, the extent of investments made by the distributor and the existence of non-competition obligations. Minimum notice periods in the range of six to 12 months are not uncommon – for automotive distribution relationships the courts have even applied minimum notice periods of up to two years.
- The distributor can usually claim an indemnity 'for loss of clientele' upon termination of the distribution relationship. The exact calculation of the indemnity is rather complex and requires a detailed analysis of various criteria. As a matter of principle, the indemnity amounts to the value of the benefits that the principal after the termination continues to derive from the business developed by the distributor. The maximum indemnity is the amount calculated from the distributor's average annual net margin with the relevant products over the past five years.
- Standard contract terms (such as model distribution agreements of OEMs) that are not individually negotiated by the parties are subject to judicial control according to the German law rules on standard terms (AGB-Recht). Under these rules, standard contract terms are unenforceable if they are considered to result in an unreasonable disadvantage to the other party. The requirements to meet this reasonableness test have been specified by case law for different types of contract clauses. Rather strict requirements apply, for example, for limitation of liability and warranty clauses.

Mergers, acquisitions and joint ventures

- 5** | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

Since the suspension of the obligation to file for insolvency proceedings that applied during the covid-19 pandemic legislation is no longer applicable, we are recording an increase in

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the number of insolvencies of automotive suppliers. Increased energy costs and rising inflation have reinforced this trend. Thus, distressed M&A is currently gaining in importance.

Overall, there are no major differences between automotive M&A transactions in Germany and elsewhere in Europe.

There are, however, key features that warrant attention during the due diligence process and the negotiation of the transaction documents. Depending on the relevant business, areas that should be carefully reviewed include environmental issues, sanctions, product liability (including insurance coverage), intellectual property rights regulatory (including compliance with emission standards) and, in light of global supply bottlenecks due to the covid-19 pandemic, the situation in the Ukraine and the general shortage of semiconductors, alternative sourcing and the reliability of customer and supplier relations. Purchasers will regularly seek protection against risks in these sensitive areas through adequate representations and warranties and indemnities. Warranty and indemnity insurance is becoming increasingly popular in Germany and is often taken out when the sellers are private equity firms or private individuals.

Furthermore, under German foreign direct investment law, the competent ministry may object – even after closing – to an acquisition of 25 per cent or more of a German entity by a non-EU/EFTA acquirer if the public order or security of Germany or another member state of the European Union is likely to be impaired by the transaction – depending on the business of the target this may already be triggered by the acquisition of 10 per cent or more of the German target. Even stricter rules may apply where the products sold by the target company are also used in more sensitive industries such as defence.

While there used to be an assumption that this only applies to key industries (eg, infrastructure, energy, defence and certain IT security functions) and this objection right was rarely exercised, the German government tends to take a broader view these days – especially in the case of Chinese acquirers. It is possible to apply for a non-objection certificate, which is deemed to be granted if no official investigation is initiated within two months of receipt of the application. The receipt of the certificate is regularly included as a closing condition in the sale and purchase agreement in critical transactions.

Furthermore, the competitive environment for OEMs and suppliers has changed substantially. Nowadays, technology companies increasingly qualify as competitors. This is particularly relevant in the context of non-compete clauses or permissible purchasers when a joint venture partner intends to exit the venture.

Incentives and barriers to entry

6 | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

There are no special incentives for investment in the automotive market in Germany. There are rather indirect general incentives for investment, in particular in the e-mobility sector. To reach the self-set target of 15 million electric vehicles on the road by 2030, Germany incentivises the purchase and use of electric vehicles particularly through the payment of

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individual purchase premiums (referred to as an environmental bonus, the federal share of which was doubled as part of the economic recovery programme due to the covid-19 crisis), the granting of individual tax advantages under the German Motor Vehicle Tax Act and the offer of free parking and special parking zones in many municipalities. In addition, specific measures have been adopted to promote the expansion of charging infrastructure in Germany. There are various funding programmes for the procurement and installation of publicly accessible charge points. In addition, a revision of the 38. Ordinance on the implementation of the Federal Immission Control Act (38. BImSchV) has opened up a new revenue stream for operators of public charge points to make the operation of public charge points more lucrative. Since 1 January 2022, charge point operators can sell the greenhouse gas reduction quota (GHG quota) – namely, the CO₂ savings associated with the supply of electricity from their charge points – to fuel suppliers, who in turn can fulfil their stringent greenhouse gas emission reduction obligations with the GHG quotas.

Likewise, there are no special barriers to entry into the automotive market in Germany. Instead, there are established rules such as special terms and conditions and certain common practices developed by traditional automotive players, which generally apply to the automotive market when companies that are new to the industry enter the automotive market and deal with automotive companies in Germany.

At the same time, new entrants into the automotive market challenge established rules and common practices by applying new or at least redefined rules and practices in a situation where mostly technology-driven disruptions take place in a rapidly changing automotive world.

PRODUCT SAFETY AND LIABILITY

Safety and environmental

- 7** | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

Product compliance safety

Under German law, general product safety aspects are primarily governed by the recently revised German Product Safety Act (ProdSG) and the newly passed German Systems Subject to Monitoring Act (ÜAnlG). The ProdSG implements the EU General Product Safety Directive 2001/95/EC (GPSD). However, while the GPSD only applies to consumer products (eg, passenger cars but generally not to B2B supply parts exclusively intended for the production of passenger cars by professional car manufacturers), the ProdSG applies to both consumer and non-consumer products.

Environmental aspects are primarily in the line with EU type-approval requirements. As of 1 September 2020, the (previous) Type-Approval Framework Directive 2007/46/EC was replaced by the (new) Type-Approval Framework Regulation (EU) 2018/858. There are several special type-approval exhaust emissions provisions such as Regulation (EC)

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715/2007 and Regulation (EC) 661/2009. In Germany, type-approval requirements are codified in the EG-FGV.

There are additional market surveillance provisions codified in the (new) Market Surveillance Regulation (EU) 2019/1020.

Regarding enforcement in Germany, the competent market surveillance and product safety authority for motor vehicles and motor vehicle parts (including B2B supply parts) is the German Federal Motor Transport Authority (KBA). In addition, the KBA is the competent type-approval authority. The KBA's headquarters is based in Flensburg. It is a federal authority that is generally controlled by the German Federal Ministry for Digital and Transport. The KBA is structured into several departments with individual subject groups. Regarding product safety, subject group number 512 'Product Safety' in department number 5 'Market Surveillance' is generally in charge. As the competent enforcement authority in Germany, the KBA has issued an official codex on the implementation and interpretation of the ProdSG as well as certain corrective actions aspects (the KBA Codex). In doing so, the KBA's initial codex of November 2011 is under constant revision, and it was replaced and updated in September 2019, June 2020 and August 2021. With its codex, the KBA's intention is to provide car manufacturers and suppliers with additional guidance on certain product safety aspects, particularly on the KBA's expectations towards automotive companies. Moreover, the KBA codex outlines the KBA's approach towards certain product safety issues including best practices and internal procedures.

Regarding the enforcement of the European Union's Rapid Exchange of Information System (RAPEX) for unsafe products, the competent German RAPEX contact point authority is the German Federal Institute for Occupational Safety and Health (BAuA). The BAuA's headquarters is in Dortmund, with branches in Berlin, Dresden and Chemnitz. It is a federal governmental research institution controlled by the German Federal Ministry of Labour and Social Affairs.

One of the most important features is the implementation and enforcement of the notification obligation. In Germany, product safety notification aspects are generally in line with EU requirements, particularly with the GPSD. Section 6, paragraph 4 ProdSG implements the European authority notification obligation of article 5, paragraph 3 GPSD into German law. Accordingly, the producer of a consumer product 'shall immediately inform' the KBA if it 'knows or ought to know' that the consumer product 'poses risks to the consumer that are incompatible with the general safety requirement'. Besides, article 14 of the (new) Type-Approval Framework Regulation (EU) 2018/858 also requires certain product safety or product conformity and compliance authority notification obligation. In particular, pursuant to article 14(1), a manufacturer 'shall immediately inform the approval authority that granted the type-approval in detail of the non-conformity and of any measures taken'. Pursuant to article 14(2), where 'the vehicle, system, component, separate technical unit, part or equipment presents a serious risk, the manufacturer shall immediately provide to the approval authorities and market surveillance authorities detailed information on the risk and on any measures taken in relation thereto'.

The KBA decides on a case-by-case basis whether and what kinds of notifications or corrective actions are necessary and reasonable. In doing so, the KBA generally drafts a product safety risk assessment, often pursuant to the RAPEX risk assessment guidelines

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in Commission Implementing Decision (EU) 2019/417 (repealing Commission Decision 2010/15/EU), to assess potential product safety risks.

If deemed necessary due to the result of the risk assessment, the KBA has the power to order a corrective action (eg, a withdrawal or recall as well as certain publications). However, depending on the respective case, the KBA often trusts the car manufacturer or supplier to voluntarily carry out a suitable corrective action. In doing so, the KBA often refrains from issuing a formal order but closely monitors the case, particularly by asking for update reports. However, there is a recent trend that indicates that the KBA is now taking a stricter view (ie, that the KBA is increasingly relying on formal recall orders instead of a company's voluntary actions). This trend significantly increases a company's legal risks in the event of a product crisis.

As a general rule, companies should consider a proactive and cooperative approach when it comes to the German authorities. Proactively approaching and properly cooperating with the authorities is often crucial in solving a product crisis and reducing potential legal risks.

Environmental regulations

Many environmental regulations are harmonised at EU level, but enforcement of such EU environmental regulations is generally done on a national level. As a general rule, non-compliance with environmental regulations in Germany will mainly entail withdrawal of relevant licences, mandatory corrective measures and administrative fines, though there may be specific, and even criminal, sanctions depending on the subject matter.

See the following examples for important automotive-related environmental regulations and, if applicable, their German implementation.

Emissions

Regulation (EC) 715/2007 on type approval of motor vehicles concerning emissions from light passenger and commercial vehicles (Euro 5 and Euro 6) and its implementing Regulation (EU) 2017/1151 establish common technical requirements for the type approval of light passenger and commercial vehicles with regard to their emissions and set out specific emissions limits. Potential sanctions for non-compliance in Germany include, for example, administrative fines, withdrawal of type approval, prohibitions on putting the relevant vehicles on the market and ordering of other appropriate measures (such as recalls). Since 1 September 2020, Regulation (EU) 2018/858 also entitles the European Commission under certain circumstances to initiate EU-wide enforcement and remedial actions in addition to the foreseen competences of the enforcement authorities of the member states.

On 10 November 2022, the European Commission presented a proposal for a regulation on type approval of motor vehicles and engines and of systems, components and separate technical units intended for such vehicles, concerning emissions and battery durability (Euro 7). The proposed Euro 7 regulation replaces Regulation (EC) 715/2007 and Regulation (EC) 595/2009 and establishes, for the first time, common emission requirements for the type approval of cars, vans, lorries and buses under a single set of rules. The new rules are fuel and technology neutral, hence . This means the same emission limits apply to all

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vehicles of the same category regardless of engine type (eg, internal combustion engine or hybrid) and fuel (eg, diesel or gasoline). Further key points of the proposal include:

- stricter emission limits for lorries and buses, and application of the lowest existing limits for cars and vans for all fuel types;
- new specific emission limits for previously unregulated pollutants such as nitrous oxide from heavy-duty vehicles and new requirements for emissions from brakes and tires;
- an extension of the boundaries of Real Driving Emissions testing conditions; and
- extended durability requirements.

European lawmakers are currently in the process of passing legislation that will prohibit new internal combustion engine vehicles after 2035 (presumably with an exception for e-fuels).

Carbon dioxide

Regulation (EU) 2019/631, setting carbon dioxide emission performance standards for new passenger cars and new light commercial vehicles and repealing Regulations (EC) 443/2009 and (EU) 510/2011 as part of the European Union's integrated approach to reduce carbon dioxide emissions, establishes mandatory carbon dioxide emissions targets for new vehicles. These targets do not apply to individual vehicle models or manufacturers but relate to the entire European fleet average. It is not necessary for each individual manufacturer to comply with the European fleet value. However, each individual manufacturer is allocated a manufacturer-specific value depending on the products it sells. If a manufacturer's average emissions levels are above this value, the manufacturer will have to pay an excess emissions premium. The penalty is €95 for each gram per kilometre of exceedance. Starting with registrations in 2021, manufacturers also need to report to the Commission real-world carbon dioxide emissions and fuel or energy consumption of passenger cars, collected by on-board fuel and energy consumption monitoring devices.

On 8 June 2022, the European Parliament adopted an amendment to Regulation (EU) 2019/631 based on a proposal from the European Commission. According to the amendment, from 1 January 2035, a new EU fleet-wide carbon dioxide emissions target will apply for new passenger cars and light commercial vehicles equal to a 100 per cent reduction of the target in 2021.

These provisions are supplemented by Implementing Regulation (EU) 2021/392. This Regulation sets out detailed rules on the procedures for the monitoring and reporting of data relating to carbon dioxide emissions from new passenger cars and light commercial vehicles, as well as of data on real world carbon dioxide emissions and fuel or energy consumption of those vehicles.

For heavy-duty vehicles, carbon dioxide emission performance standards are provided for by Regulation (EU) 2019/1242. On 14 February 2023, the European Commission adopted a proposal for an amendment of the Regulation.

Waste

Directive 2000/53/EC on end-of-life vehicles, which is implemented into German law by the End-of-Life Vehicle Ordinance, lays down measures that aim, as a first priority, to prevent

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waste from vehicles. In addition, they aim at promoting the reuse, recycling and other forms of recovery of end-of-life vehicles and their components to reduce the disposal of waste, as well as at the improvement in the environmental performance of all economic operators involved in the life cycle of vehicles and especially the operators directly involved in the treatment of end-of-life vehicles. The End-of-Life Vehicle Ordinance provides for administrative fines in the event of non-compliance with certain obligations.

In addition, Directive 2005/64/EC on the type approval of motor vehicles concerning their reusability, recyclability and recoverability lays down administrative and technical provisions for the type approval of cars and vans with a view to ensuring that their component parts and materials can be reused, recycled and recovered in a specific minimum percentage.

The European Commission is currently working on a proposal for a revision of Directives 2000/53/EC and 2005/64/EC.

Product liability and recall

- 8** | Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

Under German law, there are numerous provisions that generally allow product liability claims, particularly claims under contract or warranty, general tort law as well as strict product liability law.

Most consumer claims in the automotive industry are brought under the strict liability regime of the German Product Liability Act (ProdHaftG), implementing the European Product Liability Directive 85/374/EEC. Accordingly, a 'producer shall be liable for damages caused by a defect in his product', and a product is generally defective 'when it does not provide the safety that a person is entitled to expect'. This test generally takes into account 'all circumstances', particularly 'the presentation of the product, the use to which it could reasonably be expected that the product would be put and the time when the product was put into circulation'. Potential defects can be linked to design, production and instruction aspects as well as certain product monitoring shortcomings. However, the burden of proof for the (alleged) defect, the damage and the causal relationship between defect and damage is generally upon the claimant. Besides, a producer's liability is limited to €85 million per case (pursuant to section 10 ProdHaftG).

There is a great deal of automotive product liability case law in Germany. Many courts, including the German Federal Court of Justice, have ruled on alleged vehicle defects. In doing so, German courts decide cases by appointing independent technical court experts to assess whether a vehicle – design, production and instruction alike – has a defect. The courts typically ask the technical expert to apply a state-of-the-art test (ie, taking into account the respective date when the vehicle was placed on the market).

In the event of a recall, there can be substantial follow-on litigation. To mitigate risks, it is crucial to take effective and sophisticated measures to prevent unnecessary risks (eg, by

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avoiding unnecessary acknowledgement or by creating an incorrect impression as to the scope and meaning of a recall).

Under German law, there is generally no class action system regarding consumer litigation in automotive product liability cases. Hence, lawsuits must be brought individually before the respective courts.

However, in 2018, a collective redress system – called *Verbandsklage* – was established to strengthen consumer protection rights. This collective redress system allows certain consumer protection associations to file collective redress lawsuits against automakers, suppliers, dealers and so on. As a result, individual consumers will be able to approach automotive companies based on the outcome of the collective redress lawsuit. Therefore, automotive companies should consider implementing proper defence mechanisms.

European lawmakers are currently discussing new product liability legislation, specifically a potential new product liability directive and a new artificial intelligence product liability directive.

DISPUTES

Competition enforcement

9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

Notably, in the past few years the European Commission has investigated a number of car parts cartels and heavily fined original equipment manufacturers (OEM) suppliers located all over the world for anticompetitive practices, such as price fixing, bid rigging and the exchange of competitively sensitive information. These illegal practices concerned very different components, such as alternators and starters, wire harnesses, parking heaters and automotive bearings. In addition, in July 2016, the Commission imposed fines of €2.93 billion on five European truck manufacturers for coordinating prices. This is the highest cartel fine the Commission has imposed so far. According to the findings of the Commission, the truck cartel existed for 14 years and was partly organised through the truck manufacturers' German subsidiaries.

In 2018, the Commission opened an investigation to assess whether German car manufacturers agreed not to compete against each other on the development and roll-out of technology to clean the emissions of petrol and diesel passenger cars. This case was concluded in 2021 with a decision in which the Commission found that the German OEMs breached EU antitrust rules by colluding on technical development in nitrogen oxide cleaning. The Commission has imposed a total fine for the five OEMs of €875 million.

In parallel to the European Commission cases, the Federal Cartel Office (FCO) has conducted several investigations in the automotive sector over the past few years. For example, in June and December 2015, the FCO sanctioned six automotive part manufacturers for agreeing to

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fix prices in relation to acoustically effective components (ie, textiles such as flooring and car mats). The manufacturers were fined a total of €90 million.

In 2015, the FCO initiated proceedings against three car manufacturers for restricting cooperation between brand retailers and independent online agencies. The manufacturers had implemented 'internet standards' for the introduction of end customers to brand retailers via internet-based new car portals. The FCO found that such standards reduced cooperation between retailers and car portals and therefore restricted competition by reducing market transparency. The proceedings of the FCO were discontinued in December 2015 after the car manufacturers revised their clauses.

In November 2019, the FCO imposed fines totalling around €100 million on German car manufacturers for exchanging information with steel manufacturers, forging companies and Tier 1 suppliers on surcharges for the purchase of long steel products.

The cartel decisions of the European Commission and the FCO have led to several follow-on damages actions before the German courts. Germany is generally regarded as one of the major forums within the European Union for competition law damages claims. Implementation of the EU Cartel Damages Directive 2014/104 through an amendment of the German Act against Restraints on Competition (ARC) in June 2017 further boosted private enforcement, for example, through collective claims brought against cartelists in Germany. The recent cartel damage claims against truck manufacturers are mainly carried on by professional claim funding companies and US class action law firms (which have established offices in Germany).

In January 2021, the last amendment of the ARC entered into force. Implementing the ECN Plus Directive 2019/1, the German legislator enshrined an antitrust compliance defence in German law, making effective compliance efforts both before and after the infringement relevant to the assessment of a cartel fine. Companies with effective antitrust compliance systems for the prevention and detection of cartel infringements, as well as those that contribute to the detection of a cartel infringement as leniency applicants, can in the future be rewarded to a greater extent when fines are imposed, while companies that do not (immediately) opt for such contribution can now be forced to cooperate in the investigations. When reviewing their dawn raid procedures and antitrust compliance systems, companies should therefore pay increased attention to ensuring that these comply with the new investigative powers and the new requirements for appropriate and effective compliance precautions.

Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

Apart from disputes concerning antitrust, insolvency and intellectual property matters, disputes in the automotive industry arise regularly along the supply chain.

The most frequent disputes between customers and the supplier include the following.

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- Claims for damages based on defects of the product developed and delivered by the supplier (section 434 et seq of the German Civil Code): these also include product liability claims when defects of the product affect the safe usage of the delivered product. These disputes are either settled at an early stage with a view to the strength of the business relationship or, failing that, are brought to court, less often to arbitration. As they are often decided by technical questions, some cases are settled by the parties based on the result of an independent expert opinion or an independent procedure of taking evidence performed by the court.
- Supply chain disruption cases where a supplier threatens to or actually implements a supply stop: these kinds of disputes have become more frequent in German courts in recent years. In times of complex supply chains, just-in-time or just-in-sequence production and single sourcing, customers in the automotive industry are highly dependent on on-time-delivery of parts. Even a short period of disruption of the supply chain can cause severe damage. While formerly an exception, German courts increasingly accept the need to act quickly in order to prevent significant damage that otherwise could often not be reclaimed by suppliers. Thus, in urgent cases it is possible to file for interim injunctions requesting continuation of the supply under the contractual terms. Straightforward cases are sometimes decided by the courts *ex parte* in a matter of days after the filing. In more complex cases a hearing of the defendant is sometimes necessary, and a decision can take up to a few weeks. In this context, the impact of cost increases or scarcity of semiconductors or rare earth materials on the automotive industry and the supply chains in particular is relevant where judges will have their own views developed in their reception of the issues from the media under force majeure or frustration aspects. The majority of cases arising out of covid-19 or the semiconductor shortage have so far been handled through out-of-court solutions. On cost increase cases, we are seeing more court activities in recent months and will see how that develops further.
- Disputes in connection with the termination of the supply contract: disputes often arise in scenarios where a customer wants to discontinue the business relationship with its supplier and switch production to a new supplier. This can now more imminently be driven by concerns of viability of business cases of suppliers in times of high interest rates, increasing costs and in particular increasing costs of labour, while the business case of the supplier requires high investment into new technology and shift towards electric cars and automated digitalised cars. When customers do not trust in the efforts of their suppliers and in the sustainability of their business models, they might consider changing horses. Deriving disputes centre on the term of the contract, termination rights, IP rights and duties to compensate the supplier for frustrated investments. In this context, the customer sometimes switches to a new source for the supply of the product. The former source sometimes regards its IP rights or trade secrets violated by the production or development of the alternate product. The Trade Secrets Directive of the European Union, which was implemented into German statutory law in April 2019, provides for some guidance in this context. Other disputes relate to the transfer of tools from the former to the new supplier. The punctual transfer of tools to a new supplier is often crucial for a smooth transition. Delays can cause severe damage for the customer. In urgent cases, these disputes can be resolved in interim proceedings seeking repossession of tooling.
- OEMs and suppliers still recognise the effects of the squeeze on semiconductor supplies since 2021. Disputes in this context focus in particular on the question of whether an allocation is permissible at all and, if so, how it is appropriately executed. Anticipating the

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uptake of OEM production in 2021, the German Association of the Automotive Industry issued a best practice guideline to provide for guidance on allocation of limited supplies among customer demands. This guideline is a recommendation and can be deviated from: it is not a binding law and does not specifically say to which circumstances it applies. Therefore, parties argue their cases based on the terms of their individual agreements on force majeure, inability to supply and default. It will have to be seen whether any of these cases go to court. The semiconductor shortage is expected to ease in 2023. However, semiconductors and processors are increasingly becoming the core of an automobile as was the engine for the past decades. This development, combined with the interest of semiconductor manufacturers in improving their business model and evolving from a parts manufacturer to a sharer of the revenues from the automobile itself, could lead to further allocation problems in the future. Also, considering the rise of alternative driving systems and the focus on sustainability, the scarcity of certain raw materials and products, such as batteries, is expected to continue to be a cause for disputes along the value chain.

- A current source of disputes is the conflict on price increase requests. Covid-19, semiconductor shortages and Russia's war on Ukraine have led to price increases in certain areas, such as energy, and thus ultimately to rising production costs. The statutory law, however, provides for an adjustment of agreed prices during the term of a contract only upon the fulfilment of a narrow set of preconditions following the legal principle of 'frustration of contract'. This has been confirmed by recent case law of German courts taking the latest crisis into account. Several precedents have been decided in recent months that support the view that where a good cause for a supply right for customers exists, they can obtain injunctive relief where suppliers do not fully comply with negotiation requirements under the frustration of contract concept and resort to supply stop threats. In such cases, injunctions have been granted on short notice to require suppliers to continue supplies at the agreed prices urging them to return to the negotiation table while supplies are re-established and therefore continue. In view of the combustion engine phase-out and the resulting consolidation of the market, it can be assumed that extraordinary price increase requests will continue to keep procurement and legal departments busy.

Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

From a customer's point of view, there may be early warning signs of the distress of a supplier, such as the supplier's request to shorten the term of payment, increase the prices or from case to case, or a deterioration of the quality standard. If it is not possible to transfer the supply relationship to a second source, the customer of a distressed supplier may effectively be forced to renegotiate the relevant supply contracts in order (at least temporarily) to ensure continuous supply. In this case, the customer should ask for a guarantee or comfort letter issued by the supplier's parent company to limit the risk of non-performance. It should be kept in mind that actions of the distressed contracting party (ie, renegotiating existing supply contracts or the performance of contractual duties under the supply contract) could be subject to clawback in a subsequent insolvency. The customer should seek legal advice to mitigate these risks.

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If the supplier is no longer able to pay its debts as they fall due or the entity is over-indebted in the terms of the German Insolvency Code, the company's management must file for the opening of insolvency proceedings without undue delay (if promising restructuring attempts are undertaken by the management at the latest within three weeks in the case of illiquidity or within six weeks in the case of over-indebtedness). The local insolvency court will then institute preliminary insolvency proceedings and usually appoint a preliminary insolvency administrator. During the preliminary insolvency proceedings, which last for about three months, the company's business operations are typically continued. To facilitate that, the employees' wages are paid by the employment agency (insolvency pay). During the preliminary proceedings, any business correspondence should be addressed to both the company's management and the preliminary insolvency administrator. It should be carefully reviewed whether payments must be made to an escrow account set up by the preliminary insolvency administrator and whether the court has ordered additional measures aimed at the protection of the insolvency estate. As regards existing contractual relationships, the preliminary insolvency administrator may ask customers for payments in advance or other (financial) support to fund the business continuation. In this case, it will be crucial to find a way to safeguard such payments.

After the preliminary insolvency proceedings, the court will open (final) insolvency proceedings and appoint a (final) insolvency administrator. At this point, the power of disposal transfers from the company's management to the insolvency administrator, whose administration must always focus on what is best for the company's creditors. Generally speaking, the insolvency administrator has the possibility to continue the company's business and (later) restructure it by way of an insolvency plan or sell it to an investor (by way of an asset deal) or liquidate the company. If the company is liquidated, the customer will have to transfer its business to a second source or – if that is not possible – think about acquiring the debtor's business itself. If selling the debtor's business to an investor is the most promising option from the insolvency administrator's point of view, the insolvency administrator will usually start a formal bidding process. Potential investors may then place offers for the assets they are interested in. The debtor's business or a part thereof is transferred by way of an asset deal, and according to German employment law the relevant employees (including the existing employment contracts) will be transferred to the investor. However, the insolvency administrator has (limited) possibilities to influence how many and which employees will be transferred to the investor. In the case of a sale of the debtor's business to an investor via asset deal, existing supply agreements do not automatically transfer to the investor, which means suppliers and the investor need to agree on the transfer of the existing supply agreement to the investor or negotiate a new supply agreement.

The company's management may also apply for debtor-in-possession proceedings. In that case, a (preliminary) supervising trustee will be appointed by the court instead of the (preliminary) insolvency administrator. The main difference between regular insolvency proceedings and debtor-in-possession proceedings is that the power of disposal remains with the company's management after the opening of insolvency proceedings. Debtor-in-possession proceedings also aim at the best possible satisfaction of the company's creditors, thus the management is also bound by this maxim.

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Intellectual property disputes

12 | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

For most car manufacturers and auto suppliers, Germany is a main venue of choice to enforce their IP rights against any type of infringement. The experience, reliability and efficiency of German IP courts are among the main reasons for this preference. Another reason is the rather broad scope of protection that German IP courts attach to all relevant IP rights at stake, be it patents, trademarks or designs. As a result, the amount of case law is high and constantly growing.

In the field of patents, plaintiffs appreciate that German patent judges are happy to handle difficult technical subject matters without needing a court expert. Plaintiffs like that infringement proceedings are fast (eg, injunctions available in the Mannheim and Munich courts in less than a year) and relatively inexpensive owing to procedural efficiency. Two sorts of disputes are particularly common. First, many automotive suppliers take cases against their competitors to the German courts. The German courts have recently dealt with cases regarding a large variety of components, including, for example, crankshaft bearings, turbo chargers, brake systems, brake pads, airbags, tyre repair kits, structural reinforcement, electrical connectors, ventilation, seats, air filters, side-impact protection, fuel feed valves, windshield wipers, engine immobilisers, driver assistance systems and mudguards. Second, there is an increasing number of attacks by patent owners from outside the traditional automotive industry, including non-practising entities (NPEs), against the car industry. The majority of these cases relate to standard-essential patents for communication technology (eg, 3G, 4G and WiFi) implemented in the car. We expect this second category of cases to continue in the future parallel to the implementation of new standard generations that are not fully licensed by the automotive industry.

Furthermore, the launching of the new Unified Patent Court (UPC) in June 2023 has the potential to further increase the number of patent litigation cases in the automotive industry. In particular, given that an injunction from the UPC will be valid in all of the 17 member states of the UPC, including Germany, France, Italy and the Netherlands, cases against automotive companies before the UPC may become worthwhile for NPEs or other patent owners from outside the traditional automotive industry, even in scenarios where they are not worth the costs and efforts before national courts (eg, cases against non-European OEMs that have no or only limited production facilities in Europe and less significant market shares on the key national markets in Europe).

So far, automotive-related litigation has been particularly agile in the area of design law where German courts used to take a very favourable view towards design owners, including designs for car parts. It remains to be seen whether that will remain the case after the full harmonisation of design law in the European Union has been completed – now excluding design protection for repair parts under certain circumstances in all EU countries.

In the field of trademark law, many cases deal with the misuse of car brands for maintenance services offered by third parties. German IP courts have forced unauthorised service providers to limit the use of the brand to a significant degree. Such service providers must

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not use the manufacturer's logo to advertise their offer. Rather, they are typically limited to the use of the car's word mark. This makes advertising for unauthorised maintenance service much harder.

Another area of significant trademark litigation refers to accessory products and merchandising articles – such as keyrings, mugs, shirts and many other items. German IP courts try to close possible gaps of trademark registrations for such unrelated goods.

One area where German IP courts are hesitant to protect design or trademark rights against unauthorised forms of use relates to scale model replicas of original cars. In this area, German IP courts have developed a long-standing exception to the successful enforcement of car brands and designs for the benefit of all those who like to collect cars – but cannot afford the original.

EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

The major sources of German employment law are federal laws, collective bargaining agreements, works council agreements and case law, the latter playing a key role. There is not one consolidated Labour Code; instead, minimum labour standards are laid down in separate laws on various labour-related issues. The legislation of the European Union as well as the jurisdiction of the European Court of Justice have increasingly affected German employment law in recent decades and will continue to do so.

Key provisions of German employment law that apply across all industries include:

- the statute provides minimum standards regarding, among other things, sick pay, annual leave and notice periods; and
- the German social security system provides mandatory insurance for employees in five areas: health, nursing care, unemployment, accidents at work and pensions. With the exception of company pension schemes, the provision of further social security benefits is unusual.

Employees working in operations with regularly more than 10 employees are protected against unfair dismissal after completion of a six-months period of employment. There is no statutory claim for severance pay for loss of employment; the amount of severance, if any, is subject to negotiation between the employer and the employee or, in the event of mass dismissals or similarly far-reaching operational changes, subject to a social plan concluded between the employer and the relevant works council (where applicable).

The current national minimum wage amounts to €12 gross per hour. It is to be increased from time to time, with the next increase expected with effect as of 1 January 2024.

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Given the need for flexibility and just-in-time production, on the one hand, and the strictness of German employment laws, on the other hand, the automotive industry often seeks to work with freelancers, companies providing work and services and external staff provided by temporary work agencies. By law, the hiring period for agency temps is restricted to a maximum of 18 months in principle. Collective bargaining agreements can provide for more flexibility in this regard, and the metal and electrical industry has made use of this option by extending the maximum hiring period to 48 months. For this extension to apply, the affected employee does not necessarily have to be a member of the trade union concluding the collective bargaining agreement, as the Federal Labour Court ruled in September 2022 in a case concerning the metal and electrical industry. Hiring companies that are not bound by collective bargaining agreements can, in principle, also adopt these collective bargaining rules by means of works council agreements. The collective bargaining agreements of the metal and electrical industry also stipulate premiums that automotive companies need to pay to agency temps to comply with equal pay legislation.

Although precise figures are not available, the collective bargaining agreements of the metal and electrical industry are relevant for many employees in the automotive industry. Compared to other German industries, the level of unionisation in the automotive industry is still fairly high. However, at large supplier companies and original equipment manufacturers (OEMs), the level of unionisation tends to be significantly higher than in small and medium-sized supplier companies where the relevant trade union of the metal and electrical industry (IG Metall) hardly plays a role. By law, the application of collective bargaining agreements usually requires that both parties to an employment contract are also members of the parties that concluded the collective bargaining agreements. But even employees who are not members of IG Metall often benefit from their employer's membership in the employers' association of the industry. This is because these companies often apply the industry's collective bargaining agreements regardless of the individual employee's trade union membership, namely by a contractual commitment to apply these agreements.

In the western states of Germany, the collective bargaining agreements of the industry provide for a regular weekly working time of 35 hours. Since 2018, employers can benefit from enhanced options to agree a weekly working time of 40 hours with individual employees. Conversely, full-time employees may under certain conditions reduce their weekly working time from the current 35 hours down to 28 hours for between six months and 24 months. Moreover, employees in particularly stressful private situations (eg, with family members in need of care) can opt for a release from work of up to eight days annually by converting their tariff supplement into free time. In the eastern states of Germany, the sectoral collective bargaining agreements still provide for the 38-hours working week to be the rule. As a result of tariff negotiations in 2021, however, employers may now negotiate with the works council at company level a gradual reduction of the working hours to 35 hours per week. As a consequence, a working week with less than 38 hours has been introduced in many operations since 2022.

Several of the industry's regional collective bargaining agreements provide for special protection against dismissal for older employees. In the southwest, for example, employees who are 53 or older can only be dismissed for a good cause provided they have been employed by the company for at least three years. Further specifics and exceptions from this special protection against dismissal differ from tariff district to tariff district.

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With a collective bargaining agreement reached in March 2021, IG Metall pushed through a 'transformation payment', a collectively agreed annual special payment. In 2022, this one-off payment amounted to 18.4 per cent of the employees' regular individual monthly pay. Initially, the 'transformation payment' was to increase to 27.6 per cent of the regular monthly pay in 2023; however, in 2022 it was agreed that the amount was to remain at 18.4 per cent, while other tariff allowances were increased in return.

In October 2022, the German legislator introduced the 'inflation compensation payment' allowing employers to make additional one-off payments to their employees of up to €3,000. Such payments are free of taxes and social security contributions if made until 31 December 2024. As a result of recent collective bargaining negotiations, employees were to receive an inflation compensation payment of up to €1,500 by 1 March 2023 at the latest if certain conditions were met. Another €1,500 is to be paid by 1 March 2024. Moreover, wage increases of 5.2 per cent as of June 2023 and a further 3.3 per cent as of May 2024 were agreed.

When it comes to employee representation at operational level, there is no legal obligation in Germany to establish a works council – even after the operation has reached a certain size. Rather, employees are entitled to establish a works council (provided that the operation has a minimum size of at least five employees over 18 years of age), but they may also choose not to. It is fair to say, though, that most companies in the industry, in particular OEMs and larger suppliers, do have works councils.

Where established, works councils have substantial co-determination rights regarding personnel, social and economic matters. In many instances, this means that the employer cannot introduce policies or implement material changes relevant to the workforce without the works council's prior consent or without having gone through litigation or arbitration procedures. In view of the continued growth of digitalisation and automation of the industry, the co-determination right concerning the introduction and application of technical equipment suitable to monitor employees' conduct and performance will become even more important than it is today. This topic is particularly susceptible to disputes, given the works councils' growing awareness for employee monitoring and privacy issues, especially after the entry into force of the General Data Protection Regulation.

Works council agreements providing for protection against dismissal are also quite common, in particular at large OEMs. Such agreements, which may, among other things, provide for a commitment not to close certain production sites or not to implement forced redundancies for a certain period of time, can significantly limit a company's ability to react to changing market conditions.

The covid-19-related obligation to work from home (where possible) expired on 19 March 2022. A general right to work from home has not been implemented by the German legislator yet. Although the coalition treaty of the current German government addresses this issue, no draft bill containing more details has been produced.

The automotive industry in Germany, like many other sectors, is currently struggling with a shortage of skilled professionals. Suggestions reach from offering improved working conditions to legislative reforms concerning taxation, childcare and the immigration system. It remains to be seen whether and which industry-relevant changes will be initiated.

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NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

The most important legal developments relating to automotive technological and mobility advances continue to evolve around autonomous driving, electric vehicles and connected and shared mobility solutions.

In the field of autonomous driving, technological advances and the industry landscape are rapidly evolving. This goes hand in hand with regulatory developments addressing the question of legality of operating autonomous vehicles (AVs) on public roads and setting out the appropriate technical requirements for AV technology. This challenge is currently being faced by legislators around the globe to ensure the safe (commercial) deployment of (SAE/ISO Level 4) AVs. We monitor a wide variety of legislative developments and initiatives currently taking place at international, EU and domestic German levels.

The Vienna Convention on Road Traffic of 1968 (the Vienna Convention), to which Germany is a signatory party, may authorise the use of AV technology, but may still require the presence of a human 'driver' who can take control of the vehicle at any time. In September 2020, the Global Forum for Road Traffic Safety (WP.1) voted for an amendment to the Vienna Convention that will facilitate the responsible use of automated driving systems (ADSs). A new article 34-bis provides that the driver requirement 'is deemed to be satisfied' while the vehicle is using an ADS that complies with domestic technical regulations (type-approval requirements) and domestic legislation on operation. The amendment entered into force in 2022 and signatory parties to the Vienna Convention may incorporate the amendment into their domestic legal road traffic framework. Since signatory parties can impose additional hurdles for the vehicles equipped with ADSs, the respective national approach to waiving the requirement of a driver may vary. WP.1 continues to work on these topics and has adopted a resolution on safety consideration for activities other than driving undertaken by drivers when automated driving systems issuing transition demands exercise dynamic control in 2022.

At the level of technical vehicle regulations, there are further ongoing work streams within the United Nations Economic Commission for Europe's (UNECE) World Forum for Harmonization of Vehicle Regulations (WP.29) focusing on adapting existing UNECE Regulations as well as on defining work priorities for WP.29 and indicating deliverables (eg, setting out the functional requirements), timelines and working arrangements for the safety and security of automated and autonomous vehicles. WP.29 has further extended UN Regulation No. 157 on Automated Lane Keeping Systems (ALKS) to cover higher speeds (up to 130 kilometres per hour) and automated lane changes.

While the UNECE regulator is still in the process of developing an approach to regulations for higher automation, the European Commission's Implementing Regulation (EU ADS Regulation) laying down rules for the application of Regulation (EU) 2019/2144 (new General Safety Regulation) as regards uniform procedures and technical specifications for the type approval of motor vehicles with regard to their automated driving system (ADS) has

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already entered into force and builds the basis for EU ADS type approval covering 'fully automated vehicles' (SAE/ISO Level 4). For the time being, the whole-vehicle type approval of ADS-equipped vehicles will be limited to small series type approval pursuant to the requirements of the new Commission Delegated Regulation (EU) 2022/2236 amending Regulation (EU) 2018/858, and certain use cases, until the necessary requirements for unlimited series type approval are established (the current target date is July 2024). Accordingly, the current developments of the European Union on the regulation of artificial intelligence and liability rules for artificial intelligence, as well as the recast of the Machinery Directive, should be observed; the relationship between these regulations is likely to raise some questions, especially in the area of automated and connected vehicles.

Germany adopted a new Act on Autonomous Driving in July 2021 amending the legal road traffic framework to allow 'autonomous driving functions' at SAE Level 4 to be used in regular operation in defined operating areas. Instead of a driver, the new role of a 'technical supervisor' who is a natural person responsible for ensuring compliance with road traffic law, has been introduced. The technical supervisor has a variety of obligations, such as being able to activate alternative driving manoeuvres or switch off the ADS and communicate with the passengers. Typical use cases under the new Act may include robot shuttles and people movers. The new legal road traffic framework is supplemented by an ordinance setting out the necessary requirements and approval procedures. We expect that the interrelation between German domestic laws and the EU type-approval requirements, once in force, will raise further legal questions. In December 2021, Germany was the first country to grant a type approval under UN Regulation No. 157 for an ALKS (Mercedes-Benz Drive Pilot). In December 2022, Mercedes was granted the first national approval under the Act on Autonomous Driving for its Automated Valet Parking (AVP) driving function and the Federal Motor Transport Authority released the first catalogue with technical requirements for autonomous vehicles in this context.

As for testing of automated driving functions and the overall concept of automated road traffic, German statutory provisions provide the legal basis for German authorities to grant specific exceptional permissions. On this basis, numerous tests and pilot projects (including regular passenger service with 'autonomous' shuttles) have been conducted on German roads in public traffic (eg, by Volkswagen, Audi, BMW, Daimler, Bosch, Continental, Delphi and ZF), as well as by a number of research institutes and organisations for several years. The testing options have been further harmonised and centralised by the Act on Autonomous Driving.

At the same time, the increased connectivity of vehicles has enabled the development and growth of new mobility solutions, particularly in the area of digital intermediation of rides and ridesharing services.

Recognising the increasing public demand for such services and their potential to contribute to a reduction of greenhouse gas emissions in the traffic sector, the German legislator is encouraging their adoption and integration in daily traffic. For instance, the German Passenger Transport Act provides for a specific legal basis for the authorisation of ride pooling services, which may become a central component of the future passenger transport in Germany.

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The increased automation and connectivity of vehicles has also led to new challenges. A major concern in this regard is the increased cyber threats to vehicles (eg, in the form of unauthorised remote access to in-vehicle data and the illegal modification of vehicle software over the air). Also, regular software updates to fix bugs, improve vehicle performance, add new features and protect against recently discovered vulnerabilities are becoming increasingly important in automated and connected vehicles. To address these challenges, two landmark UN regulations entered into force in January 2021:

- UN Regulation No. 155 on Cyber Security and Cyber Security Management Systems (CSMS), which requires OEMs, in particular, to establish and maintain a CSMS, including processes to identify and manage cybersecurity risks, such as supplier-related risks, during the whole vehicle life cycle (ie, development, production and post-production); and
- UN Regulation No. 156 on Software Updates and Software Updates Management Systems (SUMS), which requires OEMs, in particular, to establish and maintain a SUMS, including processes that ensure that software updates are executed safely, securely and verifiably during the whole vehicle lifecycle (ie, development, production and post-production).

The two regulations are implemented in the EU type-approval regime for the most relevant cases through the following steps:

- as of 6 July 2022, compliance with UN Regulation No. 155 and, where the manufacturer executes software updates that affect type-approved characteristics of vehicles after their registration, compliance with UN Regulation No. 156 is mandatory to obtain EU type approval; and
- as of 7 July 2024, compliance with UN Regulation No. 155 and, where the manufacturer executes software updates that affect type-approved characteristics of vehicles after their registration, UN Regulation No. 156 will also be mandatory for the registration the placing on the market and entry into service of new vehicles.

Finally, as more and more data are collected by vehicles, questions of data ownership, the legality of data collection and processing and the accessibility of vehicle data (eg, by actors in the supply chain and aftermarket, authorities and mobility service providers) are becoming increasingly important. In addition to data protection, competition and contract law aspects, particularly also regulatory requirements must be observed in this regard. For instance, in Germany, the Act on Autonomous Driving has introduced certain data processing requirements for vehicles with automated driving functions.

UPDATE AND TRENDS

Trends and new legislation

15 | Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

Throughout 2022 and 2023, emissions of motor vehicles have remained the focus of authorities and courts at a national and European level. The ruling of the European Court of

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Justice (ECJ) of December 2020, which provided for the first time an interpretation of relevant provisions regarding the admissibility or inadmissibility of defeat devices, is still of utmost importance. In its decision, the ECJ applied a rather broad interpretation of the term 'defeat device' and defined the scope of the exemptions to the general prohibition of defeat devices rather narrowly. On 14 July 2022, the ECJ rendered judgments on further questions of interpretation concerning, in particular, the legality of thermal windows. In this respect, the ECJ ruled, in essence, that a thermal window may generally only be justified under two strict conditions. First, it seems that both requirements under article 5(2)(a) of Regulation (EC) 715/2007 must be fulfilled (ie, the thermal window must be required for the protection of the engine against sudden and irreparable damage, and for the safe operation of the vehicle). In this respect, the ECJ reiterated that the (mere) clogging up and ageing of the engine are not sufficient reasons. In addition, no alternative technical solution to ensure the protection of the engine and the safe operation of the vehicle may have been available at the time of type approval. Second, the thermal window may not reduce the effectiveness of the emission control system for means of engine protection and the safe operation of the vehicle during most of the year based on its specific parameters. Since the rulings by the ECJ, the legality of thermal windows has increasingly become a focus of national EU authorities and courts. For example, on 20 February 2023, the German Administrative Court of Schleswig declared Federal Motor Transport Authority approvals for software updates for Volkswagen vehicles unlawful, among other things, as the software update would still contain thermal windows that the Higher Administrative Court of Schleswig-Holstein considers inadmissible in light of the requirements established by the ECJ. However, the judgment is not yet legally binding. It remains to be seen how this case and other similar cases will develop and how EU authorities and courts will deal with the open questions and legal uncertainties that remain after the ECJ rulings. This includes the question of what it means that a thermal window may not reduce the effectiveness of the emission control system 'during most of the year'.

On 21 March 2023, the ECJ decided that articles 18(1), 26(1) and 46 of Directive 2007/46/EC, read in conjunction with article 5(2) of Regulation (EC) 715/2007, must be interpreted as protecting, in addition to public interests, the specific interests of the individual purchaser of a motor vehicle vis-à-vis the manufacturer of that vehicle where that vehicle is equipped with a prohibited defeat device, within the meaning of the latter provision. In the absence of provisions of EU law governing the matter, it is for the law of the member state concerned to determine the rules of compensation for damage actually caused to the purchaser of a vehicle equipped with a prohibited defeat device, within the meaning of article 5(2) of Regulation (EC) 715/2007, provided that that compensation is adequate with respect to the damage suffered. It remains to be seen whether the German Federal Court of Justice will stick to its view that a claim can only exist if the manufacturer acted intentionally and immorally when installing an unlawful defeat device. Prior to the decision of the ECJ, the Federal Court of Justice had already announced that it would publish a clarifying decision setting out how it interprets the European regulations in the light of the decision of the ECJ. The next opportunity to comment on the ECJ decision is a hearing before the German Federal Court of Justice (BGH) in proceedings against Volkswagen. Due to their potential impact on emission litigation, the developments in the case law of the BGH and other national courts should be closely monitored.

Going forward, the automotive industry will be particularly impacted by the stepwise implementation of the goals of the European Green Deal, as part of which the European

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Commission has, among other things, presented a strategy for sustainable and smart mobility together with an action plan containing 82 initiatives.

Several legislative initiatives with relevance for the automotive industry stemming from these roadmaps are expected to progress further in 2023, after being delayed in the past year. These are, for example:

- the proposal of a new Battery Regulation that, among other things, foresees sustainable production, deployment and waste management requirements for electric vehicle batteries (repealing Directive 2006/66/EC);
- the planned revision of Regulation (EU) 2019/631 on CO₂ emission performance standards for new passenger cars and new light commercial vehicles;
- the proposal for the revision of Regulation (EU) 2019/1242 on CO₂ emission standards for new heavy-duty vehicles;
- the proposal for a regulation establishing stricter emissions standards (Euro 7) for all petrol and diesel cars, vans, lorries and buses;
- the planned revision of Directive 2000/53/EC on end-of-life vehicles and Directive 2005/64/EC on the type approval of motor vehicles concerning their reusability, recyclability and recoverability; and
- the planned revision of the Regulation on the Registration, Evaluation, Authorisation and Restriction of Chemicals (REACH).

Moreover, automotive supply chains will be subject to increasing scrutiny due to evolving due diligence and ESG requirements, such as the German Supply Chain Act, which was passed in 2021 and has been affecting companies since January 2023. Similarly, a proposal for a directive on corporate sustainability due diligence is currently being discussed at the European level. In this context, the developments concerning the proposal for an EU regulation establishing the framework for ensuring a secure and sustainable supply of critical raw materials should also be observed.

Despite these constantly evolving regulatory requirements and the challenges they pose, German and global automotive industries have set themselves the goal of redefining the mobility of the future. In addition to the development and commercialisation of electric vehicles, as well as the introduction of new concepts for shared mobility and connected vehicles, the automotive industry is continuously advancing the degree of automation of vehicles on the path to autonomous driving. In doing so, the automotive industry, subject to further technical, political and public challenges, still seems some steps ahead of the legislation. But the legislator may be catching up, particularly on an EU and German national level. Thus, it remains to be seen how the German and global automotive industry will manage to mitigate the legal risks associated with the constantly changing regulatory landscape and the introduction of innovative technologies and business models to the German and international markets.

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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

The Hungarian automotive industry is composed of four major car and motor factories and foreign and domestic-owned supplier companies. Opel and Suzuki started manufacturing

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their cars in Hungary in 1992 and soon after Audi set up a factory in Győr in 1994. In 2012, Mercedes-Benz opened a car manufacturing plant in Kecskemét, and in 2018 the construction of a new BMW automobile factory in Debrecen was announced. With more than 700 companies involved in the automotive industry, the sector has the greatest number of employees (150,000) and a manufacturing output of 9,300 trillion forint. The automotive industry contributes to 25 per cent of national exports and offers business opportunities to countless small and medium-sized enterprises and suppliers. Of the world's 100 largest automotive suppliers, 49 are present in Hungary, including Bosch, Continental, Knorr-Bremse and ZF.

In 2022, in parallel with the above, there were major announcements regarding e-mobility developments. For example, Contemporary Amperex Technology Co announced the investment of €7.34 billion to build a 100GWh battery plant in Debrecen. Once built, it is set to be Europe's largest plant making battery cells and modules for carmakers in its proximity, including Mercedes-Benz, BMW, Stellantis and Volkswagen.

COMMERCIAL OPERATIONS

Regulation

- 2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

Since 1 September 2020, [Regulation \(EU\) 2018/858](#) of the European Parliament and of the Council of 30 May 2018 provides for the administrative provisions and, by reference, the technical requirements for the type approval and placing on the market of all new motor vehicles (categories M and N, and their trailers of category O), that are intended to be used on public roads, including those designed and constructed in one or more stages, as well as systems, components and separate technical units, and for individual vehicle approvals. The Regulation also lays down provisions for the placing on the market and the entry into service of parts and equipment that may pose a serious risk to the correct functioning of the essential systems of the above vehicles. Furthermore, the Regulation sets out the requirements for the market surveillance related to the above. On the above date, [Directive 2007/46/EC](#) of the European Parliament and of the Council of 5 September 2007 was repealed. The Regulation is directly applicable across the EU.

The Regulation aims to raise the quality level and independence of vehicle type approval and testing, increase checks of vehicles that are already on the EU market and strengthen the overall system with EU oversight, including the Commission's right to order EU-wide recalls and impose sanctions on the manufacturers of up to €30,000 per car in cases where manufacturers are in breach of type-approval legislation. The Regulation itself does not modify the technical requirements for vehicle approvals. Such technical standards are laid down in the regulatory acts listed in the relevant Annex of the Regulation.

Based on the Regulation, there are two kinds of type approvals:

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- the national type approval, which is the procedure whereby the relevant approval authority certifies that a type of vehicle, system, component or separate technical unit satisfies the relevant administrative provisions and technical requirements laid down by the law of a given member state, the validity of such approval being restricted to the territory of that member state; and
- the EC type approval, whereby a member state certifies that the same satisfies the relevant administrative provisions and technical requirements of the Regulation.

As a general rule, manufacturers must ensure that the vehicles, systems, components and separate technical units they have manufactured and that are placed on the market have been manufactured and approved in accordance with the relevant requirements, and will be responsible to the approval authority in all aspects of the approval procedure and for ensuring conformity of production. Vehicles for which whole-vehicle type approval is mandatory (or for which the manufacturer has obtained that type approval) will only be made available on the market, registered or entered into service if they are accompanied by a valid certificate of conformity. Components and separate technical units, including those intended for the aftermarket, may only be made available on the market or entered into service if they comply with the requirements of the relevant regulatory acts listed in the relevant Annex of the Regulation and are marked in accordance with the respective provisions.

On a national level, the regulatory framework for the approval of automobiles and automobile parts is currently set forth by [Decree No. 5/1990 \(IV.12\)](#). The Decree has a wider scope than that of the Regulation and mainly covers the administrative procedure, while the technical requirements of automobiles and automobile parts are included in the relevant EU regulations, [Decree No. 6/1990 \(IV.12\)](#) of the Minister of Construction and Transport, which transposes the relevant EU directives and implements EU regulations, and also the applicable United Nations Economic Commission for Europe regulations. The competent department of the Ministry of Construction and Transport is responsible for granting vehicle type approvals.

As a general rule, a vehicle may only be operated on public roads if the vehicle is officially put into traffic, which is carried out by registering the vehicle, issuing the relevant registration certificate and the registration plate. The competent government offices are responsible for putting a vehicle on the road. Based on [Act LXII of 2009](#), all operators of motor vehicles registered in the territory of Hungary are required to have an insurance policy covering any injury arising from the use of motor vehicles, and to pay the relevant premium charged. As a rule, this obligation applies from the time when the vehicle is registered until it is deregistered (not including any period of discontinuance).

Development, manufacture and supply

- 3** | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

To date, several OEMs have chosen Hungary for their manufacturing, engineering and services activities. In addition, more than 700 suppliers and several hundred other market players are active in the territory of Hungary. Regarding ownership structures, companies with a foreign majority owner are dominant in the country.

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In terms of development, manufacture and supply, the prevailing model in Hungary follows the one established by major players in western European countries. More specifically, Hungary leans towards the German model, where a significant part of the supply is provided by means of purchase orders placed by the OEM based on its actual needs with limited obligation to purchase. The supply chain is split into distinct tiers:

- Tier 1 suppliers – being the first level suppliers – supply directly to manufacturing plants;
- Tier 2 suppliers produce parts based on designs provided by major Tier 1 suppliers and OEMs; and
- Tier 3 suppliers are mostly responsible for basic products, such as engineered raw materials.

The contractual framework is determined by the OEM or major Tier 1 suppliers, usually applying their own general terms and conditions with only limited possibility for lower-tier suppliers to negotiate. Such contractual terms go down the supply chain. It is also common for OEMs and Tier 1 suppliers to apply further standardised contractual documents relating to the implementation of the contracts covering, in particular, issues of purchasing, production process and quality assurance, logistics, sustainability and environmental protection.

However, in line with the direction of global trends, in certain cases a stronger relationship may exist between OEMs and major Tier 1 suppliers, including long-term development agreements to ensure full use of potential synergies in highly resource-intensive areas, such as the development of automated, driverless systems.

Distribution

4 | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

There are no specific regulatory requirements in Hungary concerning new vehicles for importers, distributors, dealers or dealer networks.

The Hungarian new vehicle distribution sector is characterised by mixed-type selective distribution systems. Accordingly, one or more car brands are usually promoted by a domestic undertaking acting as the importer. Very often the importer is a subsidiary or branch office of the manufacturer. Based on the selective distribution system, similar to several other EU member states, only authorised dealers may market and sell new vehicles in Hungary if they have entered into a distribution agreement with the manufacturer or its importer. It is a fundamental characteristic of the selective distribution system that the manufacturer undertakes not to supply new vehicles to unauthorised dealers for the purpose of reselling. There are certain limitations applicable to such vertical distribution agreements under the EU and the Hungarian competition law as set out in Commission Regulation (EU) No. 461/2010 (expiring on 31 May 2023), Commission Regulation (EU) 2022/720, [Government Decree No. 204/2011 \(X.7\)](#) and [Government Decree No. 306/2022 \(VIII.11\)](#)

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Nevertheless, the marketing and selling of vehicles through a commercial agent within the framework of an agency agreement is a possible way to organise distribution of vehicles and this approach appears to have increasing importance based on the latest market trends.

There are no specific compulsory rules under Hungarian law relating to restructuring or termination issues in distribution agreements. Such issues are usually regulated by the manufacturer or importer and the authorised dealer within the framework of the distribution agreement, where it is not uncommon that the parties agree on a notice period exceeding 12 months. However, if the marketing and selling of the vehicles is carried out through a commercial agent within the framework of an agency agreement concluded for an indefinite term, the agreement may be terminated by complying with certain statutory minimum notice periods. The Hungarian Civil Code sets out a minimum notice period of one month during the first contractual year, a minimum notice period of two months during the second contractual year and a minimum notice period of three months during the third and following contractual years, none of which may be validly shortened. Moreover, termination of the agency agreement may trigger the commercial agent's entitlement to financial compensation in the form of an indemnification claim, pursuant to the provisions set out in the Hungarian Civil Code. In this case, the indemnity amount may not exceed the commercial agent's average annual remuneration over the preceding five years or the average annual remuneration during the actual term if it is less than five years. Any agreement of the parties prior to the termination of the agency agreement will be null and void if it derogates from the provisions of the Civil Code on indemnification to the detriment of the agent.

Mergers, acquisitions and joint ventures

5 | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

There are no specific or sectoral rules on M&A or joint venture transactions relating exclusively to the automotive industry in Hungary; however, the general regulations regarding concentrations still need to be observed. Based on Act LVII of 1996, as a general rule, a concentration must be notified to the Hungarian Competition Authority if the combined net turnover of the relevant undertakings of the previous financial year exceeded 20 billion forints, and there are at least two groups involved with net turnover of at least 1.5 billion forints. Furthermore, a soft threshold may also apply to the notification of concentrations, with a reduced turnover value of 5 billion forints, if it is not obvious that the contemplated transaction would not significantly decrease competition in the relevant market. The government may – in the public interest, to preserve jobs and for the security of supplies – declare a merger of strategic importance at the national level. Such concentrations do not need to be notified to the Hungarian Competition Authority.

If the product range of the target company includes certain products (for example, military products) pursuant to Act LVII of 2018, a prior approval of the competent minister is needed should a foreign investor directly or indirectly or together with other foreign investors acquire an interest exceeding 25 per cent (in the case of a publicly listed company an interest exceeding 10 per cent) or gain dominance within an existing or yet-to-be-established company registered in Hungary. In addition, to protect the Hungarian economy with respect to Russia's invasion of Ukraine, the Hungarian government introduced an amended

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foreign investment screening mechanism for strategic industries including, among others, the automotive industry. The relevant regulation was originally set out by [Act LVIII of 2020](#) and was amended by Government Decree No. 561/2022 (XII.23).

From a transactional point of view, thorough due diligence is always recommended for M&A transactions in the automotive industry. The most important areas that should be covered from a Hungarian legal perspective include environmental and safety issues, contractual relationships with distributors, dealers and suppliers, employment issues and intellectual property rights.

Incentives and barriers to entry

6 | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

Although there are no special incentives for investment in the automotive industry, general incentives, such as subsidies granted in individual decisions for large-scale investments, and normative incentives, such as tax allowances, may apply. In this regard, the automotive industry is one of the key sectors specified in [Government Decree No. 210/2014 \(VIII.27\)](#) regulating the use of the Hungarian investment incentive earmarked scheme. As the national investment promotion organisation of Hungary governed by the Ministry of Foreign Affairs and Trade, the Hungarian Investment Promotion Agency is responsible for the government's investment incentives and is also the managing body of the 'VIP' cash subsidy system based on individual government decisions. VIP cash subsidy is a non-refundable, post-financed regional investment aid. The amount of the subsidy, as well as the maximum aid intensity, may be influenced by several factors, in particular the location of the project and the development of the region where the project is planned to be implemented, as further regulated under Government Decree No. 210/2014 (VIII.27).

In addition to the above, various local business tax and corporate income tax incentives are available in Hungary for investments and R&D activities. While the fundamental rules of corporate income tax incentives are set forth by [Act LXXXI of 1996](#) on corporate and dividend tax, the specific details are set out in further legislation, such as [Government Decree No. 165/2014 \(VII.17\)](#) on the development tax incentive, providing the relevant rules for aid intensity.

Moreover, pursuant to [Act LIII of 2006](#) on the acceleration and simplification of the implementation of investments of strategic importance at the national level, the government may provide simplified procedural frameworks and grant legislative exemptions to support and promote investments. To date, several individual decisions favouring market players in the automotive industry have been adopted pursuant to Act LIII of 2006, proving the potential of the legislation.

Collaboration between universities and automotive market players is also supported in Hungary. A good example is the cooperation agreement concluded between Hungarian universities and joined by several major players, including Audi Hungaria, Continental Hungaria, General Motors Powertrain-Magyarország Autóipari, Knorr-Bremse Fékrendszerek Kft and Mercedes-Benz Manufacturing Hungary.

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There are no specific barriers to entry into the automotive market in Hungary. However, depending on the actual circumstances, the provisions of [Act LVII of 2018](#), [Act LVIII of 2020](#) and Government Decree No. 561/2022 (XII.23) need to be taken into account.

PRODUCT SAFETY AND LIABILITY

Safety and environmental

7 | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

Hungary, being a member state of the European Union, is subject to the directly applicable regulations of the European Union in the context of product compliance safety and environmental matters. The relevant directives of the European Union, including Directive 2001/95/EC on general product safety, have been implemented into Hungarian law. The basic rules of product safety are set out in the Hungarian Market Surveillance Act, while detailed procedural rules on automotive-related products safety matters are laid down in ministerial decrees.

General rules on product safety include the manufacturer's obligation to:

- design and manufacture its product in accordance with the applicable laws of the European Union and other laws applicable to the relevant product;
- prepare the technical documentation;
- carry out the necessary conformity assessment procedures; and
- offer compliance throughout the serial production.

The manufacturer is also bound to supervise its product and take the necessary measures, including the recall of its product if any non-compliance is revealed. The manufacturer is obliged to notify the competent supervisory authority of any such measures. The importer and the distributor are subject to similar obligations.

In terms of automotive-specific regulations in the context of safety and environmental matters, local Hungarian legislation includes rules for periodic tests of vehicle safety, roadworthiness and emissions, as well as rules for end-of-life vehicles in accordance with Directive 2000/53/EC.

The supervisory authority in automotive matters is the National Transport Authority, which enforces automotive-related regulations in Hungary. Product recalls and other safety measures affecting motor vehicles must be notified to the National Transport Authority. In accordance with the harmonised rules on motor vehicle recalls, Hungarian law provides that product recalls must be notified to the authority that issued the type approval. The authority will issue recommendations on the appropriate measures and will notify the responsible authorities in other EU member states. If the measures taken by the manufacturer are insufficient or delayed, the issuer of the EC type approval is notified that the EC type approval may be withdrawn. The National Transport Authority publishes all relevant

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information on motor vehicles that are hazardous to the health and safety of consumers or that do not comply with the applicable safety provisions.

With respect to the entry into effect on 16 July 2021 of Regulation (EU) 2019/1020 on market surveillance and compliance of products, the Hungarian Market Surveillance Act was amended with effect from the same date. As a result of the amendment, Hungarian authorities are now in a position to take enforcement measures against fulfilment service providers as well as importers and distributors, if the relevant conditions apply. In addition, the amendment also introduced regulations concerning liaison offices among EU member states and the requirement for the National Transport Authority to use the information and communication system for market surveillance in exchanging helpful information with other market surveillance authorities.

Product liability and recall

- 8** | Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

The rules of product liability under Hungarian law are set out in the Civil Code of Hungary based on Directive 85/374/EEC and apply to damages caused by a defect in a manufacturer's product. Product liability typically applies in the absence of a contractual relationship as the liable party is the manufacturer or the importer of the motor vehicle and motor vehicles are typically sold through distributors and dealers. In addition, product liability only applies to consequential damages (ie, damages causing death or personal injuries, health damages and damage to, or destruction of, any item of property other than the defective motor vehicle itself), with a lower threshold of the Hungarian forint equivalent of €500. In addition, product liability may only be relied on in the case of private use; thus, product liability can be typically applied to consumers.

Consequently, product liability may not replace warranty claims, whether statutory or contractual, and is not applicable to business use, narrowing down the applicability of product liability provisions. In addition, motor vehicle owners frequently rely on their insurance and do not pursue claims against manufacturers. As a result, notwithstanding the manufacturer's or the importer's objective liability and a fairly long limitation period of 10 years, product liability law cannot be considered as significant in Hungary in the automotive industry.

In the absence of a significant presence of product liability cases in the automotive industry, there are no class actions or other noticeable published consumer litigation in these cases. As class actions have only been recognised since 2018 under Hungarian civil procedural rules, there are no notable examples of class actions in general under Hungarian law either.

In terms of the significance of product recalls in the automotive industry, there were only 14 alerts concerning Hungary and only five alerts were made by Hungarian authorities over the past 10 years in the Rapid Alert System, which is rather insignificant compared to other EU member states and the overall number of notifications.

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DISPUTES

Competition enforcement

- 9** | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

Competition and antitrust issues are not uncommon in the Hungarian automotive industry. The Hungarian Competition Authority initiates investigations to determine, among other things, if there is an agreement in place between market players that may distort competition or if there is a violation to the consumer protection acts. In these matters, there have been numerous automotive industry-related examinations in the past two decades.

The most frequent proceedings are examinations concerning the concentration of companies. There have been several cases involving investigations of mainly Hungarian suppliers. From the annual report issued by the Hungarian Competition Authority to the parliament, it is apparent that in 2019 the automotive and automobile component manufacturing industry was the fifth most investigated industry in Hungary. The automotive and automobile component industry remains a focus of the Hungarian Competition Authority, with one out of the five initiated antitrust proceedings in 2020 concerning the automotive industry.

The recent European truck cartel case has also had its effects in Hungary. Hungarian carriers are joining ongoing lawsuits against European truck manufacturers in Munich, and lawsuits have also started before several Hungarian courts. According to the latest procedural developments, the European Court of Justice established in an interim decision that damages may be claimed before local Hungarian courts, even against a cartel member with whom the injured party had not established a direct contractual relationship. In November 2022, the first decision by the Competition, Regulation and Supervision Court in Santarém, Portugal ordered DAF Trucks to pay €12,904 to Transfrugal, plus interest, for having committed a breach of competition law. This decision might have an impact on Hungarian proceedings as well.

Dispute resolution mechanisms

- 10** | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

In recent years, there has been a growing tendency in the European automotive industry to insert detailed dispute resolution clauses into contracts. In Hungary, this often leads to the inclusion of non-Hungarian laws and various arbitration forums. As a result, similar to intellectual property disputes, cases are on many occasions settled before reputable international judicial forums instead of in Hungary.

Owing to the increasing number of suppliers present on the Hungarian automotive market as well as the growing complexity of the solutions offered and used in the industry, such as various software developments, one of the current issues in relation to Hungarian liability

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disputes is determining the ultimate liable party, especially if there are more than two tiers of suppliers.

In addition, apart from distribution agreements, defects and product recalls are likely to affect companies involved in the Hungarian automotive industry. Unfortunately, there are no official statistics or data available on the number and the subject of these disputes.

Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

In Hungary, the reasons for and the risks causing the distress and the process of dealing with them are dependent on numerous factors, such as the size of the company and whether the company is new to the market or well established.

For suppliers, generally the most relevant risk factor is the potential insolvency of the buyer company. This risk is especially relevant these days, with the covid-19 pandemic, Russia's invasion of Ukraine, rise of energy prices, inflation rates, component shortages and temporary shutdowns of automotive manufacturing plants severely impacting Hungarian automotive suppliers, of which a number are considered close to bankruptcy according professional market analysts. In insolvency cases, loss does not only pertain to the goods or services ordered but also additional costs, such as temporary storage and auxiliary tasks.

While it is not possible to prepare for every scenario caused by a distressed supplier or supply chain, certain preliminary measures may be taken by market players in the automotive industry to mitigate the impacts. The buyer company may source the production of the part to a new, healthy supplier. Alternatively, the buyer can help the supplier by improving its operations and finding a suitable third party to buy the supplier. If neither of these options are applicable and the component is critical, the buyer company may consider acquiring the troubled supplier.

In terms of precautionary measures, it is not unusual that principals implement a protocol dealing with distressed suppliers to identify and address such unwanted situations in the most effective way possible. For this purpose, companies in the automotive industry continuously gather data on their suppliers and their financial status, including turnover and solvency data, credit reports, number of employees, cash flow and whether any court proceedings were initiated against a given supplier. The continuous monitoring of these data, which are publicly available in official Hungarian databases, gives the automotive companies the opportunity to find signs of upcoming or potential distress. Scenario simulations are also prepared on the basis of the information gathered.

Act LXIV of 2021 on business restructuring entered into force on 1 July 2022, implementing the directive of the European Union on business restructuring. The main goal of the European and the national legislator is to combat the above-mentioned issues regarding insolvency.

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Intellectual property disputes

- 12** | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

Intellectual property plays a significant part in the automotive industry in both the fields of aesthetics and technical design. Intellectual property law offers many indirect and direct ways of protecting the design of automobiles, as well as patents, trademarks, copyright and design. Disputes easily arise in cases involving infringement of a patent or breach of copyrights.

However, the main players of the Hungarian automotive industry are car plants where the manufacturing of various components or the assembly of the automobiles takes place, and not the actual designing. It is, therefore, uncommon for the participants of the automotive industry to initiate legal proceedings before Hungarian courts concerning intellectual property or to register a Hungarian national design or trademark. Legal disputes that arise with the involvement of automotive parent companies are usually dealt with at the national courts of the countries where these companies are registered or before arbitration courts of their choice. This is also the case if the dispute concerns an alleged infringement of a European patent, since there is currently no common European patent court.

EMPLOYMENT ISSUES

Trade unions and work councils

- 13** | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

Labour relations in the automotive sector in Hungary were recently discussed in the context of working time arrangements and employers' ability to designate working time, work schedules and shift patterns in a flexible manner.

Under Hungarian law, employers are entitled to designate and amend work schedules unilaterally subject to protective mandatory provisions regulating, for example, working time and rest time. Employers are entitled to designate regular working hours unevenly within a certain period; thus, through planning, employers may significantly reduce the number of paid overtime hours compared to a regular work schedule. A longer working time cycle thus serves the interests of those employers whose business can be scheduled further ahead.

In the automotive industry, the maximum working time cycle is typically six months (or 26 weeks) without a collective bargaining agreement. If justified by objective, technical or work organisation reasons, a collective bargaining agreement may set out a maximum 36 months' working time cycle. In practice, most employers have been unable to justify having a cycle longer than one year, and most trade unions have been reluctant to agree to such a working time cycle.

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Since, as noted above, the agreement of trade unions is required for a number of working time arrangements – compared to other industries where unionisation is not as widespread – collective bargaining agreements are fairly common in the manufacturing industry, and particularly in the automotive sector. In the absence of an industry-wide collective bargaining agreement in the automotive sector, trade unions have more room to bargain for better working conditions and higher remuneration locally.

In addition, where an employer is not subject to a collective bargaining agreement and there is no trade union to conclude such an agreement, works councils are entitled to settle in a works council agreement all matters – except remuneration – that can be settled in a collective bargaining agreement. This gives works councils wider negotiating opportunities on top of their traditional participation rights, albeit with a weaker bargaining power and, potentially, a stronger dependence on the employer compared to trade unions.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

In the past few years, one of the most important legal developments relating to automotive technological and mobility advances has been the implementation of certain new provisions on the testing of self-driving motor vehicles. The Hungarian government considers the testing of autonomous driving as a priority area of development that has resulted in various investments in the country recently.

The legal framework for the testing of autonomous motor vehicles was first implemented in 2017 through the amendment of ministerial decrees that regulated the entire testing process. Based on these provisions, developers are entitled to perform tests on both closed test tracks and in-road traffic. The relevant regulations adhere to international standards, such as the automation level definitions adopted by the Society of Automotive Engineers, and take into consideration foreign codes of practices.

The first set of rules was followed by an amendment that entered into effect in December 2018. As a result of the amendment, various registration and notification obligations in relation to the testing process of autonomous motor vehicles were simplified, including the abolition of the requirement to register Level 2 (hands-off) car tests on closed test tracks, the elimination of an itemised notification requirement in relation to self-driving motor vehicles placed on the road (the notification of an approximate number is sufficient) or the extension of acceptable standards beyond ISO 26262. Certain recording obligations have also been simplified. For instance, in the context of the recording of test periods, a daily recording is sufficient compared to the previous requirement to record tests down to the minute. In addition, the recording time of accidents in the black box has decreased from 24 hours before and one hour after the accident to one hour before and one minute after the accident.

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The above amendment indicates efficient communication between developers and government officials, and the government's aim to create a proper legal environment to foster new developments in Hungary.

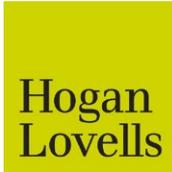
However, some of the most significant legal challenges are yet to be resolved, including the investigation of liability matters and the implementation of a special liability regime that will most probably be necessary to provide an appropriate response to the dilemmas that have already been heavily discussed in the context of damage caused by self-driving cars. In addition, the legal framework of telecommunication law (which is fairly rigid in Hungary compared to the continuously evolving technical and technological solutions in the industry) needs to be adapted to autonomous vehicles, as legal issues (including regulatory and privacy matters) that are currently in the background will most likely be of high priority in the context of connected vehicles and connectivity services.

UPDATE AND TRENDS

Trends and new legislation

15 | Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

As of 2022, to promote the use of electric motor vehicles and electromobility, in the construction of new buildings and major refurbishment of the electric infrastructure and parking spaces of buildings with more than 10 indoor or adjoining outdoor parking spaces, the installation of charging stations and relevant infrastructure for the charging of electric motor vehicles is a requirement. Similar requirements apply in this context to both residential and non-residential buildings. Non-residential buildings with more than 20 parking spaces will be subject to a general requirement to install charging stations as of 2025.



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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

The Indian automotive market is currently the fourth largest in the world and is one of the most dynamic sectors of the country's economy, with most of the global automotive giants already present in the market and contributing to its growth. The industry is worth more

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than US\$222 billion, comprising 8 per cent of India's total exports and accounting for 7.1 per cent of the country's GDP.

Over the years, India has established itself as a strong base for automotive manufacturing and is now the second largest manufacturer in two-wheelers, seventh largest in commercial vehicles, sixth largest in passenger vehicles and the largest in tractors.

Starting as an Indian government initiative, Maruti Udyog was the only major player for a decade until the floodgates for foreign investment in India were opened in 1991. Both the country's primary and secondary automobile markets have developed to the point where the most reputable international automotive manufacturers compete for market share. Although there is a wide array of automobile brands available to customers in India, Maruti Suzuki India – owned by Japan-based Suzuki Motor Corporation – continues to be the leading brand with approximately 46 per cent of the market share in the passenger vehicle segment, followed by Hyundai Motor India and Tata Motors.

In terms of foreign direct investment in the automotive industry, there was growth of almost 62 per cent during the first four months of financial year 2022. The inflow of FDI was the highest in comparison to any other sector, demonstrating the attractiveness of the Indian market. India received US\$33.77 billion worth of FDI in the automotive industry from April 2000 to September 2022, which accounted for approximately 5.48 per cent of the country's total FDI for that period.

Factors such as directives for easing business in India and economic reforms have contributed to growth in this sector and the government has driven and continues to drive the implementation of a fully liberalised foreign direct investment policy, as well as a host of incentives ranging from tax and customs benefits to concessions for producing electric vehicles. India is expected to attract approximately US\$100 billion of FDI during financial year 2022–2023.

The industry suffered a certain amount of degrowth in financial years 2020–2021 and 2021–2022, primarily on account of the unprecedented circumstances created by the covid-19 pandemic. The two-wheeler segment, which accounted for 81 per cent of the market, faced a decline of 27.25 per cent in sales, whereas the sale of passenger vehicles was down by 6.53 per cent. The three-wheeler segment also faced a decline of over 2.2 per cent.

Although the Indian market faced setbacks during the pandemic, including supply-side issues, relaxations offered by the government encouraged the creation of further domestic demand and promoted export, paving the way towards normalcy. Commercial vehicle sales, which were down by almost 20 per cent in 2021, increased by 7.41 per cent in 2022, and the market is expected to receive a significant boost in automotive retail sales in 2022–2023. According to the Society of Indian Automobile Manufacturers, the market trend in March 2021 showed a 76.75 per cent growth rate in sales compared to March 2020 sales figures. It even crossed the sales figures of the first quarter of 2019. From 2021, four-wheeler sales grew by 115.2 per cent and two-wheeler sales were up by 72.67 per cent. In 2022, the automotive industry recorded its highest ever sales in a single calendar year, standing at nearly 38 million dispatches. This figure beats the previous sales record of 33.3 million dispatches in 2018 by an increase of 14 per cent.

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India is also a prominent automobile exporter. As of 2022, 24 per cent of the country's automobile production had been sent to the United States, South Africa, Mexico, Bangladesh, the United Arab Emirates, Saudi Arabia, Turkey, Colombia, Brazil, Nigeria, Nepal, Indonesia and the Philippines as the main export destinations. The initial stages of the national lockdown imposed in India in 2020 strongly affected the production of vehicles and, added to the disturbance caused in the economies of several countries importing vehicles from India, led to considerable reduction in exports from 2019–2020 to 2020–2021. However, as the lockdown was lifted and manufacturing activities recovered to match pre-covid-19 levels, exports have seen a surge with Maruti Suzuki India leading the way and have experienced a growth as high as 148 per cent in financial year 2022 compared to financial year 2021 in the passenger vehicle segment. In the two-wheeler segment, Bajaj Auto saw a whopping 45 per cent growth in exports in financial year 2022 compared to financial year 2021.

A shift in the preference of consumers towards larger and more powerful vehicles across all segments has been observed. According to these reports, demand for utility vehicles (passenger vehicles) increased to 49 per cent in the financial year 2022 compared to 39 per cent in financial year 2021, while demand for medium and heavy commercial vehicles increased to 33 per cent in financial year 2022 compared to 28 per cent in financial year 2021.

COMMERCIAL OPERATIONS

Regulation

2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

The [Motor Vehicles Act 1988 \(MVA\)](#) along with the [Central Motor Vehicles Rules 1989 \(the CMV Rules\)](#) framed thereunder by the central government constitute the principal regulatory framework for the manufacture, registration and insurance of automobiles and their parts. The MVA vests authority with the central and state governments to make and implement regulations on the construction, equipment and maintenance of automobiles with respect to several aspects including dimensions, emission norms, automobile parts – such as brakes, steering gears and safety devices – and aftersales warranty. The central government primarily administers and regulates the industry through the Ministry of Road Transport and Highways.

The manufacturing and maintenance of automobiles must comply with the parameters and standards prescribed under the CMV Rules and those notified by the central government. Checks and controls are formulated at the following stages:

- the proposal to manufacture or import a new automobile;
- during the manufacturing process;
- the sale and use of an automobile; and
- the recalling of automobiles in the case of defects.

A manufacturer or importer that proposes to manufacture or import a new automobile is required to obtain approval for its prototype from the designated testing agencies. The

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procedure for type approval and certification of automobiles for compliance with the MVA and CMV Rules accords with the Automobile Industry Standards published by the central government. While the production of automobiles is ongoing, the CMV Rules require tests to be conducted periodically on automobiles drawn from the production line to verify that they conform to the approval certification. On the completion of the manufacturing process and the sale of an automobile, the manufacturer must issue a certificate of roadworthiness and quality to the owner. Thereafter, for in-use vehicles, owners are required to obtain a 'pollution under control' certificate a year after the date of its registration from an agency authorised by the relevant state government.

As in most other jurisdictions, every vehicle is required to be registered by the owner with the concerned authority, where either the individual resides or conducts business, and cannot be driven on public roads prior to registration. An automobile's registration certificate is valid for a period of 15 years for petrol automobiles and 10 years for diesel automobiles from the date of issue of the registration certificate, and it can be renewed for five years subject to an inspection of the roadworthiness of the automobile. The Ministry of Road Transport and Highways' notification dated 26 August 2021 introduced a separate category of registration, namely, the Bharat (BH) series registration mark. The BH registration period is dependent on car type (ie, petrol, diesel or electric vehicle), and it is advantageous for vehicle owners who must move from one state to another, as it avoids the hassle of seeking repeated registration after transfer to a new state.

The registration of a vehicle is deemed complete only on the issue of a certificate of fitness by an authorised testing station and is valid for two years. The certificate must be always valid during the use of the vehicle. The certificate of fitness for transport vehicles (ie, a public service vehicle, a goods carriage, an educational institution bus or a private service vehicle) up to eight years old can be renewed for up to two years. For transport vehicles older than eight years, the renewal is only for a year.

Automobile insurance is compulsory before the vehicle can be driven on a public road. Insurance is provided by an authorised insurer that issues a certificate to the policyholder. An insurance policy is usually valid for a period of one year and must be renewed before the due date. The MVA requires the insurance policy to cover third-party risks.

An important development in the regulatory regime of the sector was the implementation of certain crucial and much-awaited amendments to the MVA, introduced in the [Motor Vehicles \(Amendment\) Act 2019 \(the MV Amendment Act\)](#) in a staggered manner in notifications dated 28 August 2019 and 25 September 2020. One of the most important amendments was the addition of a mandatory recall mechanism, which includes prescribed grounds and obligations for conducting a recall, notification requirements, assignment of responsibility, destruction of defective parts, record-keeping, auditing and penalties. The CMV Rules impose hefty fines on the manufacturers, importers or retrofitters of motor vehicles based on the number of vehicles recalled, starting from 1 million rupees to a maximum of 10 million rupees.

The MV Amendment Act holds criminally liable manufacturers, importers and dealers of motor vehicles that fail to comply with the provisions of Chapter VII of the MVA and CMV Rules concerning the construction, maintenance, sale and alteration of motor vehicles and their components. The penalty includes mandatory recalls, with imprisonment for a term

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that may extend up to a period of one year or a fine that may extend to 100,000 rupees in the usual cases, or to a maximum of 1 billion rupees in matters involving contravention of provisions on construction, maintenance, sale and alteration of motor vehicles and components, and other rules made thereunder by the central or state government.

A significant development in the regulatory structure is the introduction of the Motor Vehicles (Registration and Functions of Vehicle Scrapping Facility) Rules 2021 (the Vehicle Scrapping Rules) effective as of 25 September 2021.

The regulations on the standards for manufacturing electric vehicles have also been strengthened and improved in favour of the end user of the product, due to the growing focus that has been placed on these vehicles and building their infrastructure in India.

More specifically, certain amendments to the CMV Rules in notifications dated 19 December 2022 and 31 October 2022 require additional tests conducted on electric vehicles and hybrid-electric powertrain vehicles. The standards for battery-operated vehicles have also been revised and updated.

Certain safety testing parameters with respect to the batteries used in electric vehicles were implemented in two phases, with phase one coming into effect on 1 December 2022 and phase two on 31 March 2023. The purpose of the phased implementation was to allow the OEMs enough time to comply with the revised standards.

Development, manufacture and supply

3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

Although foreign direct investment in the automotive sector is permitted for up to 100 per cent without conditions, most foreign companies have been carrying out manufacturing and distribution businesses in India by setting up joint ventures with local counterparts. Automotive parts manufacturers follow the same commercial model.

In a typical joint venture arrangement in the automotive sector, the Indian party is responsible for obtaining all local licences and approvals required for manufacturing operations. The foreign investor, besides bringing in capital contribution, is primarily the source of technology, technical assistance and R&D. Support, technology and technical assistance are usually licensed by the foreign partner to the joint venture subject to certain standard conditions (such as limited use by the joint venture for the purposes of manufacturing specified products). The foreign partner often negotiates a royalty (usually based on the total sales made by the joint venture company) as a consideration for licensing the technology to the joint venture.

With the growing interest and increased regulation surrounding electric vehicles in the Indian market, several foreign manufacturers have shown willingness to produce EVs in India. For instance, Mercedes-Benz is now producing four of its luxury and all-electric cars in India, and Volvo has shown interest in directly manufacturing in the country.

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Most of the leading auto parts and component manufacturers and suppliers, including Bosch, Lucas TVS, Delphi, Visteon, Autoliv, WABCO, BorgWarner, DENSO and Nippon Seiki, have followed the multinational automotive companies in setting up their plants and shops in India. They have entered supply arrangements with automotive manufacturing companies.

Automotive manufacturing companies distribute and sell their products to retail customers through an authorised dealership network. The manufacturers enter into contractual distribution arrangements with the dealers. Standard conditions for the eligibility and continuity of dealership include adequate infrastructure, personnel, investments and working capital. The dealership agreements usually prohibit the dealer from engaging in distribution of automobiles manufactured by competing brands.

Distribution

- 4 | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

Distribution

As a general commercial practice, vehicles are distributed in accordance with contractual arrangements between manufacturers and authorised dealers.

There are no specific pieces of legislation regulating the distribution or dealership of automobiles. All commercial terms including provisions relating to termination and restructuring are agreed on between the manufacturer and the distributors or dealers in private contracts. Parties are often allowed to terminate the contract with a reasonable notice period. Given that automobile distribution agreements have come under the scrutiny of the Competition Commission of India for alleged malpractices – such as exclusive supply agreements, resale price maintenance, exclusive distribution agreements and tie-in agreements – caution must be exercised to ensure that such distribution agreements are not anticompetitive in nature and do not breach the provisions of the Competition Act 2002.

Dealers are typically family-owned concerns or businesses. Recently, however, we have witnessed several automobile manufacturers concentrating more on the management structure of family-owned and run dealerships. Indeed, some automotive manufacturers have been contemplating amendments to the dealership contracts to ensure that the dealer entities are organised or reorganised with a consolidated management control vested in the family leader or the key person in control, rather than the shareholding of the dealer companies being spread and fragmented across numerous family members.

Imports

The conditions for importing new and second-hand automobiles into India are specified in the Foreign Trade Policy (FTP) and regulated by the Directorate General of Foreign Trade. The FTP prescribes certain requirements regarding the import of automobiles, for instance:

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- new automobiles can be imported into India through Indian customs seaports in Mumbai, Cochin (Kerala), Visakhapatnam, Chennai and Kolkata, while second-hand automobiles can be imported only through the customs port in Mumbai;
- only certain identified categories of second-hand automobiles can be imported into India;
- imported automobiles are required to conform to the MVA and CMV Rules; and
- the importer is required to submit a certificate from a notified testing agency at the time of importation that the automobile conforms with the MVA and CMV Rules.

Mergers, acquisitions and joint ventures

5 | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

There are no specific particularities for M&A or joint venture transactions in the automotive industry as such. However, due to the size of the automotive industry, due diligence is generally considered desirable in relation to real estate, waste management processes, environmental approvals and compliance with employment-related laws. With rapidly changing technology becoming a critical part of the automotive industry, considerable focus and attention are also vested on the ownership and protection of intellectual property rights.

Incentives and barriers to entry

6 | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

The government of India has played a major role in promoting investment in the Indian automotive sector. The central government primarily extends support and incentives to the automotive industry by way of tax exemptions and reductions in, for example, customs duty charged on imports of automotive components when these are imported in completely knocked-down kits (meaning units that contain a pre-assembled engine or gearbox or transmission mechanism, or a chassis where such parts or sub-assemblies are installed).

The recently introduced Vehicle Scrapping Rules will also boost motor vehicle sales by reducing the number of unfit vehicles on the road and encouraging the purchase of new vehicles equipped with better technology. As part of the vehicle scrapping policy, it was announced in the budget on 1 February 2023 that 900,000 vehicles owned by central and state governments, transport corporations and public sector undertakings will be scrapped from 1 April 2023.

The central government has also endeavoured to extend tax-related reductions to exporters of auto components under the Merchandise Exports from India Scheme, notified in the FTP of 2015–2020 and applicable until 30 September 2022, and now the current FTP policy has been extended for a period of six months from 1 October 2022.

During the past couple of years, the government launched several schemes to encourage growth in the automotive sector, such as:

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- the Automotive Mission Plan 2016–26, which aims to increase the domestic production of automobiles and automotive exports, and to address environmental and safety challenges;
- the National Automotive Testing and R&D Infrastructure Project, set up to enable the industry to adopt and implement global performance standards by establishing nationwide automobile testing agencies;
- the Faster Adoption and Manufacturing of (Hybrid) and Electric Vehicles (FAME) Scheme, which provides monetary incentives to producers and purchasers of eco-friendly vehicles. The government of India approved the second phase of the scheme in February 2019 for a period of five years with a budget of around 100 billion rupees, in effect until financial year 2023–2024. Phase II of the FAME scheme is implemented through demand incentives, the establishment of a network of charging stations and administration of the scheme through publicity and other activities;
- the government of India has recently entered into a Comprehensive Economic Partnership Agreement with United Arab Emirates that is projected to increase automobile exports to the UAE in the next five years; and
- to promote the use of electric or hybrid vehicles, the government has introduced various schemes and incentives:
 - the National Electric Mobility Mission Plan 2020, to provide incentives to manufacturers of electric cars;
 - in 2021, the Indian government approved a production-linked incentive scheme for manufacturing advanced chemistry cells in India to facilitate a reduction in the price of batteries, leading to reduction in the price of electric vehicles. A similar scheme for the automotive sector was also approved by the Indian government, namely, the Production Linked Incentive Scheme for the automobile and auto component industry. It enhances India's manufacturing capabilities for advanced automotive products. This scheme also provides incentives for determined sales of advanced automotive technology products (vehicles and components) manufactured in India from 1 April 2022 for a period of five years. The Production Linked Incentive Scheme consists of two components: the Champion OEM Incentive Scheme (it is a sales value-linked scheme, applicable to battery-run electric vehicles and hydrogen fuel cell vehicles of all segments); and Component Champion Incentive Scheme (a sales value-linked scheme, applicable to the advanced automotive technology components of vehicles, completely knocked-down or semi-knocked-down kits, vehicle aggregates of two-wheelers, three-wheelers, passenger vehicles, commercial vehicles and tractors). Applications by major automotive manufacturers in the Indian market, such as Ashok Leyland, Ford India, Kia India and Tata Motors, have been accepted for the Champion OEM Incentive. Battery-operated vehicles are given green number plates and are exempt from permit requirements and payment of fees for the issue or renewal of registration certificate and assignment of a new registration mark. The government has also provided a 2 per cent concession on tax for BH series non-transport vehicles at the time of registration;
 - the goods and service tax on electric vehicles has been reduced from 12 per cent to 5 per cent, and goods and service tax on chargers or charging stations for electric vehicles has been reduced from 18 per cent to 5 per cent. Tax deductions up to 150,000 rupees are available for electric vehicles under the Income Tax Act 1961;
 - active steps have been taken to demonstrate that electric vehicles or battery-operated vehicles are safe by increasing the safety standards a manufacturer is required

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- to comply with, through implementation of safety tests and by ensuring that components used in a traction battery comply with the prescribed safety standards; and
- in the union budget of 2022–2023, the government introduced a battery-swapping policy, which will allow drained batteries to be swapped with charged ones at designated charging stations, thus making electric vehicles more viable, convenient and user-friendly for potential customers. These strategies and policies are intended to promote greater use of electric vehicles in response to the growing need and demand for cleaner transportation options.

State governments have been actively involved in offering incentives to the automotive sector, especially to attract foreign automobile manufacturers to set up in their states. The incentive offers usually involve lease and sale of land at concessional rates, reductions in land-related levies or duties and power tariffs, concessional rates of interest on loans and investment subsidies. Very often state governments offer special incentive packages for mega projects. They are also providing incentives and subsidies on the purchase of electric vehicles that are separate from those granted under the FAME scheme, Phase II. States such as Rajasthan, Karnataka, Tamil Nadu, Uttarakhand and Punjab, acting on the advice issued by the Ministry of Road Transport and Highways in January 2019, have provided exemptions to electric vehicle users from paying road taxes. This benefit has been renewed in the state of Uttar Pradesh and its government has exempted road tax and registration fees on the purchase of electric vehicles for three years from 14 October 2022.

The Indian automotive industry does not impose any specific entry barriers on the market. Being a capital-intensive sector, as may be the case in other countries, production has proven to be cost-effective only if large volumes are achieved. The new entrants thus often face financial challenges until economies of scale have been achieved. In an extremely competitive market such as India, building up a brand is challenging and can be time-consuming, specifically in this sector owing to customer loyalty with the established manufacturers (such as Maruti). The other general commercial issues are the huge costs involved in technological advancements and modifications to the product to suit the Indian customer base.

Over the past several years, the Indian market has been experiencing an upward trend in the entry of foreign automotive manufacturers including in the luxury and sports car segments, with companies such as Maserati, Aston Martin and Lamborghini setting up dealerships and aftersales infrastructure in the country. Large or small, it is a fact that even well-established automobile manufacturers must make continued efforts and investments to retain their customer base in view of increasing competition. For instance, MG entered the Indian market by setting up its first manufacturing facility in the western state of Gujarat in 2019. After making huge investments, MG has significantly increased its market presence in India and registered a 69 per cent growth in the first quarter of the financial year 2022. Its expected growth in the financial year 2023 is approximately 70 per cent to 80 per cent above the previous year, and its operations may soon become profitable.

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PRODUCT SAFETY AND LIABILITY

Safety and environmental

7 | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

The Motor Vehicles Act 1988 (MVA) and the Central Motor Vehicles Rules 1989 (the CMV Rules) authorise the central government to publish quality, safety and performance standards in relation to any part, component or assembly used in the manufacture of an automobile. Every manufacturer is required to obtain approval for the prototype of the part, component or assembly for which standards have been notified and approved by an agency referred to in the CMV Rules. After obtaining approval, the manufacturer is required to certify its compliance under the statutory form prescribed under the CMV Rules. Recent amendments to the CMV Rules include setting improved and stronger safety standards for components during the production of traction batteries for electric and battery-operated vehicles.

The Ministry of Environment and Forests has laid down rules to ensure that standards for air-pollutant emissions from automobiles are kept in accord with international standards. Schedule IV of the Environment (Protection) Rules 1986 provides standards for emissions of smoke or vapour from automobiles. The Bharat Stage emission standards (based on European regulations) have been set up by the central government to regulate the air pollutants emitted from internal combustion engine equipment, including motor vehicles. Currently, the vehicle emissions standard adopted throughout the country is the Bharat Stage VI (BS-VI). The MVA requires every automobile owner to carry a valid 'pollution under control' certificate issued by designated facilities. The MVA prescribes punishment by way of a fine in the event a person is found to be driving an automobile that violates the standards of road safety and pollution in a public place.

The Ministry of Road Transport and Highways amended the CMV Rules to require every vehicle manufactured on or after 1 April 2020 to be compliant with the new and stricter BS-VI emission standards. BS-VI standards were also made mandatory for quadricycles, the new category of vehicle introduced on 22 May 2020 in line with the European Union's World Motorcycle Test Cycle. The ministry proposed to further revise the BS-VI emission standards to bring rules and regulations governing hydrogen and ethanol- or biodiesel-based vehicles. The draft notification dated 6 September 2022 amending the CMV Rules provides that vehicles or engines with biodiesel adulteration of up to 7 per cent will be tested with diesel, and vehicles with more than 7 per cent adulteration will be tested with the respective adulteration. Vehicles powered with hydrogen will be assigned NOX emissions only.

The CMV Rules require that special purpose vehicles – constructed or altered to transport goods or passengers – comply with prescribed automotive industry standards until the corresponding bureaux of Indian standard specifications are notified under the Bureau of Indian Standards Act 2016. The Ministry of Road Transport and Highways has, in a notification dated 3 August 2022, mandated that vehicles of categories N2 (maximum weight not exceeding 3.5 tons but below 12 tons) and N3 (exceeding 12 tons) carrying hazardous and dangerous goods are required to be fitted with a vehicle tracking system device.

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One of the most important developments in the automotive sector for pollution reduction is the introduction of the Motor Vehicles (Registration and Functions of Vehicle Scrapping Facility) Rules 2021 (Vehicle Scrapping Rules) that came into effect on 25 September 2021. The Ministry of Road Transport and Highways has formulated these rules to ensure that all vehicles that have not renewed their certificate of registration, have not been granted a certificate of fitness, have been damaged due to fire or accident, have been declared obsolete or outlived their utility are taken off the road.

The Vehicle Scrapping Rules broadly provide for the following:

- They lay down the procedure to receive and record end-of-life vehicles (ELVs), including depolluting, dismantling, segregation of material, safe disposal of non-reusable parts and issuance of certificate of vehicle scrapping to the registered owner of a motor vehicle. ELVs are defined as vehicles that are not validly registered, or are declared unfit through automated fitness centres, or their registrations have been cancelled or they are declared as waste vehicles by a court of law or through self-declaration.
- Registered vehicle scrapping facilities are those that hold a registration for dismantling and scrapping ELVs. They have been provided connectivity and access to the VAHAN database of vehicle registration and are authorised to make suitable entries about vehicle scrapping. They issue a certificate indicating transfer of ownership from vehicle owner to registered scrapper (certificate of deposit) and a certificate recognising the final disposal of a vehicle (certificate of vehicle scrapping), and ensure that the minimum technical requirement for collection and dismantling centres and removal or recycling or disposal of hazardous parts of the scrapped vehicle are in accordance with the pollution board norms and guidelines. This warrants the environmentally sound management of ELVs.
- Additionally, to promote the registration of vehicles under the Vehicle Scrapping Rules, tax concessions are offered to automobiles registered against submission of certificate of deposits. The tax concession is offered in the range of 15 per cent to 25 per cent for a period of eight to 15 years, depending on type of vehicle.

Earlier recalls in the Indian automotive sector were voluntarily undertaken by companies in accordance with the Voluntary Code on Vehicle Recall 2012 introduced by the Society of Indian Automobile Manufacturers (SIAM). However, in 2019, the MV Amendment Act introduced a mandatory recall provision through the insertion of section 110A in the Act for automobiles pursuant to which recalls in the automotive sector have now become regulated. This amendment seeks to empower the central government to direct manufacturers to recall their motor vehicles of a particular type or its variants if they suffer from a defect that may cause harm to the environment, drivers or occupants or other road users, and in the event of the defect being reported to the central government by a prescribed percentage of owners, testing agencies or any other source. If a defect lies in a component of a motor vehicle, the manufacturer is bound to recall all such vehicles and their variants that contain the component.

Under this framework, the manufacturer is liable for every such vehicle recalled. The manufacturer is required to:

- fully reimburse the buyers subject to any hire-purchase or lease-hypothecation agreement;

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- replace the recalled vehicle with a vehicle having similar or better specifications that complies with standards under the MVA; or
- repair the vehicle, and pay such fines as deemed fit by the central government.

However, the manufacturer will not be held liable to a fine if it notices the defect and informs the central government.

The CMV Rules provide detailed provisions on various scenarios involving a recall, such as the recall procedure, grounds for conducting a recall and obligations thereto, notice requirements, assignment of responsibility, investigation related to safety defects, destruction of defective parts, role of the designated officer, record-keeping or auditing. Furthermore, the CMV Rules stipulate the levy of hefty fines by the designated officer to be imposed on the manufacturer, importer or retrofitter of the motor vehicle depending on the number of motor vehicles recalled, starting from 1 million rupees up to a maximum fine of 10 million rupees. The Ministry of Road Transport and Highways has recently, in a notification passed in March 2021, prescribed a formula based on the percentage of complaints received from owners of automobiles that will trigger the mandatory recall of a particular model. The formula is based on percentage and is different for each category of vehicle, such as two-wheelers, three-wheelers, M1 or M2.

As per reports, vehicle recalls in India hit a five-year high in 2021 with more than 700,000 recalled, which was more than the total number of recalls during the previous three years. According to SIAM, four-wheeler and two-wheeler recalls during 2021 stood at 707,318 units. The industry had seen 380,615 recalls in 2020, 159,992 in 2019 and 138,755 in 2018. Vehicle recall was at its third highest in 2022.

Product liability and recall

- 8** | Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

At present, there is no legislation that deals with product liability specifically for automobiles. In the event a customer suffers losses because of a defect in a vehicle, the customer has a remedy against the manufacturer or supplier of the automobile (as the case may be) under the Consumer Protection Act 2019 (the CP Act), which is a specific legislation for the protection of the rights of all consumers. Claims under the CP Act can be made before various forums at the district, state and national levels (consumer forums). The term 'defect' has been widely defined in the CP Act to include any fault, imperfection or shortcoming in the quality, quantity, potency, purity or standard that is required to be maintained or claimed by the trader under any law in force or any contract, express or implied, in any manner whatsoever in relation to any goods or product.

A purchaser of an automobile has a remedy against the manufacturer or the supplier of an automobile under the CP Act, as mentioned above. The usual and bare minimum remedy granted by the Central Consumer Protection Authority or District Consumer Disputes Redressal Commission is a refund of the price of the automobile along with interest, or replacement of the automobile in cases of a manufacturing defect. In addition, consumer

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forums often grant damages for harassment and mental harm caused to the consumer if the consumer proves that the injuries and losses were a result of the manufacturing defect.

It is within the power of the consumer forums to award damages in a case involving death or very serious permanent injury, but there is no typical range of such damages, and they generally vary on a case-to-case basis. There is no limit on the damages that can be awarded, and the consumer forum will take into consideration factors such as loss of income, family members dependent upon the injured or deceased person, mental pain and harm suffered.

The Civil Procedure Code 1908 provides for class actions or group actions where one person may, with the permission of the court, sue or defend on behalf of all persons having the same interest. The CP Act also provides for consumers as a group or class to institute a complaint against a manufacturer or supplier. However, this approach has not been popular compared to class actions, which lie before the high court of each state or the Supreme Court of India in the form of a public interest litigation (PIL) for the enforcement of public interest.

A PIL may be moved not only by an aggrieved party, but also by a public-spirited individual or a social action group for the enforcement of the fundamental or legal rights of an aggrieved party who is unable to approach the court for reasons such as being in a disadvantaged position on account of poverty, disability or other social or economic impediments. PILs form part of the writ jurisdiction of the high courts and the Supreme Court of India, and accordingly can only be filed against an aegis of the state or any other party exercising public functions. Over the past decade, there has been an increasing number of PILs filed in the court concerning several issues. For example, pursuant to a very well-known PIL filed by an environmentalist before the Supreme Court of India, the higher or stringent emission standards for automobiles were introduced by the Delhi state government. The stand taken by the auto manufacturers was that they were meeting the standards laid down under Indian laws and, after the court order, the emission standards were tightened to reduce vehicular pollution.

The vehicle recall procedures introduced in the MVA now become relevant. With the change in law and introduction of recall reforms, if the manufacturer does not initiate voluntary recall of defective vehicles, the government has the power to direct a recall. It may also impose a penalty on the manufacturer. This amendment is bound to ensure that there are fewer class actions or group litigation and PIL situations arising with respect to product liability in the automobile market in India, thereby avoiding overburdening the courts.

DISPUTES

Competition enforcement

- 9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

The Competition Commission of India (CCI), which is the authority regulating competition, actively investigates allegations of anticompetitive behaviour in the automotive sector. The investigations carried out by the CCI are either initiated of its own accord, based on press

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reports and information flowing from parallel cases, or based on information provided by third-party informants.

The most notable competition-related issue in the automobile sector was *Shamsher Kataria v Honda Siel Cars India Ltd & Ors*, Case No. 03 of 2011 (CCI, 25 October 2014), in which the CCI investigated various automobile manufacturers for anticompetitive practices – it is understood they denied market access to branded spare parts and diagnostic tools, and thereby hampered the ability of independent repairers to provide aftermarket repair and maintenance services to automobile owners.

Such practices have allowed automobile manufacturing companies not only to have monopolistic control over the spare parts and diagnostic tools market under their respective brands, but also to charge arbitrary and steep prices for said products, in violation of the provisions of the Competition Act 2002 (the Competition Act).

The CCI observed that owing to the technical specifications of the cars manufactured by each OEM, the spare parts of one brand cannot be used for the repair and maintenance of cars manufactured by another OEM. Therefore, each OEM is shielded from competition in the aftermarket from existing competitors in the primary market.

Furthermore, agreements entered into by OEMs with their original equipment suppliers and authorised dealers prohibit the sale of spare parts to independent repairers in the secondary market. The CCI was of the view that each OEM holds a position of strength, which enables it to affect its competitors in the secondary market or aftermarket, thereby limiting consumer choice and compelling consumers to behave in a manner beneficial to the OEMs by allowing them to enjoy a dominant position in the aftermarket for spare parts.

In addition to levying a heavy penalty, the CCI directed OEMs not to place any restrictions on the operation of independent repairers and to allow original equipment suppliers to sell spare parts freely in the open market. However, OEMs were permitted to charge royalties or fees where they hold intellectual property rights on parts, provided that this is not in violation of the Competition Act. The order of the CCI was appealed by some automotive manufacturers before the Competition Appellate Tribunal (COMPAT) established under the Competition Act. The COMPAT concurred with the findings of the CCI and upheld the penalty that was levied. The order of the COMPAT was stayed by the Supreme Court of India in November 2018. On 20 January 2020, the Supreme Court disposed of the matter while confirming the COMPAT order stays or remains operative during the pendency of the National Company Law Appellate Tribunal (NCLAT) appeal.

While some automotive manufacturers chose to appeal to the COMPAT, others filed a writ petition in the High Court of Delhi, among others, challenging the constitutional validity of the decision-making process adopted by the CCI. This writ petition was successful, and the High Court of Delhi in April 2019 held that the decision-making process provided for in the Competition Act was unconstitutional. In its order, the court allowed the appellant automotive manufacturers to file an appeal against the order of the CCI to the NCLAT (the appellate authority) and directed the NCLAT to entertain the appeals on their merits, unhindered by any period of limitation. This order of the High Court of Delhi was appealed against before the Supreme Court.

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Currently, the matter is sub judice before the NCLAT. It is now on the appellate tribunal to hear and dispose of appeals against any direction issued or decision made or order passed by the CCI. The next hearing in the matter is on 26 April 2023.

In 2021, the CCI also dealt with matters relating to alleged anticompetitive conduct against Tata Motors and its related companies providing financial services, namely, Tata Capital Financial Services and Tata Motors Finance. The CCI dealt with *Neha Gupta v Tata Motors Ltd and Ors* and *Nishant P Bhutada v Tata Motors Ltd and Ors*, cases No. 21 of 2019 and No. 16 of 2020 (CCI, 4 May 2021) together as the anticompetitive activities alleged against Tata Motors and its related companies were similar in both cases. The matter was initiated based on complaints filed by the informants (automotive dealers having dealership contracts with Tata Motors) against Tata Motors and its related companies for their alleged anticompetitive conduct.

The informants primarily alleged that the terms and conditions imposed by Tata Motors in its dealership agreements were unfair and in contravention of the Competition Act. Some of the conditions indicated by the informants were imposition of high interest rates and other illegal charges and adjustments on the channel finance loan facility extended by the related companies of Tata Motors to automotive dealers. The informants claimed that these types of arrangements were detrimental to the financial health of the automotive dealers. Also, it was stated that consumer loan instalments, if unpaid by the borrowers, were adjusted arbitrarily against the channel finance loan facility provided to the automotive dealers. The informants further alleged coercion by Tata Motors in relation to the list of vehicles the dealers were required to order.

In response to the allegations, Tata Motors and its related companies questioned the jurisdiction of the CCI in dealing with contractual disputes and claimed that the related companies do not have a dominant position in the market as they attribute only a miniscule presence of 6 per cent share to the Indian corporate lending market. The CCI, while rejecting the contentions of Tata Motors and its related companies on its jurisdiction, directed the Directorate General to conduct an investigation within 60 days from an order dated 4 May 2021. It seems that the investigation is ongoing and, as per the information publicly accessible to date, no further orders are available.

Another landmark case relating to alleged anticompetitive practices against automotive companies was the *re: Alleged anti-competitive conduct by Maruti Suzuki India Limited (MSIL) in implementing discount control policy vis-à-vis dealers*, case No. 01 of 2019 (CCI, 4 July 2019). The CCI initiated an investigation into the matter based on an email sent by a Maruti Suzuki dealer anonymously alleging that MSIL resorted to resale price maintenance in Maharashtra, Mumbai and Goa. It was alleged that MSIL's independent agency performs 'mystery shopping audits' wherein a fake customer visits every dealer in Pune, for example, to check whether extra discounts are being offered. Based on this audit a penalty is levied where extra discounts are offered to end customers by dealers, and MSIL uses proceeds from these penalties for its expenses. MSIL, however, contended that it did not exercise control over its dealers, except to maintain uniformity in schemes, and that no agreement between MSIL and its dealers involved a discount control policy.

On investigating the alleged practice of resale price maintenance agreements between the dealers and MSIL, CCI concluded that MSIL's conduct of controlling discount given by

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dealers amounts to resale price maintenance, which causes an appreciable adverse effect on competition in India in the downstream market that is in violation of the provisions of the Competition Act. Consequently, CCI imposed a penalty of 200 million rupees on MSIL for its anticompetitive actions.

In another matter, *re: Cartelisation in the supply of Electric Power Steering Systems* (EPS Systems), Case No. 7(01) of 2015 (CCI, 9 August 2019), anticompetitive conduct was alleged in the electric power steering (EPS) systems market. The case was initiated on a lesser penalty application filed by NSK Limited, Japan, which revealed the existence of the cartel, and was followed by a lesser penalty application from JTEKT Corporation, Japan, during the investigation by the Directorate General. Through the investigation report and presented evidence, the CCI held both NSK and JTEKT liable for cartelisation in the EPS systems market for a period of about six years by directly or indirectly determining prices, allocating markets, coordinating bid responses and manipulating OEM bid responses. However, NSK was granted a 100 per cent reduction in penalty and JTEKT was granted a 50 per cent reduction in penalty, in view of their approaching the CCI with applications for lesser penalties.

Recently, in *Samaleshwari Automobiles v Tata Motors Ltd*, Case No. 44 of 2021 (CCI, 3 February 2022), allegations of anticompetitive practices against some of the major players in the Indian automotive industry such as Tata Motors and Tata Motors Finance were dealt with. The CCI found them guilty of contravening section 3 (anticompetitive agreement) and section 4 (abuse of dominant position) of the Competition Act, and ordered them to stop such practices while imposing a penalty. The case highlights the importance of fair competition in business practices, demonstrates how regulatory bodies work to ensure a level playing field for all market participants and serves as a warning to other companies that engaging in anticompetitive practices can result in significant penalties and legal consequences.

Over the years, investigations initiated by the CCI have been mainly based on claims brought by private parties or government authorities, either directly or indirectly aggrieved by the industry or party in question. There has not been much change in informants over the years, and they remain a mixture of private individuals, trade associations, chambers of commerce, direct competitors in the market, enterprises engaged in distributing activity for a dominant manufacturer and others. As a trend, we have seen the aggrieved parties approaching the higher courts in appeal, resulting in follow-on litigation in most cases.

Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

In the past few years, disputes relating to the automotive industry that have made headlines have primarily involved hurdles encountered during the acquisition of large pieces of land for setting up manufacturing plants, employee-related matters, product safety and quality, intellectual property, contractual issues and competition law violations.

Until early 2014, land acquisition was regulated solely by the Land Acquisition Act 1894, which was an archaic law. Although the Act permitted land acquisition by automotive companies, it became a platform for numerous farmers to challenge the adequacy of compensation

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given by the manufacturers and non-adherence of due process at the time of acquisition. This resulted in the stalling of projects until the matter had been decided by the courts or the companies reached an out-of-court settlement with the owners of the land. The most talked-about of such cases involved Tata Motors. In 2006, Tata Motors announced plans to set up a factory in Singur, West Bengal, for its small car project. Shortly after, it faced protests by farmers against the state government's proposal to acquire 997 acres of farmland. The unrest continued until 2008, when Tata Motors was forced to relocate its factory to the state of Gujarat. However, the government has made continued efforts to bring about legislation that makes the acquisition of land easier for the manufacturing industry. In 2014, the Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement Act 2013 was enacted with the aim of making the process fairer and more transparent. The government plans to propose new laws providing further benefits to the industries acquiring land.

Given the scale of the automotive industry, which involves the setting up of large manufacturing plants, often trade unions and worker associations are very strong and have the ability to influence the workers. Lately, one of the concerns for several automotive manufacturers has been unrest among workers who have been working as contract labourers continuously for a long period, but have not been absorbed by the companies as permanent employees. It was often found that these contract workers lacked the statutory benefits and protections available to a permanent employee. There are judicial precedents where the courts have come down heavily on industries for adopting such practices. However, with the changes introduced in the structure of Indian labour law, wherein the laws have been categorised in four labour codes, such issues are likely to be settled. Specifically, the draft Code on Social Security 2020 provides for contract labour to be entitled to receive social benefits as prescribed under this code, similar to the benefits applicable to employees of a company.

Over the years, automotive companies have experienced disputes with consumers in relation to quality control issues during aftersales services or the malfunction of the car on the roads.

Arbitration has become popular in the Indian automotive industry as it provides a speedy and efficient means of resolving disputes. In addition, automobile manufacturers have the option to seek interim injunctions from the courts, which are granted on a case-by-case basis after taking into account several factors and the circumstances of a case. In relation to labour issues, Maruti and other automobile companies have been seen to engage in negotiations and settlement with workers. This has been a quick solution for some but not for companies that spend a long time negotiating with their workers.

Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

There is no prescribed procedure or process for dealing with distressed suppliers of automobile components or spare parts. However, to avoid any slowdown or breakdown in the manufacturing process, it is usually considered in the best interest of the automobile manufacturers to provide financial support to extricate suppliers from their crunch.

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It has been seen that since the automobile manufacturers provide proprietary information to automobile part suppliers and vendors, several manufacturers are reluctant to let go of their suppliers and often take the commercial decision to extend financial help to the suppliers that would enable them to continue business.

Intellectual property disputes

12 | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

The automobile industry is one of the most innovative industries where intellectual property is a vital asset. Over the years, the industry has witnessed significant IP disputes ranging from patents to industrial designs and copyrights.

The aesthetic look of an automobile is the ultimate commercial feature for any company. Automobile leaders such as Mercedes-Benz, GM, Honda, Toyota, Tata, Bajaj and many more have established their own brands with unique design impressions. These industrial designs are extended protection under the Design Act 2000 upon registration with the relevant authority.

The Trade Marks Act 1999 provides, among others, for the registration of a trademark, filing of multiclass applications, increasing the term of registration of a trademark up to 10 years as well as recognition of the concept of well-known marks. The Indian courts provide a plethora of precedents wherein infringement or violation of the Trade Marks Act has been analysed, and the law has developed over the years through these precedents.

The Patent Act 1970 also plays an important role in the automobile industry. Any new invention in terms of technology can be granted protection when registered with the concerned authority. The software developed by automotive industries is also protected under the Copyrights Act 1957.

In recent years, the automotive industry has experienced a surge in patent applications, both domestically and internationally, with key players such as Tata Motors, Mahindra, TVS Motor, BMW and Ford leading the way. This is mainly due to the integration and wide use of computer applications in automobiles resulting in an upward trend in patent filing. In a study commissioned by the Federation of Indian Chambers of Commerce and Industry's Committee against Smuggling and Counterfeiting Activities Destroying the Economy, it was found that counterfeiting has been a major problem the automotive industry has been fighting for years. The Indian automobile industry is particularly vulnerable to counterfeiting, with 25 per cent of the market consisting of counterfeit components. Thus, as is apparent from the current scenario pertaining to IP laws in India and their application in the automotive industry, it can be said that registering an IP goes a long way and is extremely helpful when it comes to protection against IP theft.

The ease or difficulty with which IP disputes can be resolved vary from case to case depending on factors such as the defence of the opposing party, available evidence and the ability of the adjudicating authority or officer. Generally, disputes involving issues relating to trademarks

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are resolved relatively faster as opposed to those involving patents. This is primarily because trademark issues are less complex than those relating to patents.

There can also be delays because of the misadministration of such matters, but this has not gone unnoticed and the state high courts have been questioned by the Supreme Court of India over such delays. For example, in December 2007, Bajaj Auto filed a suit before the Madras High Court for an injunction against TVS Motor for the infringement of Bajaj's patent. The relief was awarded in February 2009 in terms of an interim injunction in favour of Bajaj restraining use of the patent by TVS. On an appeal by TVS before the superior division bench of the Madras High Court, the earlier order of the single judge was revoked. On further appeal by Bajaj before the Supreme Court of India, the Supreme Court expressed its discontent at the pendency of the IP matter before the state high court since December 2007 at the interlocutory stage and directed the state high court to commence the hearing of the suit on a day-by-day basis.

In March 2020, the High Court of Delhi granted a temporary injunction restraining the e-rickshaw manufacturer Om Balajee Automobile from manufacturing, exporting, importing, offering for sale, advertising or dealing goods (not just limited to e-rickshaws) bearing the mark DMW or any other mark that may be identical or deceptively similar to the BMW trademark. The court found the two marks DMW and BMW to be visually and phonetically similar, and acknowledged the reputed nature of the BMW trademark, thereby restraining Om Balajee Automobile from using similar marks.

EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

A unionised workforce is common in an organised industry such as automobile manufacturing. Companies with manufacturing operations in India have on many occasions witnessed labour unrest for a plethora of reasons, ranging from demand for an increase in wages to demand for reinstating terminated employees. One of the most talked about example is the fiasco that occurred at the manufacturing plant of Maruti Suzuki in 2012. The growing unrest among the workers was mostly owing to miscommunication between the management and the employees, demand for wage hikes, permanent employment, reinstatement of dismissed workers and demand for recognition of labour unions, among other reasons. Several automobile companies came under scrutiny for adopting the practice of hiring contract labour to do almost every job in a factory and keeping them without permanent employment, which would have required the provision of minimum statutory benefits to the workers. There seems to be growing consciousness among workers about this practice and a large proportion of workers are dissatisfied with the offered salaries and benefits. However, with the introduction of changes in the structure of labour laws in India, this matter has been addressed in the Code on Social Security 2020. Though the Code is yet to be published, it provides that contract labour must be entitled to prescribed social benefits, similar to those enjoyed by the employees of a company. In fact, even inter-state

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migrant workers are now included in the definition of contract labour, thereby expanding the provision of social security benefits to all workers.

In March 2013, a down-tools strike took place at Mahindra's automotive plant in Nashik, Maharashtra, because of differences over wage negotiations and suspension of a few workers. Similarly, in July 2016, workers at Honda Motorcycle & Scooter India held large-scale protests with the objective of reinstating employees who were leaders of the labour union. In October 2018, a large number of employees working at the plants of several motorcycle manufacturers located in Chennai, including Eicher Motors and Japan-based Yamaha Corporation, staged a walkout demanding higher wages and permanent employment for contract employees. Meanwhile, in March 2019, the employees from Asahi India Glass, a joint venture between Asahi Glass Japan and Maruti Suzuki India, went on strike against the unlawful dismissal and suspension of employees and demanded a wage increase.

In January 2020, the production of Honda Motorcycle & Scooter India's Manesar plant in Haryana and factories of various automotive component manufacturers in Manesar-Bawal industrial belt were affected by a day-long strike by 10 major trade unions pressing for a 12-point charter of demands of the working class relating to minimum wage, social security and other matters.

Toyota Kirloskar Motor faced a significant backlash from its workers (at their plant in Bidadi in the southern state of Karnataka) who went on a four-month-long strike from November 2020 until March 2021. The main concern of the employees seemed to arise from excessive workload without being allowed sufficient bathroom breaks or time to drink water. After various efforts by the state government and the concerned labour department, the differences were reconciled and the strike was lifted with a final appeal from Toyota Kirloskar Motor to its employees requesting them to return to work from 5 March 2021.

In February 2022, in the case of *Shankar Bhimrao Kadam and Ors v Tata Motors Ltd* (MANU/MH/0760/2022), the Bombay High Court held Tata Motors liable for unfair labour practices under the Industrial Disputes Act 1947. The dispute, which spanned over 17 years, was finally decided in favour of the workers. The High Court of Bombay held that Tata Motors was responsible for hiring hundreds of workers in its manufacturing unit as temporary employees, depriving them of the status and privileges of permanent employment. The court directed the company to pay compensation to the workers.

In May 2022, a strike involving over 2000 employees took place at Ford's plant in Chennai, causing production to come to a standstill. The strike was reportedly triggered by the workers' demand for improved compensation benefits.

In October 2022, around 350 permanent workers associated with the Renault-Nissan India Thozhilalar Sangam (RNITS) protested outside the United Labour Federation (ULF) – a trade union – office for a salary increase after working without a contract for four years. The ULF, the leading representative of RNITS, has been unable to improve workers' wages or demands. Some workers padlocked the ULF office and put up a notice expressing frustration with the lack of benefits achieved in the past three years. As a result, a group of workers is planning to form their own organisation to defend their rights.

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Over the years, one of the major reasons for employment disputes has been lack of proper communication channels leading to poor management of the employer–employee relationship. This can be attributed to the fact that the management often prefers to deal with an employees' representative, but the representative is usually driven by the agendas of only a section of the employees. This results in employees mistrusting the management.

There have been numerous cases brought before the courts involving unrest among workers owing to suspension or termination of employment, which have been challenged as being unfair or arbitrary by the trade union or the employee. These cases have been decided by the Indian courts depending upon the merits of each case.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

There have been some legal developments related to technology and incentives for using technology in the automotive sector. The government has introduced an electronic system of monitoring and enforcing road safety through notification GSR 575(E) dated 11 August 2021. It has introduced electronic enforcement devices that include speed cameras, closed-circuit television cameras, speed guns, wearable cameras, dashboard cameras, automatic number plate recognition, weigh-in machines and other prescribed technology specified by the state government (EE devices). Rule 167A of the Central Motor Vehicles Rules 1989 (the CMV Rules) provides that EE devices are installed by the state government at high-risk and high-density corridors on national and state highways and in critical junctions in major cities with a population of more than one million. EE devices are used to issue fines for offences such as speeding, not wearing a seat belt while driving or jumping red lights. The auto-generated challans issued by EE devices are accompanied with clear photographic evidence, date, time and place of the offence. EE devices have also paved the way towards paying e-challans electronically on the portal specified by the state government, making it convenient for the public to make payments in a timely manner.

In addition, a new Chapter XI has been introduced in the CMV Rules for recognition, regulation and control of automated testing stations that provide registration certificates to vehicles after they pass the prescribed tests. Automated testing stations file an application for registration to the transport commissioner who is nominated by the appropriate state government and is empowered to issue and renew registration certificates. Chapter XI lays down the procedure for fitness testing of vehicles through automated equipment, and explains the eligibility criteria for automated testing stations, their infrastructure requirement, manpower requirement, detailed testing process and procedures for all kinds of automobiles, as well as equipment required for testing and fees for granting registration certificates depending on test results. The appointment for a fitness test by any automated testing station is booked electronically through a portal set up by the central government. In the event the vehicle owner is aggrieved by the test results conducted by the automated testing station, he or she can appeal before the appellate authority (an officer not below

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the rank of regional transport officer nominated by the state government) on the electronic portal.

The government has attempted to introduce legislation to regulate advancements in automotive and mobility technology. However, most of these have not yet become law and are still in the nascent stages of development.

Such legislation includes the Geospatial Information Regulation Bill 2016, which proposes to regulate the acquisition, dissemination, publication and distribution of geospatial information. This includes geospatial imagery or data acquired through space or aerial platforms such as satellites, aircraft balloons or graphic or digital data depicting natural or man-made physical features, phenomena or boundaries of the earth. The bill proposes the creation of a Security Vetting Authority to carry out security checks on the geospatial information in India. The government has also launched a number of schemes to encourage growth in the automotive sector, such as:

- the Automotive Mission Plan 2016, which aims to increase domestic production of automobiles and automotive exports, and to address environmental and safety challenges;
- the National Automotive Testing and R&D Infrastructure Project, which has been set up to enable the industry to adopt and implement global performance standards by establishing nationwide automobile testing agencies;
- the National Electric Mobility Mission Plan 2020, which provides incentives to manufacturers and purchasers of electric cars;
- the Faster Adoption and Manufacturing of (Hybrid) and Electric Vehicles (FAME) Scheme, Phase II, which provides monetary incentives to producers and purchasers of eco-friendly vehicles in the country;
- the Production Linked Incentive Scheme introduced by the government in 2020 for large-scale electronics manufacturing including in the automotive sector. The scheme offers an incentive of 4 per cent to 6 per cent on incremental sales (over the base year) of goods manufactured in India to eligible companies, for a period of five years from the base year. Automobile manufacturers also view the scheme as an opportunity to reduce dependency on import to become net exporters; and
- private cab aggregators such as Ola and Uber have revolutionised public transport in India by introducing the concept of pool rides, aimed at providing cheaper rides to customers while being eco-friendly. The central government, by way of the MV Amendment Act, provides for conditions for the issuance of a licence to such aggregators and penalties in the case of contravention of relevant provisions applicable to them.

India is expected to witness the advent of self-driving vehicles due to the remarkable advancements in software and artificial intelligence across the board. Autonomous vehicles (AVs) are classified into six levels, ranging from zero (no autonomy) to six (complete autonomy), with level three autonomy vehicles gradually gaining popularity in India. Currently, vehicles are equipped with driver-assistance systems such as cruise control, lane departure warnings and some more advanced features. Given the nature of roads in India, it may be a while before higher or complete autonomy vehicles are introduced in the market.

Furthermore, India is yet to establish any laws regulating AVs, which may lead to disputes relating to intellectual property rights of the technology used in semi-autonomous and fully autonomous vehicles. The lack of regulations for AVs in India may also lead to uncertainties

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regarding licensing, usage and responsibility in the event of an accident. Additionally, the use of connected AVs raises privacy concerns as they collect vast amounts of data from both the environment and vehicle occupants, which could be vulnerable to cyberattacks, malware or hacking.

Currently, India is at a nascent stage when it comes to connected vehicles. Only a handful of connected cars are available in the country, including MG Hector, Kia Seltos, Nissan Kicks and Hyundai Venue. Moreover, as at now, there are no laws regulating connected vehicles or connectivity services in India.

Electric vehicles have become the topmost priority of the government recently. Several initiatives have been taken by the Ministry of Heavy Industries to promote adoption of electric vehicles, such as FAME scheme Phase II, where 745,713 electric vehicles have been supported with a resource of 3,200 million rupees, while 6,315 e-buses have been sanctioned to 65 cities and state entities across 26 states and union territories. The scheme provides incentives to buyers of electric vehicles via upfront reduction in the purchase price.

Currently, India is lacking an integrated regulatory framework to govern shared transportation and mobility services. The International Association of Public Transport, supported by Shakti Sustainable Energy Foundation, has come up with recommendations in the existing regulatory and financing mechanisms governing public transport by reviewing international scenarios and their feasibility for adoption in India. The study recognises the need for providing a multimodal shared transport system in Indian cities with high-quality public transport systems as its core.

UPDATE AND TRENDS

Trends and new legislation

15 Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

The amendments to the Motor Vehicles Act 1988 in 2019 through the MV Amendment Act have been one of the most important developments in the Indian automotive sector in recent years, for instance through introducing a mandatory recall mechanism. Another important development was the implementation of the Bharat Stage VI (BS-VI) emission standards with effect from 1 April 2020.

In relation to vehicles transporting tourists all over India, an important development has been the issuance of new draft rules for their operation under an all-India permit proposed by the Ministry of Road Transport and Highways.

Starting from 1 April 2023, the Indian automotive sector is complying with the Bharat Stage VI-B emission standards and other provisions. With the introduction of Bharat Stage VI-B engines for all new vehicles, including passenger vehicles, two-wheeler and commercial vehicles, the government is moving towards a cleaner and pollution-free tomorrow.

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This will make Indian vehicular emission standards equivalent to that of EURO VI. Some of the compliances required under the standards include:

- the government mandating passenger vehicles to reveal their Corporate Average Fuel Economy (CAFE-II) ratings; and
- car manufacturers being required to comply with Real Driving Emission (RDE) criteria. The RDE criteria mandate that car companies conduct the testing and measurement of the pollutants emitted from their vehicles in real-world driving conditions.

From April 2023, the government has also mandated that all cars must be manufactured with materials compatible with ethanol. By 2025, cars should be able to run on a blend of up to 20 per cent ethanol, in addition to gasoline. The goal of this mandate is to decrease the country's reliance on imported fuel and make progress towards achieving environmentally friendly transportation.

The Indian government's National Green Hydrogen Mission has been allocated 197 billion rupees in the national budget for 2023. The aim of this initiative is to encourage the use of hydrogen as a renewable and environmentally friendly energy source. This funding is expected to significantly contribute to achieving the country's green mobility objectives and ambitions.

The Ministry of Road Transport and Highways has issued various notifications, including:

- a procedure for accreditation of automobile testing agencies;
- a proposal for an amendment to the Central Motor Vehicles Rules 1989 (the CMV Rules) indicating that any vehicle carrying a dangerous or hazardous goods must be equipped or fitted with a vehicle tracking system device following automotive industry standards. This will enable owners to keep a track of all such carriages and ensure that goods that are hazardous and dangerous to human life are transported to the right locations;
- the introduction of Motor Vehicles (Registration and Functions of Vehicle Scrapping Facility) Rules 2021 and automated testing stations include the option to voluntarily cancel the registration of certificate, no dues application for vehicle scrapping, changes in the scrapping procedure, a definition clause, a procedure for testing automobiles and being declared as end-of-life vehicles, and other clauses to remove ambiguities in the procedure;
- taxes on automobiles to be levied online;
- the introduction of Inter-Country Non-Transport Vehicle Rules 2022, which regulate vehicles registered in countries other than India. However, these rules will be superseded by any bilateral agreements between India and other countries;
- through a notification dated 24 November 2022, a proposal for an amendment to the CMV Rules indicating that all government vehicle registration certificates must be cancelled on completion of 15 years from initial registration of the vehicle – except for special purpose vehicles used for operational purposes in defence of the country and for the maintenance of law, order and internal security;
- through a notification dated 2 February 2022, the government has mandated that starting from 1 April 2023 fitness testing for heavy commercial vehicles are allowed only through automated testing stations. Fitness testing for all other classes of commercial

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- vehicles and personal vehicles will be mandated through automated testing stations in a phased manner, starting from 1 June 2024; and
- through a notification dated 13 March 2023, the Ministry has amended the CMV Rules to include definitions of electric power train, pure electric vehicle and hybrid electric vehicle and its variations.



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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

The increasing popularity of electric vehicles is viewed as a significant trend in the automotive industry, and 5 per cent of the total car sales in Indonesia are expected to be electric vehicles by 2023. However, high prices, underdeveloped charging infrastructure and a

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nascent incentive and regulatory framework may pose challenges to a widespread adoption of electric vehicles. The government's incentive schemes and consideration of a reduced VAT on electric vehicle sales from 11 per cent to 1 per cent are strategic measures taken to facilitate a long-term transition to electric vehicles and sustain the overall growth of the automotive industry.

COMMERCIAL OPERATIONS

Regulation

2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

The manufacture and distribution of cars are governed and authorised by multiple government authorities, namely, the Ministry of Industry (MOI), the Ministry of Trade (MOT) and the Ministry of Transportation (MOTR). MOI generally authorises the automotive production process, which requires the manufacturer to obtain a business identification number (NIB) and standard certificate issued by the ministry. Distribution of automotive products falls under the supervision of MOT. Any party who undertakes the distribution of automotive products also requires an NIB.

Prior to production, assembly or importation of automotive products, vehicle type testing is required. Vehicle type testing is organised by MOTR through the Motor Vehicle Roadworthiness Testing and Certification Centre (BPLJSKB), which will examine multiple aspects of the products (eg, fuel tank, dimension, brakes, lights, speedometer and gas emission). By no later than three business days, BPLJSKB will issue a report based on the vehicle testing to MOTR, and MOTR will issue a vehicle testing approval or rejection within five business days of receipt of the report.

There is no mandatory insurance requirement for automotive products in Indonesia, although in practice almost all vehicles are insured to cover any potential damage or loss risk.

Development, manufacture and supply

3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

The Indonesian automotive supply chain structure is divided into three layers:

- the first layer is made up of assembler companies or OEMs that manufacture end products for the consumer market;
- the second layer is made up of Tier 1 companies that are suppliers to assembler companies; and
- the third layer includes Tier 2 companies that supply automotive parts directly to Tier 1 companies and do not offer automotive parts directly to assemblers or OEMs.

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Indonesian automotive manufacturers make and assemble intermediate goods (parts) and final goods (vehicles). Distributed vehicles in Indonesia may be built in the country of their origin (completely built up). In most cases, innovation, design, research and development are handled by parent companies. For vehicles that are manufactured or assembled domestically, several parts and components may be imported into Indonesia.

The relationship between manufacturer or producer and its supplier is usually business-to-business in nature and not strictly regulated by the government. The development of an automotive company can be conducted by product intensification, M&A transaction or OEM cooperation.

To avoid any supply issues, the Indonesian government has established several policies to nurture the automotive industry, including the Domestic Level Component policy and local production policy for technology transfer from foreign partners.

Distribution

- 4** | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

Distribution of vehicles by manufacturers is carried out by appointing distributors or dealers for the establishment of outlets, workshops and authorised sales or aftersales services (including the sale of spare parts).

Manufacturers are prohibited from selling the product directly to end customers. They must appoint distributors or dealers to distribute their products. Once the manufacturer appoints a distributor to sell the product, the distributor must further appoint a retailer or dealer to sell the product to end customers. Only the retailer or dealer is allowed to sell products (including automotive products) to the end customer.

Termination of distributor appointment can only be conducted on a clean-break basis, which must be reported to MOT. In such cases, vehicle manufacturers undertake to provide spare parts and aftersales services to be carried out by newly appointed agents or distributors. If there is no intention to nominate a new agent or distributor, the law requires the manufacturer to supply spare parts or aftersales services through the terminated agents or distributors for a minimum period of two years from termination. This is intended to protect customers.

Mergers, acquisitions and joint ventures

- 5** | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

There are no specific requirements for M&A or JV transactions for the automotive industry. In general, M&A transactions must comply with requirements under the Indonesian Company Law and satisfy requirements under a target company's articles of association, including

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the requirement to obtain approval from the shareholders of the target company, and the transfer of shares must be made in a notarial deed and reported to or approved by the Ministry of Law and Human Rights. Specific to acquisition transaction (involving majority shares of the target company), there is a mandatory pre- and post-acquisition announcement (in at least one daily newspaper), which is intended to inform the target company's creditors, and also an announcement to the target company's employees. Any objections from the creditors must be settled before the acquisition transaction can proceed. However, objections from the employees have no effect on the transaction process.

Considering that the automotive industry usually involves significant investment, it is also worth checking whether the acquisition transaction needs to be notified to the Indonesia Competition Commission if the notification threshold is met (ie, 2.5 trillion rupiahs of global assets or 5 trillion rupiahs of domestic sales or revenue).

Incentives and barriers to entry

6 | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

The Indonesian government has provided several incentives for investment in the automotive industry, especially in the production of electric vehicles. These incentives are aimed at accelerating the transformation of the Indonesian economy towards a green economy, which is expected to result in high-value-added economic activities, job creation, energy subsidy efficiency and a reduction in carbon emissions. These measures include:

- tax holiday of up to 20 years for investments in the manufacturing of motor vehicles and their main components;
- supertax deduction of up to 300 per cent for companies conducting research and development related to electric vehicles; and
- electric vehicles running on battery power are exempt from the luxury goods sales tax, while conventional vehicles are subject to a tax rate of 15 per cent to 95 per cent depending on emission levels.

In addition, the Indonesian government has exempted import duty for the importation of incomplete knock-down electric vehicles.

These policies aim to grow public interest in buying automotive products, which in turn will increase sales figures.

Underdeveloped charging infrastructures and public reluctance to convert from conventional vehicles to the relatively new electric vehicles may cause significant entry barriers to the market. These entry barriers, however, could be eliminated in the future through the government's expansive promotion of and support for the development of electric vehicles.

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PRODUCT SAFETY AND LIABILITY

Safety and environmental

- 7** | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

Type tests and periodical tests are conducted to ensure the safe operation of motor vehicles. Type tests concern the physical condition of the motor vehicle and assess its compliance with technical and roadworthiness requirements, as well as its design and engineering prior to production, assembly or mass importation. Tests are carried out periodically for all motor vehicles and the Ministry of Transportation (MOTR) issues a certificate for both tests when passed by motor vehicles.

In addition to the above, manufacturers are required to register types of motor vehicles that are produced, assembled, imported or modified through filing an application to the relevant directorate general at MOTR, along with a copy of the type test certificate and the application fee for the issuance of a type test registration certificate. The type test registration certificate is a prerequisite document for registering and identifying the motor vehicle, and for obtaining the vehicle registration certificate and plate.

Failure to undergo the type test and registration will result in administrative sanctions in the form of warnings and fines imposed by MOTR.

MOTR governs the requirements and technicality of product recalls.

Product liability and recall

- 8** | Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

With respect to product recalls, the Indonesian Consumer Protection Law generally provides that business owners or applicants are prohibited from producing or selling goods or services that do not meet or are not in accordance with the required standards and provisions of laws and regulations, or are not in accordance with the condition, guarantee, speciality or efficacy stated on the label, tag or information provided about the said goods or services. Failure to comply results in the business owner or manufacturer or importer having to recall the goods from circulation.

With respect to automotive products, if the type test certificate is obtained and later on a defect in the motor vehicle is discovered, it must undergo a recall. Manufacturing defects comprise design flaws (concerning systems or components that are not in accordance with the established design quality standards) and manufacturing errors (during the assembling or manufacturing process, resulting in the motor vehicle not performing optimally). MOTR, through its ministerial regulations, requires manufacturers, importers and agents to have standard operating procedures in place for recalls.

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In January 2021, a group of consumers brought a class action suit against a Chinese automobile manufacturer at the South Jakarta District Court due to certain 1.5 CVT Turbo cars' performance. Prior to submitting the claim, the consumers had reported the issues to the manufacturer and had tried to repair their cars. As the problem persisted, the consumers escalated their complaint to a local consumers community and decided to submit a claim to the South Jakarta District Court. The consumers claimed that the cars' inability to perform uphill acceleration has caused material, as well as immaterial, losses and this can be deemed as a hidden defect that was not disclosed by the dealers. The South Jakarta District Court issued a decision in favour of the Chinese automobile manufacturer due to lack of evidence submitted by the claimants. Accordingly, the tort accusation against the Chinese automobile manufacturer was not substantiated. This decision was reinforced by a Jakarta High Court decision in 2023.

DISPUTES

Competition enforcement

9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

The Indonesia Competition Commission (KPPU), through its multi-faceted role, can monitor, investigate, prosecute and enforce any violations related to the Indonesian Competition Law.

The KPPU has investigated and decided on several past cases in relation to the automotive industry, namely, the tyre cartel case and the automatic scooter cartel case investigated in 2014 and 2015, respectively. More recently, in 2023, KPPU conducted a preliminary examination on two vehicle component manufacturers for allegedly violating market arrangements regarding air conditioning systems. KPPU has continued to have a heightened interest in the automotive industry – as with any competition authority around the world – and has investigated distribution schemes in the motorcycle industry, exclusivity arrangements in the distribution of automotive lubricants and pricing of low-cost green cars. Therefore, both horizontal (between competitors) and vertical (with suppliers or distributors) market competition in the automotive industry are under KPPU's scrutiny.

In several instances, KPPU has raised concerns regarding association meetings in the automotive industry, especially when there is potential for exchange of information on production capacity and plans.

There was a follow-on litigation in relation to the scooter cartel case; however, the Supreme Court of the Republic of Indonesia upheld the lower court's decision that the case is inadmissible. However, this was the first follow-on litigation and business owners must remain vigilant.

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Dispute resolution mechanisms

- 10** | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

Issues in the automotive industry commonly arise due to contractual as well as product liability, involving either the manufacturers, dealers or consumers. Alternative dispute resolution seems to be the preferred mechanism for resolving consumer disputes in the automotive industry. Litigation or arbitration appear not to be the first choices in resolving issues as there is very limited case file history in the public case repository.

From the consumer protection perspective, issues relating to the use of automotive products can also be resolved by the Consumer Dispute Settlement Agency.

Indonesia recognises the interim injunctions procedure for intellectual property and civil cases, but a full lawsuit must be lodged with the court, as an injunction cannot be sought independently under procedural law.

Distressed suppliers

- 11** | What is the process for dealing with distressed suppliers in the automotive industry?

Current prevailing regulations in Indonesia are silent on the process of dealing with distressed suppliers in the automotive industry. Commercial discussions, as well as negotiations, are common and are undertaken to either mitigate or resolve issues surrounding the distressed suppliers. Should commercial discussions be deemed ineffective, the aggrieved party may pursue a legal remedy by following general dispute mechanisms, preceded by filing warning letters, right up to submitting a claim either to the relevant court or arbitration body as the preferred forum under the agreement.

Intellectual property disputes

- 12** | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

The legal framework of intellectual property (IP) protection in Indonesia has been established, comprising the protection of trademark, copyright, patent, industrial design, geographical indication and trade secrets, as well as the layout design of an integrated circuit. The regulations govern the rights and obligations of the IP owners, as well as registration procedures up to dispute resolution mechanisms. In addition, Indonesia has a designated authority for matters relating to IP, namely the Directorate General of IP (DGIP) of the Ministry of Law and Human Rights.

In general, IP disputes can be resolved either through litigation in court or alternative dispute resolution. For the in-court litigation process, IP disputes on trademark, copyright and patent infringement need to be filed with the relevant commercial court, while disputes on

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trade secrets must be filed with the relevant district court in Indonesia. Within the past three years, there have been some trademark infringement cases in the automotive industry. IP disputes are settled in the commercial courts that are only available in certain major cities, namely, Jakarta, Semarang, Surabaya, Medan and Makassar.

With respect to alternative dispute resolution, the DGIP concluded a memorandum of understanding (MOU) with the World Intellectual Property Organization on the provision of alternative dispute resolution services to parties involved in cases filed with the DGIP in May 2014. The MOU was deemed necessary as Indonesia reasoned that alternative IP dispute resolution needs to be improved in the country. Prior to the MOU, in 2012 Indonesia established an IPR Arbitration and Mediation Agency (BAM HKI). However, the Supreme Court of the Republic of Indonesia directory does not disclose the registration statistics of the BAM HKI award at the district court for enforcement purposes. In addition, through arbitration proceedings, parties can resolve IP disputes by negotiation or mediation, as well as conciliation between the parties.

EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

Apart from the ratification of the Convention No. 98 of the International Labour Organization concerning the application of the principles of the right to organise and to bargain collectively, the Indonesian law recognises trade unions through Law No. 21 of 2000 on the Labour Union (Labour Union Law) – enacted on 4 August 2000. The Labour Union Law guarantees the employees' rights to establish trade unions to create harmonious dynamics and fair industrial relations with employers. There is a minimum requirement of 10 employees to establish a trade union, which must be registered with the local human resources office, as well as the employer. The Labour Union Law also allows the establishment of a trade union federation, which comprises a minimum of five trade unions, as well as a trade union confederation with a minimum of three trade union federations.

As a rule of thumb, Law No. 13 of 2003 on Manpower (the Manpower Law), as amended by Government Regulation in Lieu of Law No. 2 of 2022 (the Job Creation Law) – enacted on 25 March 2003 and amended on 30 December 2022 – provides that company regulations and obligations of the employer and its employees must be notified to the relevant human resources office if the number of employees is 10 or more. If the employees then decide to form a trade union, a collective labour agreement can be concluded and must also be registered with the relevant human resources office.

Another notable provision relating to employment issues is the amended termination grounds, as well as the multiplier of severance payment for terminated employees. Prior to the enactment of the Job Creation Law, termination grounds were governed under several provisions in the Manpower Law. Currently, the provisions have been unified under article 154A of the Job Creation Law where termination is allowed due to inefficiency, either to prevent losses or after losses have been suffered by the employer. In addition, the Job

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Creation Law introduces different multipliers of severance payment for certain termination grounds. These new provisions have sparked controversy as they are deemed to adversely affect the terminated employees' rights.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

The Indonesian government has announced its intention to develop electric vehicles in the country. This is reflected by the issuance of specific regulations pertaining to electric vehicles, such as:

- Presidential Regulation No. 55 of 2019 regarding Acceleration of Battery-Run Electric Vehicle Programmes (PR 55/2019) – enacted on 12 August 2019;
- Ministry of Transportation (MOTR) Regulation No. 44 of 2020 regarding Type Testing for Electric Vehicles (MOTR Regulation 44/2020) – enacted on 22 June 2020, as amended by MOTR Regulation No. 86 of 2020 on 16 December 2020;
- Ministry of Industry (MOI) Regulation No. 6 of 2022 regarding Specification, Road Map Development and Local Content Calculation for Battery-Run Electric Vehicles (MOI Regulation 6/2022) – enacted on 11 March 2022;
- MOI Regulation No. 28 of 2020 regarding Electric Vehicles in Completely Knocked Down and Incomplete Knocked-Down Conditions (MOI Regulation 28/2020) – enacted on 17 September 2020, as amended by MOI Regulation No. 7 of 2022 on 11 March 2022;
- Presidential Instruction No. 7 of 2022 regarding the Use of Battery-Run Electric Vehicles as Official Operational Vehicles for the Central and Regional Government Institutions (PI 7/2022) – enacted on 13 September 2022;
- Ministry of Finance (MOF) Regulation No. 153/PMK.010/2020 regarding the Granting of Gross Income Tax Deduction for Certain Research and Development Activities in Indonesia – enacted on 9 October 2020;
- MOF Regulation No. 130/PMK.010/2020 regarding the Provision of Corporate Income Tax Reduction Facility – enacted on 9 October 2020; and
- Government Regulation No. 74 of 2021 regarding the Amendment to Government Regulation No. 73/2019 on Taxable Goods Classified as Luxury in the Form of Motor Vehicles Subject to Sales Tax on Luxury Goods – enacted on 2 July 2021.

PR 55/2019 serves as an umbrella regulation on the development of electric vehicles in Indonesia. Several key provisions under PR 55/2019 include the calculation of local content for automotive products from 2019 until 2026 and onwards, ensuring the availability of charging depots for electric vehicles and provision of fiscal and non-fiscal incentives for manufacturers of electric vehicles.

The local content requirement for electric vehicle manufacture is further regulated under MOI Regulation 6/2022, as follows:

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- 50 per cent for 2020–2023 and 58 per cent for 2024 and beyond, for local content for the manufacture of main components;
- 10 per cent of local content for the manufacture of supporting components;
- 20 per cent for 2020–2023 and 12 per cent for 2024 and beyond, for local content for assembly activity; and
- 20 per cent of local content for development activity.

Similar to conventional vehicles, electric vehicles need to pass type testing conducted by the Motor Vehicle Roadworthiness Testing and Certification Centre (BPLJSKB). However, the electric vehicle accumulator testing can be provided by another entity, such as:

- a domestic type-testing laboratory that has been certified by the National Accreditation Body of Indonesia;
- a foreign type-testing laboratory body that has been certified by Asia Pacific Accreditation Cooperation and International Laboratory Accreditation Cooperation; or
- another accredited international laboratory.

The result of accumulator vehicle testing will be a preliminary document on type testing by the BPLJSKB. The type testing by BPLJSKB will focus on direct contact components in electric vehicles, functional safety and hydrogen emission.

The Indonesian government has also issued a regulation that provides additional tax breaks for electric vehicles, and is currently drafting a new regulation to boost sales of electric vehicles.

UPDATE AND TRENDS

Trends and new legislation

15 Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

In the Jakarta metropolitan area, electric vehicles are exempted from the odd-even licence plate policy currently being imposed in the city. The aim is to encourage people commuting around Jakarta to move from using conventional vehicles to electric vehicles.

Indonesia is making significant strides towards sustainable energy, with the government taking a proactive approach to reducing carbon emissions. The issuance of Presidential Regulation No. 7 of 2022 is a clear indication of the government's commitment to support the use of electric vehicles in the country. The regulation further emphasises the government's seriousness about reducing carbon emissions and promoting the transition to sustainable energy. It aims to reduce carbon emissions by deploying electric vehicles, which were used expansively during the G20 Summit held in November 2022. The government's commitment to reducing emissions is further demonstrated by its plan to provide subsidies for the purchase of electric vehicles in 2023.

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The Indonesian automotive industry is experiencing significant transformation, with the government aiming to have at least two-million electric vehicles on the roads by 2025. The growth in the middle- and upper-class households in the country provides a vast potential for the development of electric vehicles. The domestic automotive industry is aiming to produce 600,000 units of electric cars and electric buses by 2030, which would significantly reduce fuel consumption and CO₂ emissions. Furthermore, the government has introduced tax policies that incentivise the use of environmentally friendly vehicles.

One of the challenges facing Indonesia's electric vehicle industry is the diversity of the market and the types of vehicles available. Small cars or B-segment cars account for about 50 per cent of the market, while commercial vehicles or light commercial vehicles make up 20 per cent of the market. To support electrification in the transportation sector, the government needs to understand the market and its diversity and strengthen the potential of the nation's renewable energy sector. Development of nickel and battery cell industries would also support the growth of the electric vehicle industry by providing cheaper and more efficient battery technologies.



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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

The Italian car market is among the largest in Europe alongside Germany, the UK, Spain and France (which represent 70 per cent altogether).

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Based on the estimates in a recent study by the Italian Association of the Automotive Industry (ANFIA), under normal circumstances Italy's automotive industry and supply chain accounts for approximately 5 per cent of the GDP with (roughly) €90 billion overall turnover, involving some 5,700 enterprises, many of which are small and medium-sized, employing around 250,000 workers.

In 2022, the Italian car market continued to suffer the devastating economic impact of the covid-19 outbreak. ANFIA reports that in December 2022 there was a 21 per cent increase in industrial production of vehicles compared to 2021. However, compared to 2019, the delta in industrial production of vehicles is negative with a 9.7 per cent decrease. Indeed, for the third year in a row, the automotive industry has lost a significant share of returns with double-digit contractions.

Factors such as the impact of employee sickness, supply chain issues and the major chip shortage should be taken into consideration. The first two months of 2023 seem to show signs of improvement – notwithstanding the persisting chip shortage and the war in Ukraine. For example, in January 2023, 128,437 registrations were reported, a 19.7 per cent increase compared to the 107,826 registrations in January 2022 (but a 22.4 per cent decrease compared to January 2019).

Moreover, in 2023, the automotive sector – on the one hand still severely impacted by the covid-19 outbreak and the enduring chip shortage as well as the financial effects of the war in Ukraine, but on the other experiencing six months of recovery – shows signs of upturn even if the road to a complete recovery is still full of obstacles.

Among other issues, the European Council's discussion concerning the approval of a regulation that prevents companies from selling combustion vehicles starting from 2035 deserves our attention. Such a proposal, according to Confindustria Lombardia, will endanger 15,000 to 20,000 jobs. The timing of the outcome of approval proceeding is not currently known, as COREPER has postponed its green light to a date yet to be set. Before the regulation's approval, companies working in the automotive sector may lobby the European Commission in favour of e-fuels – innovative fuels that can be used in combustion engines and lower or offset CO₂ emissions. If the e-fuel approach is adopted, combustion vehicles can be sold after 2035.

A final matter concerns the discussion at the European Commission of a proposal about new Euro 7 provisions regarding diesel and gasoline engines aimed to fulfil the EU's ambitious emissions goals. Automotive industry representatives have expressed their doubts about this proposal. Following this approach, companies would be forced to pour financial resources into engines that may cease to reach the market after 2035.

It remains to be seen how these two issues will intersect. In fact, allowing companies to sell combustion engine vehicles starting from 2035 may facilitate the approval of new provisions concerning Euro 7.

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COMMERCIAL OPERATIONS

Regulation

- 2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

In Italy, the applicable rules are based on European legislation.

Type approval

Effective from 1 September 2020, Regulation (EU) 2018/858 (as amended by Regulation (EU) 2019/2144, implemented by Commission Delegated Regulation (EU) 2021/535 of 31 March 2021 and supplemented by Commission Delegated Regulation (EU) 2021/1243 of 19 April 2021; Commission Delegated Regulation (EU) 2021/1244 of 20 May 2021 as regards Annex X; Commission Delegated Regulation (EU) 2021/1445 of 23 June 2021 as regards Annex II and VII; Commission Delegated Regulation (EU) 2022/2236 of 20 June 2022; and completed by Commission Delegated Regulation (EU) 2022/1209 of 5 May 2022) regulates the approval and market surveillance of motor vehicles and their trailers, and of systems, components and separate technical units intended for such vehicles, repealing Directive 2007/46/EC that had been implemented in Italy by the [Ministry of Infrastructures and Transport Decree of 28 April 2008](#).

Regulation (EU) 2018/858 contains administrative provisions and technical requirements for type approval and placing on the market of all new vehicles, systems, components and separate technical units and for individual vehicle approvals. It also lays down provisions for the placing on the market and the entry into service of parts and equipment that may pose a serious risk to the correct functioning of the essential systems of the vehicles, as well as requirements for the market surveillance of vehicles, systems, components and separate technical units that are subject to approval, and of parts and equipment for such vehicles. According to article 13 of the Regulation, manufacturers must ensure that the vehicles, systems, components and separate technical units that they have manufactured and that are placed on the market have been manufactured and approved in accordance with applicable requirements. Manufacturers will be responsible to the approval authority for all aspects of the approval procedure and for ensuring conformity of production.

Regulation (EU) 2018/858 has been implemented by:

- Commission Implementing Regulation (EU) 2020/683 of 15 April 2020 (concerning the administrative requirements for the approval and market surveillance of motor vehicles and their trailers, and of systems, components and separate technical units intended for such vehicles), as recently amended by Commission Implementing Regulation (EU) 2022/195 of 11 February 2022;
- Commission Implementing Regulation (EU) 2020/1812 of 1 December 2020 (concerning the online data exchange and notification of EU type approvals);
- Commission Implementing Regulation (EU) 2021/133 (concerning the basic format, structure and the means of exchange of the data of the certificate of conformity in electronic format);

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- Commission Delegated Regulation (EU) 2021/1445 of 23 June 2021 (amending Annexes II and VII to Regulation (EU) 2018/858 of the European Parliament and of the Council);
- Commission Delegated Regulation (EU) 2022/1209 of 5 May 2022 (supplementing Regulation (EU) 2018/858 of the European Parliament and of the Council, as regards the procedure for the imposition of administrative fines and the methods for their calculation and collection); and
- Commission Delegated Regulation (EU) 2022/2236 of 20 June 2022 (amending Annexes I, II, IV and V to Regulation (EU) 2018/858 of the European Parliament and of the Council).

Regulation (EC) 715/2007 on type approval of motor vehicles with respect to emissions from light passenger and commercial vehicles (Euro 5 and Euro 6) – which has been updated by Regulation (EU) 2018/858, as amended by Regulation (EU) 2019/2144 – provides emissions requirements related to the type-approval process. In addition, some rules for in-service conformity, durability of pollution control devices, on-board diagnostic systems, measurement of fuel consumption and accessibility of vehicle repair and maintenance information are provided (the latter are also contained in Annex X of Regulation (EU) 2018/858 as amended by Commission Delegated Regulation (EU) 2021/1244 of 20 May 2021). In November 2022, the Commission proposed new Euro 7 standards to reduce pollutant emissions from vehicles and improve air quality.

Manufacturers have an obligation to demonstrate that all vehicles sold, registered or put into service in the European Union are type approved in compliance with this Regulation. In addition, manufacturers' obligations include meeting the emission limits set out in Annex I of the Regulation.

Regulation (EC) 661/2009 on type-approval requirements for the general safety of motor vehicles, their trailers and systems, components and separate technical units intended therefor sets out the technical requirements and the procedures to ensure that new motor vehicles (motor vehicles with at least four wheels used to transport passengers, motor vehicles with at least four wheels intended for goods transport and trailers) meet EU safety and energy efficiency standards. In particular, this regulation establishes requirements for type approval of the safety of motor vehicles and their trailers, the energy efficiency of motor vehicles (the installation of tyre pressure monitoring systems and gear shift indicators is mandatory), and the safety and energy efficiency of tyres and their levels of noise emission.

According to article 5 of the Regulation, car manufacturers must ensure that their vehicles are designed, constructed and assembled 'to minimise the risk of injury to vehicle occupants and other road users'. This regulation has firstly been amended by Commission Regulation (EU) 2019/543 and will eventually be repealed by Regulation (EU) 2019/2144, which is already in force and applies – with specific regard to the above repeal – effective from 6 July 2022.

Very recently, Commission Delegated Regulation (EU) 2022/545 of 26 January 2022 supplemented Regulation (EU) 2019/2144 (as amended by Commission Delegated Regulation (EU) 2022/1398 of 8 June 2022) by laying down detailed rules concerning the specific test procedures and technical requirements for the type approval of motor vehicles with regard to their event data recorder and for the type approval of those systems as separate technical units (including in accordance with UN Regulation No. 160) and amending Annex II to that Regulation. These rules apply as of 6 July 2022.

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EU-type approval is granted by the Italian authorities if the concerned vehicles comply with the applicable regulations.

In Italy, the Directorate-General for Motor Vehicles of the Department of Land Transport and Intermodal Transport of the Ministry of Infrastructures and Transport, pursuant to article 75 of the [Italian Highway Code](#), grants type approvals to vehicles that are in compliance with the European regulations mentioned above.

Registration requirements

Owners of motor vehicles have an obligation to register their vehicles pursuant to article 75 et seq of the Italian Highway Code.

Pursuant to the [Decree of the Ministry of Sustainable Infrastructures and Mobility of 26 May 2021](#), vehicles of an approved type intended for the carriage of persons as well as vehicles not complying with Regulation (EU) 2018/858 or Directive 2007/46/EC or type approved with derogations from the requirements of previous EU provisions are subject to the requirements of suitability for circulation and type approval.

With [Circular No. 28779 of 15 September 2022](#) (Supplementing Circulars Nos. 27072 of 31 August 2022 and 27885 of 7 September 2022, in line with prior Circulars Nos. 414 of 10 January 2022, 26311 of 24 August 2021, 26584 of 30 August 2021, 26878 of 1 September 2021, 27566 of 7 September 2021, 29095 of 21 September 2021, 30589 of 5 October 2021, 31963 of 15 October 2021, 32585 of 22 October 2021 and 33952 of 4 November 2021), the Ministry of Infrastructures and Transport authorised some derogations from registration of end-of-series vehicles, pursuant to article 49, paragraph 1 of EU Regulation 2018/858 for vehicles not conforming to Regulation ECE-R58.03, with effect for registrations from 1 September 2021.

However, the registration of the vehicle can only succeed if the vehicle has been type approved by the authorities.

Insurance requirements

Directive 2009/103/EC of 16 September 2009 relating to insurance against civil liability in respect of the use of motor vehicles, and the enforcement of the obligation to insure against such liability is transposed in the [Italian Private Insurance Code](#). Pursuant to article 122 of the Code, car owners have an obligation to insure their vehicles. In addition, [Decree of the Ministry of Economic Development of 11 March 2020, No. 54](#) provides for the conditions of the mandatory insurance standard contract for civil liability posed by the use of motor vehicles.

Development, manufacture and supply

- 3** | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

Overall, the motor vehicle production output nosedived considerably during the covid-19 pandemic. Indeed, in April 2020, the total motor vehicle production volume (which includes

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finished motor vehicles and bodies, trailers and semi-trailers, as well as parts and accessories) across the 27 European member states had a volume index of only 16.4, compared with the 2015 baseline of 100.

Production levels began to climb back towards the end of 2020, but chip shortages and other supply chain uncertainties became the main cause of concern between December 2020 and March 2021. In 2022 and, in particular, between August and September, the Italian automotive market sector registered a growth of 14.6 per cent compared to October 2021, which with 101,103 units had recorded a 36 per cent year-on-year decrease. However, the fragility of the global scenario and the risk of a technical recession in the latter part of the year have impacted the automotive sector, leading it to close 2022 at about 1,300,000 registrations, a 10.8 per cent decrease compared to 2021 and 158,000 fewer units, a volume equal to the historical minimum recorded in 2013 with 1,304,000 cars. The beginning of 2023 has been positive for the automotive market, which has recorded 128,301 registrations in Italy, up by 18.96 per cent compared to January 2022. This brought volumes back to the first month of 2021, although the figure remains 22.4 per cent lower than the pre-pandemic situation in January 2019.

Although the sector in general is growing in Europe, new vehicle registrations are still being affected by weak demand due to the pandemic and the negative events that have followed, from the war in Ukraine to the energy crisis, to the return of inflation and the rising cost of living.

Notwithstanding the above, the number of motor vehicles registered in Italy secures the country's position as one of the largest markets in the European Union, together with Germany, France and Spain, thus confirming its attractiveness to global motor manufacturers. The Italian automotive market is still dependent on Italian brands, with Fiat alone taking up to 15 per cent of the market share, a percentage that goes up to 38.9 when considering the new Stellantis Group. According to recent European trends, the development of mechanical and technological components for city and family cars is a result of collaboration agreements with other leading European or US companies, or between car manufacturers. Designs, however, tend to be developed internally as they constitute one of the core commercial assets of car companies.

Differences arise with respect to luxury brands, as they represent one of the leading manufacturing sectors in Italy. In the case of luxury brands, nearly all phases of the development, design, assembly and sales of vehicles are protectively dealt with internally by Italian automotive companies.

As for components and spare parts, there is a tendency in Italy to outsource, on the one hand, and to directly (or indirectly) manage secondary businesses, on the other hand. Leading Italian companies tend to own or indirectly invest in the companies in charge of manufacturing and supplying their main mechanical components, body components and spare parts.

Both the transportation of vehicles, by means of car carriers, and that of spare parts is outsourced to professional transporters that also take care of customs duties.

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The selection of external companies is usually on a semi-exclusive or non-exclusive basis, takes place by means of bidding invitations and is addressed to pre-selected competitors on the market. Often these companies tend to enter into subcontracting agreements with authorised local and family-owned entities.

Distribution

4 | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

Generally, in Italy vehicles are distributed through selective distribution agreements entered into by local manufacturing companies, or the local representatives of foreign manufacturers, and autonomous Italian entities. The business dimensions of dealers vary depending on the geographical regions in which they are located. In the central and northern regions and within the main Italian cities, dealers are usually representative of rather structured and economically sound companies owning more than one dealership. In the south of Italy and in smaller towns, where there might be a more evident economic depression, dealers tend to be small, family-owned companies.

With respect to contractual relationships, sales agents are often linked to dealers by means of agency agreements.

Notwithstanding the general distribution mechanism, leading Italian automotive brands have recently developed new forms of sales chains through which they set up fully owned large dealerships where manufacturers promote and sell multiple vehicle brands. Clients are, therefore, offered the chance to see different car types and receive different services (sale, maintenance, repairs, post-sale assistance and so on) within the same vast premises. Following the Italian lead, German and French-based manufacturers have adopted the same business model in Italy and have opened fully owned car dealerships in major cities such as Rome and Milan.

With reference to distribution agreements, due to the automotive market crisis experienced in the past decade, the number of mono-brand dealers has largely diminished over the years leaving space for multi-brand dealers, which are increasingly specialising in post-sale assistance services (eg, car registrations, services for disabled people accessing state benefits, maintenance, repairs and contractual warranties) and captive services (eg, loans, insurance contracts, leasing and car rentals).

The recent economic developments in the automotive sector have prompted the expansion of new smart mobility models in Italy with the aim of minimising traffic, making driving safer and smoother, and reducing travel by individuals in high-consumption vehicles in favour of alternative means of transport such as rentals and car-sharing. This development has been promoted as a way to avoid overcrowding public transport, decongest urban traffic and improve air quality. That said, since the covid-19 pandemic, cautious behaviour has kept citizens away from shared mobility options. To reverse this cautious approach and increase public trust in shared mobility, sharing operators and short-term rental companies apply thorough vehicle hygiene protocols to reassure users as much as possible and safeguard

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these forms of mobility from future shocks. With this aim, national and local legislation is fostering the use of alternative means of transport, in particular in the biggest Italian cities, by offering cashback on vehicle-sharing services or purchase of new bicycles or other electric micro-mobility vehicles such as e-scooters.

According to recent data, after the pandemic, the mobility sector registered a very positive increase in the use of alternative means of transport including bicycle and scooter sharing and, most of all, e-scooters, which represent 40 per cent of the total offer of shared mobility services. In general, data from 2021 shows that use of vehicle sharing services (car, scooter and bicycle sharing) has increased to its pre-pandemic level: the total number of trips made in shared mobility was about 35 million, plus 61 per cent compared to 2020 and 25 per cent more than in 2019, and 83 per cent of rentals consist of micro-mobility vehicles, which now play a crucial role in sustainable urban mobility. Sharing mobility fleets also continue to grow, from 84,600 vehicles in 2020 to around 89,000 vehicles in 2021, split between scooters (51 per cent), bicycles (31 per cent) and cars (7 per cent). In addition, fleets are becoming lighter, smaller and more electric: electric vehicle usage rose from 63 per cent to 77 per cent in the past year. Shared mobility is also becoming increasingly green with 94.5 per cent of shared vehicles having zero emissions. The sector's turnover is likewise growing, reaching 130 million. The market is indeed consistently promoting long-term rentals of vehicles as opposed to vehicle purchase (especially hybrid and electric), leveraging on the advantages given by the lack of bureaucracy (from an insurance, tax and maintenance perspective) and by deferred fees without the need for an upfront payment. Seeking to benefit from this growing market, in recent years car manufacturers have been willing to get directly involved in offering long-term rental services, which often include a recurrent option to update the rented vehicle to a new model in exchange for a small additional fee, therefore generating a virtuous circle in terms of new vehicle production. The increasing trend is also moving towards more efficient, eco-friendly, luxury and high-performing cars becoming available to a wider share of users than before.

Interestingly, the Italian Council of State has reformed the previous government's position on the matter and ruled in favour of sales of vehicles online through e-commerce channels. Despite this new overture, the practice of selling cars online has still not caught on in Italy, probably owing to practical difficulties and a cultural approach to the purchase of cars, which is still linked to traditional schemes. However, things may evolve in the future.

From a contractual point of view, there is no specific national legislation in Italy on distribution agreements, which are governed by general contract law rules with reference also to sales, supply and franchising agreements.

Under EU legislation – Regulation No. 2022/720 (Vertical Block Exemption Regulation or VBER), Regulation No. 461/2010 (Motor Vehicle Block Exemption Regulation or MVBBER) and the Supplementary Guidelines on Vertical Restraints No. 2010/C 138/05, – certain limitations apply to these kinds of vertical distribution agreements with specific reference to automotive distribution (ie, contracts entered into by two or more companies at a different level of the production or distribution chain, and relating to the conditions under which the contracting parties may purchase, sell or resell certain goods or services). Selective distribution may be based on qualitative or quantitative grounds.

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In purely qualitative selective distribution schemes, dealers and repairers are selected based on objective criteria required by the nature of the product or service (eg, technical skills of sales personnel, layout of sales facilities, sales techniques and the type of sales service to be provided). These types of distribution agreements are usually deemed as not having anticompetitive effects, provided that three conditions are satisfied:

- first, the nature of the product in question must necessitate a selective distribution system, in the sense that such a system must constitute a legitimate requirement, having regard to the nature of the product concerned, to preserve its quality and ensure its proper use;
- second, resellers must be chosen based on objective criteria of a qualitative nature that are laid down uniformly for all, made available to all potential resellers and not applied in a discriminatory manner; and
- third, the criteria laid down must not go beyond what is necessary.

On the other hand, distribution agreements based on quantitative grounds are seen as more restrictive as they set numerical limitations such as a maximum given number of permitted dealers or repairers, or a minimum level of sales.

Under the aforesaid EU legislation, there is a presumption that both qualitative and quantitative selective distribution agreements in the automotive sector do not limit competition if the parties' share of the market does not exceed 30 per cent, provided they do not:

- impose fixed sale prices on dealers;
- impose geographical restrictions (with some exceptions, such as in the case of exclusive or selective distribution);
- restrict active or passive sales to end users (with some exceptions, such as in the case of exclusive or selective distribution);
- restrict cross-supplies between distributors within the same selective distribution system;
- restrict the manufacturer's ability to sell components as spare parts to end users or repairers or to others who have not been entrusted by a specific dealer; and
- restrict the sales of spare parts by members of a selective distribution system to independent repairers that use those parts for the repair and maintenance of a motor vehicle.

It is worth noting that the new VBER allows for greater protection of the selective distribution system by permitting suppliers to:

- prevent their selective distributors from selling actively or passively outside the selective distribution system; and
- ask their selective distributors to restrict their clients from selling (actively or passively) to unauthorised distributors within the territories where the supplier operates a selective system. This solution was not contemplated under the previous VBER.

With reference to exclusive distribution, the new VBER has introduced the possibility to assign an exclusive territory or group of clients to up to five exclusive distributors. It also authorises a supplier to adopt different distribution systems in different countries, and to introduce measures for the protection of various distribution systems.

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The new VBER permits non-compete obligations for a maximum period of five years from the date the distribution contract is entered into. The new Guidelines on Vertical Restraints (2022/C 248/01), however, specify that non-compete obligations that are tacitly renewable beyond a period of five years can benefit from the block exemption, provided the buyer can effectively renegotiate or terminate the vertical agreement containing the obligation with a reasonable period of advance notice and at a reasonable cost.

The new VBER has likewise introduced provisions concerning the particular form of car distribution represented by sales on online platforms, in light of the evolution of the case law. While it is confirmed that general restrictions to online sales are considered as hard-core restrictions to competition, suppliers are now allowed to set different criteria for online and offline sales as long as such criteria do not substantially impede online sales. In addition, it is also allowed to set wholesale prices differently depending on whether a product is sold through online or offline channels (dual pricing) when this reflects differences in the investments and costs incurred by the buyer to make sales in each channel. However, dual pricing must not pursue the aim of limiting sales to particular territories or clients, nor to reduce the ability to sell online.

Similarly, the new VBER and Guidelines on Vertical Restraints indicate that certain restrictions to online advertising are allowed, provided they do not have the object of preventing the use of an entire advertising channel by the buyer.

Finally, the new Guidelines on Vertical Restraints allow restrictions to sales through marketplaces when they restrict only one of the online channels the distributor can use, provided that such restrictions do not have the effect of entirely preventing online sales.

Concerning termination provisions, there is no specific time requirement under Italian law for a valid notice to be given, provided it is adequate and reasonable. The adequacy of the term provided within the termination notice very much depends on:

- the reason for termination (eg, breach of obligations by the dealer and justified or unjustified withdrawal by manufacturer);
- the contractual relations between the parties (eg, duration of the contract, exclusivity regime, number of dealerships, participation in the dealer's capital share by the manufacturer and existence of an economic dependency); and
- the reliance by the dealer on the manufacturer's business strategies or the manufacturer's assurances or guarantees, which proved to be wrong or that induced the dealer to, as an example, get mortgages or loans, make infrastructural and technological investments, buy new premises, hire new personnel and so on.

There have been criticisms with respect to the restructuring of dealers. Recent trends have proved that most automotive manufacturing companies establish their own banks. On top of rendering financial services to private consumers, automotive banks also financially sustain dealers. This causes problems in insolvency matters.

Indeed, considering that products, presale and post-sale services, technological infrastructure, platforms, business and sale conditions and strategies are supplied, developed and often imposed by manufacturing companies, it is frequently the case that dealers are subject to economic dependency on manufacturers. Understandably, distributors also tend

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to resolve their financial issues by seeking more available financial allowances, and at better interest rates, from the manufacturers' banks. Automotive companies have a high interest in ensuring that dealers do not become insolvent, but they also need to make sure they do not contribute to the further indebtedness of the distributor by financing it when it becomes apparent that the distributor will not be able to repay its debt, as this conduct is prosecutable under Italian legislation.

To mitigate the risk of not recovering the purchase price of vehicles and spare parts to be paid by distributors in case of insolvency, manufacturers usually subject the sale of vehicles to a right of retention of title. According to this provision, title of ownership on vehicles will be transferred to dealers only upon full payment. This measure, albeit valid from a legal standpoint, often does not prove to be as effective considering that, in the case of receivership proceedings against dealers, the receiver often disregards the retention title, leaving the manufacturer with the burden of starting long and costly legal proceedings to enforce its rights and recover its vehicles.

Italy has adopted a series of measures that can help prevent and manage insolvency in the automotive sector. More precisely, Law-Decree No. 17/2022, known as Decreto Bollette, entered into force on 2 March 2022 and established a €700 million fund for 2022 – later implemented through Directorial Decree 10 October 2022 – and €1 billion per year from 2023 to 2030 for the automotive sector. In particular, these incentives are targeting 'green transition, research, investments in the automotive sector aimed at the establishment, reconversion and requalification towards innovative and sustainable forms of production, in line with the European objectives of reduction of emissions harmful to the environment and digital development, as well as for the recognition of incentives to the purchase of non-polluting vehicles and to encourage the recovery and recycling of materials'. As made public by the Ministry of Enterprises and Made in Italy through [Directorial Decree of 23 February 2023](#), the first tranche of available resources for some northern regions in Italy has already been terminated.

Mergers, acquisitions and joint ventures

5 | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

There are no particularities for M&A or joint venture transactions in the automotive industry as such. As for other large industrial assets, the main areas to be carefully considered in the due diligence phase and in the preparation and negotiation of the transaction documentation (representations and warranties, special indemnities, price and price adjustment) are:

- production – the business is capital and labour-intensive and it may have an environmental impact. So, real estate properties and other assets, employment, environment and waste management are areas to cover. Likewise, slow-moving inventory may be an issue. Single sourcing may be another issue to tackle;
- distribution chain – the dealers' network is part of the value, and dealership agreements may require careful analysis (eg, prices, competition restrictions, duration and change of control clauses); and

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- finance – given the size of capital expenditure and operating expenses, financing agreements are key to business sustainability. Again, change of control clauses are a common practice.

More generally, the automotive industry is likely to go through an unprecedented consolidation process driven by the huge investments needed for automation and electrification. This, in turn, according to some commentators, may result in relatively smooth clearances with respect to concentrations, leading to the combination of enormous assets and, in principle, to a significant increase of market power. Against this backdrop, one of the key issues that inevitably comes to mind in the merger control area is how and to what extent the automotive revolution will reshape the boundaries of product and geographic markets and, in turn, the assessment of merging parties' competitive relationships and combined market power that still largely depends on the delimitation of the perimeter within which the latter are found to operate. One of the crucial factors in this regard is the development of business models alternative to ownership, and possibly the transition from a system of 'owned transportation vehicles' – which represents the largely predominant although declining paradigm today – to a system of rented or even just borrowed vehicles that will ultimately eliminate the need for the final consumer to purchase his or her own vehicle. The foregoing is likely to result in a radical change in the relationship between market supply and demand, and thus an unprecedented structural modification of the sector as a whole. In this respect, the Italian government is formally evaluating the Italian Competition Authority's proposal to amend the current merger control legislation with respect to both digital and more traditional sectors, so as to also include within the scope of the notification obligation transactions that do not meet the legal thresholds, in cases where an actual threat to competition nonetheless exists in the national market, or in a substantial part thereof, and within six months of the completion of the transaction.

Lastly, in terms of approvals to be sought and obtained from the Italian government, the automotive supply chain per se is not subject to the foreign direct investment (FDI) screening mechanism. However, the Italian government enacted – in late 2020 – a decree broadening the FDI scope so as to include high technological intensity 'assets or relationships', such as, among others, artificial intelligence, robotics, semiconductors, microprocessors, automated or remote piloting technologies (including onboard sensors) and automated manufacturing (a complete list is set forth in article 9 of DPCM No. 179/2020). In this light, it should be carefully evaluated on a case-by-case basis whether the automotive business of the target company (in terms of, for example, R&D activities, automatization of the manufacturing process and so on) is captured by the aforementioned decree. Should the answer be positive, Italian FDI clearance will be a condition to closing of M&A transactions.

Incentives and barriers to entry

- 6 | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

From a broad perspective, it is worth noting how the automotive industry is radically changing. A wave of vehicle innovation is emerging and reshaping even the most deep-seated features of the industry, from manufacturing processes to models of ownership. Digital transformation affects the whole automotive value chain, from design to production

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and distribution. It has been estimated that there will be US\$3.1 trillion worth of societal benefits in the digital transformation of the automotive industry up until 2025.

A true game changer is the market entry of tech giants that not only already benefit from significant economies of scale deriving from their market-leading position in transport-related services, such as mapping and artificial intelligence, but also from significant learning advantages when these firms eventually introduce prototypes of driverless cars whose data will be elaborated through cutting-edge algorithms. Silicon Valley firms are pouring substantial money into the car industry to develop new self-driving electric vehicles. It is a natural fit, given their status as prime innovators in modern technology, robotics and artificial intelligence. This entrepreneurial process constantly encourages tech firms to come up with better products and, as a result, disrupt existing market structures to ultimately benefit consumers.

Meanwhile, automakers, which have been traditionally represented by a small number of very large companies, are now facing the most profound challenge to their business models in a century. Information technology is deeply intertwined with the automotive sector and, in fact, electronic systems will be accounting for a significant part of a car's value in years to come.

With vehicles becoming more and more connected, autonomous, shared and electric, the industry is witnessing a disruptive technological tsunami that is about to bring major changes in the near future as regards both incentives and barriers to entry, with three big waves on the horizon rapidly approaching the shore: automation and connected car services, electric vehicles and alternative models of 'ownership' such as car sharing and rental. It is worth highlighting that all these features have been identified by most of the respondents to the public consultation launched by the European Commission when reviewing the MVBBER. Indeed, in their view, any changes affecting the automotive business since 2010 (eg, connected cars, digitalisation, access to in-vehicle and users' data, remote connectivity and over-the-air technology), should be reflected in the objectives pursued by the block exemption rules covering the motor vehicle sector.

There are no specific tax incentives for investment in the automotive market; however, general tax incentives linked to R&D activities and investments in tangible and intangible assets are also available to the automotive industry.

In the past few years, Italian tax rules have provided for incentives aimed at fostering the purchase of certain less-polluting means of transportation by both individuals and corporate entities (normally small and medium-sized enterprises). At present, a contribution (Ecobonus Auto) – whose specific rules, limits and requirements are set out by Ministerial Decree of 6 April 2022, as amended and supplemented by Ministerial Decree of 4 August 2022 – is available for the purchase or financial lease in 2023 or 2024 of:

- new manufacturing M1 category vehicles (used for the transport of passengers with no more than eight seats, in addition to the driver's seat) falling in a class not lower than Euro 6 (whether or not jointly scrapping a vehicle of a class lower than Euro 5);
- new manufacturing L1e, L2e, L3e, L4e, L5e, L6e and L7e vehicles falling in a class not lower than Euro 5, provided that the purchaser jointly scraps a vehicle falling in category

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- from zero to three, or a vehicle that was subject to mandatory re-registration with a new plate;
- new manufacturing L1e, L2e, L3e, L4e, L5e, L6e and L7e vehicles fully electrically powered; and
 - new manufacturing N1 and N2 category commercial vehicles fully electrically powered, provided that the purchase is made jointly with the scrapping of an old vehicle falling in a class below Euro 4.

More details on the requirements and conditions to be met to be eligible for the above contribution are available on [a dedicated page](#) of the Ministry of Enterprises and Made in Italy.

PRODUCT SAFETY AND LIABILITY

Safety and environmental

7 | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

At the European level, the most relevant automotive-related product compliance safety and environmental regulations are:

- Regulation (EU) 2018/858 of 30 May 2018 (as most recently amended by Commission Delegated Regulation (EU) 2022/2236 of 20 June 2022), on the approval and market surveillance of motor vehicles and their trailers, and of systems, components and separate technical units intended for such vehicles;
- Commission Regulations (EU) 2017/2400, (EU) 2017/1347, (EU) 2017/1151, (EU) 2017/1154, (EU) 2018/1832, (EU) 2019/318 and (EU) 2019/543;
- Regulation (EU) 2019/2144 (as supplemented by Commission Delegated Regulation (EU) 2021/1243 of 19 April 2021), on type-approval requirements for motor vehicles and their trailers, and systems, components and separate technical units intended for such vehicles, as regards their general safety and the protection of vehicle occupants and vulnerable road users, in turn implemented by Commission Implementing Regulation (EU) 2021/535. This Regulation is expected to make the adoption of the most advanced security technologies mandatory for obtaining type approval for certain vehicles: among the many, this security technology includes intelligent speed assistance, alcohol interlock installation facilitation, advanced driver distraction warnings and the installation of a black box on each vehicle;
- Regulation (EC) 715/2007 (on type approval of motor vehicles with respect to emissions from light passenger and commercial vehicles, and on access to vehicle repair and maintenance information), as subsequently amended and supplemented by Commission Regulations (EU) 2017/1151 and (EU) 2017/1154; and Regulation (EC) 595/2009 (on type approval of motor vehicles and engines with respect to emissions from heavy-duty vehicles and on access to vehicle repair and maintenance information). Regulations (EC) 715/2007 and (EC) 595/2009 are likely to be repealed soon: on 10 November 2022, the European Commission adopted the 'Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND COUNCIL on type-approval of motor vehicles and engines and of systems, components and separate technical units intended for such vehicles, with

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respect to their emissions and battery durability (Euro 7) and repealing Regulations (EC) No 715/2007 and (EC) No 595/2009', which addresses the reasons why Euro 6 emission standards do not sufficiently contribute to the reduction of pollutant emissions. The main objectives of this draft are: 1) reduction of the complexity of the current Euro emission standards; 2) provision of up-to-date limits for all relevant air pollutants; and 3) improving control of real-world emissions; and

- Regulation (EU) 2019/631, setting CO₂ emission performance standards for new passenger cars and for new light commercial vehicles (as amended by Commission Delegated Regulations (EU) 2020/22, (EU) 2020/1590, (EU) 2020/2173 and (EU) 2021/1961) that repealed, as of 1 January 2020, both Regulation (EC) No. 443/2009 on emission performance standards for new passenger cars and Regulation (EU) No. 510/2011 on emission performance standards for new light commercial vehicles.

Against such a backdrop, Legislative Decree No. 285/1992 (the Italian Highway Code) and Presidential Decree No. 495/1992 (the regulations implementing the Italian Highway Code), which are implemented in Italy by a number of ministerial decrees, set forth the technical specifications that must be fulfilled by motor vehicles in order to obtain type approval by the competent department of the Italian Ministry of Infrastructures and Transport. Recently, Legislative Decree No. 68/2022 (converted into law by Law No. 108/2022) amended the Italian Highway Code, introducing several provisions aimed at reducing the administrative burdens on users, promoting the development of sustainable mobility and increasing safety of road traffic.

Under Regulation (EU) 2018/858:

- the approval authority must refuse to grant EU type approval if it finds that a vehicle, system, component or separate technical unit, albeit in compliance with the required prescriptions, presents a serious risk to road safety or seriously harms the environment or public health (article 26.5);
- the approval authority that has granted an EU type approval must take the necessary measures (including, where needed, revocation of the EU type approval) in order to ensure compliance with the type it has approved if it finds that the manufacturer no longer produces the vehicles, systems, components or separate technical units in conformity with the approved type, or establishes that the certificates of conformity no longer comply with the prescriptions of the Regulation (article 31.7);
- a manufacturer that has obtained an EU type approval and, under certain circumstances, the importer is required to take all appropriate corrective measures where a vehicle, system, component, separate technical unit, part or equipment that has been placed on the market or that has entered into service is not in conformity with the Regulation or where the type approval has been granted on the basis of incorrect data and to immediately inform the competent authority that issued the relevant EU type approval. The corrective measures may include withdrawing the vehicle from the market or recalling it (articles 14.1 and 17.1); and
- an economic operator is required to take all appropriate corrective measures if the market surveillance authority of one member state finds that a vehicle, system, component or separate technical unit presents a serious risk to the health or safety of persons or to other aspects of the protection of public interests. If it does not take such corrective measures, national authorities are entitled to adopt restrictive measures (including the withdraw or recall of the vehicle from the market) (article 52).

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In principle, non-compliance with applicable law requirements is, per se, punished by administrative sanctions that will be effective, proportionate and dissuasive. Further details regarding the procedure for the imposition of administrative fines and the methods for their calculation and collection have been set out by Commission Delegated Regulation (EU) 2022/1209 of 5 May 2022.

There are no industry-specific rules for product recalls.

Product liability and recall

8 Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

Italy has a fairly strong tradition in product liability litigation, particularly since the adoption, in 2005, of [Decree No. 206/2005](#) (known as the Italian Consumer Code), which incorporates previous Italian laws implementing Directive 85/374/EEC and Directive 2001/95/EC. The Italian Consumer Code has been amended by Legislative Decree No. 170/2021 transposing Directive (EU) 2019/771 so as to lay down new rules on conformity of goods and commercial warranties. Product liability law is particularly significant to the automotive industry, given the large number of components (eg, braking systems, airbags and seat belts) that might in theory be subject to manufacturing or design defects, and because of the seriousness of the risks in the case of defective parts.

Product liability litigation in the automotive sector can also be particularly complex, in light of the fact that consumers or users generally tend to direct their claims to the manufacturer, which, in turn, might need to involve the litigation suppliers or manufacturers of the allegedly defective components.

As regards recalls – regulated by articles 104 to 107 of the Italian Consumer Code (implementing the General Product Safety Directive 2001/95/EC) – the automotive industry has long been one of the most affected. According to the European Rapid Exchange of Information System, throughout 2021 Italy submitted two alerts for ‘motor vehicles’ and both were concluded with the manufacturer recalling the product from end users. The risks associated with these alerts were injuries and environmental risks. In 2022, there was an alert concerning ‘a motor vehicle not complying with the Regulation on the approval and market surveillance of motor vehicles and their trailers, and of systems, components and separate technical units intended for such vehicles’. The adopted measure was recalling the product from end users. In 2022, Italy also submitted an alert for a motorcycle for the reason that ‘hydrogen could leak into the brake fluid, causing an extended brake lever travel, decreasing the braking capacity and increasing the risk of accident’. The motorcycle model at stake was recalled from end users.

Class actions have been allowed in Italy since 2010 and have not yet represented an actual major risk for automotive manufacturers. Indeed, there are strict conditions for a class action to be considered admissible (and decided on the merits), which have historically discouraged consumers and consumer associations from relying on the class action system. Up until now, based on publicly available information, very few class actions have been filed

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against motor vehicle manufacturers. For example, in recent years, Altroconsumo – one of the most prominent and active Italian consumer associations – started:

- a class action against Volkswagen regarding emission tests (which is still pending before the Court of Appeals of Venice since Volkswagen challenged the first instance judgment);
- a class action against Volkswagen for a specific version of one of its passenger cars (in relation to which the parties entered into a settlement agreement); and
- another class action against Fiat Chrysler for a different type of passenger car (in relation to which the parties entered into a settlement agreement).

All these lawsuits are grounded on the companies having declared different emissions or fuel consumption values than the actual ones (even through the 'defeat device'), leading plaintiffs to claim damages for conducts affecting the consumers' choice. Altroconsumo also started a follow-on class action (still pending) in late 2019 concerning almost all automotive captive banks on the Italian market, seeking compensation for damages suffered by consumers due to the allegedly inflated costs for their financial services purportedly suggesting the existence of a cartel among the defendants.

As class action did not turn out to be an effective dispute resolution mechanism unlike in other countries, a reform of the Italian class action law (aimed at removing some obstacles) was envisaged and discussed. Following years of gestation, the Italian class action reform was approved on 3 April 2019 and entered into force on 19 May 2021 after several postponements. It applies to illicit conduct occurring after its entry into force. Its key features include:

- a broader scope of application: it is no longer reserved to consumers and end users, and it is open to all kinds of damage claims. From now on, class actions may be brought for the enforcement of 'homogeneous rights' by anyone (including legal entities and in B2B relationships) claiming damage redress against the 'author of the harmful behaviour'. Indeed, the new class action regime is included in the Italian Civil Procedure Code and no longer in the Consumer Code;
- a long opting-in window whereby individuals can join the class action even after issuance of the decision on the merits;
- new figures in the class action management (ie, a 'common representative' of the class who will manage the merits and the subsequent enforcement phases on behalf of the individual class members); and
- a success fee for the attorneys of the winning party and for the common representative of the class.

The reform also modified the 'collective action for injunctive relief'. This action is aimed at obtaining a court ruling:

- inhibiting any conduct that is detrimental to the interests of multiple individuals or entities (whereby this action is defined collective);
- ordering appropriate measures to correct or eliminate the harmful effects of the assessed violations; and
- possibly ordering the publication in the media of the injunctive relief.

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The court may also establish a sum of money to be paid as a penalty for each day of delay in the event of non-compliance.

On 24 November 2020, Directive (EU) 2020/1828 on representative actions for the protection of the collective interests of consumers (repealing Directive 2009/22/EC) was approved. The Directive requires EU member states to transpose it by 25 December 2022 and adapt their procedural collective action and redress mechanism, with application from 25 June 2023. On 9 March 2023, the Italian government approved the final text of the Implementing Decree. We are now waiting for it to be published in the official journal.

As the scope of application of the existing class action system provided by the Italian Civil Procedure Code is broader than the Directive's, as regards both the subject matter and the entities entitled to bring representative actions, only minor adjustments of the class action regime included in the Italian Civil Procedure Code are expected. Quite surprisingly, the Implementing Decree includes a new section in the Consumer Code instead of modifying the existing provisions on class action set forth in the Italian Civil Procedure Code, thus creating alternative systems for Italian consumers.

The new provisions are related to:

- 'qualified entities' entitled to carry out, against professionals, domestic and cross-border judicial initiatives aimed at representing consumers' collective interests;
- available remedies to increase deterrence actions against illicit conducts and decrease the prejudice suffered by consumers. In this respect the possibility to ask, simultaneously, for redress and injunctive measures is foreseen; and
- representative actions (both redress and injunctive measures) brought against professionals only in the case of breach of Regulations or Directives (implemented in Italy) listed in the Implementing Decree's Annex.

DISPUTES

Competition enforcement

9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

In recent years, the automotive industry has been subject to market monitoring, competition advocacy and antitrust enforcement activities carried out by both the European Commission and the national competition authorities of the various member states. The pending review of Regulation No. 461/2010 (Motor Vehicle Block Exemption Regulation or MVBBER) by the European Commission is a noteworthy example.

Together with the new Regulation No. 2022/720 (Vertical Block Exemption Regulation or VBER), MVBBER is one of the key pieces of EU legislation when it comes to the development, manufacture and supply of vehicles as it sets out the general framework for the antitrust analysis of agreements in this sector. MVBBER creates a safe harbour (under the block-exemption mechanism) for particular categories of agreements that are key to the automotive

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industry and sets a handful of clear-cut rules about the requirements for benefiting from such safe harbour. MVBER lists the hardcore restrictions that, if included in the agreement, prevent the applicability of a safe harbour. It also provides for a list of specific non-exempted clauses. Conversely, MVBER does not lay down any 'white clauses', that is, rules that the parties to the arrangement must comply with for MVBER to apply.

MVBER was set to expire on 31 May 2023, however its validity has been prolonged to 31 May 2028 to allow the Commission to react in a timely manner to probable market changes, such as those stemming from vehicle digitalisation.

In addition, the Commission has updated the Supplementary Guidelines. The main aspects concern:

- the nature of data generated by vehicle sensors as possible essential input for the provision of repair and maintenance services, as a consequence of which authorised and independent repairers must have access to such data on a non-discriminatory basis;
- clarification that vehicle suppliers must apply the proportionality principle when considering whether to withhold inputs, such as vehicle-generated data, on the basis of potential cybersecurity concerns; and
- the indication that should a supplier unilaterally withhold from independent operators an essential input, such as vehicle-generated data, this might entail a violation of article 102 of the Treaty on the Functioning of the European Union.

The updated Supplementary Guidelines reflect some of the points that were raised during the MVBER consultation phase carried out with the stakeholders:

- ensuring a level playing field with regard to access to in-vehicle data, including technical information and data linked to connected vehicles, for all stakeholders (while taking into account consumers' choice to share such data);
- guaranteeing cybersecurity of vehicles while enabling fair competition to protect the interests of the consumer; and
- considering the impact of over-the-air diagnoses allowing vehicle manufacturers and authorised dealers to contact customers directly and offer innovative services.

The consultation showed the need to take into consideration the emergence of new technologies and the increasing role of data in competitive dynamics in the industry, particularly in the aftermarket.

Indeed, one of the key antitrust issues will be the evolution of car maintenance services throughout the digital era. Traditionally, car maintenance activity starts when the consumer's vehicle enters the repairer's workshop, as repairers physically inspect vehicles in their workshop using advanced diagnostic and repair tools to identify and fix malfunctions. Against this backdrop, competition law rules are primarily aimed at safeguarding competitiveness in terms of an equal level playing field between independent service providers and authorised repairers, in terms of equal access to spare part supplies and diagnostic and repair tools. Digitalisation changes this paradigm.

Car maintenance in the digital era, however, starts within the vehicle thanks to remote communications achieved via diagnostic software embedded in cars. Competitiveness will

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thus be increasingly measured against the possibility of carrying out preventive maintenance, while having remote access to predictive information about the vehicle, before any problems occur and the vehicle has to be brought to the repair shop. Such a paradigm shift may have an impact on the conditions required to enable a fair and competitive vehicle service industry. In particular, competition agencies are likely to monitor car manufacturers' ability to act as gatekeeper for access to in-vehicle data, and to the incentives and ability to design telematic systems that provide timely access to such data along with the possibility of being in direct contact with the driver.

Also, it is interesting to see how competition rules in this area will increasingly cross paths with another key body of EU and national provisions (ie, data protection rules), if and to the extent that the exchange and circulation of in-vehicle information underlies the exchange and circulation of personal information on vehicle drivers (such as drivers' habits or movements). Although the European Commission and the European Court of Justice have stressed on a number of occasions that issues concerning the processing of personal data are not as such a matter for competition law, nowadays it seems that these issues cannot be overlooked in the enforcement of antitrust rules. Notably, the European Court of Justice remarked in judgment ECLI:EU:C:2006:734, paragraph 63, that: 'any possible issues relating to the sensitivity of personal data are not, as such, a matter for competition law, they may be resolved on the basis of the relevant provisions governing data protection.' Personal data is becoming more and more of an asset and, as a result, privacy protection has become a central point of concern on the agenda of EU and national competition agencies.

At a national level, in the vast majority of merger decisions, the Italian Competition Authority (ICA) has decided (without applying any EU or national rules, such as MVBBER, specific to the motor vehicle industry) not to open an inquiry because of a lack of detrimental effects on competition. These decisions, which are apparently not likely to have relevance at an enforcement level, are instead highly important in defining the relevant markets in the spare parts industry.

According to the ICA, each spare part is, in principle, intended for a separate product market, and each individual market identified as such can be divided between the spare parts that have been produced by car manufacturers (the original equipment suppliers) and those that are distributed in the market with brands different from those of the car manufacturers (whose producers constitute the independent aftermarket). With regard to the geographical extent of these markets, the ICA has recognised that they have a local dimension.

In antitrust cases, the ICA's concerns mainly focus on the exchange of sensitive information, especially through trade associations. In 2015, the ICA closed an investigation of restrictive practices implemented in the market of car seat foam by the main market players. In this case, it was ascertained that the parties had significantly exchanged information about their production and commercial activities, therefore violating article 101 of the Treaty on the Functioning of the European Union (TFEU) (Case I776 of 10 June 2015). By contrast, in Case I791 of 30 March 2017, the ICA stated that an exchange of sensitive information between automotive companies also active in the long-term vehicle rental sector and the related industry associations did not infringe article 101 of the TFEU, as it did not restrict or eliminate uncertainty about the parties' conduct in the market. Even though the relevant market was highly concentrated, with significant barriers to entry, and the information was detailed, not public, individualised and referred to the past but frequently provided and

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related to multi-annual contracts, there was no connection (direct or indirect) between the information exchanged and their commercial policy. Finally, on 20 December 2018, the ICA sanctioned nine captive banks and their parent companies as well as industry associations for having engaged in an exchange of commercially sensitive information concerning economic and other contractual terms applied to dealers and financing agreements and thus violated article 101 of the TFEU (Case I811).

The decision was appealed by the parties before the Administrative Court of First Instance (*TAR Lazio*), which, after having issued an interim order suspending the effects of the ICA's decision, ultimately quashed it on 24 November 2020, on grounds of unreasonable duration of the pre-investigation phase, erroneous identification of the relevant market, inconsistency of the investigation and absence of sufficient objective elements to establish the existence of a single and complex cartel. In January 2022, the Council of State upheld the *TAR Lazio* decision.

The fining decision has been followed by a collective damages action brought by an Italian consumer association before the Court of Milan. The court has issued an order suspending the trial until the completion of the administrative proceedings.

More generally, as regard follow-on litigation, Italy has approved [Legislative Decree 3/2017](#) that implements Directive 2014/104/EU on certain rules governing actions for damages under national law for infringements of the competition law provisions of the member states and of the EU. This Legislative Decree, adopted on the basis of the aforementioned Directive to introduce a common regulation for claims for damages caused by infringements of competition law throughout the EU, will probably encourage the implementation of private enforcement litigation in Italy.

Concerning the automotive industry's 'digital dimension', which is rapidly increasing its momentum in Italy as elsewhere in the world, on 27 April 2021 the ICA sanctioned a major global player in the digital economy for abuse of dominance by refusing a deal affecting the android auto environment for an app developed to provide end users with information and services for charging electric car batteries (Case A529). The decision was confirmed by *TAR Lazio* in July 2022.

Moreover, in the context of its advocacy activity, in December 2018 the ICA issued a report pursuant to article 21 of [Law No. 287/1990](#), concerning the regulatory provisions governing road testing of autonomous driving in Italy and, in particular, article 14 of the [Decree of the Ministry of Infrastructures and Transport of 28 February 2018](#) on the concept of Smart Road. The ICA considered that the obligation to apply for a vehicle manufacturer's authorisation to be allowed to test autonomous driving programmes is restrictive of competition, since it reduces the possibility for independent developers to compete to the advantage of car manufacturers already strongly active in a rapidly evolving sector. This causes a slowdown in scientific progress and limits interoperability among proprietary autonomous driving systems.

The ICA's proposals to the Italian government (No. AS1824 of 31 March 2022) focus on the need to ensure that no distortions of competition are created in the development of infrastructures for charging electric cars. Some of the proposals made by the ICA have been accepted and adopted by the Italian government in the new [Annual Market and Competition](#)

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[Law](#) entered into force on 5 August 2022. In particular, article 12 imposes the installation of high-powered charging points on highway concessionaires, ensuring that the infrastructure offers electric car users waiting times no longer than those offered to users of internal combustion vehicles.

Furthermore, it is indicated that if the concessionaires themselves fail to provide an adequate number of charging points, they are required to activate a tender procedure aimed at selecting the operator, through competitive, transparent and non-discriminatory procedures, in compliance with the principle of rotation and on the basis of the technical characteristics of the proposed solution, commercial conditions that enhance the efficiency, quality and variety of services as well as contractual models suitable to ensure the competitiveness of the offer in terms of quality and availability of services.

Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

Most disputes in the automotive industry in Italy relate to bodily harm, supply chain issues, disputes with dealers' networks (and connected aftersales repair and maintenance services), disputes with consumers over unfair advertising, violation of competition law, IP disputes and disputes over defective components.

Damages claims by consumers can be brought against:

- the manufacturer for product liability pursuant to article 114 of the Consumer Code or under the general provision on tortious liability (article 2043 of the [Italian Civil Code](#)); and
- the seller for hidden defects pursuant to article 1494, paragraph 2 of the Italian Civil Code.

Supply chain disputes are also common in Italy, but tend to be resolved via settlements (except when the dispute involves a bankrupt supplier). However, there are no specific interim injunctions under Italian law, and these are available only in summary or urgent proceedings, and only in the case of urgency and prima facie strong grounds for the claim.

In relation to disputes on compensation claims arising from unfair practices, publicly available information reveals that very few class actions have been filed against motor vehicle manufacturers. For example, Altroconsumo started three class actions claiming damages ensuing unfair practices. Specifically, summoned companies were sued either for having installed the 'defeat device' or for their declarations on fuel consumption in relation to a particular version of one of their passenger cars.

These procedures tend to be initiated with the main aim of raising an issue and allowing parties to develop a constructive dialogue in the interest of both consumers and enterprises. Indeed, in early 2021, two of the three class actions initiated by Altroconsumo were terminated with a settlement between the latter and the defendants. The third class action is pending before the Court of Appeal. One of the involved automotive companies has recently decided to appeal against the first instance judgment condemning it to compensate

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consumers admitted to the class action initiated by Altroconsumo. The appeal judgment is expected by the end of 2023.

Covid-19 does not appear to have impacted the disputes arena in the automotive sector, except for the general slowing down of all procedures already in progress.

Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

First, the general rules of Italian insolvency law also apply to the automotive sector, and no specific provisions exist that allow a different treatment for distressed suppliers in the industry.

The new [Italian Insolvency Code](#) was published in the official journal on 14 February 2019 and (with the exclusion of limited articles that entered into force in 2019) most of its provisions entered into force in July 2022, as a result of [Legislative Decree No. 83 of 17 June 2022](#). The new rules provide for measures aimed at preventing insolvency of entities, such as suppliers, through certain early-warning tools (ie, internal reporting obligations by the statutory auditors of the company and external reporting obligations by qualified public entities such as social security agencies, tax agencies and tax collectors), in the presence of certain indicators of a distress situation. Should the debtor fail to react promptly by taking the necessary measures, the auditors and above-mentioned entities must inform a newly created non-jurisdictional distress composition body named OCRI, established within the Chambers of Commerce. The reporting is aimed at triggering a 'composition procedure' to enable the distressed company to return to solvency through agreements with the creditors. Failing this (and recurring a state of insolvency), the Chambers of Commerce inform the Public Prosecutor, who can file before the court a motion seeking the opening of bankruptcy proceedings, defined as 'judicial liquidation'. Appropriate incentives are provided to companies that voluntarily and in a timely manner resort to the composition procedure (including tax reductions, extra time for filing restructuring plans or debt restructuring agreements, some criminal exemptions or reduction of sanctions). Some entities (such as listed companies, banks and large-sized groups) are not obliged to apply the early-warning rules, but will benefit from the rewarding measures if they do.

In any event, caution should be adopted when dealing with a supplier showing clear signs of distress. Following the last reforms on creditor arrangements, an irreversibly distressed supplier will inevitably be declared bankrupt; however, if the degree of economic distress is not serious, typically a troubled supplier will try to avoid bankruptcy liquidation through the new composition procedure described above, or by seeking to be admitted to a creditor arrangement scheme by either filing a motion for a composition with creditors or presenting a debt restructuring agreement, both of which set aside any motion for bankruptcy liquidation filed by third-party creditors in the meantime, and entail a clawback exemption.

These creditor arrangement procedures lead to drafting plans or restructuring agreements between the distressed supplier and its creditors to agree on a way to repay the debt – by liquidating the company's assets and assuring a higher satisfaction for creditors than in a bankruptcy liquidation scenario – and possibly continue the business including all pending

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contractual relations with creditors and third parties (which will be allowed to terminate only for a valid cause), thus avoiding a bankruptcy liquidation scenario where pending contractual relations are suspended and resumed only on the bankruptcy receiver's election.

As opposed to bankruptcy liquidation, these procedures can be activated only on the initiative of the distressed supplier, and solely at a later stage will creditors be entitled to intervene and even propose concurrent plans. If the legal requirements for the arrangement schemes are not met, the supplier may ultimately be declared bankrupt.

Aside from creditor arrangements, bankruptcy liquidation is the ultimate procedure to ensure debt recovery for creditors. A bankruptcy declaration is issued by the competent bankruptcy court on a motion that can be submitted by the distressed supplier, or by any creditor or interested third party. The former management is divested of its powers and a court-appointed receiver will take control over the bankrupt entity with the aim of liquidating assets and maximising the outcome of the liquidation to assure the highest satisfaction for creditors, whose claims will be repaid proportionally based on their ranking.

Bankruptcy liquidation rarely assures adequate percentages of satisfaction, especially for unsecured creditors. Moreover, whenever a supplier is declared bankrupt any pending contractual relations with creditors and third parties are automatically suspended, and will be resumed only if the receiver decides for their continuation – and obtains specific court leave – because they may prove useful for the recovery and liquidation process.

Another important aspect characterising bankruptcy liquidation is that receivers will typically try to maximise income for the bankrupt estate, and often do so by attempting clawback actions to reverse the effects of payments (or other asset disposals) performed by the distressed supplier in the look-back period prior to the bankruptcy declaration (or prior to the creditor arrangement, if this was unsuccessful and led to bankruptcy). These actions are more likely to succeed if there is evidence of the payee's awareness of the debtor's distress when the payment was made. Another option sought by receivers to maximise income for the bankruptcy estate is to sue the distressed company's former managers for company mismanagement.

The way the automotive industry deals with suppliers that face distress indicia is determined on a case-by-case basis, depending on the factual circumstances at hand. In any event, a cautious approach is advised, especially in relation to changing the existing contractual terms and conditions, by seeking authoritative approval in a creditor arrangement context, and by avoiding changes in a bankruptcy liquidation scenario to avoid a significant risk of clawback.

Intellectual property disputes

12 Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

A significant portion of intellectual property disputes in Italy involve business operators in the automotive industry, particularly in relation to spare parts covered by trademark or design rights. Italian courts have recently addressed a number of cases on whether the

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overall shape of automotive products (eg, motorcycles or even engines) may be protected both as a registered or unregistered trademark and as a copyright work, under specific circumstances where the products in question can be regarded as design icons having both creative character and artistic value (such as the Piaggio Vespa or the Ferrari 250 GTO).

In this vein, the Court of Milan recently found that the unauthorised display of Ferrari cars in the advertising campaign of a clothing collection entailed a misuse of the well-known Ferrari trademark, giving rise to an illicit association with the Italian sports cars brand and an undue advantage for the fashion house producing the advertisement (Court of Milan, 3 June 2020, No. 3109, DeJure).

However, the threshold for recognising the artistic value of the overall shape of an automotive product has been set particularly high by Italian courts. In a recent proceeding, Jaguar Land Rover enforced its shape trademarks allegedly covering the old Defender vehicle design and its copyright-protected shape. The Court of Rome, rebutting the plaintiff's claims, declared the design of the well-known British off-road vehicle not protectable as a copyrighted work. In its reasoning, the court highlighted that the Defender shape lacks the artistic value required by the law (with creative character) to enjoy such protection. Indeed, Jaguar Land Rover failed to provide the court with any evidence proving the artistic recognition of the old shape of the British car. The court also excluded any likelihood of confusion between the defendant's product and the Defender's shape trademark (Court of Rome, 4 August 2021, Sprint).

Still, trademarks protecting shapes of iconic cars are subject to the general rules on trademark cancellation for non-use. Ferrari recently saw the revocation for non-use by the European Union Intellectual Property Office of the Ferrari GTO 250 EU shape mark (EUIPO, 29 May 2020, No. C 30 743). Some IP-related disputes have also occurred between car and toy manufacturers. The typical case regards the scale reproduction of iconic supercars by toy models. The outcome of those disputes is often uncertain and depends on the factual circumstances of the case. Recently, the Italian Court of Cassation ruled that the unauthorised use of the famous Ferrari logo as well as the reproduction of the iconic car bodies by toy models – manufactured and marketed by a third party – do not give rise to an infringement. In its reasoning, the court explained that such use did not cause any prejudice to the distinctive character and reputation of the trademarks enforced by the Italian supercar manufacturer (Italian Court of Cassation, 3 November 2022, No. 32408, DeJure) and that the car body of the Ferrari model reproduced in scale could not enjoy copyright protection for lack of artistic value.

Patents and utility models are also at stake in many automotive disputes, concerning for instance braking systems, engine features or electronic functionalities of vehicles.

The number of patent disputes in this field is expected to escalate in the near future as a consequence of the upcoming innovations relating to self-driving and connected car technologies. In fact, an increasing number of patent applications concerning said technologies are being filed with the European Patent Office and further complexity may derive from circumstances where some of the resulting patents are standard essential patents.

Most provisions covering intellectual property rights in Italy are embodied in the [Italian Intellectual Property Code](#) and in the [Copyright Act](#), as amended from time to time to

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implement international agreements and, most importantly, EU directives. EU regulations, such as those on the European Union trademark and on community designs, are directly enforceable in Italy.

Specialist courts dealing with intellectual and industrial property matters were established in Italy in 2003 and reformed in 2012, when they became subsections of the newly introduced commercial courts. The commercial courts are also European Union trademarks and community designs courts.

Generally, proceedings before the commercial courts follow the procedural rules of ordinary civil proceedings, including the possibility to institute preliminary proceedings before initiating a full-blown case on the merits, or in the context of a pending case on the merits. The Intellectual Property Code, however, provides for some specific evidentiary, precautionary and enforcement measures, also according to Directive 2004/48/EC on the enforcement of intellectual property rights and to Directive (EU) 2016/943 on the protection of trade secrets, as implemented in Italy by [Legislative Decree No. 63 of 11 May 2018](#), which came into force on 22 June 2018.

Preliminary proceedings are a cost- and time-effective solution for IP right holders to tackle infringements. Indeed, a preliminary injunction may be obtained in around six months, whereas it takes no less than two to three years to obtain a first-instance decision on the merits.

Italian courts grant a preliminary injunction when the petitioner's claims appear prima facie grounded as regards both validity of the relevant IP rights and infringement thereof, and the claimant substantiates that he or she would suffer irreparable harm until the outcome of ordinary proceedings on the merits (urgency requirement or periculum in mora). In this regard, Italian courts usually find the urgency requirement to be met even if up to 10 months have passed from the moment when the right holder discovered the allegedly infringing activity. Other forms of preliminary relief available to IP right holders in Italy are seizure (to prevent disposal of the infringing goods) and, most importantly, preliminary search orders to secure evidence of the infringement, which is usually requested in the first place and granted with an ex parte order. A preliminary injunction is then granted at a second stage, following a discussion hearing, subject to the relevant requirements (prima facie case and urgency) and based on the evidence collected during the search. If the preliminary injunction is granted, additional measures such as penalties and publication of the decision are available and commonly ordered by Italian courts.

Most intellectual property disputes are resolved based on the outcome of preliminary proceedings, often by means of settlement agreements. If this is not the case, and some material damages are claimed by the right holder, ordinary proceedings on the merits follow their regular path up to a first-instance decision, which may then be appealed before the Court of Appeals and ultimately challenged before the Court of Cassation on purely legal issues.

Over the past few years, the Italian Court of Cassation has affirmed the principle that patent infringement proceedings must be stayed, under certain circumstances, when invalidity proceedings concerning the same patent are pending and until a final judgment on validity is issued (Italian Court of Cassation, 4 April 2019, No. 9500, Sprint). This principle was followed

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by a recent decision of the Court of Genoa, still subject to Court of Cassation review, in a case between two major players in the automotive sector concerning milling machines, even though the patent invalidity proceedings were initiated by the alleged infringer after the institution of the infringement proceedings.

According to the Italian Intellectual Property Code, damages are based primarily on the right holder's lost profits, taking into account all the relevant circumstances. Lost profits cannot be lower than the reasonable royalty corresponding either to the amount the right holder would have received if a normal licence agreement had been entered into or to a typical licence fee in the industry. In any event, the right holder may claim the disgorgement of the infringer's profits, when the amount is higher than the compensatory damages that would be awarded or as an alternative to the right holder's lost profits.

The court may appoint a technical expert to assess damages. Where an analysis of the defendant's business is necessary, the court may issue a search order or may order the disclosure of the defendant's accounting records.

Alternative dispute resolution methods such as mediation and assisted negotiations are available and increasingly used in Italy, although they are not mandatory in intellectual property disputes.

EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

The automotive sector is historically characterised by a high level of unionisation.

In recent years, due to the fluctuating profitability of the sector, automotive companies operating in Italy reduced their workforce and made significant use of welfare measures to cushion periods of reduced demand.

The covid-19 emergency over the past years and its implications on the national economy caused huge losses in market demand. Such losses have been reiterated by the lack of chips and the crisis of raw materials and energy, which in recent years has led – and will likely continue to lead – many companies in the automotive sector (including those operating side businesses) to implement additional furlough programmes and to interrupt their economic operations in Italy. Moreover, the ongoing ecological transition (that will bring a gradual transition to electric cars), will surely have a strong impact on the sector in terms of reduction of component production and, as a consequence, of jobs.

In this context, the government and the representatives of the main Italian companies in the automotive sector, sometimes also together with the trade unions, have started to periodically hold roundtables aimed at discussing the problems affecting the sector and studying measures to mitigate the effects of the ecological transition on companies and their employees.

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With a view to safeguard the sector's employees – following the renewal of the National Collective Labour Agreement of the manufacturing sector of 5 February 2021 (CCNL) – a number of agreements integrating the CCNL were signed by the employees' and employers' trade unions (the latest was signed on 8 March 2023, regarding salary increases based on the changes in the consumer price index). The main items covered by the renewal of the CCNL and the additional agreements are:

- employee salaries;
- levels of classification;
- the complementary pension system and supplementary healthcare;
- involvement of trade unions in the case of change of provider or public service contracts; and
- the professional training of employees (with specific regards to digital skills) and smart working.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

In order to achieve the goal of climate neutrality by 2050, the EU is taking measures to reduce vehicle emissions, as road transport accounts for one-fifth of the EU's CO₂ emissions. In June 2022, the European Parliament approved the Commission's proposal for new zero-emission cars and vans by 2035. Gasoline- or diesel-powered vehicles are to be replaced with zero-emission alternatives, such as electric cars. Emission reduction targets for 2030 are set at 55 per cent for cars and 50 per cent for vans. In February 2023, the agreement was ratified by the Parliament and now must be formally approved by the Council. The automotive revolution in the EU's vision marks a decisive step towards putting the continent on the path to zero emissions.

As a matter of fact, from a mobility standpoint, one of the main concerns in Italy is the necessity to implement all relevant measures to achieve a technological neutrality aimed at reducing emissions. To boost the sales of electric, hybrid and low CO₂ emission vehicles, the Italian lawmaker introduced some economic subsidies, regulated in the latest version for 2022 and following years by the DPCM of 6 April 2022. With this measure, the government allocated a total of €630 million for each of the years 2022, 2023 and 2024 from the Automotive Fund, which boasts a total allocation of €8.7 billion until 2030.

The hybrid and electrically chargeable car market recorded a significant increase in volume in 2022. Overall, in 2022, the European hybrid market (specifically, hybrid electric vehicles) accounted for 22.6 per cent of all car sales (compared to 5.7 per cent in 2019, 11.9 per cent in 2020 and 19.8 per cent in 2021), and the battery electric vehicles (BEVs) accounted for 12.1 per cent (compared to 3 per cent in 2019 and 9.1 per cent in 2021). Indeed, the total sales percentage of hybrid and electric cars is higher than the total sales percentage of diesel vehicles (which amounts to 16.4 per cent). In 2022, new BEV registrations continued to grow, despite the overall decline of the EU car market. As a result, market share of BEVs expanded

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to 12.1 per cent, a 3 per cent improvement compared to 2021. It was a strong year also for hybrid cars, which achieved a market share of 22.6 per cent. By contrast, traditional petrol and diesel fuel-types continued to lose ground; though, combined, they still accounted for more than half of EU car sales in 2022.

According to the Italian Competition Authority (ICA), the development of electric infrastructures for the recharging motor vehicles as envisaged by the EU and Italian regulatory framework represents an important step towards sustainable mobility. ICA considers the development of the electric mobility sector in accordance with competitive dynamics to be highly desirable for the benefit of consumers and the entire economic system and society. In this respect, legislative measures have been adopted to, on the one hand, simplify procedures and provide incentives for the installation of recharging infrastructures, and, on the other hand, to require the Italian Regulatory Authority for Energy, Networks and Environment to regulate the price of energy distributed through recharging infrastructures. Furthermore, the National Recovery and Resilience Plan 2021–2026 is set to invest heavily in green mobility infrastructures for a grand total of approximately €25 billion; these investments include the installation of 21,355 fast and ultra-fast public charging stations for electric and hybrid vehicles. In January 2023, the Ministry of the Environment and Energy Security published two decrees indicating modalities and criteria for the awarding of grants useful for the construction of charging stations in Italian urban areas and on highways. Funds are allocated annually over a three-year period from 2023 to 2025. More than 21,000 charging stations for electric vehicles will be operational within the next three years on dual carriageways and in urban centres, contributing to the upgrading of the current fuel distribution network by adapting them to sustainable mobility. In addition, the development of 40 hydrogen fuelling stations for wheeled vehicles and nine for rail transport is expected to be realised by June 2026.

Directive No. 2014/94/EU, implemented in Italy by means of Legislative Decree No. 257 of 16 December 2016 and further integrated by Regulation (EU) 2019/6, sets out, for the first time, a common framework of measures aimed at establishing alternative fuel infrastructure, including the minimum requirements for the construction of charging points for, among others, electric and hydrogen vehicles, with the purpose of mitigating the environmental impact of transportation across Europe. In 2020, the European Commission invited the public and stakeholders to express their opinion and share information on the effects of the Directive on the evaluation and the impact assessment that the European Commission is currently carrying out, as well as possible additional policy measures for its revision. It is hoped cooperation at a European level will lead to satisfactory results in the short term. Indeed, with respect to technological advances, all European countries have recently been focusing their attention and investments on autonomous cars, also known as self-driving or driverless cars. By means of sensors, radars, navigators and highly technological computers, autonomous cars can identify their surroundings and assess whether there are any obstacles or external phenomena that may impact driving. This innovation is deemed extremely useful in lowering the risks associated with collisions and injuries, reducing insurance costs, lowering fuel consumption, easing traffic, facilitating transport for elderly and disabled persons and avoiding intoxicated driving.

On 14 July 2022, article 34-bis was added to the Convention of Vienna, introducing the concept of automatic driving and removing obstacles to assistance systems that allow the driver to let go of the steering wheel under certain conditions (starting with Level 3

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advanced driver-assistance systems). Still, the driver remains responsible for his or her car and must intervene if it has malfunctions or electrical problems. The Convention states that automated driving will only be able to move out of its current experimental or otherwise limited status if it is transposed into national laws. But many states, including Italy, have not yet legislated.

Having achieved great technological results, the main concern appears now to be of a legal and social nature. Principally, there is a general concern and resistance among the public because of safety issues (relating both to system defaults and possible hacker attacks).

From a legal standpoint, great concerns have arisen over potential liability for defects, especially since cars will remain under the control of owners who may not diligently carry out all the relevant maintenance checks.

Moreover, it appears obvious that corrective measures will have to be set forth in Italy, from a legislative point of view, to enable the driving of autonomous cars. By way of example, article 46 of the Italian Highway Code, implemented through Legislative Decree No. 285 of 30 April 1992, defines as 'vehicles' cars of any type that circulate on roads and are driven by human beings.

The first steps towards legal innovation have already been introduced by Directive No. 2010/40/EU for the establishment of a framework for the deployment of intelligent transport systems (ITS) in the field of road transport and for interfaces with other modes of transport, implemented in Italy by [Law-Decree No. 179 of 18 October 2012](#) and transposed by [Law No. 221 of 17 December 2012](#). This legislation, as subsequently integrated by the [Decree](#) issued on 1 February 2013 by the Ministry of Infrastructures and Transport, finally resolves one of the main juridical uncertainties: with reference to liability relating to systems and ITS services, it is stated that the applicable regulation will be the same for product liability under the 2005 Italian Consumer Code.

In addition, the Ministry of Infrastructures and Transport has passed the Smart Roads Decree with the aim of closing the gap between Italy and other EU countries, as well as the United States, where driverless car field testing programmes have been under way since 2010. According to the Smart Roads Decree, the Ministry of Infrastructures and Transport can authorise driverless car field testing on specific stretches of roads, subject to specific requirements and surveillance, aimed at ensuring that the testing programmes are carried out in conditions of utmost safety. Request for ministerial authorisation is available to various entities, including university research institutes, private and public research organisations, manufacturers of vehicles equipped with automated driving technologies and so on. In May 2020, the Ministry of Infrastructures and Transport signed a memorandum of understanding with the Ministry of Technological Innovation and Digital Transition to further support research, experimentation, definition of prototypes and identification and training of new professionals in the field of innovative self-guided and connected vehicles and means of transport. Lastly, in September 2020, the technical support commission for smart roads, created under article 20 of the Smart Roads Decree, published its first report on the activities carried out and the state-of-the-art initiatives identified on the national territory in the field of smart roads and connected and self-driving vehicles, proposing some amendments to the Smart Roads Decree to further promote innovation.

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At the same time, the Italian legislator is working to provide ground rules on the shared use of private vehicles in the form of either car sharing or carpooling. The aim is twofold: to foster sharing-economy activities carried out by non-professional individuals through third-party platforms, to ultimately reduce the number of vehicles circulating in the cities and their economic and environmental impact; and providing national rules offering a secure legal base for commercial businesses to operate, in contrast with the current panorama where commercial car-sharing activities offered by professional businesses via mobile applications are regulated at local level – mainly via public calls of interests published by the competent municipalities looking to share mobility services.

As a side note, under article 1-ter of [Law-Decree No. 121 of 10 September 2021](#), effective from 30 September 2022, e-scooters must be marketed with turn and brake light indicators on both wheels and those already in circulation must be adapted by 1 January 2024. In addition, e-scooters may not exceed the speed limit of 6km per hour when riding in pedestrian areas and 20km per hour in all other circumstances. To this end, all e-scooters must be equipped with a speed regulator configurable according to said speed limits.

UPDATE AND TRENDS

Trends and new legislation

15 Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

Hot topics for prospective regulation and legislation at either EU or local level include:

- Directive (EU) 2019/1936 amending Directive 2008/96/EC on road infrastructure safety management, to be implemented by all EU member states by the end of December 2021. The Directive aims at the establishment and implementation of procedures relating to road safety impact assessments, road safety audits, road safety inspections and network-wide road safety assessments by member states. The deadline for its national transposition was 17 December 2021. Italy transposed the Directive by means of Legislative Decree No. 213/2021, containing provisions for the establishment and implementation of procedures for road safety impact assessments, applying to roads that are part of the trans-European road network, freeways and main roads (whether they are planned, under construction or already open to traffic), and other roads and road infrastructure projects that are located in suburban areas, which do not serve public or private areas bordering them and have received funding from resources allocated by the EU, with the exception of roads that are not open to the general automobile traffic, such as bicycle paths, or roads not intended for general traffic such as access roads to industrial, agricultural or forestry sites;
- Regulation (EU) 2019/2144 amending Regulation (EU) 2018/858 on the general safety of vehicles and the protection of vulnerable road users. The Regulation aims at significantly reducing deaths and serious injuries on EU roads by introducing state-of-the-art safety technologies as standard vehicle equipment, and to enhance the competitiveness of EU car manufacturers on the global market by providing the first-ever EU legal framework

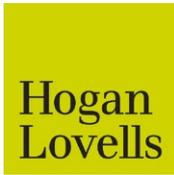
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- for automated and fully automated vehicles. It entered into force in September 2020 and will apply from 6 July 2022;
- on 9 March 2021, the European Data Protection Board adopted its [guidelines](#) on processing personal data in the context of connected vehicles and mobility-related applications. It has factored in the feedback received from several stakeholders during the public consultation period and addressed, from a data protection standpoint, the evolution of cars from an expression of freedom and autonomy to another 'controlled' environment;
 - the EU Regulation on privacy and electronic communications is still being debated and aims at ensuring respect for private life and protection of personal data in electronic communications between connected and autonomous vehicles and users;
 - the European Battery Alliance, launched in 2017 by the EU Commission, continues to grow. To date, 440 industrial and innovation actors have joined the alliance, which aims to develop an innovative, competitive and sustainable battery value chain in Europe. On 12 March 2021, Vice President Maroš Šefčovič gave a speech highlighting that Europe will continue to push forward closing the investment gap with Asian competitors by supporting more than 70 industrial projects, which is expected to create three to four million jobs by 2025;
 - on 23 February 2022, the EU Commission proposed the Data Act, which includes measures for a fair and innovative data economy. More specifically, these rules specify who can use and access data generated in the EU across all economic sectors. The proposal for the Data Act includes, among other things, measures to allow users of connected devices to gain access to data generated by them, which is often exclusively harvested by manufacturers, and to share such data with third parties to provide aftermarket or other data-driven innovative services. This proposal would impact a variety of services, including information collected in machinery and connected devices such as cars;
 - the proposal for a regulation of the European Parliament and of the Council amending Regulation (EU) 2019/631 with regard to strengthening CO₂ emission performance standards for new passenger cars and new light commercial vehicles in line with EU's increased climate ambitions provides for a ban on the production and sale of cars and vans with combustion engines from 2035. The decision, which was to be made on 1 March 2023, has been postponed due to the opposition of some member states, including Italy;
 - in Italy, Legislative Decree No. 17/2022 provides for specific measures for the automotive sector with the aim of promoting conversion, research and development. In particular, the main goals are green transition and investments in the rapidly changing automotive sector with the development of innovative and sustainable manufacturing techniques. Indeed, in line with the European aims to reduce emissions, promote recovery and recycling of materials and foster the purchase of clean vehicles, the Italian government, as of January 2022, has allocated a fund of €150 million to support dealers operating in the automotive sector that have been much impacted by the covid-19 pandemic, including by postponing the term to use the bonus to replace old engines with electric ones in cars; and
 - the Ministry of Infrastructures and Transport has developed the Road Mobility Strategy for the period between 2022 and 2026, with the dual objective of providing smart mobility services and enabling the operator to take infrastructure surveillance and monitoring measures and to increase the safety of the network by adopting a predictive maintenance approach. Such innovation, accompanied by the increasing implementation of artificial intelligence in cars, will only be achieved through infrastructure capable of

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communicating with the vehicle and the user through specific devices. As a result, roads and highways will be transformed into smart roads, that is, infrastructure equipped with technologies enabling the development of smart mobility and prepared for future scenarios involving autonomous vehicles.

- * *The authors would like to thank Francesca Angeloni, Emanuela Cocco, Domiziana Carloni, Luigi Mansani, Andrea Schettino, Simona Loro, Sabrina Borocci, Francesca Moretti, Aurora Muselli, Alessandro Medolago Albani, Vittorio Moresco, Giada Cagnes, Alessandra Chironi, Serena Pietrosanti, Maria Cristina Conte, Francesco Stella, Martina Di Nicola, Marina Massaro, Federica Poretti, Filippo Andrea Chiaves, Enrica Ferrero, Pietro Orlandi, Sveva Cuccurullo and Niccolò Sciortino for their support in writing this chapter.*



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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

The automotive industry is one of the most important sectors in Japan. Japanese automotive manufacturers have been increasing localisation of their production, and the country manufactured over 6.6 million passenger vehicles and exported over 3.8 million in 2022.

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Japan also produced over 640,000 motorcycles, and 64 per cent of these were exported in the same period. The production amounts to over ¥21.6 trillion. The OEMs complement the complex ecosystem of parts suppliers whose production amounted to ¥20.4 trillion in shipment value in 2019. In fiscal year 2019, OEMs and parts suppliers employed approximately 912,000 persons across Japan, and the workforce employed in the automobile-related sectors – including sales, transportation, service and maintenance, and electronics or other manufacturing industries – amounted to approximately 5.42 million persons, which is equal to 8.1 per cent of the country's working population. The automotive industry in Japan is supported by ¥2.9 trillion of research and development investment (financial year 2018) and ¥1.5 trillion of capital investment (financial year 2018).

Japan is the third-largest automotive market in the world. By the end of 2019, approximately 5.2 million vehicles were sold in the country, of which 4.3 million were passenger vehicles and 900,000 were buses and light or heavy trucks. Approximately 28.5 per cent of the passenger vehicles were Japanese 'kei'-standard light vehicles (vehicles designed with limited size and equipped with an engine no larger than 660 cubic centimetres). Japan imported approximately 300,000 vehicles from non-Japanese manufacturers in 2019. The number of registered passenger vehicles at the end of 2019 was over 78 million, and 80 per cent of Japanese households have at least one vehicle.

COMMERCIAL OPERATIONS

Regulation

- 2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

Automotive regulation is generally governed by the Ministry of Land, Infrastructure, Transport and Tourism (MLIT) and its related governmental entities such as the National Agency for Automobile and Land Transport Technology (NALTEC). Every automobile in Japan is required to comply with extensive safety and environmental standards – the Safety Standards for Road Transport Vehicles, Ministry of Transport Ordinance (Ordinance No. 67 of 1952, as amended) (the Safety Standards) – pass an inspection and be registered before being operated on public roads under the Road Transport Vehicle Act (Act No. 185 of 1951, as amended) (RTVA).

Type approval

Mass production automobiles need type approval before being launched onto the market. Filings for type approval are reviewed from the perspective of compliance with the Safety Standards and quality control measures. Vehicle manufacturers are required to file for type approval pursuant to the RTVA, the Vehicle Type Approval Regulations (Ministry of Transport Ordinance (Ordinance No. 85 of 1951)) and the Automobile Type Approval Handbook for Japanese Certification by applying for testing at NALTEC, the agency that handles vehicle certification and homologation matters under MLIT.

The relevant framework for type approval of vehicles in Japan is as follows.

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- Type-approval system (TAS): this is the standard type-approval regime for most passenger vehicles, which includes inspections of sample vehicles and quality control systems to ensure uniform quality of the models. Vehicle manufacturers are required to have their vehicles inspected by qualified staff members before shipping out of the factory pursuant to the Automobile Type Approval Handbook for Japanese Certification (Notification No. 1252 of 1998 of the Road Transport Bureau Type Approval and Recall Division of MLIT). For imported cars, NALTEC dispatches its staff overseas to conduct sample inspections and examine data produced by overseas test institutions. Type approval will be granted generally within two months of applying. The manufacturer of type-approved vehicles is required to ensure the quality of the vehicles and issue a completion inspection certificate upon the transfer of the vehicles. Owners of type-approved vehicles are allowed to register their vehicle with the local MLIT Transport Branch Office by submitting the completion inspection certificate issued by the vehicle manufacturer and some simple paperwork.
- Preferential handling procedure for imported motor vehicles (PHP): this is a simplified system to promote the sales of imported cars and is applied to models imported in quantities of 5,000 or fewer per year. The procedure consists of the submission of documents and presentation of the actual vehicle to NALTEC. The data and specifications submitted to the authority of other jurisdictions where the original type approval was granted can generally be used for the application of PHP, but an emissions test must be implemented anew under the Japanese standards. No sample inspection is required, but one in 50 vehicles is tested for emissions.

On 11 November 2020, MLIT announced that it had approved type approval for a vehicle produced by one of the Japanese vehicle manufacturers, being the world's first production car equipped with Level 3 automated driving technology.

Vehicles that are not type approved can also be registered and operated on public roads, which is the case for parallel import vehicles and heavily customised vehicles produced in a small number. The owner is required to have the vehicle inspected to confirm compliance with the Safety Standards.

TAS incidents from 2017

Pre-shipping inspection under TAS must be conducted by the manufacturer's internally qualified inspection staff by passing certain internal screenings and identified to MLIT in advance. In September 2017, an on-site investigation by MLIT discovered that a vehicle manufacturer's pre-shipping inspection certificates for completed vehicles had been signed by non-qualified staff. The vehicle manufacturer voluntarily stopped shipment of its products for two weeks. After MLIT requested that other car manufacturers check their operations, an additional vehicle manufacturer was also found to have had the same non-compliance issues. During investigations, it was discovered that both vehicle manufacturers had not been complying with TAS (which requires inspection by qualified inspectors) for more than 30 years. Following the investigation, in November 2017, MLIT established a commission to review the current TAS inspection regime. In April 2019, a third vehicle manufacturer was also found to have the same non-compliance issues that had continued for years. This series of incidents resulted in bitter criticism of vehicle manufacturers by the market and cost billions of Japanese yen to conduct recalls to redo completion inspections. However, some experts also point out that this TAS requirement is an outdated formality, and there is

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no equivalent inspection requirement for vehicles manufactured for export. As such, Type Approval Regulations for vehicles were amended and promulgated on 30 June 2019.

Mutual recognition

The UNECE World Forum for Harmonization of Vehicle Regulations (WP.29) held in November 2017 adopted the International Whole Vehicle Type Approval (IWVTA) together with UN Regulation No. 0 (UNR0), which came into effect in 2018. Under the IWVTA, countries that ratify UNR0, including Japan and European countries, will reciprocally accept vehicle inspection certificates enabling effective and speedy vehicle approval as well as promotion of higher safety and environment standards. MLIT has announced that it will take the lead in furtherance of UNR0 to developing countries in Asia.

Registration and periodic inspection

Under the RTVA, vehicles are required to be registered before being operated on public roads. The registration procedure is handled by the local MLIT Transport Branch Office where a licence number plate is issued. As a prerequisite for registration, vehicles need to comply with the Safety Standards. With regard to TAS-approved vehicles, owners who intend to register their vehicle are not required to conduct an inspection of each vehicle by presenting the vehicle at the registration centre. On the other hand, the PHP process requires the presentation of each actual vehicle as part of the registration process, although inspections for these types of approved vehicles are more simplified than those without type approval. Automobiles without type approval (eg, those that are produced in very small quantities or imported by individual users) may also be registered and placed on public roads, but need to go through a full-scale inspection in advance. To register, the owner of a vehicle is also required to certify at the local police station that an appropriate parking area is secured for the vehicle. Any change in the registration details, such as the transfer of ownership, should be registered within 15 days. Three years from the first registration, vehicles need to be re-inspected at a designated service centre (and every two years thereafter) to ensure compliance with Safety Standards; this is commonly referred to as 'shaken'.

Insurance

Every driver is required to participate in the liability insurance scheme under the Automobile Liability Security Act (Act No. 97 of 1955, as amended) which automatically pays a specified amount to the victim of a traffic accident without identifying the person at fault or apportioning negligence between the parties involved. This is commonly referred to as compulsory vehicle insurance and provides minimal basic coverage with a cap of ¥1.2 million for injuries, ¥750,000 to ¥40 million for permanent disability, and up to ¥30 million for death. It does not provide any compensation for damage to vehicles or other property. Thus, approximately 90 per cent of drivers also take out additional insurance, and the annual net premium in the auto insurance sector amounts to over ¥4 trillion.

Type approval of automobile parts

Automobile parts manufacturers are also entitled to take advantage of the separate automobile parts type-approval regime pursuant to the RTVA and the Type Approval Regulations for Devices (No. 66 of 1998). Once the model for a part is approved by NALTEC,

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the manufacturer is not required to undertake further inspections of the part regardless of the vehicle model into which the part is incorporated. Japan is also a party to United Nations-sponsored Agreement concerning the Adoption of Uniform Conditions of Approval and Reciprocal Recognition of Approval for Motor Vehicle Equipment and Parts signed at Geneva on 20 March 1958 and the Agreement concerning the Adoption of Uniform Technical Prescriptions for Wheeled Vehicles, Equipment and Parts Which Can Be Fitted and/or Be Used on Wheeled Vehicles and the Conditions for Reciprocal Recognition of Approvals Granted on the Basis of These Prescriptions, dated 5 October 1995, which provide technical prescriptions for wheeled vehicles, equipment and parts that can be fitted or used on wheeled vehicles, and the conditions for reciprocal recognition of designations granted on the basis of these prescriptions. Japanese regulators have been increasingly promoting the harmonised standard and reciprocal recognition of designations, and as of December 2020, Japan has adopted 93 categories of rule out of 159, including categories regarding brakes, safety belts and tyres.

Development, manufacture and supply

3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

The development, manufacturing and supply of automobiles and auto parts involve close and long-term relationships between vehicle manufacturers and suppliers. Such long-term relationships usually consist of a master agreement covering terms and conditions common to the entire transaction between the parties, and a relatively simple individual agreement or purchase order form is used to conclude each individual transaction. Vehicle manufacturers usually enter into supply agreements with auto parts manufacturers or other suppliers with respect to manufacturing. Supply agreements are also governed by regulations to protect 'weak' suppliers from unfair trade practices of 'strong' vehicle manufacturers and high-tier suppliers (the Act against Delay in Payment of Subcontract Proceeds, Etc to Subcontractors (Act No. 120 of 1956, as amended)). Some generic parts and maintenance parts are handled not only by suppliers but also by Japanese trading houses, companies specialised in import, export, distribution and marketing of goods.

Traditionally, Japanese vehicle manufacturers have formed strong alliances with parts suppliers, acting in close and exclusive cooperation with regard to the supply of parts and semi-processed components as well as research and development. Such business networks are hierarchical structures with the vehicle manufacturers at the top and several layers of suppliers broken down into Tier 1, Tier 2 and Tier 3 suppliers, securing a stable supply of high-quality components optimised to the vehicle manufacturer's end product. Some of these companies often have equity relationships; however, contractual relationships are more common and so are de facto continuous transactions without any specific written agreements. However, car manufacturers are increasingly procuring parts from diversified suppliers because of competition in the global market, complex supply chains and the development of common architecture and modularisation. Therefore, the traditional business-network structure is said to be gradually dissolving. This means that suppliers newly participating in the market will have more business opportunities, while contracts with new suppliers that do not have a history of previous transactions will need closer review. Also, in this context, some vehicle manufacturers and high-tier suppliers are insourcing their

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supply by means of acquisitions of other suppliers and emerging high-tech companies, resulting in increasing M&A demands.

Distribution

4 | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

Vehicles are usually distributed through dealerships of distributors, some of which are subsidiaries of the vehicle manufacturer's group, and others are independent local companies. One dealership, sometimes that of an independent local company, usually handles vehicles of only one vehicle manufacturer and does not mix vehicles from several manufacturers in its product line-up. Generally, distributors purchase vehicles from the vehicle manufacturer and sell them to customers pursuant to the standard terms instructed by the vehicle manufacturer. Vehicle manufacturers provide extensive instructions regarding the service quality, promotions and incentives, and the use of trademark and signage. Often vehicles are distributed on a built-to-order basis – manufactured with customised options in the customer's purchase order – instead of being sold from the stock stored in the backyard of the dealership. Imported vehicles are generally sold from the dealer's stock.

A vehicle importer who has obtained type approval is identified as the vehicle manufacturer in Japan and is responsible for the purpose of a recall. Many dealerships provide financial arrangements for customers such as auto loans and leases (with or without a buy-back option), and vehicle manufacturers usually have their own financing company and contract with credit companies to facilitate such financial arrangements. This area is heavily regulated by the Money Lending Business Act (Act No. 32 of 1983, as amended) and the Instalment Sales Act (Act No. 159 of 1961, as amended).

Contracts with distributors are governed by the Civil Code Act (Act No. 89 of 1896, as amended) (the Civil Code). As the automotive industry is brand oriented and each vehicle manufacturer is keen to control the vertical channels for its automobiles, they pay close attention to dealership-related competition issues such as dealership zoning, restrictions on methods of sale and selective distribution. For example, abuse of dominant bargaining power such as the exercise of excessive control or undue influence is prohibited under the Act on Prohibition of Private Monopolization and Maintenance of Fair Trade (Act No. 54 of 1947, as amended) and the Guidelines Concerning Distribution Systems and Business Practices (JFTC, 11 July 1991, as amended). Since vehicles must be inspected every two years, many dealers provide qualified vehicle mechanic services to enhance customer loyalty and to market new cars. Vehicle maintenance services require certain physical facilities and qualified staff, as well as regulatory certifications by a local MLIT Transport Branch Office. To trade in second-hand vehicles a second-hand dealer licence is required.

Restructuring of dealerships can be achieved through the termination, amendment, transfer or assignment of the dealer contract. Under the general principles of the Civil Code, when termination of a dealer agreement is disputed, the court generally tends to favour the continuation of the existing agreement, to provide support for the 'weak' distributor against the 'strong' vehicle manufacturer. If the contractual relationship between a

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vehicle manufacturer and a dealer has continued for a protracted period, it may be difficult for the vehicle manufacturer to terminate the contract easily, even if there is a right to terminate in the contract. In other words, the Japanese courts sometimes do not interpret the contract at face value, but require the terminating party to have a justifiable reason for wanting to terminate the contract. There are judicial precedents where a contractor (dealer) of a vehicle importer challenged the validity of the termination of the dealer contract by the importer owing to a poor sales record and the dealer's non-compliance with the importer's business strategy. To minimise this risk, manufacturers may prefer to enter into fixed-term contractual arrangements with dealers without automatic renewal, and instead review the relationship every year. Even where a unilateral termination right exists, a car manufacturer still might attempt to have the dealer agree to voluntarily terminate the contract to minimise the risk of future disputes.

Other main concerns, specific to these kinds of transactions, include competition issues, the provision of maintenance services, warranties, auto loans and lien arrangements with customers. Although there are no special requirements in the restructuring of dealerships in the automotive industry as compared to other industries, restructuring is always a tough challenge owing to the above-mentioned principle protecting long-term relationships and the significant impact on both the distributor and the vehicle manufacturer. In November 2018, a vehicle manufacturer, in the course of a major restructuring of its dealer network, announced a sweeping sales channel reform. This will involve a merger of dealers in Tokyo directly held by the vehicle manufacturer in April 2019. The vehicle manufacturer has approximately 280 partner distributors with 5,000 stores across Japan, which are currently classified into four channels that sell different combinations of branded vehicles. Many of these partner distributors are local businesses with no equity relationship with the vehicle manufacturer's group. The vehicle manufacturer has announced that it will integrate these four channels and reduce its product line-up from 40 to approximately 30 models effective from 2022 to 2025. A third vehicle manufacturer announced a merger of its two 100 per cent affiliated distributors in February 2019. In November 2020, two vehicle manufacturers announced that they will integrate four affiliated parts suppliers and completed the transaction in January 2021.

Mergers, acquisitions and joint ventures

5 | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

There are generally no particularities in terms of M&A or joint venture transactions for the automotive industry. However, given the complex and highly regulated nature of the industry, key features in terms of due diligence and drafting of relevant agreements include regulatory compliance, employment, competition and intellectual property issues.

Regulatory compliance is a key concern in M&A and joint venture transactions in the automotive industry today. After a series of non-compliance incidents in recent years, the regulator is keen to ensure compliance by exercising its supervising authority, and brand and market reputation are the most vulnerable assets even for well-established companies with decades of tradition.

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Although the rate of employees who are unionised has been drastically decreasing in the past decade, the traditional-style labour unions still have a certain level of presence in the automotive industry. Under the labour-management harmonising style in Japan, although strikes and aggressive negotiations are rare, in some companies the cooperation of the union is indispensable for the smooth closing of an M&A deal and the subsequent post-merger integration.

Competition issues are also important. Under the Japanese merger control regulation, the merger and acquisition of companies exceeding certain thresholds require prior filing with the Japan Fair Trade Commission and may not be closed within a 30-day waiting period, which can be shortened upon request from the parties.

A notable recent trend is M&A involving companies outside of the traditional automotive industry, such as carbon fibre, image sensor, laser radar, next-generation battery and automated drive technologies. This trend is supported by the dissolution of the traditional business-network regime and divergence in the automotive industry itself.

Incentives and barriers to entry

6 | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

There are no special incentives for investment in the automotive market. Government branches, including the Small and Medium Enterprise Agency, have been providing financial aid to ventures and small-scale enterprises with innovative business models, and some municipalities offer financial aid and tax reductions through by-laws to attract investment in factories and regional business hubs. These benefits are also applicable to the automotive industry.

The Ministry of Economy, Trade and Industry (METI), through the Next Generation Vehicle Promotion Centre provides financial aid for the purchase of plug-in hybrid vehicles, electric vehicles (EVs) and fuel-cell vehicles (FCVs), depending on the energy efficiency of the vehicle as well as the investment in EV charging facilities and hydrogen stations for FCV, and some municipalities have similar arrangements. As a result, for example, FCVs can receive a governmental incentive of over ¥3.4 million (¥2.3 million from METI and ¥1.1 million from the Tokyo Metropolitan government).

The safety and environmental standards are increasingly conforming to those of other jurisdictions. However, the type-approval process and regulations on environment and safety standards are prepared only in Japanese, and the procedures are quite complicated, which may represent short-term practical barriers to entering the market. Also, there are established common market practices and standards. Thus, it is advisable for new market participants to consult appropriate experts.

The traditional manufacturing and distribution sectors have many powerful incumbent players in Japan. Therefore, the impact of new entrants will not likely be significant. However, at the dawn of new technologies such as autonomous vehicles, connected vehicles and ride sharing, entrants from other industries could be game changers.

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PRODUCT SAFETY AND LIABILITY

Safety and environmental

- 7** | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

The Road Transport Vehicle Act (Act No. 185 of 1951, as amended) (RTVA) is the fundamental statutory source of product compliance, safety and environment regulations. Under the RTVA, vehicles will not be put into operational use unless their structure complies with the technical standards for safety, pollution prevention and other environmental conservation as specified by ministerial ordinances of the Ministry of Land, Infrastructure, Transport and Tourism (MLIT) with regard to certain matters including length, width and height, total vehicle weight load applied to the wheels and ratio of the load on the wheel to the total vehicle weight. Guidelines prepared by the MLIT provide detailed numerical standards for each component of the vehicle as well as the testing methodology. Driving a non-conforming automobile may result in administrative and criminal charges.

Environmental standards

Fuel economy

The standards for fuel economy are regulated by the Act on the Rational Use of Energy (Act No. 49 of 22 June 1979). This Act has provided the unique 'top-runner programme' fuel economy standards since 1998, which takes the fuel consumption of the most fuel-efficient vehicle in the segment currently on the market, and sets that consumption level as the standard for the next generation of vehicles. The standard requires vehicle manufacturers to keep the average fuel consumption of their products below the standard established by MLIT and the Ministry of Economy, Trade and Industry for a certain period depending on vehicle weight. Underachievement is publicly announced. The most recent standard was announced on 31 March 2020, which includes electric vehicles and plug-in hybrid cars with 2030 as the target year.

In addition to the top-runner programme, MLIT introduced the corporate average fuel efficiency (CAFE) regime where vehicle manufacturers are required to keep the CAFE value, which is calculated through the weighted average of fuel economy achievement in each category of vehicle weight, above the CAFE standards calculated through the weighted average of fuel economy standard in each category of vehicle weight.

The weight, type of engine, fuel consumption – in four testing modes: Worldwide Harmonised Light Vehicle Test Procedure (WLTP), urban, suburban and motorway – and other specifications are required to be stated in the catalogue for each vehicle. Vehicle owners are entitled to receive preferential tax treatment and incentives depending on the achievement of standards by their vehicles; however, vehicles that do not comply with the standards are not prohibited from being driven.

The testing method for compliance with environmental standards for passenger vehicles is the WLTP, which replaced the previous JC08 in October 2018, and is applicable to vehicles with a weight of less than 3.5 tons. The test consists of several driving cycles representing

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real-world vehicle operations on urban and suburban roads and motorways. Although the fuel consumption tested under the Worldwide Harmonized Light Vehicles Test Cycle (WLTC) usually indicates a lower score than that tested under the JC08 procedure, some manufacturers have already started to indicate fuel consumption of their vehicles in the WLTC mode.

Fuel consumption was not traditionally regulated by the RTVA, but after a series of world-wide fuel consumption incidents, MLIT included fuel consumption under the prescribed testing methods in the Safety Standards for Road Transport Vehicles, Ministry of Transport Ordinance (Ordinance No. 67 of 1952, as amended) (the Safety Standards), and the type approval can be revoked if the vehicle manufacturer falsifies fuel consumption. False or misleading statements regarding emissions may also trigger enforcement under the Act against Unjustifiable Premiums and Misleading Representations (Act No. 134 of 1962, as amended), including administrative surcharges of up to 3 per cent of the relevant sales. In 2017, the Consumer Affairs Agency imposed an administrative surcharge of ¥480 million on a vehicle manufacturer for false representation of fuel consumption in its advertisement materials. The Consumer Affairs Agency imposed an administrative surcharge of ¥3.17 million on another vehicle manufacturer for selling the vehicle manufacturer-badged version of virtually the same model procured from a different vehicle manufacturer; however, interestingly, the vehicle manufacturer later challenged this enforcement and was successful in having it overruled in December 2018. In March 2022, a vehicle manufacturer publicly announced that it had falsified engine performance in relation to its applications for certification concerning the emissions and fuel economy performance of its engines for the Japanese market. It further confirmed that the engines in question have performance issues.

Emissions

The regulation of emissions consists of the three following components.

- Individual regulation: this applies only once when the new vehicle is registered, and regulates CO, non-methane hydrocarbon, NOx and particulate matter (PM), based on the RTVA and the Safety Standards. With regard to heavy-duty vehicles, the Safety Standards have incorporated the worldwide harmonised heavy-duty certification procedure and off-cycle emission testing, which from 1 October 2016 are gradually being applied to each class.
- Vehicle type regulation: this applies to vehicles with diesel engines and prohibits the operation of underachieving vehicles in designated zones to prevent diesel air pollution in metropolitan areas pursuant to the Act Concerning Special Measures for Total Emission Reduction of Nitrogen Oxides and Particulate Matter from Automobiles in Specified Areas (Act No. 70 of 1992, as amended).
- Traffic regulations: some local governments provide emission control rules. For example, Tokyo and its three surrounding prefectures have by-laws restricting diesel vehicle PMs under stricter standards than the above-mentioned regulations.

After the emissions issues in 2015, MLIT and the Ministry of Environment conducted a series of real-world driving emission tests for eight models with diesel engines via a portable emission measurement system (PEMS) and published the results; however, MLIT has decided not to impose mandatory testing via PEMS for all vehicles, because of difficulties in homogenising test conditions to account for variations in weather and traffic.

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Recycling

End-of-life automobiles are mandatorily recycled pursuant to the Act on Recycling of End-of-Life Vehicles (Act No. 87 of 2002, as amended) (the Automobile Recycling Act). Vehicle owners pay a recycling fee when purchasing a new vehicle and the fee is pooled by the Japan Automobile Recycling Promotion Centre (JARC), as designated by the government. The scrapping work is conducted by a wrecker registered with a relevant local authority, and the manufacturer and importer are required to take over and destroy or recycle the shredder dust, airbags and chlorofluorocarbons using funding from JARC. According to Waste Management and Public Cleansing Act No. 137 of 1970, as amended, Customs Act (Act No. 61 of 1954, as amended) and Foreign Exchange and Foreign Trade Act (Act No. 228 of 1949, as amended), criminal liability may result from breach of recycling procedures, such as:

- scrapping by an unauthorised wrecker;
- failure to collect airbags, batteries, waste oil and fluid;
- wrecking without sorting hazardous materials; and
- unauthorised export of automobile wreckage.

Recall of vehicles

The key Japanese laws and regulations relating to recall are the RTVA and the Safety Standards.

There are three types of corrective measures under Japanese law:

- improvement measures (ie, a recall) under article 63(3), paragraph 1 of the RTVA (the Recall Provision), where a notification to MLIT is legally required if certain conditions are satisfied; and
- two types of voluntary countermeasures under MLIT's Guidelines for Handling Recall Notifications, Etc (the Recall Guidelines), where a notification to MLIT is not legally required but should be filed if the countermeasures are to be taken. The two types of countermeasures are:
 - improvement countermeasures; and
 - service campaigns.

While, strictly speaking, notifications to MLIT or customers are not legally required under the Recall Guidelines as they are not law, in practice they should be and typically are complied with.

Under the Recall Provision, a notification to MLIT is legally required if a vehicle manufacturer:

- finds that the structure, a device or the performance of a vehicle (ie, a vehicle within a certain range of a type-approved vehicle manufactured, or imported into Japan, by the vehicle manufacturer) may not or does not comply with the Safety Standards;
- finds that the cause of that noncompliance arises in the design or manufacture process; and
- intends to take improvement measures to rectify the issue.

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Recall of automobile parts

With regard to defective automobile parts, the defect should be dealt with by way of a recall of the entire vehicle by the car manufacturer, except for two categories of parts.

As exceptions, tyres and child-safety seats are subject to an independent recall procedure pursuant to the Order for Enforcement Regulations for RTVA (Ordinance No. 185 of 1 June 1951) and parts manufacturers are to carry out the recall process rather than the car manufacturer.

Technically, vehicle manufacturers can claim compensation for loss or damage incurred because of conducting a recall owing to defective parts from a supplier. However, this type of litigation has historically been relatively rare in the traditional business-network structure. Therefore, it might have been a surprise to many in Japan when a Japanese vehicle manufacturer sued one of its major Tier 1 suppliers in 2014, claiming more than ¥15.6 billion as compensation for damage incurred as a result of a recall caused by a defective power steering device produced by the parts manufacturer.

Product liability and recall

- 8** | Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

Product liability is an important subject in the automotive industry. Customers who have incurred losses owing to a vehicle may bring claims against the vehicle manufacturer and the dealer based on a tort or warranty theory under the Civil Code. In the tort claim under the Civil Code, coupled with the Product Liability Act (Act No. 85 of July 1994), if the product has a defect, or lacks the level of safety that it ordinarily should have, and if such a defect has caused damage to the life, body or property of others, then the manufacturer or importer will be liable for such damage. This regime imposes strict liability, regardless of whether the manufacturer or the importer has been negligent; however, where the defect could not have been discovered given the state of scientific or technical knowledge at the time of delivery, the manufacturer will not be liable for the defect. Dealers, rent-a-car companies, repair service providers and suppliers of parts are not subject to strict liability and may be held liable only when they have been found to have been negligent. The judgment is solely made by the judge. There is no jury trial in the Japanese litigation system. The parties to the case as well as the court may request expert witnesses to testify or produce documents regarding the analysis of issues in the case, but the judge is not bound by the expert's opinion. The plaintiff may claim actual damages, as well as consequential or incidental damages attributable to the defect or negligence; however, the court does not grant punitive damages, and an award for punitive damages in other jurisdictions is not enforceable in Japan. Overall, product liability claims for a defective vehicle or a recall are relatively rare.

On 1 October 2016, a new class action-like regime was introduced in Japan (Special Provisions for the Civil Procedure for Collective Recovery of Loss of Assets of Consumers Act (Act No. 96 of 2013)). This regime is two-tiered. At Tier 1, a qualified consumer organisation must prove that the relevant manufacturer owes common liability to several consumers. Then, at

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Tier 2, each consumer can have a consumer organisation file its claim with the summary court. The Tier 1 action may only be taken by a qualified consumer organisation (QCO) that has received the required designation to act from the prime minister pursuant to the Consumer Contract Act (Act No. 61 of 2000, as amended). As at February 2023, there were four QCOs (out of a total of 23 QCOs in Japan) that had designation from the prime minister.

This class action-like regime does not cover strict product liability. Furthermore, it only entitles the recovery of actual losses and specific performance and does not extend to an indemnity for any consequential losses, loss of profits, injury or bodily harm. The action can only be made against a defendant who has direct privity of contract with consumers – not against third-party car manufacturers, importers or parts suppliers. Thus, the regime has limited application, and it does not significantly impact the automotive industry in Japan.

DISPUTES

Competition enforcement

- 9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

Antitrust enforcement

Antitrust measures are enforced by the Japan Fair Trade Commission (JFTC) based on the Act on Prohibition of Private Monopolisation and Maintenance of Fair Trade (Act No. 54 of 1947, as amended) (the Antitrust Act). Traditionally, the JFTC has been active in the automobile parts sector in terms of enforcement against cartel activities. The JFTC undertook major enforcement actions against cartels in this industry in 2012 and 2013 – comprising antitrust surcharges of nearly ¥12.9 billion against four major wire harness manufacturers in 2012, nearly ¥3.4 billion against seven electrical component manufacturers, and nearly ¥4.7 billion against three headlamp manufacturers.

In recent years, however, the JFTC has not implemented aggressive enforcement. The JFTC issued only nine cease-and-desist orders in financial year 2021 imposing aggregate surcharges of approximately ¥2.18 billion; nine cease-and-desist orders in financial year 2020 imposing aggregate surcharges of approximately ¥4.32 million; 11 cease-and-desist orders in financial year 2019 imposing aggregate surcharges of approximately ¥69.27 billion; eight cease-and-desist orders in financial year 2018 imposing aggregate surcharges of approximately ¥260 million; and 13 orders in financial year 2017 imposing aggregate surcharges of approximately ¥1.89 billion.

The rate of surcharges is generally up to 10 per cent of sales in the event of a cartel for large-scale manufacturing companies. Companies can take advantage of leniency by voluntarily reporting the violation to the JFTC, and the first reporter before initiation of the JFTC's investigation may receive a 100 per cent reduction in the surcharges. In practice, many cases are closed without formal cease-and-desist orders or surcharges. Companies subjected to the JFTC's investigation are entitled to hearings at the JFTC.

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However, as the automotive industry is becoming increasingly competitive and is facing the rise of game-changing new technologies, manufacturers are becoming keen to participate in joint development and procurement of new technologies (electric vehicles, next-generation batteries, radars and sensors), horizontally with their competitors in the market as well as vertically with suppliers and parts manufacturers. This trend inevitably increases tension with antitrust regulations, and participants in the market should be aware of this risk when developing new business models.

Brand owners are becoming more conscious of the brand strategy of increasing control of dealerships to develop a more effective distributorship network and redefine their brand image. Japanese competition regulations provide extensive rules against unfair trade practices and abuse of superior bargaining power, and in this context brand owners should be aware of the risk that heightened control over dealership and service providers may give rise to competition law concerns.

Follow-on litigation

There are three types of follow-on litigation in competition cases:

- litigation against the JFTC;
- civil litigation raised by a party who has incurred damage; and
- a derivative suit by shareholders against the directors of a company that has participated in cartel activities.

Litigation against the JFTC

A company that is subject to a JFTC enforcement action may challenge the same in court. This type of litigation is relatively rare but includes large-scale disputes involving important Antitrust Act issues.

Civil liability to affected parties

Private parties affected by a violation of the Antitrust Act, such as consumers, suppliers, distributors and competitors, can bring a civil action for damages and an injunction against the company that allegedly committed the violation. A company that has been subjected to enforcement by the JFTC as having been involved in cartel activities could have civil liability for damages incurred by customers and end users. Once subjected to enforcement by the JFTC, the company may not raise a defence that they had no wilful misconduct or negligence. This type of litigation can be used not only in a protective manner, but also in an aggressive manner to attack unfair trade practices or abuses of superior bargaining power of vendors, customers or competitors.

Director's liability

Directors of a company that has participated in cartel activities can be sued by shareholders of the company by way of a derivative suit. In the wire harness cartel case, the shareholders of a related company sued its 22 directors in a derivative suit for negligence based on their participation in the cartel and, in particular, failure to apply for leniency by cooperating with

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the JFTC. This case was finally settled with the payment of ¥520 million by the directors to the company in 2014.

Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

There is no specific type of dispute especially significant to the automobile industry. Automotive industry companies should be prepared for contractual disputes with customers or suppliers, product liability and consumer issues, and intellectual property issues (including disputes). Typical types of disputes involve termination of the supply or distribution agreement; product liability; and misleading advertisement and employment issues. However, automotive-related disputes are relatively rare in Japan as compared to other jurisdictions. Disputes between domestic companies that have not been successfully resolved through negotiation are usually submitted to the courts for litigation, while large-scale international cases are submitted for arbitration. Japanese courts tend to resolve disputes by in-court settlement.

Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

To ensure a continued supply of parts, automotive manufacturers tend to have two choices: finding an alternative supplier or assisting the distressed supplier to continue its operations. As disruption of a supplier's business may potentially have a substantial impact on the automotive industry, vehicle manufacturers and suppliers sometimes support distressed suppliers to mitigate the systemic risk. Banks are another key player that can exercise initiative and consultancy while dealing with a distressed supplier under the Japanese traditional 'main bank' regime. M&A is also common in this context.

The distressed suppliers may go into insolvency procedures including:

- a bankruptcy procedure (Bankruptcy Act (Act No. 75 of 2004, as amended));
- a civil rehabilitation procedure (Civil Rehabilitation Act (Act No. 225 of 1999, as amended));
- a corporate reorganisation procedure (Corporate Reorganisation Act (Act No. 154 of 2002, as amended)); and
- a special liquidation procedure (Companies Act (Act No. 86 of 2005, as amended)).

Among these, the bankruptcy and the special liquidation procedures are classified as liquidation-type processes, while the civil rehabilitation and the corporate reorganisation procedures are recovery-type processes where the focus is on preserving the business as a going concern.

Companies seeking restructuring tend to choose civil rehabilitation procedures where the existing management can keep control of the company as a debtor-in-possession (DIP). The management of the distressed company may ask for assistance from banks, vendors

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and customers to rebuild the distressed business, or transfer the intact part of its business to a competitor to raise the liquidity available to inject in the distressed business. In cases where the distressed company has made an early decision to initiate restructuring, a pre-packaged bankruptcy strategy is often used to mitigate the impact. On the other hand, the use of non-DIP-style corporate reorganisation procedure is limited to a small number of bankruptcies of large-scale or listed companies.

After an airbag defect issue, one supplier filed an application for the civil rehabilitation process with the Tokyo District Court in June 2017, and its 14 affiliate companies around the world filed similar insolvency procedures in their respective jurisdictions. This civil rehabilitation process became the largest insolvency procedure of the manufacturing industry in the post-war era in terms of its debt amount of ¥1,082 billion. Pursuant to the civil rehabilitation plan submitted to the court in February 2018, the supplier transferred its assets, including its intact seat belt and child safety seat businesses, to a Chinese-owned US company in the same industry in April 2018, and distributed compensation to its creditors, which appears to cover only ¥500,000 and 1 per cent of any amount exceeding ¥500,000 for each creditor. Vehicle manufacturers were exempt from this settlement and will be compensated at a later stage from the rest of the fund after repayment to non-vehicle manufacturer debtors, which will not cover a significant percentage of the aggregate debt amount. Despite the impact of the case, no bankruptcy owing to the supplier's issues was reported. This is because the supplier had been continuing to make payments to its suppliers based on the existing contractual conditions, which is allowed under the Civil Rehabilitation Act. Affected suppliers may take advantage of the safety net guarantee by the Small and Medium-sized Enterprise Credit Insurance Act (Act No. 264 of 1950, as amended), as well as the safety net loan from the Japan Finance Corporation, a government-affiliated financial institution, both of which are designed to minimise systemic risk or domino effects on the whole industry.

Another route for distressed suppliers is business rehabilitation alternative dispute resolution (ADR). On 30 January 2019, Akebono Brake filed an application for business rehabilitation ADR with the Japanese Association of Turnaround Professionals – the only specified certified dispute resolution business operator as of March 2019. In this regime, the debtor, with the involvement of a specified certified dispute resolution business operator, under the Act on Promotion of Use of Alternative Dispute Resolution (Act No. 151 of 2004, as amended) and the Act on Strengthening Industrial Competitiveness (Act No. 98 of 2013, as amended), requests that financial institutions allow the rescheduling of loan payments and that the financial institutions not file for insolvency procedures. If the rehabilitation plan is approved by a unanimous vote of the financial institutions that are creditors, the loan arrangement is collectively modified in accordance with the rehabilitation plan. Business rehabilitation ADR only covers debts to financial institutions and does not affect transactions with other parties including suppliers, distributors and customers. This regime is designed to combine the advantages of private rehabilitation such as flexibility, speediness, confidentiality and preservation of the going-concern value of the distressed company, with the fairness and stability of the statutory procedures.

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Intellectual property disputes

12 Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

The automobile industry is one of the most intellectual property-oriented sectors. For example, three of the top 10 companies that were granted the most patents in Japan in 2018 were automobile-related companies and many more companies with automobile parts divisions are listed in the top 100.

However, intellectual property disputes are actually rare in the Japanese automotive industry. Vehicle manufacturers and parts suppliers tend not to resort to aggressive measures even if they suspect infringement of their intellectual property. This is in part because the intellectual property divisions in the automotive industry are like a small society, and it is often more profitable to cooperate than dispute, typically through a cross-licence agreement. In addition, an increasingly common strategy for vehicle manufacturers is to disclose, instead of monopolise, core intellectual property such as hybrid vehicles and fuel-cell vehicles, in view of leading the technology trends.

Other reasons may include the fact that intellectual property litigation is usually costly and lengthy, and the expected recovery awarded by the court does not cover the cost. In 2019, the average timeline for all types of IP litigation was 14.9 months and many cases are settled without the court issuing any judgment. Subsequently, intellectual property disputes are not resolved easily.

EMPLOYMENT ISSUES

Trade unions and work councils

13 Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

Although the automotive industry has long outgrown the traditional labour-intensive industry, employment is still a critical issue. There remains a hard-working culture in some Japanese companies, especially in the countryside where many manufacturing facilities are located, and this may cause issues such as overwork, harassment and non-compliance with regulations. The major sources of employment law include the Labour Standards Act (Act No. 49 of 1947, as amended), the Labour Contracts Act (Act No. 128 of 2007, as amended) and the Industrial Safety and Health Act (Act No. 57 of 1972, as amended). In the course of the government-led work style reform initiatives, a package of regulatory updates came into effect from 1 April 2019, which set shortened overtime limitations and mandatory paid leave requirements.

Japanese employment law provides extensive protection for employees against termination and salary cuts, and it is extremely difficult to terminate employees even for redundancy or underperformance. Many OEMs and suppliers, therefore, use temporary staff and dispatched workers to procure a workforce with flexibility to deal with the volatile market demands. This

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area of employment law is heavily regulated, and employers should be aware of the detailed regulatory requirements. For example, if an employer hires a fixed-term employee for an aggregate period of over five years, the employee is entitled to indefinite employment under the same conditions (the employer may reset the aggregate periods by placing a six-month non-hired period in between). A survey by the Labour Standards Bureau of the Ministry of Health, Labour and Welfare revealed in December 2017 that seven out of 10 major OEMs in Japan have limited the term of fixed-term employees to avoid lapsing into indefinite employment. At the same time, as Japan is facing population decline and a shortage of workers, it is crucial to secure competent employees without incurring inadvertent future risks.

One characteristic of the employment environment in the automotive industry is the labour union. Many OEMs and auto parts suppliers have active labour unions, and the industry-wide Confederation of Japan Automobile Workers' Unions (JAW) purportedly has approximately 790,000 members. While the unionisation rate is drastically decreasing across all industry sectors (17 per cent on industry average in 2019), JAW maintains a relatively high unionisation ratio. This is supported by a union shop arrangement, or a type of collective bargaining agreement between an employer and a labour union under which the employer will ensure that all employees belong to the labour union and fire those who do not wish to join any union (Labour Union Act (Act No. 174 of 1949, as amended)). The unions negotiate the following year's salary review every spring, which is referred to as 'spring labour offensive', but strikes and serious labour disputes have been relatively rare in recent years under the Japanese collective bargaining culture described as 'labour-management harmonisation'.

The conservative government party has been promoting a campaign to raise wages to boost the economy and requested that major automotive companies increase wages, while the Japan Business Federation – an association composed of the management of major companies and industry associations – has been reluctant to take on major salary reform.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

Automated or autonomous vehicles

The Japanese government has established a roadmap for the introduction of automated driving. The roadmap has defined the five automated driving levels in Japan, with fully autonomous driving at Level 5. It also addresses the steps required for the implementation of automated driving levels from Level 2 to Level 5, with the goal of realising the operation of autonomous vehicles on public roads. In accordance with a previous discussion, the government issued the outline of the legal framework preparation for automated driving in April 2018, setting out necessary regulatory updates and potential legal issues posed by automated vehicles.

On 1 April 2020, amendments to the Road Transport Vehicle Act (Act No. 185 of 1951) (RTVA), the Safety Standards for Road Transport Vehicles, Ministry of Transport Ordinance

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(Ordinance No. 67 of 1952) (the Safety Standards) and the Road Traffic Act (Act No. 105 of 1960) (RTA) took effect, making it permissible for vehicles operating with automated driving systems (ADS) classifiable as SAE Level 3 to be generally driven on public roads in Japan. (The SAE Levels of driving automation, developed and published by SAE International, offer one of the most globally recognised systems for defining the different levels of driving automation. They are set out in SAE International's Recommended Practice J3016, last published in June 2018.) More specifically, 'automated operation device' was added to article 41, paragraph 1 of the RTVA, which sets out the list of parts and devices that may be incorporated within vehicles subject to compliance with the Safety Standards. Article 48 of the Safety Standards and article 72(2) of the Notice Providing for Details for the Safety Standards were newly added to set out the standards that must be satisfied with respect to the functions and performance of the automated operation device. And the definition of 'driving' under the RTA was amended to include driving by the use of an automated operation device.

As the RTA continues to prohibit the general use on public roads of vehicles relying solely on SAE Level 4 ADS technologies, the guidelines issued by the Ministry of Land, Infrastructure, Transport and Tourism (MLIT) and the National Police Agency (NPA) provide useful guidance for conducting tests using vehicles equipped with SAE Level 4 ADS technologies.

From 2017, insurance companies are offering a discount of up to 10 per cent on the insurance premium for vehicles equipped with advanced safety technologies including pre-crash brakes.

Requirements

MLIT issued guidelines for the safety technologies of automated vehicles in September 2018. These guidelines, although not legally binding, set out 10 elements to ensure the safety of automated driving:

- setting of Operational Design Domain;
- safety of the automated driving system;
- compliance with the Safety Standards;
- human-machine interface;
- data logging;
- cybersecurity;
- emergency measures for the autonomous transportation system;
- safety evaluation;
- in-use improvement; and
- provision of information to the user.

These guidelines were designed to be interim standards for the development of automated vehicles until legally binding standards are established. Some of these standards are now provided for in the newly added clauses of the Safety Standards, which are legally binding. The RTA sets the obligation of safe driving upon the driver, and the government maintains the concept that the driver should be responsible for driving and any resulting accidents, even in Level 3 automated driving.

Level 4 is still under debate owing to the Convention on Road Traffic (Geneva, 1949) and the RTA assuming the existence of a driver on board. However, MLIT has announced an

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amendment to the Safety Standards enabling experimental operations of a Level 4 autonomous vehicle without a steering wheel, or acceleration and brake pedals on a public road under certain conditions including the time, weather, speed limit, route of operation, emergency kill switch and safety staff.

Experiments on public roads

MLIT requires no special designation for the experimentation of automated vehicles on public roads if it satisfies the Safety Standards and a driver is in the vehicle. MLIT may also grant special permission for vehicles that do not comply with the Safety Standards to enable experiments on public roads. In both cases, testing must comply with the specific guidelines issued by the NPA in May 2019.

A number of exceptional permissions for testing have been granted, for example:

- in January 2019, as part of a series of experiments ongoing since 2018, MLIT and the Ministry of Economy, Trade and Industry (METI) jointly conducted an experiment for automated truck platooning using cooperative adaptive cruise control that will enable autonomous driving in platooning trucks on the motorway. One impetus for this programme is Japan's ageing society and workforce shortage. MLIT successfully completed demonstration tests for automated truck platooning in February 2021 and, in September 2022, the International Organization for Standardization issued an international standard for truck platooning systems proposed by Japan;
- an IT venture company and a major taxi operator conducted a series of experiments with autonomous taxis (with a security attendant in the driver's seat) and provided services to passengers on public roads in the urban area of Tokyo;
- the prefectural government of Aichi tested an autonomous vehicle on public roads in a suburban area in December 2017;
- an OEM and IT venture jointly conducted a series of experiments of autonomous taxis (with a security attendant in the driver's seat) and provided services to passengers on public roads in the urban area of Yokohama; and
- METI and MLIT started experiments on public roads in Fukui. This experiment tested autonomous vehicles controlled by a remote autonomous driving system and has been authorised as Level 3 autonomous driving, a first for Japan.

The National Agency for Automotive Safety and Victims' Aid has included pre-crash braking systems and lane keep assist systems in the list of test items from 2014.

Expected legislation

In December 2018, the NPA announced the draft of an amendment to the RTA to allow the use of a mobile phone in Level 3 autonomous driving. The amendments to the RTVA and the Safety Standards that introduce the automated operation device also require that the vehicle maintains a log of automated driving and that the driver submit the log to the police under certain circumstances.

Legislative reform also extends to the civil liability of the driver. Under the Automobile Liability Security Act No. 97 of 1955, as amended, the primary liability for losses caused by a traffic accident is assigned to the operator of the vehicle (eg, the owner of the vehicle or the business

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owner of a transportation service – not necessarily the driver). The burden of proof (to disprove negligence) in an accident is shifted to the operator, and the operator will be held liable for damages caused by the accident unless the operator successfully proves that the operator exercised due care; the victim or a third party was at fault; and the vehicle did not have any defects. An MILT working group confirmed on 20 March 2019 that this framework will be maintained for autonomous vehicles.

On 4 March 2022, the Japanese government made a cabinet decision for a draft amendment to the RTA, which once incorporated into law will permit Level 4 automated vehicles to be driven on public roads in their fully automated driving modes under certain conditions. A Diet session passed the bill on 19 April 2022, and the RTA amendment took effect on 1 April 2023. One condition is that Level 4 automated vehicles may need to be able to run on unmanned, automatic mobile services in depopulated areas. The permission acquisition process for the autonomous operation of vehicles that the RTA amendment establishes is summarised as follows:

- a person who wishes to engage the Level 4 autonomous operation of a vehicle without a driver must obtain the permission of the Prefectural Public Safety Commission;
- the Commission must hear the opinions of the mayors and other heads of municipalities of the prefecture before granting the permission; and
- the RTA amendment will set out the matters to be observed by permitted persons and the measures to be taken in the event of a traffic accident, such as the establishment of a system for remote monitoring.

Connected vehicles

OEMs and suppliers should note that advanced equipment for connected vehicles may be subject to additional regulations; for instance, radio devices and wireless communication are as regulated as automobiles. The available bandwidths and requirements for the use of radio devices are regulated by the Radio Act (Act No. 131 of 1950, as amended), and on-board communication services for automobiles may trigger filing obligations with the Ministry of Internal Affairs and Communications under the Telecommunication Business Act (Act No. 86 of 1984, as amended).

The amendment to the RTVA requires that online updates of automated driving programmes are approved by the National Agency for Automobile and Land Transport Technology in advance.

The use of big data will raise concerns regarding personal information protection.

Hybrid, plug-in hybrid, electric vehicles and fuel-cell vehicles

The strategy for low- and zero-emission vehicles varies depending on the vehicle manufacturer. Hybrid vehicles (HVs) are commonplace today and are also increasing in popularity for heavy-duty vehicles. METI has been promoting plug-in hybrid, electric and fuel-cell vehicles (FCVs) by offering financial aid for the acquisition of such clean energy vehicles and the establishment of battery chargers and hydrogen stations. The Tokyo Metropolitan Bureau of Transportation and Keihin Kyuko Bus have placed fuel-cell buses on regular service.

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On 12 March 2019, the Agency for Natural Resources and Energy under METI revised its roadmap for the promotion of FCVs, first published in June 2014 and later revised in March 2016. According to this ambitious roadmap, the agency is aiming to increase the number of FCVs to approximately 200,000 by 2025, and to 800,000 by 2030, and to increase the number of hydrogen stations to 320 by 2025, and to 900 by 2030. In addition to revising old targets and setting new targets (such as reducing the price gap between FCVs and HVs from ¥3 million to ¥700,000 and halving the cost of fuel-cell buses to ¥52.5 million), the 2019 roadmap establishes a committee of experts for evaluating and following up on progress in each field under the roadmap.

Also, the Safety Standards are constantly being updated to accommodate the requirements for these clean automobiles, including in relation to batteries, high-voltage cables, fuel cells and hydrogen tanks.

Car or ride sharing

Pursuant to the Road Transport Act (Act No. 183 of 1951), a licence is required for operating a taxi or passenger vehicle transportation business, which is defined as a service that gives rides in a car to others for consideration on demand. Paid ride-sharing services cannot operate under the current legislation in Japan (though one ride-sharing service limits its services to hailing of high-end licensed taxis with a professional chauffeur). By the same token, a Chinese transportation network company recently launched a taxi booking service, instead of a ride-sharing service, in Japan.

In 2015, one ride-share application service provider started testing its service in Japan without the passenger paying the tariff to the driver. Instead, the driver received remuneration from the ride-share company on the basis of a data provision fee. Nevertheless, MLIT requested that the service provider stop the tests on the basis that such a payment still falls within the definition of 'consideration'. However, MLIT also noted that the payment of a small amount that can be seen as a voluntary expression of gratitude or reimbursement of the actual expenses incurred, such as fuel, motorway and parking fees, will not be regarded as 'consideration' and is, therefore, acceptable. Other companies have launched similar matching apps.

A car-sharing service is feasible as a sort of rent-a-car service subject to the licence requirement under the Road Transport Act, and several rent-a-car companies have been operating car-sharing services in urban areas making use of vacant parking lots. However, it is prohibited for individuals to hire out cars as a business. In addition, drop-offs in places other than registered parking spots are not permissible, because the vehicle registration system requires the specification of a 'primary place of use' where the vehicle is usually parked.

However, in contrast with the above, the government has been promoting various sharing economy policies and designated a rural town in Kyoto prefecture as a national strategic special zone to experiment with deregulation. The first ride-sharing service operating without a taxi licence was launched in May 2016.

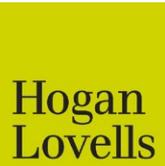
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UPDATE AND TRENDS

Trends and new legislation

- 15** | Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

There are no updates at this time.



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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

In recent years, the automotive industry has continued to be a vital pillar of the Mexican economy, representing approximately 3.6 per cent of Mexico's gross domestic product and 18 per cent of the national manufacturing GDP, standing as the second most important

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manufacturing activity after the food industry. It creates roughly one million direct jobs (even considering the 62,000 jobs lost in the industry during the pandemic). In 2022, the automotive industry remained one of the primary sources of foreign investment in Mexico, with over US\$50 billion invested in the country. The sector has also been a significant contributor to the country's exports, with vehicles and auto parts accounting for approximately 30 per cent of Mexico's total exports.

The automotive industry in Mexico has been growing at a fast pace. The country offers advantages to OEMs, as well as to Tier 1 and Tier 2 companies, such as a skilled workforce, a privileged geographical location and access to multiple international markets thanks to the number of international treaties signed (over 45 countries and counting).

In terms of production, the industry is divided into three main categories: light vehicles, heavy vehicles and auto parts. In 2022, around 4,038,366 light vehicles were produced, representing a 9.1 per cent increase compared to 2019. The production of heavy vehicles also increased by 12 per cent compared to 2019, with a total of 240,035 units produced. The auto parts sector also saw growth, increasing by 5.1 per cent compared to 2019 and reinforcing Mexico's position as the fifth-largest auto parts producer in the world and the largest in Latin America. Mexico dropped one position to become the seventh-largest vehicle manufacturer globally with the United States being its largest export market.

The national auto parts industry predicts that Mexican production will continue to grow in the coming years, along with the generalised recovery of the global economy and an expected 3.2 per cent increase in the Mexican economy alone.

Currently, Mexico has over 22 assembly plants (with further plants being planned for construction) and a powerful Tier 1 supplier network with over 700 suppliers countrywide (at least 95 per cent of all Tier 1 companies are present in Mexico). Historically, the states of Sonora, Coahuila, Puebla, Mexico, Guanajuato, Nuevo León, Querétaro and Aguascalientes have generated the vast majority of the total vehicle production.

Regarding exports, Mexico ranks as the fourth-largest exporter in the industry. In 2022, Mexican vehicle exports decreased by 2.9 per cent compared to 2021, mainly due to supply chain disruptions caused by the covid-19 pandemic. Mexico currently exports over 80 per cent of its total vehicle production, accounting for approximately US\$1 out of every US\$4 received by the country from exports.

There are many destinations for Mexican exports, the main one (as mentioned above) being the United States, receiving around 77 per cent of the country's vehicle production. Canada receives around 7 per cent, Germany 5 per cent, Colombia 1.5 per cent and Brazil 1 per cent. Exports to other destinations have also increased. For example, in the past few years, China has become Mexico's sixth most important export destination.

Many predict that in the next year or two (with the arrival of Japanese and German OEMs, Tesla's Gigafactory and the expected investment from Chinese companies) the industry may reach production of 5 million light vehicles in more than 30 plants. This additional manufacturing may move Mexico's world rankings on production and exports upwards.

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Despite new plant cancellations, industrywide suspension resulting from the covid-19 pandemic and a light vehicle sales decrease, Mexico continues to attract foreign investment in its automotive industry. For instance, in early 2022, Japanese automaker Mazda announced its plan to invest US\$500 million in its Mexican plant, which will be used to produce hybrid and electric vehicles. Additionally, Chinese automaker Great Wall Motor has announced its plan to invest US\$1.1 billion to build a new plant in Mexico, marking the company's first manufacturing facility in the Americas.

Furthermore, Volkswagen is investing US\$233.5 million to expand its plant in Puebla, with a focus on electric vehicle production. Another German automaker, BMW, is also expanding its operations in Mexico, with the construction of a new plant in San Luis Potosí. Finally, Tesla has announced the construction of its Gigafactory in the state of Nuevo León. The factory is expected to produce batteries and electric vehicles.

One major trend in the Mexican automotive and mobility industry is the shift towards electric and hybrid vehicles. The Mexican government has set a target of having one million electric and hybrid vehicles on the country's roads by 2024 and has announced incentives for the purchase of these vehicles, as well as for the installation of charging infrastructure. This trend is also driven by consumer demand for more environmentally friendly vehicles.

Another trend is the use of new technologies such as autonomous driving and connected cars. Companies in Mexico are investing in research and development in these areas, and some have already introduced connected features such as advanced safety and infotainment systems in their vehicles.

Another trend in the Mexican automotive and mobility industry is the growing interest in nearshoring, which is the practice of bringing manufacturing and production processes closer to the intended market. Mexico's proximity to the United States, which is a major market for automobiles, makes it an attractive destination for nearshoring. Companies are looking to reduce supply chain disruptions, lower transportation costs and shorten lead times by moving their manufacturing operations to Mexico.

COMMERCIAL OPERATIONS

Regulation

- 2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

To export to new markets, OEMs must comply with several legal and technical requirements. In Mexico, imports and production of new vehicles are subject to a wide range of directives and regulations.

There are several Official Mexican Standards (NOMs) regulating the technical requirements of certain products. The main government agencies that are authorised to issue NOMs in the automotive sector are the Ministry of the Environment and Natural Resources regarding

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environmental issues, the Ministry of Communications and Transportation for all transportation and safety matters and the Ministry of Commerce and Industrial Promotion.

Several models have now been discontinued as a result of the application of NOMs setting minimum security measures and are currently being substituted with other models. For illustrative purposes, in 2017, a pre-eminent OEM decided to stop producing one of its historically best-selling vehicles and to terminate the production and sales of the fairly successful model that had arguably taken its place. Some other manufacturers are looking for alternate models to sell in the Mexican market because of stricter security measures required by the government (items such as ABS, airbags and defrosting systems, among others, which were not mandatory in past years). As of 2021, manufacturers are not permitted to sell automobiles that do not include the new minimum safety features. The environmental issues addressed by NOMs are mostly on fuel emissions and regulation of noise, clean energies and diesel. In the case of safety matters, the requirements are mostly about mechanical conditions and dimensions of the vehicles, as well as brakes, brake callipers and other safety devices and features.

It is essential to meet the NOM requirements and provide evidence of compliance with such standards to import or produce vehicles in the Mexican market. Under Mexican law, the NOM certificate holder is responsible for warranty, maintenance and product liability. Such certificates are not transferable, although manufacturers with NOM certificates may extend their usage rights to their distributors.

The government has historically supported companies complying with responsible environmental practices. This is part of a corporate social responsibility drive aimed at the incorporation of fair values into business practices.

Finally, a new free trade agreement (the United States–Mexico–Canada Agreement (USMCA)) has become effective and replaced the old North American Free Trade Agreement. This new treaty allows for a transition period of a couple of years for automakers to use at least 75 per cent North American-made parts in imported vehicles. Of the rule of origin, 40 per cent must be accounted for by labour that is paid at a salary not below US\$16 per hour, which means that low labour costs cannot account for the entire calculation. Automotive companies will need to adapt to this new reality within their fixed costs and implement it into their supply chains.

Development, manufacture and supply

3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

Automotive companies usually operate using the IMMEX maquiladora programme, which allows a Mexican entity to engage in manufacturing activities (mainly for exportation purposes) and temporarily import parts and materials on a duty-free basis. The usual IMMEX maquiladora structure is through a principal, which is a foreign entity residing in a country with which Mexico has a tax treaty in place. This entity will hold the manufacturing agreements, which set forth the organisational, operational and economic terms, and are entered into by the principal and the manufacturing Mexican entity.

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Maquiladoras may be established anywhere in the country and, if certain requirements are met, they can also sell a part or even all of their production locally (in which case import duties for the final products must be paid based on the corresponding harmonised tariff number). Usually, maquiladoras are incorporated as stock corporations or limited liability companies, which have very low capital requirements and allow foreign investors to own up to 100 per cent of the corporate capital of such entities.

Among the many advantages of operating under the IMMEX programme are temporary duty-free imports on raw materials, exemptions on import duties and VAT refunds.

There are also sectorial relief programmes applicable to the vehicle and auto parts industry that aim to give companies a preferential tariff rate to import goods intended for production, regardless of the country of origin, and which also foresee preferential trade tax rates to export the resulting products.

To create manufacturing clusters, lower transportation and insurance costs, and reduce idle inventory volumes, assembly plants commonly require that their suppliers be as physically near to them as possible, prompting suppliers to set up locally. This accumulation of manufacturing plants and multiple suppliers is not uncommon and has been the source of significant growth of the industry and impact on investment, employment and economic relevance.

Distribution

4 | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

Before the importation procedure begins, the vehicle's compliance with NOMs must be ensured and applicable regulations must be fulfilled. The actual importation process is handled by a customs broker.

Since 2004, it has been possible to import new vehicles from the United States, Canada and member states of the European Union without any import tariffs. Recently, Brazil and Mexico eliminated import tariffs on light vehicles and auto parts, while the import tariff on heavy vehicles was eliminated during 2020. There are many regulations on this type of import establishing several requirements for such vehicles, including maximum mileage allowed for the vehicle to be considered as new, compliance with applicable NOMs and so on.

A few years ago, governmental decrees were issued in an effort to reduce the flow into Mexico of used vehicles purchased cheaply in the United States. This was the government's reaction to growing concerns about potential damage to the industry, the increasingly ageing motor pool, higher pollution levels, fuel inefficiency, maintenance costs and difficulties identifying such vehicles. However, on 20 January 2022, the current administration issued a decree to regulate this type of cars in 10 states in the country (Baja California, Baja California Sur, Chihuahua, Coahuila, Durango, Michoacán, Nayarit, Nuevo León, Sonora and Tamaulipas). The decree is seen as a setback by the automotive industry.

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Distribution is generally handled through distributors that enter into distributorship agreements with automotive manufacturers. These agreements usually contain standard contractual termination clauses (eg, failure to reach certain thresholds for certain periods of time and other performance requirements). Mexico does not have protective laws that require statutory indemnity when distributors or agents are terminated. Freedom of contract is the substance of all conditions between the parties to such relationships.

Mergers, acquisitions and joint ventures

5 | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

Mergers and acquisitions in the automotive industry are fairly standard compared to other M&A operations and can be done by purchasing assets, stock or shares of a target company or more companies to create a new one, or merging one into another.

Joint venture companies (ie, the creation of a new entity into which two existing entities transfer assets or capital) in Mexico are independent of their parent companies and must obtain a separate Federal Taxpayer Registry number and separate permits and authorisations. Usually, these new entities have shareholder agreements in place that provide for the corporate structure, management or business plans. Of special note when entering into an M&A or joint venture transaction of this nature are the manufacturing facilities and logistics of the target entity, as this will play a key role in the entity's access to the market and ability to take advantage of USMCA provisions, considering that the North America region is likely to continue to account for the vast majority of the entity's business.

Companies should get local legal advice to comply with all applicable laws, especially those regarding antitrust and economic competition, environmental, tax, labour and administrative provisions, all applicable NOMs and authorisations, licences and permits required before beginning operations. Given the size of players and greater consolidation, the anti-trust analysis is relevant, although a mitigating factor is that the market is usually analysed with a worldwide perspective and not merely what happens in Mexico – a point of view that is not prevalent in other industries when reviewed by the Federal Economic Competition Commission.

English is widely spoken in Mexican M&A transactions and agreements are often drafted in English, while jurisdiction and applicable law may be set to Mexico or a foreign jurisdiction (most commonly New York). Arbitration clauses are not uncommon in larger deals and contracts, and are considered to be a valid trade-off with local parties to avoid domestic courts asserting original jurisdiction.

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Incentives and barriers to entry

6 | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

Among the factors that may be considered as an incentive to invest in Mexico is its geographic location as neighbour to the world's largest vehicle market, the relatively low cost of the workforce, the high-level degree of specialisation of Mexican labour and the extensive network of free trade agreements, among others.

There are incentives such as tax privileges granted to companies operating under IMMEX programmes, providing many tax and administrative benefits such as avoidance of the general import tax and VAT payment, VAT refunds, reduced customs fees and simplified import and export declarations.

Other incentives can be found in the form of sectorial promotion programmes, which through their application may reduce most-favoured-nation import duties. These programmes support 22 different sectors, including the automotive and auto parts sectors. They also enable manufacturers to import their inputs at preferential tariffs to ensure they remain competitive. Most automotive inputs can be imported duty-free thanks to this programme. In addition, companies that comply with all regulations contained in the 'eighth rule' (licence issued by the Ministry of Commerce and Industrial Promotion) may access a mechanism that allows such companies to import materials, inputs, parts and components using a zero per cent rate.

Several Mexican states such as Sonora and Yucatán have developed their own policies and benefits for the industrial sectors that can be translated into several investor incentives. These measures include reductions in real estate prices and taxes, discounts or reductions of payroll taxes and even employee training programmes.

Federal and state governments are actively attracting automotive manufacturers into Mexico, providing additional benefits that should be analysed on a case-by-case basis.

Since the USMCA has become effective, many vehicle manufacturers have communicated their interest in expanding their investments in Mexico (and some have begun doing so). In addition, Mexico is expected to continue to reap benefits from the strained US–China relationship. With the US–China rivalry not ebbing, Mexico's advantageous geographic position and the rise of electric and hybrid vehicles in the industry (in which China is a leader), Mexico and China may become natural business partners, and companies may seek relocation to Mexico to avoid potential American tariffs imposed on their Chinese interests.

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PRODUCT SAFETY AND LIABILITY

Safety and environmental

7 | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

The technical and quality standards regarding safety and emissions that must be met for the Mexican market are contained in Official Mexican Standards (NOMs). Some of the most relevant NOMs include:

- NOM-194-SCFI-2015, containing minimum security measures for new light vehicles, including provisions on the technical requirements for many parts of the vehicle such as tires, ABS, braking lights, reverse lights, evaluation methods and verification procedures;
- NOM-042-SEMARNAT-2003, NOM-044-SEMARNAT-2006 and NOM-076-SEMARNAT-1995, regulating vehicle emissions, such as the maximum emission levels for vehicles, evaluation methods and verification procedures; and
- NOM-079-SEMARNAT-1994 and NOM-082-SEMARNAT-1994, regulating the maximum noise level for vehicles and the evaluation method thereof.

There are also regulations on security measures, such as marking of doors and frames so that the vehicle is equipped with adequate and accessible information to protect consumer rights and avoid theft. Additionally, there are many safety measures regulating technical specifications on seat belts, tires, brakes and other vehicle parts to protect consumers from bodily harm. These standards are generally issued in such a manner as to be aligned with international regulations. Manufacturers must be frequently updated on any new NOMs and additional requirements for them to comply and be able to continue business operations.

As an outstanding environmental measure applicable in the Mexico City metropolitan area, there is a Hoy no Circula programme that prohibits driving certain vehicles on certain days, depending on the results that such vehicles achieved in a mandatory contaminants emissions test. This measure only applies to the Mexico City metropolitan area, but other states are constantly looking at the implementation of similar strategies. The Mexico City metropolitan area encompasses Mexico City, the State of Mexico and Hidalgo.

Recalls are handled by the Federal Consumer Protection Agency through the issuance of a non-binding recall request to the relevant party to recall certain products. These recall requests are standard and in the case of non-compliance the consumer protection authority may assist the affected parties in filing suits. Additionally, manufacturers may recall defective products, which is common in large-scale recalls with a global reach.

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Product liability and recall

- 8** | Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

Product liability law in Mexico for defective products is based only on the fault of the manufacturer or any other person in the production chain whose actions or omissions result in damage. If direct damage is not caused, and there is no direct link between the damage and the alleged guilty party, it will be difficult to support liability claims.

Mexico's civil law considers product liability as an extra-contractual obligation (similar to tort in common law countries). The law provides that whoever has acted illegally or against good custom, and has caused damage to another, must repair the damage caused. Therefore, liability can only be asserted if damage was caused by the breach. The state does not operate any compensation schemes for particular products, but consumers may be able to file a claim if the defective product damages the individual and causes civil liability. These events are ruled by the Civil Code (federal or local).

Mexican law does not provide an obligation to recall defective products. But there are many companies with recall policies for defective products or failures that are used as a quality standard and as a practical measure to prevent future damage to consumers and to protect their brand and public perception.

Although Mexican legislation does not foresee recalling products as necessary, failure to do so may result in a liability claim based on negligence. A possible defence against liability claims exists if the accused party can prove it has complied with all legal and technical specifications for a product.

In this regard, collective actions are available in Mexico to prosecute consumer claims; these actions may also be brought directly by government authorities such as the Federal Consumer Protection Agency.

DISPUTES

Competition enforcement

- 9** | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

Mexico is considered one of the most competitive countries in the automotive market in terms of available products. There are well over 50 brands present in Mexico and around 2,600 auto parts companies.

In competition matters, the 2014 Federal Economic Competition Law, along with an amendment to the Constitution, created the Federal Economic Competition Commission (Cofece).

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Even though this commission follows the legal framework established by the previous one on monopolistic practices, some changes have been introduced regarding defining entry barriers to competition and access to essential raw materials. Even though Cofece has been very aggressive with its investigations and fining activities in other sectors, there has not yet been any major competition litigation related to the automotive industry in Mexico.

Cooperation between the competition enforcement agencies of Canada, the United States and Mexico has continued to strengthen, and Mexico's participation in joint investigations has increased. If a company is being investigated by one of these countries for a possible antitrust violation, its conduct and statements can be reported to and investigated by the authorities of the other countries.

Annual trilateral meetings of the aforementioned countries take place with the objective of ensuring and improving cooperation and coordination of antitrust policies and their enforcement.

Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

Disputes in the Mexican automotive industry are often resolved through arbitration if an agreement includes such provision. If the parties involved in the dispute belong to the United States–Mexico–Canada Agreement (USMCA), they often resolve their dispute through the special arbitration provisions applicable in their countries. This mechanism has been retained from the former North American Free Trade Agreement (NAFTA), with specific provisions allowing NAFTA investment-related claims to be submitted up to three years after the USMCA came into effect on 1 July 2020. Likewise, if parties are signatories to any other trade agreement that Mexico has entered into, an arbitration solution may be available for them.

Mexican courts recognise and enforce awards obtained by these mechanisms; however, if such dispute resolution mechanisms are not available, the dispute must be resolved through the application of Mexican law by the competent courts, which may not be as expedient as arbitration.

Finally, Mexican courts do not enforce remedies such as injunctions or other equitable remedies except for preliminary relief specifically enumerated in the Commercial Code, as well as stay of execution of the claimed act (similar to injunctions or stop orders) in amparo proceedings. Mexican courts do not award damages other than actual, direct and immediate damages and lost profits, and may not enforce judgments awarding them.

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Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

To strengthen the supply chain, Tier 1 and Tier 2 companies and OEMs are generally clustered near assembly plants. Nevertheless, sometimes supply interruptions can arise and adversely impact operations. An important step to avoid these scenarios is for manufacturers to be aware of the status, finance and reputation of their suppliers.

Although there are no legally established processes for this situation (other than bankruptcy laws), generally it is recommended for the manufacturer to consider three main preventive activities regarding its suppliers:

- reviewing information such as financial statements and analysing internal performance and price trends to develop a risk profile of each supplier;
- identifying issues such as distinguishing troubled suppliers from healthy ones and determining most likely areas of distress; and
- analysing and, if necessary, undertaking different options such as changing supplier (if alternative suppliers are an option and an efficient transition is commercially feasible), investing or acquiring said supplier, developing efforts with the supplier to improve communication and material process flows or creating an inventory stock to be used as a reserve.

We recommend having provisions included in the agreements entered into by manufacturers and suppliers that cover scenarios in which the supplier is distressed or failing. Obligations for suppliers to ensure an efficient transition to a new provider are common practice in similar agreements. Like NAFTA, the USMCA contains certain regional value content specific to the automotive industry that has been increased compared to the regional value content found in NAFTA, and manufacturers with a high North America export rate must be careful to comply with those changes directly and through their suppliers. The rules of origin in the automotive industry were a driver for the US-driven effort to replace NAFTA, and thus those changes are not insignificant and must be carefully analysed and implemented by any company in the sector with cross-border trade.

Intellectual property disputes

12 | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

The current state of intellectual property (IP) protection in Mexico is an ongoing concern. The legal system is sometimes considered inefficient and violations are punished with weak penalties. Therefore, it is highly recommended for automotive companies to aim for appropriate protection of IP rights when doing business in Mexico.

Although registering IP rights in another country may offer some benefits, foreign protection does not always extend to Mexico. As such, to ensure and duly protect IP rights, they must be registered and enforced under Mexican law.

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Local legal advice is needed when licensing and transferring technology or any IP right to prepare the agreements and fully protect IP from unauthorised use; franchising is a growing option to be considered.

Notwithstanding, intellectual property rights have received improved protection under the USMCA. This treaty includes a copyright term extended to 70 years, prohibitions on circumvention of technological protection methods and criminal and civil penalties for trade secret theft, among other things.

EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

The right to work in Mexico is protected by the Constitution, specifically articles 5 and 123. The Federal Labor Law broadly regulates all main topics contained in article 123 of the Constitution and is also responsible for regulating all labour aspects between employers and workers, including establishing minimum worker protection rights.

The United States–Mexico–Canada Agreement (USMCA) also provides certain rights to the workers in the automotive industry that were not previously standard practice. The USMCA includes wage requirements that could negatively affect one of Mexico's competitive edges (low labour costs), such as a provision that requires employees in the automotive industry to pay their workers a minimum of US\$16 (at least for 40 per cent of the parts and services that count towards the regional rule of origin), which is considerably higher than the previous median wage. Although this provision puts pressure on Mexico, different solutions have been discussed to lessen the impact that higher wages may have upon the industry. This treaty also provides that Mexican authorities must allow workers to form unions and be able to vote in a secret ballot to choose their union leader.

Historically, entities tended to establish an operating company holding all relevant assets and undertaking business operations, together with a services company that 'housed' the employees and was engaged by the operating company (in such a way that the employees would be subcontractors of the operating company). However, this structure was subject to recent legal reforms that banned outsourcing structures, and only certain specialist services are now allowed to be subcontracted. As a result of these reforms, many entities decided to merge their services companies with their operating structures, or to wind up the services companies and transfer all relevant employees to the operational entity.

Mexican law provides for alternative types of labour relationships, based on season, probation period, initial training and indefinite contract for fixed and periodic tasks, among others. A six-day, 48-hour working week is standard. Overtime pay is required if this level is exceeded (double pay for up to nine hours of overtime and triple pay for overtime of more than nine hours).

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Among the main rights enjoyed by employees are holidays, paid leave after one year of service, holiday bonuses and an annual bonus equivalent to at least two weeks' pay. Employers are responsible for these additional costs, which can add 30 to 35 per cent to an average salary.

Other relevant obligations of employers are:

- compliance with safety, health and environment regulations and Official Mexican Standards;
- mandatory wheelchair access if employing over 50 employees;
- obligation to give employees access to the full text of the collective bargaining agreement that may exist in larger companies;
- informing employees of the risks and dangers associated with their activities in the workplace;
- confirmation of paternity leave; and
- establishing policies against harassment and discrimination.

Pursuant to the Federal Labor Law, at least 90 per cent of the employees of a Mexican entity must be Mexican nationals, excluding directors, managing directors and general managers. Therefore, foreign personnel must not exceed 10 per cent of the total number of workers in a Mexican company.

Trade unions in Mexico have significant influence over the labour market. The Federal Labor Law protects the right of workers to associate without prior authorisation and provides the framework to create a trade union. For unions to be valid and in force they must be registered with local labour authorities or with the Secretariat of Labor and Social Welfare. Collective negotiations and agreements are signed by representatives of unions and the employer.

In practice, employees may be forced to have their workers unionised. This may occur when a trade union discovers that any given entity is not a party to a collective bargaining agreement, and may then demand that they are contracted with. For such purposes, it is common to have 'white unions', which are practically dormant but comply with the requirement, instead of having active unions, which may cause complications depending on their nature and intent.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

As shown by recent pivots in R&D approaches by several of the most well-known automotive brands, the development of new automotive technologies has experienced growth. Although the acquisition by consumers of vehicles equipped with new technologies is somewhat limited by their relatively high prices, the Mexican government has supported consumers by creating many incentives to encourage the purchase of these types of vehicles.

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In Mexico, sales of hybrid and electric cars are not high, but they are growing. In 2022, around 45,249 hybrid and electric vehicles (which accounted for the better part of all green vehicles sold in Mexico) were sold in the country, which shows an increase of around 5.3 per cent from 2021. In November 2022 alone the green vehicle sector sold 5,772 units, 908 of those were electric and 415 were connectable hybrids. As expected, 2020 resulted in a dramatic slump for these types of vehicles, the recovery of which will depend largely on that of the Mexican economy, as these types of vehicles tend to be higher priced than their petrol-powered competition.

Among the government incentives for purchasing green vehicles is an exemption for hybrid and electric vehicles from the federal tax on new vehicles. The Federal Electricity Commission has also developed several measures to foster the use of these vehicles, such as the installation of a different type of domestic measuring device for billing purposes, as well as preferential rates on electricity consumption. Regarding local government support, the regulations of some states include exemptions on the ownership and usage local tax. These vehicles are generally not affected by the Hoy no Circula programme or subject to emissions verification processes.

UPDATE AND TRENDS

Trends and new legislation

15 Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

The Mexican automotive industry is deeply interconnected with the respective industries in the United States and Canada, and they can be considered one regional industry encompassing all three countries. The implementation of the United States–Mexico–Canada Agreement (USMCA) and the gradual recovery of the economy in both the United States and Canada has resulted in a manufacturing and sales pick-up in the Mexican automotive sector. In this regard, experts expect that the USMCA is still likely to provide a stable and inviting framework for the automotive industry. China, Brazil and Spain, among others, have also announced their intention to invest in and trade with Mexico's automotive sector.

Although its impact is yet to be seen, the recent Trans-Pacific Partnership (TPP-11) creates a free trade bloc accounting for 15 per cent of the world's global trade, and will benefit 500 million people across the 11 signatory countries. Although it came into full effect in December 2018, it is expected that the TPP-11 will increase competitiveness of the signatory countries, create better work and health standards and open new options for the Mexican market. Subsequently, Mexico will become an even more attractive country for both domestic and foreign vehicle manufacturers.

Another emerging trend in the automotive and mobility industry in Mexico is the push towards electric and hybrid vehicles. In 2020, the Mexican government announced a plan to increase the number of electric vehicles on the country's roads, including incentives for the purchase of electric and hybrid vehicles and the installation of charging infrastructure. This could lead to an increased demand for electric and hybrid vehicles in Mexico, as well

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as new business opportunities for companies involved in the production and distribution of these vehicles.

Additionally, there are pending legislative proposals that could impact the automotive and mobility industry in Mexico. One such proposal is the Electric Mobility Law, which aims to promote the development and use of electric vehicles in the country. The proposal includes provisions related to the installation of electric vehicle charging infrastructure, incentives for the purchase of electric vehicles and the establishment of emissions standards for electric vehicles.



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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

The Netherlands is a relatively large player in the global automotive industry. It hosts

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a number of car and truck manufacturers. VDL Nedcar is probably the best-known car manufacturer in the Netherlands, currently producing passenger cars for BMW. Truck manufacturers located in the country include Scania, DAF Trucks and GINAF.

The Netherlands is predominantly known for its vast number of suppliers in the automotive industry. It is said that almost every passenger car contains products that are manufactured by Dutch suppliers. Suppliers are diverse and innovative, and are active in a wide variety of sectors relevant to the automotive industry, such as auto parts, rubber and plastic, mechanical engineering and electronics. Competitors are widespread and involve a significant number of companies. This is best shown by the number of manufacturers and suppliers that are a member of the RAI Association. Almost all manufacturers and suppliers located in the Netherlands are members of this Dutch association. According to its [website](#), RAI Association represents the interest of over 700 Dutch manufacturers and importers of, among other things, passenger cars, trucks, trailers and special vehicles.

RAI Automotive Industry NL is one of RAI Association's nine organisations. With over 200 members, it represents the interests of the Dutch automotive industry on a national and international level. The organisation focuses on global automotive and mobility solutions by joining forces with industry members and stakeholders and acting as a catalyst in the fields of innovation and education.

The Dutch automotive industry has benefited from high levels of skilled labour, a multi-lingual workforce, supportive corporate tax structure as well as being close to Europe's largest automotive markets, including Germany. This has encouraged the industry's strong growth over the past five years.

COMMERCIAL OPERATIONS

Regulation

2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

In the Netherlands, type approval is required for the registration, sale and entry into service of vehicles and vehicle parts. The most important regulation in this regard is Regulation (EU) 2018/858 (amended by Regulation (EU) 2019/2144 that has been applicable as of 6 July 2022). This Regulation has repealed Directive 2007/46/EC, which was mainly implemented in the 1994 Road Traffic Act and the Vehicles Regulation.

The Regulation provides for a revision of certain parts of the type approval system and, in addition to the administrative provisions and general technical requirements, the Regulation contains new provisions on market surveillance measures for vehicles already on the market.

In principle, a regulation has direct effect and therefore does not require implementation. However, member states are required to adopt necessary implementing regulations to ensure that the regulations can be effectively applied and enforced in a member state.

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In the Netherlands, the 1994 Road Traffic Act and the Vehicles Regulation have therefore been amended. The National Vehicle and Driving Licence Registration Authority (RDW) was appointed and remains the type approval authority. The Human Environment and Transport Inspectorate (ILT) has been designated as the market surveillance authority and is responsible for all tasks assigned to the market supervision authority in EU regulations.

RDW is in charge of granting EU type approvals. Before applying for a type approval, the manufacturer must demonstrate, by submitting a wide variety of documents, that the production process is in order. RDW issues the type approval after assessing test reports, information documents and a verification on the basis of the new requirements.

Once a type approval has been granted, it may become invalid if stricter rules come into effect. In that case, the manufacturer must apply to RDW for a supplement to the approval. This must also be done in the case of technical modifications.

Registration of vehicles

Pursuant to the Road Traffic Act, all vehicle owners must register their vehicles in RDW's register and hold a vehicle registration certificate. The registration can only succeed when the vehicle has been type approved by RDW. RDW issues registration certificates in credit card format (also known as registration cards), and the card complies with all applicable European legislation. A fine of up to €410 can be imposed upon the vehicle owner if it does not have a valid registration card.

Insurance requirements

Pursuant to the Motor Vehicle Liability Insurance Act, the owner of a motor vehicle (in whose name it is registered) is obliged to take out and maintain insurance for the motor vehicle. RDW checks daily whether vehicles comply with the insurance obligation. It carries out this duty on behalf of the Ministry of Security and Justice. If the vehicle owner fails to take out any maintain insurance, he or she can be punished by imprisonment for a maximum of three months or a second-category fine. In principle, a standard fine of up to €650 will be imposed.

Development, manufacture and supply

3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

The way automotive companies are operating in the Netherlands does not seem to differ from how they operate in neighbouring European countries. The supply is usually done based on a purchase order with a contract structure that is – generally – implemented by automotive OEMs and flows down the supply chain. This includes contractual provisions to safeguard trade secrets and intellectual property rights.

Supply relationships are to a large extent based on the OEMs or higher tier suppliers' purchase terms. Special arrangements do exist, such as volume contracts with particular suppliers and, as far as distributor contracts are concerned, most often comprehensive

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written agreements are in place. In addition, OEMs use highly standardised documents to cover specific issues, such as quality requirements, warranties, logistic requirements and indemnities. In cases where parties cooperate in a joint venture or similar arrangement, often detailed individual agreements on the joint venture are concluded.

With new technology and innovative companies entering the market and connectivity becoming essential to the automotive industry, concluding strategic agreements with companies specialising in connectivity and mobility becomes more important.

Distribution

4 | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

As far as the distribution of vehicles is concerned, this generally starts (at the first level) with the OEMs (or their national importers) who have set up a network of authorised distributors. The distributors (at the second level) enter into specific arrangements with dealers who (at the third level) sell and market the vehicles in their own name to end consumers.

Contractual arrangements within the distribution chain vary depending on the type of customer. Contracts entered into with high-volume or special customers, such as fleet-owners or lease-companies, materially differ from the contractual arrangements entered into with other customers.

As a general trend, direct relationships with end users are becoming increasingly important to OEMs.

This trend is accelerated by personalised connectivity and mobility services that are made available to end users, and the offering of online vehicle services fit to satisfy the end users' needs. In turn, personalised transport services fuel the demand for mobility provided as a service (MaaS). Based on some of these MaaS concepts, customers pay a flat rate subscription fee in exchange for being provided with a car and – on top of that – a wide range of car-related services as well as the option to change car models in frequent intervals or on demand. It is expected that MaaS will continue to gain popularity, potentially causing a decline in car ownership and an increase in innovative new mobility services, such as rental or lease and car-sharing services, thus making direct relationships with the end users even more important for car manufacturers. Dutch law does not provide for any specific statutory provisions on distribution agreements. Under Dutch law, a distribution agreement is – like all other contractual arrangements – governed by general provisions on contract law and by the principle of reasonableness and fairness (article 6:248 of the Dutch Civil Code). This principle of reasonableness and fairness may, under certain circumstances, limit or extend the contractual arrangements made by parties.

Regarding termination of distribution contracts, Dutch courts may, based on the above principle, extend the notice period parties have agreed upon. Neither Dutch legal literature nor case law confirm whether this principle of reasonableness and fairness should be considered a rule of Dutch mandatory law. The general perception, however, is that the principle

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of reasonableness and fairness should have no effect on a distribution agreement that is governed by foreign law or this effect should be very limited. Dutch legal authors who defend a limited effect of the principle of reasonableness and fairness state that the effect is limited to the possibility of granting the distributor financial compensation if the contractual notice period can be considered to be unreasonably short.

Under Dutch law, a reasonable notice period is determined bearing in mind all circumstances of the case at hand. One of the critical circumstances in this regard is the term of the agreement. Other circumstances that may affect the actual length of the notice period include the following.

Purpose of a notice period

The purpose of a notice period is to give the terminated party the opportunity to adjust its position in view of the forthcoming termination of the agreement. The length of the notice period should be appropriate for allowing the terminated party to adapt its position accordingly.

The length of a notice period also depends on the question as to what extent the distributor depends on the supplier. Important factors for this assessment are:

- to what extent are there substitutes for the products; and
- to what extent do the products of the supplier form a part of the entire product range of the distributor?

Duration of the distribution agreement

The duration of the distribution agreement is also significant in determining the duration of a reasonable notice period. A long duration of an agreement would justify a longer notice period.

Reason for termination

The reason for terminating the distribution agreement and the manner in which this is communicated to the terminated party may also have an effect on the duration of the notice period.

It should, however, be noted that if a contract expressly provides for a notice period, and this notice period is observed, it is unlikely that this notice period will be considered unreasonable.

Upon a valid termination of a distribution agreement entered into for a definite or fixed period of time, in principle, there is no ground for a termination fee. It is generally assumed that a distributor makes its profit by reselling the products (at a higher price). Any investments made by the distributor must be accounted for in the purchase price of the products. This is a key difference to an agency agreement, where the agent is entitled to a termination fee (provided certain conditions are met) based on European law.

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The reason for there being two approaches is the difference between how a distributor operates and how an agent operates. A distributor makes its own (re)sales to its own customers. After termination of a distribution agreement, the distributor still has its customer base (provided no alternative arrangements were made between the supplier and the distributor regarding the transfer of customers or customer base). An agent works for and enters into agreements on behalf of its principal. After termination of an agency agreement, the agent is left with nothing (while it may have built a huge client base for its principal from which the principal can profit in the future, making a compensation for an agent reasonable).

It is not, therefore, that termination compensation for a distributor is forbidden under Dutch law; it is just not common practice and the distributor has no statutory right to ask for such compensation (save for certain exceptions based on the above-mentioned principle of reasonableness and fairness).

Dutch Franchise Act

On 1 January 2021, the Dutch Franchise Act came into force. The Dutch Franchise Act will be applicable to all contracts that meet the legal definition of a franchise agreement as set out in this Act. Accordingly, the contract will be subject to the mandatory legal framework of the Dutch Franchise Act. The intention of the parties entering into the contract will not be decisive when assessing whether the contract qualifies as a franchise agreement. If a contract falls within the scope of the Dutch Franchise Act, the position of the franchisee (eg, distributor or dealer) will be strengthened towards the position of the franchisor (eg, manufacturer). The Dutch Franchise Act includes provisions on information and compensation rights of the franchisee (eg, the distributor or dealer) in relation to the franchise formula and on goodwill and the permitted non-compete clauses. It is likely that legal disputes will be initiated to try to receive (declaratory) judgments on the qualification of dealer or distribution agreements in this respect.

Mergers, acquisitions and joint ventures

5 | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

Generally, there are no major differences in the way in which automotive M&A transactions are handled in the Netherlands in comparison to transactions in other European jurisdictions. Considering, however, that the automotive market is rapidly changing and that new entrants enter the market who have a completely different background, such as IT companies, internet companies and other major technology companies, topics that require specific attention during the due diligence process (when entering into M&A and joint venture transactions) include (among others) the reliability of customer and supplier relations, environmental issues, product liability, insurance coverage, IP rights and regulatory compliance (including compliance with emission standards).

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Incentives and barriers to entry

- 6** | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

According to RAI Association, there is a wide variety of subsidy and incentive schemes in the Netherlands to which the players in the automotive industry can subscribe. Both the national government as well as the local governments incentivise innovation and sustainability in different ways. Incentives range from facilitating vehicle purchase to developing technologies used in cleaner vehicles; for instance, subsidies or incentives for purchasing and using electric vehicles (often through the payment of individual purchase premiums) or individual tax advantages, or at the level of business processes and innovation. An actual overview of all subsidy and incentive schemes, including an explanation, can be found [here](#).

There are no specific barriers to entering the automotive market in the Netherlands. It is a rapidly changing industry sector. Although the industry has long been subject to rules set and developed by traditional (foreign) automotive players (mostly OEMs), new companies entering the automotive market have started challenging these established rules and common practices by applying new rules and practices, and the focus of competitors is rapidly shifting from traditional automotives to connectivity and mobility.

PRODUCT SAFETY AND LIABILITY

Safety and environmental

- 7** | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

Regulation (EU) 2018/858 introduces market surveillance measures for vehicles already on the market. Similar to Directive 2007/46/EC, Regulation (EU) 2018/858 does not include substantive technical requirements that vehicles have to comply with, but refers to the requirements of specific regulatory acts, such as Regulation (EC) No. 715/2017 regarding emissions and Regulation (EC) No. 661/2009 regarding general safety of motor vehicles. In addition to EU regulations, the Road Traffic Act and the Vehicles Regulation lay down rules on safety and environmental matters.

In principle, non-compliance with applicable law requirements is punished with both administrative and criminal sanctions. A violation of the requirements laid down in articles 29 and 30 of the Road Traffic Act constitutes an economic offence under Dutch law. These articles entail, among other things, a prohibition from using defeat devices, withholding information and forging test results. The National Vehicle and Driving Licence Registration Authority (RDW) – as the type-approval authority – and the Human Environment and Transport Inspectorate – as the market surveillance authority – are authorised to impose administrative penalties for violation of different provisions.

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Under Regulation (EU) 2018/858, a manufacturer is obliged to take corrective measures (such as a recall) in the case of non-conformity of the vehicle and when the type approval is granted on the basis of incorrect data. A recall constitutes an obligation for the manufacturer and not the car owner. The Dutch legislator plans to impose an obligation on the vehicle owners to respond to the recall. If the vehicle owner repeatedly fails to respond to the call to repair the vehicle, he or she will be prohibited from driving the vehicle on the road.

In the case of a serious risk, a manufacturer is obliged to provide to the approval authorities and market surveillance authorities detailed information on the risk and the measures taken to address it. Regulation (EU) 2018/858 refers to both safety and environment related risks. For the qualification of a serious risk, the Regulation refers to Regulation (EC) No. 765/2008:

The decision whether or not a product represents a serious risk shall be based on an appropriate risk assessment which takes account of the nature of the hazard and the likelihood of its occurrence. The feasibility of obtaining higher levels of safety or the availability of other products presenting a lesser degree of risk shall not constitute grounds for considering that a product presents a serious risk.

Furthermore, under Regulation (EU) 2018/858, the market surveillance authorities of all EU member states (ie, ILT) have the discretion to evaluate a vehicle if there are sufficient reasons to believe that it poses a serious risk to the health or safety of persons or presents a serious risk of non-compliance. If ILT concludes that the vehicle presents a serious risk to the health or safety of persons, it will require appropriate corrective measures by manufacturer to ensure that the vehicle no longer presents that risk.

RDW may refuse granting a type approval if it considers that, albeit in conformity with all the type-approval requirements, the vehicle constitutes a serious risk to road safety, public health or the environment.

Product liability and recall

- 8** Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

Product liability law

Directive 85/374/EEC on liability for defective products has been implemented in the Dutch Civil Code. A manufacturer is strictly liable for damages caused by a defect in its product. A product is defective when it does not meet product safety expectations. The burden of proof rests on the consumer. He or she must prove the existence of the damage, the defect and the causal relationship between the two. The consumer can claim damages up to three years from the moment he or she has knowledge of the damage, the defect and the identity of the manufacturer. The right to compensation lapses 10 years after the day on which the product was brought into circulation. Next to the strict liability framework, a consumer can also bring a claim under contract or tort law.

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If defects have been detected in vehicles, the manufacturer must notify the competent authorities, inform the consumers and recall the products. In some cases, the recall is geared towards repairing or replacing the defected product in the vehicle. In other cases, it may consist of a software update. These obligations are based on requirements of Directive 2001/95/EC. In this regard, RDW is responsible for informing the public and for supervising the process. RDW keeps a product recall register online that contains information about the product, the defect, possible hazards and the required measures.

Class actions

In the Netherlands, there are three main collective redress mechanisms available for injured parties.

- In the Dutch assignment model, several injured parties (sometimes hundreds) assign their claim to a claim vehicle. The claim vehicle starts proceedings in the Netherlands against the defendants, acting in its own name.
- In collective settlements of mass damages claims based on the Class Action (Financial Settlement) Act, the party allegedly causing damages and the association or foundation representing the interests of a group of injured parties conclude a collective settlement. Parties can request the Amsterdam Court of Appeal (by submitting a joint application) to declare this settlement binding on all injured parties falling within the scope of the settlement agreement. The injured parties can be either known or unknown and residing in the Netherlands or abroad. If interested parties do not want to be bound, they can opt out.
- In collective actions based on Act on Redress of Mass Damages in Collective Action (WAMCA), which entered into force on 1 January 2020, interest groups can file a lawsuit on behalf of injured parties and claim damages directly. (Until the end of 2019, a claim foundation or association could claim a declaratory judgment regarding liability on behalf of injured parties but could not claim damages.) Another significant change under WAMCA is the introduction of a system with an exclusive representative. An interest group must register a copy of the writ of summons to the central register for collective claims. Other interest groups can also file a writ of summons with the register within three months. After this, the judge will designate an exclusive representative who will act on behalf of all injured parties. After the designation, Dutch injured parties can opt out and foreign injured parties can opt in within one month. WAMCA is currently being amended in accordance with Directive (EU) 2020/1828 on representative actions for the protection of the collective interests of consumers.

As a result of the *Dieseltgate* incident, multiple claim foundations have been established. Volkswagen Car Claim foundation is, for example, litigating under the former legislation, whereas the Diesel Emissions Justice Foundation has issued several writs of summons and is litigating under the new legislation.

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DISPUTES

Competition enforcement

- 9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

At the end of 2020, proceedings were initiated by two claimants (Stichting Tesla Claim and the Bios-groep). In these proceedings, consumers and taxi drivers demanded compensation from car manufacturer Tesla. The claims involved at least 220 claimants represented by Stichting Tesla Claim and 70 claimants represented by BIOS-groep. The complaints were that, despite a promise from Tesla that its cars are maintenance free, consumers had experienced numerous maintenance issues. The spokesperson for BIOS-groep stated that, apart from maintenance malfunctions, the aftersales service and support were below standard. Back in 2019, a group of four taxi drivers sued Tesla for similar reasons. They demanded the full repayment of the purchase price of the cars. The district court of Midden-Nederland (29 July 2020, ECLI:NL:RBMNE:2020:2845) denied this claim on the basis that, among other things, the claimants failed to prove that the maintenance issues already existed at the time of purchase. In line with this judgment, the claim of Stichting Tesla Claim was rejected by the Dutch district court in first instance. It is unclear whether Stichting Tesla Claim is appealing the judgment.

Furthermore, the Dutch Authority for Consumers and Markets (ACM) has informed the Dutch automotive industry that more transparency is required regarding the prices of charging electric vehicles. In early 2020, members of the parliament suggested that a maximum price should be implemented. The Minister of Housing, Spatial Planning and the Environment stated that (for now) no maximum price is necessary. The ACM is currently monitoring whether the operators of electric chargers are more transparent regarding the prices and encourage consumers to report any unclear display of prices.

The Netherlands is a favourable jurisdiction for follow-on civil litigation for antitrust damage claims. Under Dutch law, it is possible to start collective claims on the basis of an opt-out mechanism for Dutch customers (ie, a procedure in which a claim is brought on behalf of the entire class of potential claimants without the need for them to proactively choose to participate). One of the recent cases where follow-on civil litigation is present relates to the well-known *Dieseldgate* case involving Volkswagen and more recently Daimler. Several claim vehicles represent customers seeking compensation. The claim vehicles consist of ad hoc vehicles, but also established claim vehicles and representative bodies.

Dispute resolution mechanisms

- 10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

No specific preference for litigation or arbitration has been observed in the Dutch automotive industry. If parties have agreed on arbitration in their contract, Dutch courts will declare themselves not competent to hear the case. It is possible to request preliminary injunctions

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in Dutch courts. Preliminary measures are available in arbitration proceedings, if Dutch law is applicable and the parties chose to be bound by the arbitration rules of the Netherlands Arbitration Institute.

Claims for damages based on defective products developed and delivered by either OEMs or suppliers are common disputes (article 6:185 of the Dutch Civil Code et seq). Other common disputes are those in connection with the termination of the supply contract. In the aftermath of the covid-19 crisis, contractual disputes were more on the question of whether contracts could be terminated or altered based on either force majeure clauses or unforeseen circumstances. If these are not included, parties are dependent on Dutch law and how it is interpreted. Whether parties may invoke the contractual or statutory provisions needs to be determined on a case-by-case basis.

The Dutch Franchise Act came into force on 1 January 2021. It is likely that distributors and dealers (and the respective representative associations) will initiate proceedings against the manufacturers to argue that their contracts fall within the scope of the Act. If a contract falls within the scope of the Dutch Franchise Act, the position of the counterparty (eg, distributor or dealer) will be strengthened towards the position of the manufacturer. The Dutch Franchise Act includes provisions on information and compensation rights of the franchisee in relation to the franchise formula and on goodwill and permitted non-compete clauses. Subsequently, PSA's dealer associations have initiated court proceedings against Stellantis Netherlands in relation to the new Dutch Franchise Act. They argue that dealer contracts fall within the scope of the Dutch Franchise Act and therefore respective dealers can rely on the rights of a franchisee.

Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

The general rules of Dutch insolvency law also apply to the automotive industry. No specific provisions exist that allow for a different treatment of distressed suppliers in this industry.

Currently, the Dutch Bankruptcy Act (DBA) provides three procedures for distressed suppliers. If a supplier foresees that it will become distressed, it can request for suspension of payments. The suspension of payments aims to help debtors in financial distress to restructure and restart their business (after suspension of payments). The suspension of payments provides temporary financial relief as it prohibits ordinary (unsecured) creditors from forcing the debtor to pay the claims when they fall due. Only the distressed supplier (debtor) may file for a suspension of payments.

If suspension of payments is requested too late or is not requested at all, creditors or distressed suppliers should request a declaration of bankruptcy at the Dutch courts. The distressed supplier may be declared bankrupt at its own request or at the request of its creditors. There are two criteria for such declaration of bankruptcy (article 6(3) of the DBA).

According to the first criterion, the given circumstances must summarily prove the debtor has ceased to pay its debts; and the claims of the creditors are summarily proven if the declaration is requested.

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The second criterion includes a plurality requirement. A single creditor cannot request a declaration of bankruptcy. To that extent, if the debtor stopped paying a specific creditor, this creditor is considered to have other legal measures to request the payment of its claim. Therefore, a single creditor who is requesting for a bankruptcy of its debtor must accompany this request with supportive claims of at least one other creditor who has been left unpaid. The claims need to be sufficiently certain. If the debtor has reasonable grounds for disputing these claims, a declaration of bankruptcy will not be given.

If the above-mentioned criteria are met, the distressed supplier will be declared bankrupt, and a receiver (curator) will be appointed. The distressed supplier loses the power to dispose of its assets, and this power is transferred to the receiver. The receiver will then distribute the proceeds from the estate to the creditors in order of priority and otherwise proportionally.

The third option came into force on 1 January 2021, the Act on the Confirmation of Out-of-court Restructuring Plans (WROA). This act allows debtors (or their creditors) to compromise certain debts and therefore prevent a possible insolvency. The new process, also referred to as the Dutch Scheme, is inspired by and based on the experience of composition plans in the United Kingdom and the United States. It enables debtors to force dissenting creditors within the scope of the composition plan to comply with the plan, provided that the majority of the creditors have approved the composition plan.

A composition plan will only be approved by the court if it meets certain criteria, including that:

- the debtor is in financial distress;
- it is reasonably expected that without the plan the debtor will become insolvent; and
- the outcome of the composition plan is the avoidance of a possible bankruptcy of the debtor.

However, the composition plan cannot put creditors in a substantially worse position than they would have been in on the debtor's bankruptcy.

It should be noted that by no means all companies that begin a WROA process (by filing the start statement) achieve a successful homologation. It is important to prepare a WROA agreement well, as this significantly increases the chance of success. A debtor will have to inform its creditors carefully and thoroughly substantiate the need for a WROA agreement. This is also apparent from the judgments in which an agreement has been homologated; great value is attached here to the scope and depth of the information supplied and the way in which creditors have been informed.

Intellectual property disputes

12 | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

The Netherlands is a frontrunner in developing technologies for the automotive industry. Its automotive industry ranges from OEMs and component manufacturers to dealerships and

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commercial vehicle manufacturers. The companies active in these areas seem to attribute great value to collaborations throughout the automotive sector.

Traditionally, disputes mostly related to collaboration (eg, performance under distribution or supply agreements), confusion regarding the origin of collaboration (eg, the distinction between a commercial dealer and a specialist in certain brand of cars) and origin of parts (eg, OEM versus non-OEM). The latter two types of disputes mostly involved the enforcement of trademark rights.

These days, the government in the Netherlands is actively endorsing the development of smart mobility solutions, such as electric, autonomous, connected and shared vehicles that can be easily updated and upgraded to satisfy customer demand. For example, truck platooning (ie, a group of trucks travelling safely and autonomously in a convoy, a short distance apart) is high on the agenda to satisfy increased logistic demand in an environmentally responsible way.

Smart mobility solutions require innovators to go beyond traditional boundaries and explore the integration of technology from other fields. For example, some manufacturers already use mobile networks to warn their own cars about congested roads or accidents. Future developments will include standardised technology such as low-latency machine-to-machine communications, which makes it possible to share sensor data, control information to allow vehicles to drive in close formation, save road space and exchange vehicle trajectories to prevent collisions.

In doing so, they rely on technology developed in the telecoms sector. This is an area where much patent litigation was seen in the Netherlands in recent years between network infrastructure developers and handheld manufacturers. These disputes related to patents covering standard essential technology (ie, common protocols to ensure interoperability among devices).

An increase of patent cases in the automotive industry is expected, for example, owing to the implementation of (standard essential) technology historically not linked to the automotive industry, such as the 4G and 5G telecom standards. While the telecom industry has developed best practices to negotiate fair, reasonable and non-discriminatory terms, it remains to be seen how this will work out in the automotive industry. For example, the business model of handheld manufacturers (ie, relatively low purchase price and high percentage of profit per device) appears to be quite different from the business model of car manufacturers (ie, relatively high purchase price and low percentage of profit per vehicle), which no doubt will have an impact on the licensing framework and related negotiations. The strategy traditionally seen in the automotive industry to collaborate could shift towards more aggressive strategies as seen in the telecom industry, in particular in issues involving non-practising entities having acquired intellectual property (IP) rights (also known as trolls).

The Netherlands provides several useful possibilities for an IP owner to successfully and quickly take action against infringements of IP rights. Especially, preliminary injunction proceedings and ex parte injunction requests provide exceptionally quick mechanisms for acting against infringements. Another important aspect is that courts in the Netherlands are prepared to grant an injunction even in the situation that no infringement has occurred,

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but there is a serious threat that it might. Also, Dutch courts are, depending on the circumstances, prepared to grant cross-border injunctions.

Owners of IP rights can initiate preliminary injunction proceedings when becoming aware of an infringement, or a threatened or potential infringement, of their IP rights. Preliminary relief proceedings are available to get injunctive relief quickly. Provisions judges of district courts are sometimes willing to also grant ancillary orders, such as a recall, rectification, account of profits and an advance payment for the damages. There is an urgency requirement in preliminary injunction proceedings, but this requirement is often easily satisfied. There is no rule that the IP owner must bring preliminary injunction proceedings within a specific time frame, but the IP owner should act in a sufficiently expedited manner. A hearing in which both parties are heard usually takes place within a few weeks of service of the writ of summons and a decision is usually rendered two to four weeks later, thus making it often possible to obtain a preliminary injunction within six to eight weeks. In very urgent cases, a preliminary injunction can even be obtained in a matter of days. The provisions judge will render a decision based on his or her preliminary findings and will normally issue a preliminary injunction if he or she is satisfied that the IP right is valid and infringed. Depending on the facts, the preliminary injunction may have cross-border effect. The party that is successful in the case will normally be awarded payment of reasonable costs that it has made in relation to the proceedings. Preliminary injunction proceedings should be followed in good time by proceedings on the merits. Otherwise, the preliminary injunction will lapse. A decision in preliminary injunction proceedings is normally provisionally enforceable notwithstanding appeal.

Ex parte measures are also available in the Netherlands. In very urgent matters, especially if there is a threat of irreparable harm to the IP owner, the IP owner can request the provisions judge to render an ex parte injunction. This is a preliminary injunction that is rendered by the provisions judge upon request of the IP owner without the alleged infringer being heard. The alleged infringer can protect itself against a possible ex parte injunction by submitting a protective letter with the district court of the relevant districts. Some, but not all, district courts in the Netherlands accept such protective letters.

Various types of seizures are also available to the owners of IP rights. One of the options is to file a petition to conduct a seizure for the surrender of infringing goods at the premises of the alleged infringer or elsewhere in the Netherlands. Another type of seizure that is available to the IP owner is the customs seizure with the customs authority in the Netherlands. If granted, the customs authority will undertake to search for infringing goods during its regular customs inspections and inform the applicant if infringing goods are found. If infringing goods are retained by the customs authority, the IP owner can examine the retained goods, confirm that the goods are infringing goods and decide whether it wants to have the infringing goods seized and destroyed in a simplified procedure or whether it wants the retention confirmed by initiating court proceedings. If no proceedings are timely initiated and no settlement is reached, the goods will be released. If the seized goods are declared by a court to be infringing goods, the customs authority can proceed to destroy the goods. Another attractive type of seizure is the seizure for the preservation of evidence. The petition for such a seizure is normally assessed and decided ex parte by the court. The evidentiary seizure is to be conducted by a civil bailiff who can, upon request, be accompanied by an independent expert (eg, a patent attorney or an IT expert). The evidence obtained can be in the form of actually seized goods, documents, materials or machinery, or a detailed

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description or sampling thereof. It should be noted that preserving evidence and getting access to the preserved evidence is a two-stage process. Once the evidentiary seizure has been made, the party levying the seizure must file a claim with the court for the inspection of the preserved evidence. Evidentiary seizures can, among others, be made against companies established in the Netherlands that infringe an IP right abroad, for the purpose of submitting the evidence in proceedings abroad. Seizures can also be conducted against foreign companies if the alleged infringing goods are located in the Netherlands. Alleged infringers of IP rights can protect themselves against a potential evidentiary seizure by filing a protective letter, as outlined above.

The owners of IP rights can also initiate proceedings on the merits, in which definitive relief can be obtained. In proceedings on the merits, it usually takes 12 to 18 months after service of the writ of summons before a decision is rendered. Besides a permanent injunction, the owner of IP rights can also obtain ancillary orders, such as declaratory judgment, recall of infringing products, rectification, information with respect to distribution channels, account of profits, destruction of infringing goods or materials for the production of infringing goods, publication of the decision, payment of damages or surrender of profits and payment of reasonable legal costs. In exceptional situations, courts are sometimes prepared to grant a moratorium (ie, an order for an infringer to refrain from dealing in the infringing product for a certain period after expiry of the IP right), to prevent the infringer from benefiting from the infringement.

The District Court of The Hague, the competent court in patent cases in the Netherlands, has a special accelerated regime in patent cases. In such accelerated proceedings on the merits, the court sets a time schedule for serving the writ of summons, the filing of the pleadings and the date of the oral hearing. Several weeks after the hearing, a decision will be rendered, and a decision is usually obtained within nine to 12 months of the date of service of the writ of summons.

The importance of trade secrets is recognised during legal proceedings as well. For example, the Netherlands has implemented the European Trade Secrets Directive, which not only ensures the effective protection of trade secrets in the field but also enables the use of confidentiality clubs (ie, a mechanism to rely on confidential information without jeopardising the confidential nature of the information) during legal proceedings. Practice shows that confidentiality clubs are not only used in trade secret cases but also in other cases in relation to IP rights.

Finally, alternative dispute resolution is also available to easily resolve IP disputes, such as arbitration or mediation.

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EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

The Netherlands is acquainted with trade unions and work councils. In fact, both trade unions and works councils play an important role in Dutch labour law.

Trade unions and works councils have different rights pursuant to Dutch labour law. The major differences are as follows.

Trade unions

Employers are, in principle, obliged to comply with collective labour agreements that they have made with the unions that are party to the collective labour agreement. A trade union that is party to a collective labour agreement can, as a contracting party, on its own behalf demand compliance with the obligations as set out in the collective labour agreement. Employers that are not members of an employer's organisation are not (automatically) affected by a collective labour agreement and, from a legal point of view, they fully retain their freedom to act. This will only change if a collective labour agreement is declared generally binding. In this case, the relevant collective labour agreement will be mandatory for all employees and employers in the relevant industry, regardless of whether they are members of one of the parties to the collective labour agreement.

Moreover, it is possible that a company concludes its own collective labour agreement and requests dispensation at the Ministry of Social Affairs and Employment from the mandatory application of the collective labour agreement.

The collective labour agreement for motor vehicle and two-wheeler companies applies to employees in garages and workshops. This agreement has been declared generally binding. Previously this collective labour agreement was part of the metal and technology agreement. The motor vehicle and two-wheeler collective labour agreement is valid from 1 April 2022 until 31 October 2023, and applies to all employers and employees in the motor vehicle and two-wheeler business, which includes the repair, modification, maintenance, assembly, overhaul or replacement of one or more parts or parts thereof of motor vehicles. A new collective labour agreement is currently being negotiated and will probably be declared generally binding as well. The fact that the collective bargaining agreement is declared universally binding means that every employer must comply with it. For example, a wage increase of €100 had to be implemented by January 2023.

In addition, trade unions play a special role in the context of collective redundancies. An employer that intends to terminate the employment contracts of at least 20 employees, working in one working area, at one or more times within a period of three months, must notify the concerned trade unions and the Employee Insurance Agency in writing for timely consultation (article 3, paragraph 1 of the Collective Redundancy Notification Act (WVCO)). The consultation should at least concern the possibilities of preventing or reducing the

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number of collective redundancies and mitigating their consequences by taking social counselling measures (article 3, paragraph 2 of the WMCO).

Trade unions can also play a role in the context of mergers and acquisitions. Pursuant to the Social and Economic Council (SER) Merger Code of Conduct, trade unions must be informed in time about merger or acquisition plans by the companies or organisations involved. Trade unions must be able to exert a substantial influence on the consequences for the workers involved. In principle, the SER Merger Code of Conduct applies to:

- companies established in the Netherlands in which 50 or more persons are working; and
- companies involved in a merger or acquisition that are part of a group of companies when 50 or more persons work together in the companies established in the Netherlands.

The SER Merger Code of Conduct may also be declared applicable to other companies by a collective labour agreement.

Collective actions (initiated by trade unions) are not uncommon in the automotive industry. A collective action can (partially) be prohibited by an employer if this is, from a social perspective, urgently necessary. The following factors play a role in this assessment:

- the nature and duration of the action;
- the proportion of the action and its intended purpose;
- the nature of damages to the employer or other third parties as a consequence of the action; and
- whether the action is used as the last resort and whether there has been a timely notification.

VDL, for example, successfully prevented a strike initiated by trade unions in 2019, because of the risk that BMW would terminate the contractual relationship as a consequence of the planned strike (Court of Maastricht, 9 January 2019, ECLI:NL:RBLIM:2019:381).

Works councils

Works councils have various rights under the Dutch Works Council Act (WOR). The special rights that Dutch law grants to a works council are advisory rights and rights of assent.

Pursuant to article 25 of the WOR, the works council has an advisory right regarding a number of decisions that can have major consequences for employees. Examples include decisions relating to restructuring, mergers and acquisitions and major investments. Unless a company's decision is in accordance with the advice of the works council, the company is obliged to suspend the implementation of the decision until one month after the day on which the works council was notified of the decision. The works council can lodge an appeal with the Chamber of Commerce in Amsterdam within these 30 days. The Chamber of Commerce assesses whether the decision was reasonable.

The works council has a right of assent regarding establishing, changing or withdrawing personnel regulations (article 27 of the WOR), such as regulations for working hours, working conditions, training, performance reviews and sick leave. Consent is not required if the matter in question has already been arranged in a collective labour agreement or a

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working conditions regulation established by a public law body (article 27, paragraph 3 of the WOR). If the company has not yet obtained an approval from the works council for the intended decision, it can ask the sub-district judge authority to take the decision. The latter will only grant permission if the works council's decision not to give consent is unreasonable, or if the intended decision of the company is required for compelling organisational, economic or social reasons (article 27, paragraph 4 of the WOR).

Other rights that are granted to works councils are:

- the right to a consultation meeting with the company (articles 23 and 24 of the WOR);
- the right of initiative (article 23, paragraph 3 of the WOR);
- the right to education (article 18 of the WOR);
- the right to information (article 31 of the WOR); and
- the right to expense allowance (article 22 of the WOR).

The works council also has a right of advice in the event of a proposed decision to appoint or dismiss a company director (article 30 of the WOR).

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

The Netherlands is widely recognised for its readiness for automated and autonomous driving. One of the latest major developments is that the Netherlands enacted the Experimental Law on Self-driving Vehicles. This new legislation enables the country to conduct public road tests involving self-driving vehicles.

The Netherlands has already allowed vehicles with automated functions on the road for quite some time. These automated functions include driver aids such as adaptive cruise control, automatic parking and lane-keeping systems. Also, large-scale testing is allowed for self-driving vehicles on Dutch public roads, permitting field operational tests with automated driving on all public roads in the Netherlands provided that a driver is present in the vehicle.

The Experimental Law on Self-driving Vehicles brings the development of autonomous vehicles to the next level. It enables driverless-vehicle experiments with automated driving systems in traffic without having to have an actual driver inside the vehicle. Supervision by a human takes place remotely. For example, experiments can include remotely operated self-driving minibuses and moving motorway roadblocks with remote drivers.

Experiments in relation to truck platooning are high on the agenda. The goal is to accelerate the development of truck platooning by implementing platooning into real-life logistics operations for different use cases running at participating companies. According to the government, the outcomes of these experiments will be used to review current legislation and whether it sufficiently accommodates the cars and transport of the future.

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UPDATE AND TRENDS

Trends and new legislation

15 Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

The Dutch government has stated that the Netherlands 'is paving the way for the traffic management system of the future. A future in which vehicles communicate with one another and with roadside systems'. This endorsement quite clearly expresses the country's ambitions on intelligent transport systems and smart mobility.

The Netherlands is a unique testing ground for smart mobility solutions. The government is supporting the development of smart mobility solutions in many ways, from providing testing facilities to adjusting rules and regulations.

Road traffic is highly regulated in the Netherlands and elsewhere throughout Europe. The Netherlands recognises that harmonisation of the legal framework for an automated and autonomous vehicle is of vital importance to mitigate the risks for all traffic users in public spaces and to achieve a joint development approach. The Netherlands recognises the importance of harmonising the legal framework for testing and placing automated and autonomous vehicles into the market. Key legislative areas include road safety, liability issues, data processing and protection and infrastructure. In addition, ethical questions regarding artificial intelligence are recognised, such as respect for human dignity and freedom of choice in self-driving vehicles.



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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

As a result of the global covid-19 pandemic and its effects, such as the lockdowns, production and assembly line halts or slowdowns, disruptions in supply chains, scarcity of

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semiconductors, increasing inflation, high interest rates and recessionary fears, along with the war in Ukraine, the automotive industry sector has been continuously facing substantial challenges since 2020, and these challenges will probably continue in 2023.

Despite adverse market conditions, however, the automotive industry sector remains one of the key drivers of Polish industry, and automotive manufacturing is one of Poland's largest industrial sectors accounting for, depending on sources, approximately 9 per cent to 10 per cent of the total value of the country's production (in recent years). In terms of production sale value, automotive manufacturing ranks second after food manufacturing, surpassing all other industry sectors, as well as many important industry branches such as mining and quarrying, energy, oil and utilities. In the pre-pandemic years, growth in Poland's automotive production has mostly been driven by extensive investment outlays. Among the many factors that make this sector attractive for investment is the qualified workforce, offered business incentives and support for hiring specialised employees in Poland.

Polish automotive manufacturing is almost entirely export-oriented; therefore, the sector's shape depends heavily on the economic situation of foreign markets.

For many years, parts and accessories, along with passenger and cargo-passenger vehicles, have been the most important export sub-sectors in the Polish automotive industry. In addition to parts and accessories, passenger and cargo-passenger cars are the second largest export sub-sector.

With respect to the Polish internal market, approximately 419,750 new passenger cars were registered in 2022 (439,700 in 2021 and 428,300 in 2020).

The growing interest in fully electric, plug-in hybrid or hybrid vehicles is a noticeable trend in Poland, but we still cannot talk about a green revolution on the Polish roads because of barriers such as the high cost of purchasing an electric car, lengthy delivery times for a new car (often exceeding 12 months), driving range and an inadequate network of charging infrastructures.

According to the Electromobility Counter report (launched by the Polish Automotive Industry Association and the Polish Alternative Fuels Association), since the end of February 2023 a total of 70,263 passenger and commercial electric cars were registered in Poland. In the first two months of the year, these number increased by 5,056 units, that is, 56 per cent more than during the same period in 2022.

At the end of February 2023, there were 66,685 electric passenger cars on Polish roads, including 33,902 fully electric vehicles (51 per cent of the total number) and 32,783 plug-in hybrid vehicles (49 per cent of the total number). Fleets of electric vans and trucks numbered 3,578 units. Furthermore, the number of hybrid cars and vans is also growing, having increased to 506,344 units.

Despite the fact that the figure is growing at an accelerated rate, it still remains well below government targets that had initially envisioned one million electric vehicles on Polish roads by 2025. Furthermore, the proportion of electric vehicles in Poland is also among the lowest in the European Union. Despite this, Poland is one of the largest centres for manufacturers of electric vehicles and their components (in 2020, Poland was the EU's largest exporter

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of electric buses). In 2022, ANP EnerTech, a Korean manufacturer of components for lithium-ion batteries, announced its investment in the construction of a manufacturing plant in Poland. Also, the Belgian firm Umicore started production of battery materials at its new plant in Poland in 2022. In July last year, SK Nexilis, a Korean manufacturer of copper foil used in electric-car batteries, inaugurated the construction of a 3-billion-zloty factory in south-eastern Poland.

Poland intends to produce the country's first home-grown electric car – the Izero. In November 2022, the state-owned company ElectroMobility Poland, which owns the Izero brand, signed a licence agreement with the Chinese company Geely (the owner of the Volvo and Lotus brands, among others) to supply the platform for the vehicle. Production of the Izero brand of electric cars is scheduled to start after 2025.

A number of regulations in Poland are currently being implemented, aimed at stimulating the growth of electromobility. These regulations introduce new definitions for the terms associated with vehicles and their infrastructure, and determine the general principles guiding the usage of alternative fuels in transport, as well as introducing incentives for vehicles using these alternative fuels.

COMMERCIAL OPERATIONS

Regulation

- 2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

The regulatory framework applicable in Poland comes from EU legislation.

Type approval

The general system for type approval in Poland is set out in the Act on Road Traffic of 20 June 1997, and in the Decree of the Minister of Transport, Construction, and Maritime Economy of 25 March 2013 on the approval of motor vehicles and their trailers, and of the systems, components and separate technical units intended for these vehicles. As far as EU regulations are concerned, the main regulation in force is the Regulation (EU) 2018/858 of the European Parliament and of the Council of 30 May 2018 on the approval and market surveillance of motor vehicles and their trailers, and of systems, components and separate technical units intended for such vehicles, amending Regulations (EC) No. 715/2007 and (EC) No. 595/2009 and repealing Directive 2007/46/EC.

The Act on Road Traffic sets out the general system for EU-type and UN/ECE approval. The Decree contains administrative provisions, samples of required documents and the general technical requirements for the approval of all new motor vehicles and their trailers, and of the systems, components and separate technical units intended for these vehicles. It sets out the procedures that need to be followed to obtain approval.

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The Act on Road Traffic (article 70(d)) imposes the obligation on OEMs of any new type of vehicle, component or separate technical unit to obtain approval before placing a product on the market. An OEM is exempted from the need to obtain approval under Polish law if this approval has already been granted by the relevant authority of another member state and has been accepted by the Polish authorities.

According to article 70(d), an OEM is responsible for all aspects of the approval process and for the conformity of production, regardless of whether the OEM directly participates in all of the production stages of the vehicle, component or separate technical unit.

Apart from the technical requirements stemming from Polish law, an OEM should also comply with the directly applicable EU law regulations, among others, Regulation (EC) 715/2007 on the type approval for motor vehicles with respect to emissions ranging from light passenger to commercial vehicles (Euro 5 and Euro 6). An exhaustive list of EU documents applicable to EU type approval is provided in Annex II to the Regulation (EU) 2018/858 of the European Parliament and of the Council on the approval and market surveillance of motor vehicles and their trailers, and of the systems, components and separate technical units intended for these vehicles.

The approval is granted by the Polish authorities once the vehicle, component or separate technical unit concerned complies with all the applicable provisions mentioned above. The approval is granted by the director of Transportation Technical Supervision.

Registration requirements

Purchasers of new and used vehicles have the obligation to register said vehicles within 30 days of purchase. Breach of this obligation can entail a fine of approximately €250. This obligation also pertains to distributors (dealers) with respect to the vehicles used by them for demonstration purposes (on the contrary, no registration obligation exists for vehicles remaining in a dealer's stock).

According to article 72 of the Act on Road Traffic, registration requires, among other things, the vehicle's compliance with an approved type. For EU type-approved vehicles this is confirmed by the certificate of conformity. According to article 70(s) of the Act on Road Traffic, an OEM must provide each vehicle that belongs to an approved type with a certificate proving its conformity.

Insurance requirements

Directive 2009/103/EC of 16 September 2009 relating to insurances against civil liability in respect of the use of motor vehicles, and the enforcement of the obligation to insure against this liability is essentially transposed in the Polish Act of 22 May 2003 on Compulsory Insurance, the Insurance Guarantee Fund and the Polish Motor Insurers' Bureau.

According to article 23 of this Act, vehicle owners have the obligation to insure their vehicles.

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Development, manufacture and supply

- 3** | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

The structure of development, manufacturing and supply in the Polish automotive sector is similar to that in other European countries since OEMs are global businesses. OEMs use a supply chain structure including Tier 1 suppliers (which supply directly to the OEMs), Tier 2 suppliers (which supply Tier 1 suppliers), Tier 3 suppliers and so on. Supply relationships are often based on the application of an OEM's general terms and conditions. Development and design are generally carried out internally; however, cooperation and partnership agreements between OEMs have recently been observed in relation to new technologies.

The usual contractual arrangements include agreements between OEMs and auto parts manufacturers (supply agreements), agreements between OEMs and local importers or distributors (importer, distribution or commission agreements) and agreements between local importers or distributors and dealers (dealership agreements). Financing agreements with banks that act as an OEM's subsidiary providing financial support for local importers or distributors and dealers are also common.

Distribution

- 4** | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

New vehicles are usually distributed by dealers acting on the basis of written contracts with local importers or distributors that are subsidiaries of OEMs (as a rule) or are independent (in a few cases). The market of second-hand vehicles is not controlled by OEMs, importers or distributors.

There is no specific legislation enacted in Poland in relation to importers, distributors, dealers or dealer networks. The general provisions of Polish anti-monopoly and contract law apply in this respect, in particular, the provisions of the Polish Civil Code relating to sales and supply. Moreover, EU legislation is also relevant, in particular, Regulation (EU) No. 461/2010 and the supplementary guidelines on vertical restraints (2010/C 138/05).

Issues relating to restructuring and termination are, as a rule, regulated by the parties at the contractual level. In the case of a lack of specific contractual clauses, the general provisions of Polish civil law apply.

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Mergers, acquisitions and joint ventures

- 5** | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

Generally, there are no specific issues for M&A or JV transactions relating to the automotive industry in Poland in comparison to transactions in the automotive industry in other European countries. The most important areas that should be investigated and covered in the transaction documentation include contractual relationships with distributors, dealers and suppliers, employment issues, environmental issues, real estate, subsidies, intellectual property rights and compliance or regulatory issues. Owing to recently introduced legislation, it needs to be verified whether the automotive entity owns any agricultural real estate, since in this situation, depending on the type of transaction, the National Centre of Agricultural Support will have a pre-emption right to the real estate or shares in the company. It also needs to be confirmed whether the transaction is subject to merger control by the European Commission, the President of the Office of Competition and Consumer Protection or an authority from any other EU member state. Last but not least, it also needs to be verified whether the new regulations on foreign investments in Poland adopted to protect the domestic market against hostile acquisition by entities taking advantage of the covid-19 outbreak do not apply to the transaction.

Incentives and barriers to entry

- 6** | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

There are no specific incentives for investments in the automotive market in Poland. However, potential investors in the automotive sector might take advantage of various forms of public support. These are as follows.

- Obtaining tax exemption (corporate income tax (CIT) or personal income tax (PIT)): this aid is intended for companies carrying out new investments on publicly as well as privately owned properties. The new investment might take the form of the establishing of a new enterprise, increasing the production capacity of an existing enterprise, diversifying the production of an existing enterprise through the introduction of products that previously were not manufactured in this enterprise or fundamentally changing the production process of the existing enterprise. The decision on granting support is issued upon the entrepreneur's request by the management of a special economic zone (acting on behalf of the Minister of Development) for a definite period (no shorter than 10 years and no longer than 15 years). To obtain a tax exemption, the entrepreneur must meet certain quantitative and qualitative criteria. The maximum amount of state aid in the form of CIT or PIT tax relief is determined on the basis of the regional aid map for 2021–2027 and varies from 10 per cent to 50 per cent. Support for medium-sized and small or micro enterprises is increased by 10 and 20 percentage points respectively. The tax exemption is only applicable to income generated from business activities carried out as part of an investment covered by the support decision. Therefore, if the entrepreneur simultaneously conducts activities that are not covered by the support

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decision, then the supported activities must be organisationally separated, and the level of exemption should be determined based on the data (revenues and costs) of the separated activity. The above mechanism is relatively new (the law was adopted in May 2018) and aims to replace the aid for establishing a business within the territory of a special economic zone (the aid granted to investors within the old special economic zones will remain in force until 2026).

- Obtaining a real estate tax exemption: this aid can be granted by a municipal council. The local authority can, by way of a resolution, decide to exempt an entrepreneur investing in its territory from real estate tax. This aid has an automatic character (ie, an entrepreneur is automatically entitled to exemption after fulfilling the conditions set out in the resolution of the municipal council). This aid is considered to be public aid falling under the scope of the de minimis regulation. Therefore, this aid should not exceed €200,000 over a period of three financial years.
- Obtaining support for research and development (R&D) initiatives: since 1 January 2016, entrepreneurs can benefit from tax relief for R&D activities, by granting an additional deduction from the tax base of part of the expenses incurred on R&D activities, previously already included in the tax-deductible costs.
- Obtaining grants for investments of 'strategic importance' for the Polish economy: investors creating new jobs in business services centres and R&D centres in Poland can apply for a cash grant from the state budget for each new job created. In addition, investors rolling out new investments meeting the criteria of a 'strategic investment', 'innovative investment' or an investment in an R&D centre can benefit from cash grants amounting from 5 per cent of the investments costs (for investors that are large enterprises) up to as much as 25 per cent of the investment costs (for investors that are still developing, medium-sized enterprises or small or micro enterprises).

There are no specific barriers to entry to the automotive market in Poland. However, Polish automotive manufacturing is almost entirely export oriented. As a result, it is heavily dependent on the situation in foreign markets, which tends to make it more vulnerable to any potential changes in these markets (mainly Western European countries).

PRODUCT SAFETY AND LIABILITY

Safety and environmental

- 7** | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

The most relevant regulations concerning safety and environmental issues at the EU level are Regulation (EU) 2018/858 and Regulation (EC) 715/2007. Polish law generally follows the EU legislation and sets out the procedural rules required for the enforcement of these provisions. However, the Polish government has announced that it is working on a new law specifically dedicated to the systems of approvals for vehicles and their equipment, to fully align the Polish legal regime with the requirements of EU Regulations (in particular Regulation (EU) 2018/858). The draft of this new law was presented in January 2023 and is currently subject to discussion in the course of the parliamentary legislative process.

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Additionally, automotive-related products are covered by the general system applicable to product safety as set out in Product Safety Directive 2001/95/EC and implemented into Polish law by the Act of 12 December 2003 on the General Safety of Products. The provisions of this Act are only applicable to those products that are intended for use by consumers.

According to the Act of Road Traffic, which complies with the relevant EU provisions:

- the director of Transportation Technical Supervision can refuse to grant EU type approval if it finds that a vehicle, component or separate technical unit, although in compliance with the required prescriptions, presents a serious risk to road safety or seriously harms the environment or public health (article 70(p)(3)); and
- the director of Transportation Technical Supervision can revoke the EU type approval granted in Poland (upon a prior demand to the manufacturer to remedy a non-compliance) if an inspection shows the non-conformity of the production of the vehicle, component or separate technical unit, or the installation of a liquefied petroleum gas (LPG) with the required standards (article 70(r)). The director of Transportation Technical Supervision can initiate an inspection if it obtains information on any non-conformity (article 70(w)).

As far as the obligations of an OEM to which EU type approval has been granted are concerned, the OEM must immediately inform the director of Transportation Technical Supervision if it discovers that a vehicle could cause road safety danger or damage to the environment (article 70(u)). The OEM must additionally undertake actions required to remove this danger or damage. To remove the danger or damage, the OEM must prepare a schedule of planned corrective actions, agree on a plan with the director of Transportation Technical Supervision and inform the owner of the vehicle about the necessity to inspect the vehicle. The costs of any corrective actions are covered by the OEM.

Apart from the requirements stemming from the specific provisions applicable to car manufacturers, OEMs are covered by the general system on product safety. An OEM is obliged to immediately inform the President of the Office of Competition and Consumer Protection as soon as it has obtained information that a car is unsafe. Failure to fulfil this obligation can result in a financial penalty imposed on the OEM of up to 100,000 zlotys.

The Polish competition authority will initiate proceedings and decide on a case-by-case basis as to what steps should be taken towards a specific product. Before issuing a final decision, the competition authority might render a temporary decision in which it prohibits the further supply of the product (for a maximum of 90 days), until a final decision has been reached. This decision can only be issued if the initial assessment provides grounds for a claim that the product might be unsafe.

If, in its final decision, the Polish competition authority claims that a product is unsafe, it can order a specific corrective action (eg, a recall or an obligation to inform consumers on the possible dangers caused by the product). In general, it is advisable for the manufacturer to cooperate with the competition authority throughout the proceedings and propose specific corrective actions to mitigate any potential legal or financial risk.

In July 2017, the Polish competition authority published results of its survey of the various automotive components: towing cables, car batteries, tyres and car parts in general. The

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objective was to determine whether the products possessed the required approval certificates and did not pose threat to safety. The inspection revealed that the majority of products met the relevant requirements.

Product liability and recall

- 8** Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

Depending on the circumstances of a given claim, product liability claims can be pursued as contractual or under the tort law system (which also includes the strict dangerous product rules).

Contractual claims encompass all of an OEM or supplier's potential breaches of an agreement (in terms of product quality), as well as any customer's warranty claims. A violation of an agreement claim is usually aimed at a payment relief, whereas a warranty allows for a wider scope of remedies: the customer might demand to have the vehicle part rectified or replaced, to have the product price reduced or to withdraw from the agreement and claim back what has already been paid.

The tort law, in turn, allows for an OEM or a supplier to be held liable regardless of whether any agreement is in force. As a rule, the general tort liability requires the customer to demonstrate that the OEM or supplier's actions leading to the damage were intentional or, at least, accidental, but still attributable to it. Therefore, a more favourable solution for a person (usually a consumer) harmed by a product is to seek damages under the strict Polish dangerous product rules.

Under this system, an OEM (or a supplier, should the OEM as a producer remain unidentified for any reason) can be sued if the product does not reach the expected level of safety. The claimant can win the case even if the damage occurred for reasons not attributable to the OEM or supplier. The OEM or supplier can be released from liability only if the unsafe features of a product were revealed just after it was placed on the market (unless they resulted from features previously inherent in the product), or if the unsafe features could not have been foreseen at that time in light of lack of scientific or technical knowledge.

The amount of damages for personal injuries that can be sought in accordance with these strict dangerous product rules is unlimited. In turn, compensation for damage to property can only be awarded if the destroyed or damaged property is ordinarily intended for personal use, and the total actual loss exceeds €500 (this sum cannot include damage to the vehicle part itself, or any benefits the party could have gained in connection with its use). Liability under the Polish strict dangerous product liability law cannot be contractually excluded or limited.

Polish law allows that all product liability claims can be pursued through class action proceedings if they have been raised by at least 10 people. The sought claims need to be of the same kind and be based on the same or identical facts. Group proceedings, however, are not commonly recognised in Poland as a normal means to claim damages within the

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automotive industry. There have been very few such class action cases in Poland, mostly unrelated to product liability. The largest class action in the automotive industry in Poland are the ongoing proceedings against Volkswagen. The action was dismissed for lack of domestic jurisdiction, since the courts of the first and second instance ruled that the manufacturer should be sued in Germany. However, the case was brought before the Supreme Court, which decided (in compliance with the Court of Justice of the European Union's ruling) that consumers are not obliged to sue the manufacturer in Germany, but are able to sue the corporation in national courts instead. In the light of a favourable ruling for consumers as well as in the context of the implementation of Directive (EU) 2020/1828, we can expect an increase of class action in litigation in the automotive industry.

On the basis of Directive (EU) 2020/1828, qualified entities will be able to represent groups of consumers in civil proceedings against businesses, which may directly affect the automotive industry. As of today, however, the Polish law implementing the Directive is still in the drafting stage and we cannot predict either its final form or the date of its enactment.

Concerning recalls, while the automotive industry is not one that is highly affected in Poland, it does raise certain concerns and the number of notifications is increasing. While in 2020 only about 4 per cent of all the alerts registered in the Rapid Alert System referring to Poland concerned the automotive industry, in 2021 this rate rose to approximately 13 per cent. Therefore, product recall cases might be considered as relevant in the context of the automotive sector.

DISPUTES

Competition enforcement

9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

In the past, the President of the Office of Competition and Consumer Protection's main focus within the automotive industry was purely concerned with consumer issues (specifically relating to product safety). However, recent developments suggest that this particular sector has now become one of its priorities when it comes to competition law enforcement. In 2019 and in the first half of 2020, the Polish competition authority instigated three proceedings pertaining to arrangements made between the distributors of trucks in Poland. In 2022, the authority issued two decisions against the dealers of DAF's trucks for illegal market sharing, price fixing and bid rigging. The total value of fines imposed in these two decisions amounted to approximately 110 million zlotys. In addition, separate fines (between approximately 13,000 zlotys and 500,000 zlotys) were imposed on seven managers who the authority found to be personally responsible for breach of competition law rules. In addition, in 2021 the authority raided the offices of four dealers of KIA cars under the suspicion of market sharing, price fixing and bid rigging. In 2022, the authority decided to formally raise charges against KIA's Polish subsidiary and 10 dealers of KIA's cars in Poland. The case is still pending before the competition authority.

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When it comes to the private enforcement of competition law, damage claims are, as of yet, still quite uncommon in Poland. However, this situation is slowly changing and the follow-on claims related to the European Commission's decision concerning truck makers (decision AT.39824 – *Trucks*, dated 27 September 2017) could change the situation in this respect. Polish companies that might have suffered losses as a result of this alleged cartel are currently bringing follow-on claims, often by joining class action lawsuits, before the German or Dutch courts.

Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

Disputes in the automotive industry concern antitrust, automotive finance, intellectual property or insolvency matters. A significant part of the disputes in the automotive industry concern the supply chain. Supply chain disputes in the automotive industry sector usually result from the following situations:

- customers' claims for damages based on defects of the product developed and delivered by the supplier, including warranty claims, claims for damages based on disruption of the supply chain, or claims for compensation for late delivery;
- OEMs or suppliers' claims for payments; and
- claims relating to the termination of a supply contract that involve, among other issues, the termination rights and duties to compensate a supplier for frustrated investments.

Contentious matters usually arise out of B2B relations. They concentrate on demonstrating whether a particular irregularity has indeed occurred, and to which party the irregularity can, in the end, be attributed.

Mediation or negotiation in these types of cases is not a common solution. These matters often go to arbitration; however, many entrepreneurs still prefer to resolve their disputes before the state courts. Claimants usually seek monetary claims. Unlike in certain other jurisdictions, in the Polish system it is not possible to enforce the continuation of supply. Therefore, it is highly recommended that, in the course of the contract negotiations, customers ensure that an adequate contractual penalty for any increasing delay is determined in order to discourage OEMs or suppliers from supply disruptions.

In addition to the types of disputes specific to B2B relations mentioned above, litigation matters involve claims pursued under product liability rules; however, they do not normally refer directly to B2B relations and are usually brought by end consumers. Defective products can trigger liability for the OEM (or a supplier, should the OEM as the producer remain unidentified for any reason). This can be pursued under general Polish tort law or under the Polish product liability rules that are more favourable for the injured party. These product liability litigation cases are resolved before the Polish state courts.

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Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

Suppliers facing a lack of financial liquidity usually request relatively high advances and afterwards delay delivery of the ordered parts. These warning signs should encourage customers to thoroughly verify a contractor's financial condition. This can be done by checking the company's financial statements that are publicly available, checking the public registers of debtors or even checking information in the media. The results of these examinations can provide grounds to consider actions that could protect the customer from any potential losses. This can mean the renegotiation or even termination of a contract and the transfer of the supply relationship to a second source. It is critical, however, that these undertakings are first consulted with a lawyer who will point out the risks related to their potential ineffectiveness, especially in the face of possible bankruptcy proceedings.

A distressed supplier might have no choice but to launch a court-directed restructuring process or commence bankruptcy proceedings. The goal of the former option is to allow for the further operation of the company thanks to arrangements with its creditors, as opposed to the latter option, which aims at the liquidation of the company. In both cases, the contractual position of customers significantly differs from that which results from the concluded contract.

In the case of a restructuring process, the supplier offers arrangement propositions. These might include different solutions to restructure its position. The distressed supplier might propose the postponement of the delivery date, earlier payments or (higher) advances, a reduction in the quality of the product or limits to the warranty or guarantee claims. Ultimately, any arrangement propositions are voted on by the council of creditors.

In turn, in the case of a bankruptcy, as of the day of the declaration of bankruptcy, the supplier's obligation to deliver the ordered products automatically becomes a cash debt. The customer is then entitled to submit its claim (if any) during the bankruptcy proceedings. If it is acknowledged, the claim is satisfied from the bankruptcy estate proportionately with the other claims falling under the same category. The decision as to whether the claim is justified is firstly vested in the bankruptcy receiver who examines its grounds. The decision is subject to challenge, which is resolved by a judge-commissioner and, finally, by a bankruptcy court. It happens less often that, instead of making the supplier's obligation a cash debt, the bankruptcy receiver decides to continue to perform the obligation, and to serve the ordered part in exchange for remuneration.

Under Polish law, contractual provisions allowing a customer to revise or terminate a contract in the event of a supplier's bankruptcy or restructuring process are invalid. Additionally, in these cases, any obtained security can also be considered ineffective even if it had been granted by the distressed supplier within the previous few months. Therefore, it is advisable that any risky contract should be specifically protected by, for example, a bank guarantee issued by the parent company.

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Intellectual property disputes

12 Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

In recent years, automobile manufacturers' interest in intellectual property (IP) in Poland has focused mainly on trademarks. Most of the cases are those between automobile manufacturers and unauthorised distributors, or between OEMs and producers of spare parts. Recently, Polish District Court in Warsaw referred questions to the Court of Justice of the European Union relating to the issue of spare parts that reproduce a trademark as an element of the appearance of the part (Case C-334/22, *Audi*). Disputes connected to other IP rights, such as patents, designs or copyrights, are still rare.

IP is well protected under Polish law. National laws contain comprehensive provisions concerning copyrights as well as industrial property rights such as trademarks, patents, industrial designs and utility models. Polish law also stipulates the rules for fair competition that are relevant for the protection of IP and are often used to support claims concerning the infringement of these rights. Since Poland is a member state of the European Union, European regulations on EU trademarks and community design are directly applicable.

Since July 2020, IP matters have been heard by IP courts, that is, separate chambers in civil courts dealing solely with IP issues. There are five district IP courts (in Warsaw, Katowice, Poznań, Gdańsk and Lublin) and two appeal IP courts (in Warsaw and Poznań). The district court in Warsaw has exclusive jurisdiction to hear cases concerning, among other things, computer programs, inventions, utility models and business secrets of a technical nature. In 2020, Poland introduced new rules of proceedings in IP matters, including separate rules for securing evidence and the request for providing information. Oppositions and cancellation matters are generally heard by the Patent Office of the Republic of Poland in the first instance and can be appealed to the administrative courts.

Proceedings before courts and the Patent Office last approximately one year in each instance. In a significant number of disputes between automobile manufacturers and IP infringers in Poland, it is possible to reach out-of-court settlements, mostly owing to the small size and lack of bargaining power of the infringers.

EMPLOYMENT ISSUES

Trade unions and work councils

13 Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

There are no specific automotive sector labour regulations in Poland. The minimum labour standards are laid down in the Labour Code, which specifies the rights and duties of the parties to an employment relationship irrespective of industry or sector. Some of the most important aspects of Polish labour law are:

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- national minimum wage (as of 1 January 2023, the statutory minimum monthly remuneration is 3,490 zlotys gross, and as of 1 July 2023 will be 3,600 zlotys gross, for a full-time employee);
- minimum standards of sick pay, annual holiday leave and statutory notice periods;
- minimum standards of working time (the working period cannot exceed, in general, 40 hours per week, within a five-day working week);
- obligatory social security insurance (health, sickness, pension and disability); and
- minimum statutory severance payments due in the case of redundancies.

Employers are obliged to implement employee capital plans (PPK) that are an additional system for collecting pension savings for employees; however, employees can opt out. The statutory contributions for PPK amount to:

- 2 per cent of the employee's gross remuneration – financed by the employee; and
- 1.5 per cent of the gross remuneration of an employee – financed by the employer.

In Poland, work can be provided under an employment contract or a 'civil law contract'. Civil law contracts are not regulated by the Labour Code and are more flexible than employment contracts. They include contracts of mandate where an employer wishes to hire a worker to perform a particular action without entering into an employment contract, or contracts for specific work that are structured around and remunerated for the completion of this specific work. The provisions of the Polish Labour Code do not apply to persons employed under civil law agreements (eg, contracts of mandate, contracts for specific work or managerial contracts and so on) since they are legally not considered to be employees. However, Polish law guarantees them the national minimum wage (in 2023, this is 22.80 zlotys gross per hour, and as of 1 July 2023 will be 23.50 zlotys gross per hour).

The automotive industry commonly uses external personnel employed by temporary work agencies. Temporary personnel cannot be employed in the same company for more than 18 months and their employment terms and conditions cannot be less favourable than those of employees employed directly by the company.

The automotive sector is quite unionised in Poland. Trade unions are voluntary and self-governing organisations of individuals who provide paid work. Apart from employees hired under employment contracts, the individuals who provide paid work on a civil law basis also have the right to create and join trade unions and benefit from certain trade union privileges. Trade unions are founded to represent and protect employees' rights, as well as their professional and social interests. Trade unions also have the right to conduct collective negotiations and enter into collective labour agreements. In addition to trade unions, in companies with more than 50 employees, employees have the right to establish a works council. Employers are obliged to inform the works council about the economic activity of the company and any expected changes in the employment situation or organisation of the work. A work council can issue its own regulations, resolutions, standpoints and opinions.

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NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

One of the most important developments concerning automotive technological and mobility advances is an amendment to the Polish Act on Road Traffic, which introduces a legal basis for testing autonomous cars on public roads in Poland. The amendment, which came into force in February 2018, contains a definition of an autonomous vehicle – a car equipped with systems controlling its movement and enabling its movement without the intervention of a driver, who remains able to take control of the vehicle at any time.

Testing autonomous vehicles in road traffic on public roads, in particular for the use of autonomous vehicles in collective transport and the implementation of other public tasks, is possible provided that the safety requirements have been met and a permit for carrying out these tests has been granted. The permit is issued by way of a decision by the traffic management body on the road where the tests are to be conducted.

Poland is considering introducing further changes to this law that would allow for the development of autonomous driving. However, works on these changes are at a preliminary stage.

UPDATE AND TRENDS

Trends and new legislation

15 | Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

The most significant legal development for the automotive industry in Poland is the entry into force of a new emission standard – Euro 6D ISC-FCM – in EU territory on 1 January 2021. The emission standard replaces the temporary standard that has been in force since 2018 – the Euro 6D Temp standard.

Under the new European emission standard, passenger car manufacturers have two new obligations. The first is to maintain the standard level of emissions not only during homologation testing but also during the subsequent usage of cars on roads. The other obligation is that, from 1 January 2021, each new car must be equipped with a device monitoring fuel consumption or use of electrical energy (in cars with electric engines). Cars without such a device cannot be registered in the European Union.

What is more, as of 2021, a new average emissions target standard of 95g per kilometre applies across the EU, which has been drastically reduced compared to previous years – from 120g per kilometre in 2020 and 130g per kilometre in 2019. The average standard does not have to be met by every passenger car manufacturer. However, this is taken into account when calculating the individual standards for each manufacturer (in addition to,

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for example, the average mass of the vehicles produced). Therefore, lowering the average emissions target will obviously lower the individual standards of each manufacturer. If a manufacturer exceeds its individual standard, it will be required to pay a fee. The fee is €95 multiplied by the number of cars sold and the excess emissions over the individual standard.

There are no other current developments, emerging trends or pending legislation of note.



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Spain

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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

The automotive industry is a strategic and significant sector in Spain. It is, alongside other strong industries (such as tourism, chemicals and agriculture and food), one of the

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important sectors of the Spanish economy. Spain is ranked second among European automotive manufacturers, and ninth globally.

Despite the above, Wayne Griffiths, president of the Spanish Association of Automobile and Truck Manufacturers (ANFAC), explains that of the major European markets Spain is currently the worst performing country compared to pre-pandemic years, with sales 35 per cent below the usual annual figure – in the past three years around one million new vehicles remained unsold in the country. The president also notes a ‘failure in electrification’; the average sales of electric vehicles in Europe is 20 per cent, while in Spain this figure is below 10 per cent.

Therefore, ANFAC has published Roadmap 2023–2025, a set of measures that should be addressed as a matter of urgency. This plan aims, among other things, to increase the sales of electric vehicles to 372,000 by 2025.

Additionally, ANFAC believes that consumers should be encouraged to adopt new electric technologies. To this end, it has proposed immediate changes to the MOVES III Plan (eg, eliminating the payment of income tax for receiving a subsidy, in line with what is happening in other countries, and eliminating waiting lists).

Among fiscal measures included in Roadmap 2023–2025, the following can be highlighted:

- a VAT deduction for the purchase of electric vehicles by self-employed individuals and companies;
- improvement of deductions in retribution in kind for efficient vehicles; and
- deduction in corporate income tax for investment in the purchase of electric vehicles and installation of their infrastructures.

COMMERCIAL OPERATIONS

Regulation

- 2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

Type approval

Pursuant to section 1 of the General Regulation on Vehicles (passed by Royal Decree 2822/1998 of 23 December 1998), the distribution of vehicles requires prior authorisation. This takes the form of type approval (homologation) granted by the Spanish Ministry of Industry, Trade and Tourism.

Vehicle type approvals are governed by Regulation (EU) 2018/858 of the European Parliament and of the Council of 30 May 2018 on the approval and market surveillance of motor vehicles and their trailers, and of systems, components and separate technical units intended for such vehicles.

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Regulation (EU) 2018/858 governs a harmonised framework containing the administrative provisions and general technical requirements for approval of all new vehicles within its scope and of the systems, components and separate technical units intended for those vehicles with a view to facilitating their registration, sale and entry into service within the EU. According to section 13(2), the vehicle's manufacturer is responsible for all aspects relating to the type-approval process and for ensuring conformity of production, whether or not the manufacturer is directly involved in all stages of the vehicle's production.

There are other EU laws regulating type approvals relating to specific aspects of vehicles:

- Regulation (EU) 2019/2144 of the European Parliament and of the Council of 27 November 2019 on type-approval requirements for motor vehicles and their trailers, and systems, components and separate technical units intended for such vehicles, as regards their general safety and the protection of vehicle occupants and vulnerable road users; and
- Regulation (EC) 715/2007 of 20 June 2007 on type approval of motor vehicles with respect to emissions from light passenger and commercial vehicles (Euro 5 and Euro 6) and on access to vehicle repair and maintenance information, supplemented by Regulation (EU) 2017/1151 of 1 June 2017 (amended by Commission Regulation (EU) 2023/443 of 8 February 2023, which will fully apply from 1 September 2023), ensuring that new car models pass new and more reliable emissions tests under real driving conditions.

Regulation (EU) 2019/2144

Pursuant to section 4 of Regulation (EU) 2019/2144, manufacturers must demonstrate that all new vehicles that are placed on the market, registered or entered into service, and all new systems, components and separate technical units that are placed on the market or entered into service are type approved.

Regulation (EC) 715/2007

The obligations under Regulation (EC) 715/2007 include meeting the emission limits set out in Annex I (Euro 5 and Euro 6 emission limits and emission limits for the evaporative emissions test).

Furthermore, manufacturers must ensure that type-approval procedures are undertaken for verifying conformity of production, durability of pollution control devices and in-service conformity.

Registration requirements

Pursuant to section 4 of Spanish Royal Decree 750/2010, manufacturers wishing to type approve vehicles, systems, components or separate technical units under the scope of application of the Decree must be registered with the Manufacturers Registry.

Following the grant of type approval, vehicles and their trailers and semi-trailers must be duly registered with the vehicles registry managed by the relevant traffic authority. The traffic authority will depend on the autonomous region where the vehicle's owner, lessee with a purchase option or long-term lessee has its legal domicile. In this sense, the registration

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request must be undertaken by the owner, lessee with a purchase option or long-term lessee. The vehicles registry, in general, aims to identify, among other things, the vehicle's holder, its technical characteristics, the inspections conducted, compliance with the applicable insurance requirements and compliance with other legal provisions.

Insurance requirements

Insurance requirements apply to private and professional vehicle use, and Spanish requirements are not materially different from those that apply in other European countries.

Development, manufacture and supply

3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

The contractual arrangements and structuring of the development, manufacturing and supply in the Spanish automotive sector do not differ substantially from those used in other European countries. Some particularities may apply in the case of the Canary Islands (which enjoys a specific tax regime to protect investment and consumption in that overseas region and represents a challenge in terms of operational and transportation costs), otherwise the situation in Spain is similar to that of its neighbouring countries.

Distribution

4 | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

As in other European jurisdictions, vehicles are distributed through networks of 'concessionaires' or authorised dealers that represent car manufacturers across the Spanish territory. There is, however, no specific distribution law in Spain (unlike in countries such as Belgium) and, therefore, general rules of contract law apply – in some cases in combination with franchise regulations, commercial agency rules or other specific subsets of Spanish contract law depending on how the relationship with a particular dealer is organised. There have been legislative efforts in recent years to introduce a new Commercial Code, including specific rules for distribution (which would encompass automotive wholesale and retail distribution), but it is not likely that a distribution law will be passed in Spain in the mid to long term.

Legal disputes between car dealers and manufacturers typically focus on the renegotiation or termination of distribution contracts, while disputes involving suppliers normally relate to purchase levels or price renegotiation (particularly with key suppliers that make ad hoc components for specific car models or agree on particular pricing based on minimum purchase volumes). We understand, however, that these types of disputes are not specific to Spain and can be found in most other European jurisdictions as well.

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Mergers, acquisitions and joint ventures

- 5** | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

The structuring and implementation of M&A and joint ventures in the Spanish automotive sector do not differ from similar transactions in other European countries. Recently, there has been a growing trend for automotive companies or automotive component suppliers to join forces (by seeking strategic alliances or repositioning their core business), particularly as a result of global changes in certain technologies and consumer behaviour. A particularly interesting development in Spain is that several automotive manufacturers have teamed up with technology start-ups and urban mobility apps to offer new services to customers (eg, e-bikes, scooters and electric vehicles available for short-term rental use).

In comparison with M&A and joint ventures in other sectors, the global microchip shortage and the supply logistic chain slowdown have added new layers of uncertainty to the automotive industry, especially with respect to valuation and in terms of price negotiations.

Incentives and barriers to entry

- 6** | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

According to the data released by the Spanish Association of Automobile and Truck Manufacturers (ANFAC) in 2022, vehicle manufacturing increased 5.8 per cent compared to 2021 (2,219,463 units were produced in 2022). If the comparison is run against the pre-covid figures of 2019 (where 2.822 billion vehicles were produced), the decrease would be of around 600,000 units less. In terms of private vehicle registrations, in 2022 there was a 5.4 per cent decrease compared to 2021.

On 9 April 2021, the Spanish government launched Plan MOVES III to boost sustainable mobility. This programme consists of direct aid of up to €7,000 to private owners, self-employed individuals and small businesses to acquire new electric vehicles, and includes a call for proposals for the installation of new charging points, which will be funded by the Next Generation EU funds.

In July 2021, the Spanish government launched the MOVES Singulares II programme with €100 million in aid to incentivise technological development projects and innovative experiences in electric mobility that serve to promote the leap towards electric- and fuel-cell vehicles, promoting the development of projects by Spanish companies, to reach the technological maturity that facilitates its commercialisation.

Likewise, in December 2021, the European Commission approved the Spanish aid scheme of €3,000 million for the recovery and economic transformation (known as PERTE) of electric and plug-in cars. The programme provides support for investments in research, development and innovation, environmental protection and energy efficiency throughout the chain

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of industry. The scheme was formally launched in March 2022 and is being financed in part by the Next Generation EU funds.

In terms of market entrance, there are no substantial legal barriers other than the usual requirements involving the establishment of a business or manufacturing plant in Spain; nor are there any particular restrictions on foreign investment (except in the case of investors from countries that are affected by international trade sanctions or embargo regulations, or in the event that the regime for foreign direct investments is triggered).

The automotive industry is immersed in a profound process of transformation that will completely change its shape as we understand it. The main drivers of this change are:

- decarbonisation (new energies);
- new paradigms in terms of mobility (car sharing and pay per use);
- internet of things; and
- autonomous driving.

These changes will generate numerous opportunities for new and existing players.

PRODUCT SAFETY AND LIABILITY

Safety and environmental

7 | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

The most relevant safety and environmental rules relating to automotive compliance are envisaged in Regulation (EU) 2018/858, Regulation (EU) 2019/2144 and Regulation (EC) 715/2007, supplemented by Regulation (EU) 2017/1151 (amended by Commission Regulation (EU) 2023/443 of 8 February 2023, which will fully apply from 1 September 2023).

Pursuant to Regulation (EU) 2019/2144 and Regulation (EC) 715/2007, respectively, manufacturers must (1) ensure that vehicles are designed, constructed and assembled to minimise the risk of injury to vehicle occupants and other road users and (2) equip vehicles so that the components likely to affect emissions are designed, constructed and assembled to enable the vehicle, in normal use, to comply with Regulation (EC) 715/2007.

Against this backdrop, the Spanish General Regulation on Vehicles provides for the following:

- registered vehicles may be removed from the vehicles registry if the relevant competent authority, owing to wear or deterioration of the vehicle's mechanical elements, certifies that said vehicle constitutes an obvious danger to its occupants or traffic safety in general (section 35, paragraph 2 of the General Regulation on Vehicles); and
- during procedures relating to the declaration of nullity, loss of validity or expiry of administrative authorisations for the traffic of vehicles, the competent authority is entitled to suspend the applicability of the relevant authorisation if it poses a serious danger to traffic safety (section 51, paragraph 4 of the General Regulation on Vehicles).

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CO₂ emission performance standards for new passenger cars and new light commercial vehicles are set out in Regulation (EU) 2019/631 of the European Parliament and of the Council of 17 April 2019. This Regulation sets EU fleet-wide CO₂ emission targets applying from 2020, 2025 and 2030, and includes a mechanism to incentivise the uptake of zero- and low-emission vehicles. As for automotive-related product recalls in Spain, these are subject to the general product safety rules, which are based on the General Product Safety Directive 2001/95/EC.

Pursuant to Act 7/2021 of 20 May 2021, on Climate Change and Energy Transition, national, regional and local authorities must take measures to ensure that from 2050 passenger vehicle fleets and light commercial vehicles do not generate direct CO₂ emissions; no new non-commercial vehicles emitting CO₂ is marketed by 2040; and all municipalities with more than 50,000 inhabitants adopt sustainable mobility plans that provide for low-emission areas similar to those that are already implemented in Madrid and Barcelona.

Product liability and recall

- 8** | Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

Spain does not have a strong tradition in product liability litigation, and there have been no major automotive-related product liability disputes in recent years. This does not mean that there have been no product recalls in the sector. The automotive industry has suffered several product recall cases in Spain, some of which are particularly relevant. However, the main consequences of these product recalls have been resolved between the parties without judicial actions being filed.

On the other hand, regarding the class actions regime, although there is already the possibility of exercising class actions in consumer matters (according to the Spanish Civil Procedural Law), we expect a significant change once the transposition of the Directive 2020/1828 of representative actions for the protection of the collective interests of consumers and users has been made in Spain. In January 2023, the Preliminary Draft Law on Representative Actions for the Protection of the Collective Interests of Consumers was published. However, the definitive law has not yet been approved.

DISPUTES

Competition enforcement

- 9** | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

EU Regulation No. 461/2010 on the application of article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices in the motor vehicle sector, as well as its accompanying supplementary guidelines, is also applied

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by competition authorities in Spain to cases decided under either EU or Spanish competition law.

The main recent investigation and sanctioning proceedings conducted by the National Commission on Markets and Competition (CNMC) in the Spanish automotive sector include the following.

- In July 2015, the CNMC imposed a record combined fine of €171 million on 21 car manufacturers and distributors and two consulting firms for an alleged cartel consisting of exchanges of commercially sensitive information relating to motor vehicle distribution and aftersales services. The sanctioned companies represented more than 91 per cent of the Spanish market for car distribution. The investigation by the CNMC was triggered by a leniency application filed by one of the automotive manufacturers in Spain.
- Between 2015 and 2016, the CNMC imposed fines totalling roughly €53 million on a significant number of car dealers of different OEM distribution networks in Spain – as well as some consultancy firms and trade associations for their role as cooperators – on grounds of their participation in several cartels, through which they fixed prices or other commercial conditions and exchanged commercially sensitive information.
- In June 2016, the CNMC imposed a fine of €638,770 on a Spanish car-wash equipment manufacturer (which also provides repair and maintenance services itself and via appointed third parties) for alleged anticompetitive conduct consisting of a refusal to supply spare parts and technical data to independent repairers.
- More recently, in November 2021, the CNMC launched an investigation (including dawn raids) on possible anticompetitive practices, consisting of agreements for the manipulation and distribution of tenders issued by the Ministry of Defence, in relation to the supply, maintenance and upgrade of military equipment, in particular military vehicles. That investigation resulted in the opening, in December 2021, of sanctioning proceedings against a number of companies.

As regards follow-on litigation, in recent years there has been a significant increase in private actions for damages suffered by victims of cartels in Spain (ie, civil law damage claims before the courts following administrative law sanctioning proceedings before the CNMC) due to the implementation of EU Directive 2014/104/EU on certain rules governing actions for damages for competition law infringements in Spain by virtue of Royal Decree-Law 9/2017.

This increase in damages actions is having a particular impact on the automotive sector.

Spain is the European country with (by far) the highest number of judicial decisions in follow-on claims deriving from the Trucks cartel.

Since 2022, following the Supreme Court rulings confirming the sanctions imposed by the CNMC on car manufacturers, thousands of follow-on claims have been lodged against OEMs. This mass litigation is being widely reported in the Spanish press, with some law firms announcing mass litigation processes and encouraging consumers to file claims for damages, promising high compensations. The effective economic impact of these claims remains to be seen as, even in follow-on actions such as this, claimants are required to prove the actual damage suffered and demonstrate the causal link with the infringement.

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Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

While class actions and litigation around recalls or product safety are rare, dispute and claims proceedings do affect the Spanish automotive industry. A great percentage of these disputes are related to distribution agreements, terminations and claims for compensation. There have also been some supply chain and insolvency related disputes.

In general, the Spanish system provides claimants with the possibility of obtaining quick and provisional solutions through interim injunctions, which are especially useful in cases of supply chain disruptions.

More recently, since 2015, a number of players in the automotive industry have been involved in antitrust litigation proceedings. Arbitration is not very common in automotive-related litigation.

Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

Distressed situations and insolvency proceedings are complex. The way the automotive industry deals with suppliers facing such circumstances is determined on a case-by-case basis, depending on the factual circumstances at hand, by seeking securities and guarantees to warrant the fulfilment of supplier obligations – and by considering not only the legal implications but also the economic impact that the relationship with the automotive manufacturer may have on a supplier's overall performance and business continuation.

One particularity of Spanish law is that the mere declaration of a company insolvency is not a valid cause for termination of agreements entered into by the company. This means that a car manufacturer cannot terminate a supplier agreement only on grounds that the supplier has gone into insolvency; the contractual relationship will continue unless other reasons for termination appear such as a material breach of the supplier's duties.

Intellectual property disputes

12 | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

Intellectual property (IP) and related unfair competition disputes in the automotive field in Spain are rather significant, in view of the number of cases the Spanish courts have handled in the past few years, which show an increasing trend, although they are still less common than in other industries (eg, pharmaceutical and TMT). IP disputes and joint unfair competition claims are heard by several commercial courts specialising in IP matters across the country, which helps guaranteeing consistency in judicial decisions and, therefore,

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predictability. The most common venues are the Barcelona and Madrid Commercial Courts, as well as the EU Trademark and Design Court located in Alicante, which handles all EU trademark and designs claims on an exclusive basis. Section 15 of the Court of Appeals of Barcelona and section 28 of the Court of Appeals of Madrid, as well as the EU Trademark and Design Court of Appeals, are the most reputed tribunals for IP matters in Spain whose decisions have a great impact in the development of IP case law in the country.

The prevalence of trademark and trade names proceedings in the automotive field is remarkable. Disputes in this sector mostly involve trademark or trade name infringement actions for likelihood of confusion (eg, *CICAR v ZIPCAR*, *Parkia v ParkVia* or *M JOSCAR Hnos v JOYCAR*) where defendants usually bring counterclaims seeking the invalidity or cancellation for non-use of the enforced trademarks. In a relevant number of cases, the claims involve the use by workshops or car sellers of well-known car brands. Case law shows that courts tend to be protectionist towards IP rights holders and have admitted the majority of the trademark or trade name infringement claims issued in the past few years.

It is also relatively common that trademark or trade name infringement claims are jointly brought with unfair competition-related actions, with claims mostly based on acts of confusion, unfair exploitation of a third party's reputation and misleading acts. Courts are less prone to uphold unfair competition actions brought by plaintiffs, not the least since IP rights holders are typically not entitled to enjoy double protection based on their IP rights and the protection granted by the unfair competition law against the same behaviour by defendants.

Patent, utility model and design infringement claims in the automotive field are still scarce. Although design cases have been traditionally upheld, in the majority of patent infringement cases the courts either dismissed the claims or declared the patent to be invalid. The first patent disputes involving standard essential patents and FRAND licensing discussion related to mobile telecommunications technologies have been launched before the Spanish courts, also involving players in the automotive sector. This will certainly be a hot topic in the automotive industry in the near future.

EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

As in other European countries, in Spain employment relations are governed by legal provisions and agreements emanating from national and international legislative bodies (international treaties, local laws and regulations), the will of the parties (collective bargaining agreements and employment contracts) and the customs and practices of the company itself (company agreements and practices).

Most of the employment regulations established in the laws apply to all companies, without specific regulations for industries or sectors (except regulations on health and safety, which may vary depending on the business activity concerned). This applies, for example, to

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working time, minimum wages, severance payments in case of dismissal, types of contracts, election and activity of workers' councils and unions.

In Spain, it is possible to enter into collective bargaining agreements (CBAs) – that is, agreements that have been negotiated and concluded by employers and employee representatives and are applicable to a more or less broad sector at both a national or provincial level, as well as, on a smaller scope, those applicable to a company or work centre.

However, most of the relevant companies in the automotive sector that operate in Spain negotiate their own CBA at company level or have side agreements with their employees.

The pressures arising from the fierce competition in a highly globalised sector such as the automotive industry are transferred to companies, affecting labour costs and working conditions. In Spain, the automotive sector is characterised by the existence of large groups, mainly multinationals, with several activities in the country and a dispersed CBA format. Some larger companies have their own CBA at company level, while the smaller ones are attached to regional CBAs.

It is also important to point out that automotive companies in Spain are highly unionised. They have not only work councils, but also national unions involved in relevant decisions. Likewise, in the case of renowned automotive companies, political involvement is common when relevant decisions are taken (such as investments, divestments and restructurings). The scope of the political involvement (regional or even national) depends on the company affected, its economic or social impact in the area and the type of measure to be taken.

Finally, we must note that trade unions have played a key role in the automotive sector in recent years. This past two and a half years, with the impact of covid-19 and the chip crisis, the automotive sector has been shaken by numerous redundancy plans that affected thousands of people. Trade union negotiation with companies has been an important factor in tackling the crisis.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

In the field of autonomous intelligent driving, on 20 December 2021, by means of Act 18/2021, various sections on automated vehicle driving were introduced into the recast text of the Act on Traffic, Circulation of Motor Vehicles and Road Safety, passed by Royal Legislative Decree 6/2015 of 30 October 2015.

Sustainable mobility-related policies have triggered some important developments concerning electric and hybrid vehicles. For instance, certain cities (eg, Madrid) have passed local mobility regulations that allow drivers of electric and hybrid vehicles to access areas restricted to other vehicles.

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The Spanish government is currently processing the draft bill for a Sustainable Mobility Act. Pursuant to some public statements coming from the Minister of Transport, Mobility and the Urban Agenda, this bill is intended to be submitted to Congress before the end of 2023. The text of the current draft bill has a chapter on automated vehicles.

Also in this field, Royal Decree 266/2021 of 13 April 2021 was passed, granting direct aid for the implementation of incentive programmes linked to electric mobility (MOVES III) in the framework of the European Recovery, Transformation and Resilience Plan. Certain incentive programmes for electric mobility are also approved by the Royal Decree, such as the programme to promote the purchase of electric vehicles or the programme to support the deployment of charging infrastructure, both within the general framework of the Recovery, Transformation and Resilience Plan.

With regards to the provision of energy recharging services for electric vehicles, the approval of Royal Decree 184/2022, of 8 March 2022 should be noted. This regulation applies to electric vehicle charging point infrastructures that are located on public roads or, if not located on public roads, are accessible to all electric vehicle users, such as public and private car parks, service stations or shopping centres.

UPDATE AND TRENDS

Trends and new legislation

15 Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

In the field of intellectual property, the Spanish Patent and Trademark Office (SPTO) is aware of emerging trends in the automotive industry and publishes, on a quarterly basis, free, schematic newsletters on the new developments regarding electric vehicles and smart car systems, where updated news and new patent applications published within these fields are listed.

Additionally, in January 2023, the SPTO published a press release examining the findings of a recent report issued by the European Patent Office and the International Energy Agency on hydrogen-related patents and global innovation trends in hydrogen technologies. The report suggests that the automotive sector has been the most relevant field of application for hydrogen-related patents, with more patent applications than all other emerging uses of hydrogen combined (including aviation, rail and shipping).

One of the main factors consumers take into account when purchasing a vehicle is sustainability. More than 80 per cent of consumers argue that sustainability and social responsibility matter more today than before the pandemic. Based on this fact, the dealer must offer the right products to customers, especially those who are more environmentally conscious.

Evidence of this is that Tesla has positioned itself as the world's best-selling electric vehicle brand. In 2022, it sold 1,249,149 units. The vast majority of sales were in the US market.

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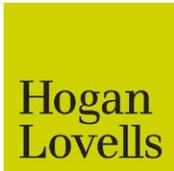
The reports suggest that the electric vehicle boom has been driven in large part by the global semiconductor crisis. They point out that this situation has forced manufacturers to prioritise the most profitable models (electric cars) by reducing production of petrol and diesel models.

In 2022, the sales of electric cars in Spain rose by 19.1 per cent. However, the sales of electric cars represents only 8.8 per cent of the total market share.

Finally, some reports foresee that the much more intensive use of vehicles and a substantial reduction in their average life will lead to a reduction in vehicle stocks in some markets – for example, Europe and the United States – and, at the same time, to a substantial increase in the number of registrations.

Specifically, in Europe, it is estimated that the number of registrations can grow by 34 per cent by 2030, from 18 to 24 million units. This growth can be 20 per cent in the United States, up to 21.6 million vehicles. In China, given its particular market situation with a significant increase in population and in the midst of urbanisation, an increase is predicted in both registrations – a 30 per cent increase to 35 million – and in the vehicle fleet – expected to reach 275 million cars in 2030.

The EU is working on new Euro 7 standards to reduce pollutant emissions from vehicles and improve air quality, which, if passed, would enter into force in 2025. The Euro 7 standards would bring new emission limits for all motor vehicles. This European legislative initiative has been strongly opposed by the Spanish automotive industry, which considers that it could put at risk the viability of some factories in Spain.



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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

The automotive and mobility sector is one of the most significant drivers of Turkish industrial production, with over 10 producers, most operating under licence or as joint ventures, over 150 research and development centres, three automotive design and engineering

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centres and a production capacity of over two million vehicles per year. In 2021, Turkey was the 13th-largest producer of motor vehicles in the world and the fifth largest in Europe, having grown steadily over the past decade. In terms of actual production, Turkey produced 810,889 cars and 591,300 commercial vehicles in 2022, a total of 1,402,189 vehicles, of which 970,124 were exported.

As of the end of 2022, there were 26,482,847 vehicles in Turkey, of which 53.9 per cent were cars and 46.1 per cent commercial vehicles. Retail sales for the same year included 592,660 automobiles and 190,623 light commercial vehicles, which represented an overall increase of 6.2 per cent compared with 2021. Although the economic recession continued in Turkey during 2022, the increase in sales can be attributed to the rise in vehicle purchases after the end of the pandemic.

COMMERCIAL OPERATIONS

Regulation

2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

The Turkish regulations on vehicle manufacturing have generally been drafted in accordance with United Nations norms and European Union legislation. The primary piece of legislation regulating motor vehicles and their registration is Highway Traffic Law No. 2918. Pursuant to the Highway Traffic Law, all motor vehicles and their trailers intended to operate on highways are obliged to have a certificate of conformity granted by a certification authority.

For vehicles to obtain a certificate of conformity, the initial step is obtaining type approval. The Ministry of Industry and Technology has authorised Turkish Standards Institution to supervise the homologation process and grant type-approval certificates. There are three regulations pertaining to the conditions for type approval based on vehicle categories:

- the Regulation on Type Approval of Motor Vehicles and Their Trailers and Type Approvals and Market Surveillance of These Parts, Systems and Separate Technical Units (AB/2018/858);
- the Regulation on Type Approvals and Inspections of Agricultural and Forestry Vehicles (AB/167/2013); and
- the Regulation on Type Approvals and Inspections of Two- or Three- Wheel Motor Vehicles and Four-Wheel Motorcycles (AB/168/2013).

All three are drafted in accordance with applicable European Union Directives and Regulations of the United Nations Economic Commission for Europe. There are no specific or additional provisions regarding the manufacture of automobile parts, and all three regulations on type approvals are applicable to automobile parts as well.

Once a vehicle obtains type approval, a certificate of conformity also needs to be received for the vehicle to be operated on highways. The terms and conditions for obtaining the certificate of conformity for highways are regulated by a comprehensive regulation applicable

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to all types of road vehicles, entitled the Regulation on the Manufacture, Modification and Assembly of Vehicles dated 26 October 2016.

Pursuant to the Highway Traffic Law, all vehicles are obliged to be registered with the traffic registry before they can be operated on highways. With new legislation that came into effect in early 2018, called the Regulation on Carrying Out the Sale, Transfer and Registration Services of Vehicles, public notaries are responsible for the registration of vehicles using an automated system (previously, registrations were undertaken by traffic registration offices).

The Highway Traffic Law also requires that vehicles have compulsory automobile liability insurance to be registered and used on highways.

The Regulation on Aftersales Services dated 13 June 2014 includes specific rules for the distribution of automotive parts. Pursuant to this regulation, manufacturers and exporters must continue to supply spare parts to customers.

In practice, the distribution of automobiles and automobile parts is undertaken through dealership agreements, which must be drafted in accordance with the Block Exemption Communiqué on Vertical Agreements in the Motor Vehicles Sector No. 2017/3 (the Block Exemption Communiqué) issued by the Turkish Competition Authority.

Development, manufacture and supply

3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

The Turkish automotive industry is engaged in both the manufacture and import of vehicles and spare parts. Primary manufacturers sell vehicles directly or through dealers. On the other hand, importers normally establish a sales network, with key importers establishing both a distribution network for sale (quantitative selective distribution) and aftersales services (qualitative or, if their market share does not exceed 30 per cent, quantitative selective repairer network).

Primary industry manufacturers in Turkey generally work with various sub-industry (parts) manufacturers for their procurement needs. There are several-hundred sub-industry manufacturers for every key industry manufacturer. However, contractual relationships among primary industry manufacturers and sub-industry manufacturers tend to be trade-based only and often short term, mostly lacking any mutual R&D efforts or other deeper collaboration.

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Distribution

- 4** | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

In terms of the distribution of vehicles, there are no special rules for importers, distributors or dealers with the exception of sector-specific arrangements under competition legislation. Owing to competition rules requirements, importers or manufacturers choose the quantitative selective distribution system to sell vehicles.

In accordance with the requirements of the Block Exemption Communiqué, an agreement between a supplier (ie, manufacturer or importer) and a distributor may have a definite or indefinite term. An agreement with a definite term must remain valid for at least five years and each party must accept a provision to notify the other party of its intention not to renew at least six months before the expiration of the agreement. For agreements with indefinite duration, the notice of termination period must be at least two years for both parties. The terms must also allow this two-year notice period to be reduced to no shorter than a period of one year when:

- the supplier is required by law or the agreement to pay appropriate compensation if it terminates the agreement; or
- the supplier terminates the agreement owing to the reorganisation of a significant portion or the entirety of its distribution system.

Mergers, acquisitions and joint ventures

- 5** | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

There are no special provisions required for M&A or JV transactions within the automotive industry, and there are no additional steps to be taken while preparing, negotiating or entering into a deal, with the caveat that competition laws play a significant role in the Turkish automotive industry.

Incentives and barriers to entry

- 6** | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

The incentives provided for investments in various markets are regulated by a Decree of the Council of Ministers entitled the Decision on Government Incentives for Investments No. 2012/3305. Through a 2013 amendment to this Decision, the automotive sector was designated as a priority sector. Pursuant to this Decision, for an investment in the automotive sector to be entitled to receive an incentive, the investment amount must be no less than 200 million lira for the main industry and no less than 50 million lira for sub-industries.

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Furthermore, if the investment is no less than 300 million lira, it will be entitled to receive top-priority incentives. Top-priority incentives include, among other things, VAT and customs duty exemptions, social security support, partial corporate tax exemptions and allocation of land free of charge. Incentives are granted individually for each party fulfilling the criteria and new entrants do not affect the incentives that incumbents are entitled to receive.

There are no barriers to entry into the automotive market, provided that the new party to the market fulfils all general criteria for investors to establish an industrial enterprise. To increase competition in the local market and in furtherance of Turkey's desire to become a major global competitor in the automotive sector, newcomers to the Turkish market are normally encouraged via the incentives described above.

PRODUCT SAFETY AND LIABILITY

Safety and environmental

7 | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

As part of Turkey's EU harmonisation process, new legislation on product compliance safety and the environment has been adopted to conform to EU legislation within the framework of the EU-Turkey Association Council Decision No. 1/95 of 6 March 1995, which establishes a Customs Union among EU member states and Turkey. The primary goal of the applicable Turkish legislation is to protect consumers from potentially dangerous and harmful products, and to ensure that businesses place safe and compliant products on the market. The Ministry of Industry and Technology regulates compliance and conducts market surveillance through related regulations implemented by other relevant ministries. The most relevant automotive-related product safety and environmental regulation is the Market Surveillance and Inspection Regulation of Automotive Products dated 22 February 2018, which regulates automotive products through the Ministry of Industry and Technology within the scope of the Law on Product Safety and Technical Regulations No. 7223.

In accordance with the new regulations brought by the Law on Product Safety and Technical Regulations No. 7223, importers or exporters who supply the market with products that are non-compliant with the safety regulations can face administrative fines of up to 1,518,153 lira, and they will also be liable for the damages caused by their products to any person or goods.

The Ministry of Industry and Technology is responsible for supervising and investigating technical compliance of vehicles with the Market Surveillance and Inspection Regulation of Automotive Products during the market distribution, import, export and assembly processes. While the regional directorates carry out market surveillance activities, the central unit of the Ministry of Industry and Technology deals with policy development, programming and monitoring of these surveillance activities. The most significant market surveillance activities carried out by regional directorates are product recalls.

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Obligatory recall process

Pursuant to the Market Surveillance and Inspection Regulation of Automotive Products, within the scope of an obligatory recall, if a vehicle is determined non-compliant, the manufacturer must submit a corrective action plan to a regional directorate within 30 days, and implement such plan within one year if approved. If the plan is not approved by the regional directorate, or the manufacturer fails to submit an appropriate plan or fails to implement the plan, administrative fines of up to 231,540 lira may be imposed on the manufacturer. Extensions will not be granted for implementing the corrective plan unless the malfunction was not the manufacturer's fault.

Voluntary recall process

If a manufacturer detects non-compliance before an administrative authority does, a voluntary recall procedure must be implemented to avoid administrative fines, which can be substantial. In the event of a voluntary recall, the manufacturer will make a submission to a regional directorate, including all necessary documentation and making an estimation as to how long it will take to conclude the recall process. The regional directorate may grant a maximum of one year for the finalisation of the recall transactions. Extensions will not be granted if the corrective plan's failure to be implemented on time is the fault of the manufacturer. The voluntary recall must be announced on the Ministry of Industry and Technology's website, and separate notices made to vehicle owners including detailed information on the recall process, technical non-compliance of the vehicle and contact information of authorised offices. If a vehicle owner does not respond to the notice, a second notice will be sent. If the owner fails to respond again, the notice will be deemed to be duly served.

Product liability and recall

- 8** | Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

Product liability issues constitute the largest number of disputes in this sector. Consumers who claim that a vehicle is defective may exercise the general rights they are afforded under the Law on Consumer Protection No. 6502. If it becomes apparent that the vehicle is defective, the consumer may exercise one of the following rights:

- rescinding the contract and returning the purchased vehicle;
- requesting a discount from the sales price in proportion to the defect and keeping the purchased vehicle;
- requesting a free of charge repair with all expenses borne by the seller, if the repair does not require extensive expense; or
- requesting replacement of the defective vehicle with a defect-free one, if possible.

The legislation provides a warranty period of two years after the date of sale of a vehicle. If the vehicle contains a manufacturing defect, the consumer may assert the rights listed above, even if the warranty period has passed. Furthermore, certain spare parts may have different statutory warranty periods.

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Although recall cases are not very common in Turkey, pursuant to the Market Surveillance and Inspection Regulation of Automotive Products, regional directorates of the Ministry of Industry and Technology conduct recall processes for vehicles deemed unsafe or non-compliant with technical regulations. Having said that, separate from the recall process, if a consumer claims that the vehicle is not in compliance with applicable technical regulations, the case is deemed a matter of product liability and examined by consumer courts within the scope of the Turkish Law on Consumer Protection.

Although the Turkish Civil Procedure Code allows a type of class action by associations or other entities on behalf of their members or groups whose interests they represent, in practice, class actions are not common for defective goods in Turkey.

DISPUTES

Competition enforcement

- 9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

Sector-specific rules

Since 1998, the Turkish automotive industry has been regulated by sector-specific rules, with the (most recent) Block Exemption Communiqué released in February 2017. These sector-specific rules lay down the conditions to be met for vertical agreements in the automotive industry to benefit from block exemptions from the prohibition on the allocation of markets, interfering with sales conditions and exclusive dealing of article 4 (akin to article 101 of Treaty on the Functioning of the European Union) of the Law on the Protection of the Competition No. 4054 (the Competition Law). The provisions of the Block Exemption Communiqué apply to vertical agreements concerning the purchase, sale and resale of new motor vehicles; the purchase, sale and resale of spare parts of motor vehicles; and maintenance and repair services.

As long as the market share of the parties to the vertical agreement does not exceed 30 per cent, exclusive distribution systems, quantitative distribution systems or qualitative distribution systems can be concluded. Vertical agreements in which the market share of the parties exceeds 30 per cent benefit from the block exemption only if they adopt the qualitative distribution system. The Block Exemption Communiqué aims to protect distributors from immediate termination by regulating the terms of their agreements and the notice periods for termination. Accordingly, to benefit from the block exemption, the agreement must have a duration of at least five years and both of the parties must accept a provision in the agreement to notify their desire not to renew at least six months before the expiration of the agreement; where the agreement is for an indefinite duration, the notice of termination period must be at least two years for both parties.

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Hardcore restrictions

The Block Exemption Communiqué contains a list of hardcore restrictions applicable to the distribution of vehicles, spare parts and the aftersales market, and is supplemented by a sector-specific guideline. The main restrictions can be summarised as follows:

restrictions on setting the distributor's resale prices, with the exception of setting maximum and recommended prices;

restrictions related to the region or customers to which the distributor may sell, with the following exceptions:

- in the case of an exclusive distribution system, restriction of active sales to an exclusive region or an exclusive customer group allocated by the supplier to itself or to another buyer, provided the restriction does not include sales by customers of the buyer;
- restriction on sales to final users by a buyer operating at the wholesale level;
- prohibition of sales by selective distribution system members to unauthorised distributors within the region allocated by the supplier for the operation of the system concerned; and
- in the case of parts procured for assembly, prohibition on the buyer selling these parts to manufacturing competitors of the supplier;
- restrictions on active or passive sales by selective distribution system members operating at the retail level to final users. However, the supplier is entitled to prohibit a system member from operating at a location where it is not authorised. Furthermore, prevention of sales and purchases between members of the selective distribution system is prohibited; and
- restrictions on an authorised service station's freedom to limit its operations to maintenance and repair services, and spare part distribution.

In its regulation of the distribution of spare parts, the Block Exemption Communiqué aims to ensure that authorised distributors, authorised spare part distributors, authorised service stations, independent spare part distributors, private service stations and end users are not forced to depend on the motor vehicle supplier for the procurement of the goods in question, and to allow other suppliers of such goods to be active in the market.

Non-compete obligations

Non-compete obligations are regulated separately under the Block Exemption Communiqué for the distribution of motor vehicles, for the distribution of spare parts and for aftersales services. A non-compete obligation is defined as any direct or indirect obligation placed on the buyer forcing the buyer to make its purchases of the relevant goods or services in the relevant market, or substitutes thereof, from the supplier or from an undertaking designated by the supplier at a level of over 80 per cent in the new motor vehicle sales market and over 30 per cent in the aftersales market.

For the distribution of motor vehicles, non-compete obligations with a period of a maximum of five years are within the scope of the block exemption. However, the distribution of spare parts and aftersales services do not benefit from the block exemption.

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Investigations in the automotive industry

The automotive industry, including the spare parts sector, is a relatively frequent investigation target of the Turkish Competition Authority (TCA). The first violation decision of the Turkish Competition Board (the Board), a part of the TCA, related to Renault's practices on vertical agreements in 2000. Renault was fined for non-compliance of its distribution agreements with competition rules, fixing discount rates, prohibiting the use of matching-quality spare parts and prohibiting fleet sales by authorised dealers to public entities. Two subsequent decisions of the Board in 2001 against Doğu Group, which imports and distributes Volkswagen Group brands in Turkey, and in 2004 against Peugeot related to vertical agreements that were not in line with the requirements of permitted block exemptions.

In its most extensive investigation of the industry, the TCA initiated an investigation of 23 undertakings active in the automotive sector (both passenger cars and light commercial vehicles) in 2009. The TCA alleged that the undertakings had discussed future pricing policies, stock data, sales targets and sales strategies. According to the Board's decision in 2011, 15 undertakings under investigation violated article 4 of the Competition Law. The Board imposed fines on these undertakings totalling approximately 277 million lira. At that time, it was the largest fine ever imposed by the Board. In its decision, the Board emphasised that exchange of future prices or price strategies can be deemed a violation of competition rules. The Board indicated that unless otherwise proven by the investigated undertakings, it is presumed that the undertakings used the exchanged information to coordinate their actions in the market. Exchange of other information such as stock data, sales targets, sales amounts and sales strategies among the undertakings was deemed as complementary to the exchange of future prices and price strategies. The appeals process against the fines was concluded by the end of 2019. The Council of State dismissed the request of 15 undertakings to cancel the fines and approved the Board's decision.

A two-year investigation by the TCA, initiated in early 2020 against 24 car distributors, which included companies such as Ford Otosan, Mercedes, Volvo, Tofaş and Doğu, concluded in March 2022. The Board decided that there was no infringement by the undertakings and did not impose any fines.

The length of the appellate process for competition law violations often prevents claims for damages by private action, as Turkish courts are unwilling to accept suits for damage claims before the final decision on the underlying infringement has been issued. Additionally, it is not possible to bring actions on behalf of multiple claimants in the form of a collective action. Although the Turkish Civil Procedure Code allows a certain type of class action, class actions are not used in practice, which can be considered as a barrier to damage claims through private action.

Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

The main types of disputes seen in the automotive industry are disputes arising from contractual relations and product liability.

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Disputes regarding contractual relations usually arise among main industry manufacturers, sub-industry manufacturers, distributors and dealers. These disputes are usually resolved by litigation. If the infringement of a contract constitutes an emergency that may prejudice a party from exercising a right, such party may file for an interim injunction before filing a case, provided it posts a deposit. After obtaining the court's decision on an interim injunction, related legal proceedings must be initiated within two weeks. The parties are also free to include arbitration and other ADR clauses in their contracts, or agree to such procedures after the dispute has arisen.

Disputes arising from product liability can be divided into two groups: disputes between automotive companies and other legal entities, and disputes between automotive companies and consumers. While product liability disputes between automotive companies and legal entities are resolved by litigation through civil courts, specialised consumer courts oversee consumer disputes. Furthermore, if the claim is for less than 66,000 lira, consumers can apply to consumer arbitration commissions for an expedited resolution of the dispute.

For both disputes regarding commercial and consumer matters, applying for mediation before filing a case is mandatory, except for applications to consumer arbitration commissions and objections filed against consumer arbitration commissions.

Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

There are no specific provisions for dealing with distressed suppliers in the automotive industry. Having said that, Turkish legislation in general aims to enable distressed suppliers to continue their operations and to provide various incentives to improve their financial status. There are various incentives foreseen for small and medium-sized enterprises, from which sub-industry manufacturers can benefit. Such incentives include, but are not limited to, loans with a low interest rate, tax deductions, debt relief and reorganisation.

Furthermore, one of the primary goals of the Turkish Code of Obligations, at the time of inability to perform obligations, is to maintain the continuity of contractual relationships rather than immediate termination. Accordingly, the Turkish Code of Obligations sets forth that in a bilateral contract, if one of the parties is distressed, the other party may grant additional time or request a judge to do the same to enable the distressed party to perform its obligations. In such a case, a claimant can request compensation or termination only if the distressed party cannot fulfil its obligation in the granted time. Having said that, as a default rule, if the rights of a party to a contract are jeopardised due to the other party's inability to perform its obligation arising from the contract, especially if the non-performing party is bankrupt or collection proceedings against it remain inconclusive, the jeopardised party may refrain from performing its obligations until the performance of the other party is secured without the necessity to grant additional time.

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Intellectual property disputes

12 | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

The most significant intellectual property disputes in the automotive industry have traditionally been due to alleged infringements caused by companies that are not OEMs, which constitute a majority of the market. The Turkish Industrial Property Law, which entered into force in 2017, adopts a new method specifically for aftermarket and non-OEM parts. Pursuant to this law, if the intended use of a good is indicated, the trademark owner can no longer prevent third parties from using accessories, repair parts and non-OEM goods in good faith, within the natural flow of commercial life.

From a design aspect, protection of vehicle parts is examined in different groups: repair parts (must-fit parts and must-match parts) and equivalent goods. Must-fit parts (engine pistons and the like) are designed in an imperative shape and size for a specific function and cannot be replaced with a different shape. On the other hand, must-match parts (headlights and the like) are visible and mandatory for the original appearance of a design, but not the function. Designs of must-fit parts cannot benefit from protection over design rights and OEMs cannot pursue any claims over must-fit parts manufactured by non-OEMs arising from design rights.

On the other hand, must-match parts can benefit from protection of design rights, and the most significant intellectual property disputes arise from the manufacturing of must-match parts. An exception to this rule is that the use of a must-match part for repair purposes after the part has been in the market for at least three years does not constitute an infringement of design rights. This exception was adopted as a part of Turkey's harmonisation process with European Union legislation.

The Turkish Industrial Property Law also protects non-OEMs with respect to their production of equivalent goods to prevent intellectual property disputes between non-OEMs and OEMs. Pursuant to this law, the use for repair purposes of equivalent goods announced by the Ministry of Industry and Technology does not constitute infringement of design rights even for the first three years of the availability of the goods on the market.

There is no fast-track option for resolving intellectual property disputes. Disputes arising from the infringement of intellectual property rights are examined by specialised civil and criminal courts for intellectual and industrial property rights. The approximate trial period is one to three years, excluding the appeal process, which may take more than two years.

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EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

Pursuant to the Turkish Constitution, all employees have right to become members of trade unions without the necessity to obtain permission from their employers. In practice, trade unions actively operate with significant influence in automotive companies. Currently, there are three trade unions whose members include automotive sector employees (in addition to other sectors), namely, Türk Metal, Birleşik Metal-İş and Özçelik-İş. These three unions have a total of approximately 339,266 members; of these, 258,928 are members of Türk Metal.

Provided that a trade union has at least 10 per cent of the employees of the sector as members and its members in the given automotive company constitute a majority of the employees, the union can apply to the Ministry of Labour and Social Security in order to be authorised to sign a collective labour agreement. If the authorisation is granted by the ministry, a collective labour agreement will be implemented at the company. Collective labour agreements can be in force for up to three years. The negotiation process takes place between the trade union that has the majority in the given automotive company and the Turkish Employers Association of Metal Industries, the major employers' union for the automotive sector, if the given automotive factory is a party thereto. If the automotive company is not a member of an employers' union, the representatives of the company take direct part in the negotiation process.

Turkish labour laws clearly forbid employers to terminate employment relationships due to employees' membership of trade unions. In the event of a company's non-compliance, the employee will be entitled to claim compensation equal to no less than one year's wages, in addition to any employment claims the employee is entitled to receive at the time of termination.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

Turkish legislation on the manufacturing of vehicles, and the automotive industry in general, is drafted in accordance with United Nations norms and European Union legislation. Furthermore, to ensure compatibility with technical developments in the automotive industry, there have been various recent amendments to Turkish legislation with respect to the manufacturing and repair of vehicles.

The manufacturing of vehicles was regulated by the 2008 Regulation on the Manufacturing, Modification and Assembly of Vehicles until late 2016, when it was replaced with a new

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regulation with the same name. With the new regulation, provisions relating to electric and hybrid cars were introduced for the first time.

Pursuant to the Motor Vehicles Law in force, electric cars are not subject to motor vehicles tax (MVT) because MVT is calculated based on the cylinder volume of the engine, which electric cars normally do not have. Having said that, pursuant to the Law on the Taxation of Motor Vehicles, MVT is applicable to electric cars too, at the rate of one-quarter of the MVT of gasoline engine vehicles within the same price range and with equivalent engines starting from 1 January 2019. On the other hand, MVT for hybrid cars is subject to the Motor Vehicles Law and is not specifically regulated in any legislation. There are also specific tax discounts foreseen for a special consumption tax for electric and hybrid cars to encourage the use of these new technologies. Although the sale of electric cars has increased significantly as a percentage (8,210 electric cars were sold in 2022, compared to 2,849 sold in 2021), sales of such vehicles are still negligible in the overall market. The sale of hybrid cars has seen a small decrease, with 19,126 hybrid cars sold in 2022 compared to 20,915 sold in 2021.

The Charging Service Regulation entered into force in April 2022. Per this Regulation, the Turkish Energy Market Regulatory Authority (EMRA) will oversee the establishment and operation of electric vehicle charging stations. According to the Regulation, charging service providers must apply for a licence to EMRA to obtain a charging service provider licence. Over 100 companies have already been granted licences. Although Tesla has not yet started to sell electric vehicles in Turkey, it is among the companies that have obtained the licence. There are currently 3,728 charging stations in Turkey, of which 646 charging stations are for fast charging (DC) and 3,082 are for slow charging (AC).

The operation of Uber and similar companies in Turkey was subject to great controversy for a long time. To transport passengers in Turkey, a certificate for commercial passenger transfer must be obtained. However, pursuant to the regulation in force, only taxis and passenger vans (minibuses) with a certain number of seats are entitled to obtain this certificate. This created a legal gap and for a period enabled ride hailing companies to operate using commercially licensed vans without being subject to the high tax rates and taxicab licence (that regular taxis incur). Martı, an e-scooter app operating in Turkey, has recently developed a ride-sharing service called TAG that can be accessed through its application. Martı currently does not obtain any commission fee for the ride-sharing service, and TAG only operates as a platform service provider. There is an ongoing court case against TAG.

In response to a lawsuit filed by the Union of Taxi Drivers, an Istanbul court ruled in 2019 that the operations of Uber constitute unfair competition between the taxi drivers and Uber operators. Accordingly, the court terminated Uber's commercial activities and prohibited access to Uber services. Uber appealed the decision and, in January 2021, the appellate court reversed the judgment. Following the reversal, the Information and Communications Technologies Authority unblocked access to Uber's services, and the company is currently operating in 16 cities, expanding from three cities compared to July 2021, albeit essentially as a taxi-hailing app. Other taxi-hailing services are currently operating in Turkey too.

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UPDATE AND TRENDS

Trends and new legislation

15 | Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

In November 2017, a consortium composed of five large Turkish companies, which later incorporated a company under the name of Türkiye'nin Otomobili Girişim Grubu (TOGG), announced a new project to manufacture a domestic car designed, engineered and manufactured solely in Turkey. In December 2019, TOGG presented prototypes of several passenger electric vehicles. TOGG announced that in the next 15 years, an investment of 22 billion lira will be made to establish a facility that can manufacture 175,000 cars a year. Recently, TOGG has announced the prices for its electric vehicles, and started accepting applications for pre-sales through a lottery for the first batch of vehicles.

In September 2019, Volkswagen incorporated a subsidiary in Turkey for the purpose of setting up a factory in the Manisa province to produce Volkswagen Passat and Škoda Superb models. Volkswagen announced it was expecting to make an investment of around €1.4 billion in this factory. However, in October 2019, due to political reasons relating to Turkey's involvement in the Syria situation, Volkswagen announced that they had frozen the investment plan. In July 2020, Volkswagen announced that because of the pandemic, it has decided to revise its investment plans and terminate its plans for expanding its production facilities. In December 2020, Volkswagen initiated the liquidation process of its Turkish subsidiary. The liquidation has been completed and the Turkish subsidiary has been closed as of September 2021.

The Charging Service Regulation entered into force in April 2022. Per this Regulation, the Turkish Energy Market Regulatory Authority (EMRA) will oversee the establishment and operation of electric vehicle charging stations. According to the Regulation, charging service providers must apply for a licence to EMRA to obtain a charging service provider licence. Over 100 companies have already been granted licences. Although Tesla has not yet started to sell electric vehicles in Turkey, it is among the companies that have obtained the licence. There are currently 3,728 charging stations in Turkey, of which 646 are for fast charging (DC) and 3,082 are for slow charging (AC).

Furthermore, the Union of Chambers of Turkish Engineers and Architects and the Chamber of Electrical Engineers are currently working on a draft regulation setting forth the conditions for the inspection of electric vehicles and charging stations. Additionally, with an amendment in March 2022 to the Regulation on the Technological Products Investment Support Program, investments regarding the establishment of fast charging stations for electric vehicles were included in the support programme. The Ministry of Industry and Technology has granted incentives to 46 projects and will be offering product and machinery support for the establishment of fast charging stations.

These pieces of legislation are clear steps towards the synchronisation of Turkish legislation with technological developments in this area, and an indication that there will be important legal developments in the near future. It is estimated that the number of fully electric

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vehicles actively used in traffic is around 15,000 in Turkey, increasing from approximately 1,700 electric vehicles in 2020. However, to establish and operate a meaningful system of electric vehicle charging stations, vehicle numbers must increase significantly.

In March 2021, Turkish conglomerate Koç Holding and Ford Otosan announced that with an investment of around €2 billion, Ford Otosan plans to establish an integrated production facility to manufacture electric vehicles in Kocaeli. The factory is expected to have a capacity of 650,000 commercial vehicles and a battery installation capacity of 130,000 per year. The factory has not started its operations yet, despite the announcement that it would start its operations in 2022.

The Law on Product Safety and Technical Regulations No. 7223 entered into force in March 2021, and with it the Law on Preparation and Implementation of the Technical Legislation on Products No. 4703 was repealed. Although the most relevant provisions have not changed drastically, the new law has brought requirements for importers and exporters on product liability that holds importers and exporters liable for damages their products may cause to any persons or goods. Furthermore, importers and exporters that supply the market with defective products may face fines of up to 1,518,153 liras.

There is also an ongoing dispute among Turkish scholars regarding the rules to be implemented for autonomous driving and responsibilities of vehicle owners in the event of accidents. Currently, there is no legislation on autonomous vehicles.

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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

According to research by Emirates NBD, the UAE is one of the largest automotive markets in the Gulf, second only to Saudi Arabia. The UAE relies heavily on imports, with nearly all cars being imported from manufacturing facilities abroad. Aside from a small number of

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factories that assemble components for trucks and buses, as well as factories that produce armoured vehicles and boutique high-performance sports cars, there is no significant large-scale, commercial automotive manufacturing activity taking place in the country.

The UAE's strong economic growth, household spending and relatively easy access to vehicle financing are likely to be the primary drivers for the automotive industry over the coming years. As the country's population continues to increase, the growth outlook for the automotive sector looks positive. The International Monetary Fund's World Economic Outlook estimated that the population of the UAE will grow to approximately 10 million between 2021 and 2025. Any increases in public spending on development projects and general infrastructure to support such an increase in population will generally bolster the automotive sector, through demand for trucks and other commercial vehicles required for such growth. Following a dip in new car sales figures of 17.8 per cent between 2015 and 2020, as a result of customers scaling back their spending, the market is forecasted to return to normal levels and, according to a Gulf News article in November 2021, obtaining enough stock to satisfy demand might even become an obstacle.

The impact of the covid-19 pandemic was felt in the UAE, with consumers nervous about discretionary spending and widespread restrictions on physical movement leading to the shuttering of car showrooms temporarily. However, demand did rebound, and automotive industry experts remain cautiously optimistic about the future, citing easing lockdowns, the world-class rollout of vaccines in the UAE and, on a more macro level, further infrastructure spending and economic development as reasons to be hopeful (including Expo Dubai 2020, which was held in October 2021). Nevertheless, the composition of the market for automobiles is changing. An article in the Abu Dhabi-based newspaper *The National* in May 2020 noted that the size of the used car market had surpassed the new car market in the previous 12 months, coming off the back of a decline in the number of new car sales in the previous four years. Data from the Roads and Transport Authority showed that the vehicle fleet of the UAE was getting older in comparison to previous years as consumers hold onto their cars for longer. A report produced by Ken Research predicts growth of 16.6 per cent in terms of revenue in the UAE used car market from 2020 to 2025, citing multiple factors including the covid-19 pandemic leading people to prefer to travel in private vehicles rather than by public transit.

The UAE is also becoming a hub and re-export centre for vehicle parts and components in the Gulf region. Abu Dhabi's government initiative to develop an 'Auto City' in the Mussafah area, southwest of Abu Dhabi, will potentially create a cluster of advanced workshops and service centres, attracting investment in automotive manufacturing and spare part logistics.

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COMMERCIAL OPERATIONS

Regulation

2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

All motor vehicles must be insured and licensed by the specific transport department in each emirate before they can be driven on UAE roads. The process of obtaining insurance and licensing is straightforward and can be dealt with by auto dealers or car owners directly at any transport department outlet. In Dubai, vehicles more than three years old must undergo an RTA safety test prior to each annual registration renewal.

In terms of the regulatory framework, all cars and buses entering the UAE must abide by the safety regulations issued by the Emirates Authority for Standardization and Metrology (ESMA) and the Gulf Standardization Organization (GSO). These regulations are primarily composed of a combination of European Union and US federal motor safety standards. By way of common examples:

- airbags for the driver and front passenger seats are compulsory for all passenger cars and buses with a capacity of up to 22 passengers;
- safety belts and anti-lock braking systems are required in all new cars; and
- all vehicles must have an alarm to notify the driver when the vehicle exceeds the speed of 120km per hour in cars and 100km per hour in buses.

In relation to homologation of new vehicles in the UAE, automotive manufacturers often conduct simulated tests at their factory facilities followed by local testing in the Gulf Cooperation Council (GCC) to confirm that prototypes of new vehicles are fit for driving in GCC countries and meet the standards set by the GSO and ESMA prior to any mass production taking place.

Certain tests are designed in part to ensure that new vehicles are capable of functioning properly during extreme heat conditions that are the norm for GCC countries, for example, between April and October in each year. The vehicle's durability, performance and stability are tested by representatives of the manufacturer driving it off-road and on highways at high speeds. Engines, transmission and other powertrain elements of the vehicle are tested through driving in standard city traffic, with an emphasis on relatively low speeds and frequent stopping and starting. The other vehicle processes such as engine lubrication, electrical systems, braking, steering and air conditioning are all monitored during these tests to ensure that they perform to the required standards of each market. If any of these systems do not perform to the required standards, then the manufacturer's factory is notified to fix minor problems prior to mass production. In the case of substantial problems with prototype vehicles, the prototype will be sent back to the factory for investigation and a new prototype will be developed to undergo the same tests. Otherwise, the prototype is left with the local distributor to increase its mileage and measure wear and tear conditions.

In relation to certification, the automotive manufacturer will normally have a representative that is familiar with ESMA and GSO standards and confirm that the vehicle (or any

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parts) meet the requirements of these organisations. After the self-certification process takes place, the new vehicle's specifications are sent to the GSO for registration of the new vehicle, which is a requirement for customs clearance and further registration of the vehicle by any consumer.

Development, manufacture and supply

3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

The majority of automotive manufacturers operating in the UAE have their regional head offices and logistic distribution centres located in Jebel Ali Free Zone to supply new cars and spare parts to their network of authorised distributors.

The contractual structure of automotive distributors or dealers may vary according to the policies of each manufacturer. However, in general terms, operations are normally governed by dealership agreements covering commercial commitments and targets, in addition to legal terms and conditions in connection with the responsibility and obligations of each party. The lengths of such dealer agreements may vary, typically from one to five years, depending on the relationship between the manufacturer and distributor and any historic performance records in achieving annual commitments and targets.

Automotive manufacturers have historically largely operated in the UAE by appointing local distributors pursuant to UAE Commercial Agency Law No. 18 of 1981 (as amended most recently in December 2022) using local Emirati agents to sell products in the region; there are analogous laws in several other GCC countries. This law has been recently repealed and replaced by Federal Law No. 3 of 2022 (the New Commercial Agency Law) that seeks to improve the balance between principal and agent and will come into force on 15 June 2023. This law reinforces the key aspects of the 1981 law (including the stipulation that only (1) UAE nationals or companies wholly owned by them or (2) public joint-stock companies with at least 51 per cent UAE National shareholding can act as commercial agents), but also allows a foreign principal (not owned in whole or part by a UAE national) to sell its products directly into the UAE without an agent, provided that there is no agent already appointed in the UAE and the principal has not had any agreement previously registered within the UAE.

Distribution

4 | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

Orders for new vehicles and parts are normally processed by the regional offices of the manufacturers. Weekly supplies of vehicles and parts are usually shipped from logistics centres by trailer within the UAE and GCC, and by ship to other destinations in Middle Eastern and North African markets. Monthly stock orders may be shipped from factories abroad directly to importers and distributors in the UAE. The importers and distributors must have trading licences issued by the Ministry of Transport and Logistic Services and

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renewed periodically by local authorities such as the Chamber of Commerce (each emirate has its own local regulatory powers and authorities).

Performance and metrics in relation to customer satisfaction are normally reviewed by automotive manufacturers and their distributors through regular meetings between senior executives from both parties. Any restructuring of a distribution arrangement is normally preceded by warning letters and potentially by arbitration proceedings in accordance with the distribution agreement.

Federal Commercial Agencies Law No. 18 of 1981 can cause significant issues for automotive manufacturers seeking to terminate their relationship with a local distributor. This was the case when a major international automotive manufacturer sought to terminate its distribution relationship in the late 1990s. The manufacturer was unable to terminate the relationship due to restrictions under the Agencies Law. The dispute that arose between the two companies proceeded before the courts of the UAE, and the manufacturer was unable to appoint a new distributor in the UAE until the dispute was resolved. The manufacturer was unable to sell its products in the UAE for several years as a result.

Mergers, acquisitions and joint ventures

5 | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

Manufacturers do not have a significant direct presence in the UAE, electing instead to operate on an agency or distributorship model. Most M&A activity, therefore, tends to occur at the distributor level, rather than the manufacturer level.

Any M&A or joint venture transactions that result in a significant change in the ownership of a distributor should be reported to the Ministry of Economy under its regulations. In addition, distribution agreements often contain change of control provisions that will require the distributor to notify the automotive manufacturer if such a change in ownership were to occur.

Incentives and barriers to entry

6 | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

The main barrier to entry into the market in the UAE is in company setup and licensing, including in relation to premises and importation; it is for these reasons, among others, that international manufacturers use authorised distributors in the UAE. In practice, this means that any new automotive manufacturer entrants into the UAE market will need to identify an appropriate distributor in the region to sell their vehicles and parts to consumers. Recent legal changes have permitted companies in most sectors established in mainland UAE to be 100 per cent owned by foreign nationals, in contrast to the previous requirement that at least 51 per cent of such companies be owned by UAE nationals, and we have not yet seen

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the impact of the legal changes permitting 100 per cent foreign ownership on the automotive industry.

Abu Dhabi's government initiative to develop an 'Auto City' in the Mussafah area is likely to lead to the creation of new production plants for cars, light vehicles and trucks, as well as assembly lines for manufacturing spare parts and vehicle accessories. This strategy could increase opportunities for automotive manufacturers and distributors in the country. More generally, the Dubai Chamber of Commerce has announced the formation of the Automotive Manufacturers Business Group, which will be tasked with developing and advancing Dubai's automotive industry.

PRODUCT SAFETY AND LIABILITY

Safety and environmental

7 | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

There are no specific product recall rules that exclusively apply to the automotive industry in the UAE. The general principles in relation to product recalls and compliance safety are set out below.

Consumer safety and protection are regulated by the Ministry of Economy (MOE). The safety and quality of products are further standardised in the UAE by the Emirates Authority for Standardization and Metrology and local authorities such as the Department of Economic Development, the Dubai Municipality and Abu Dhabi Quality and Conformity Council. Together with the emirate-level authorities, the MOE has the power to investigate and enforce the recall of defective products based on consumer complaints and reports from international markets.

The main law relating to product recall is Federal Law No. 15 of 2020 on consumer protection (the New CP Law), which replaced Federal Law No. 24 of 2006. Executive regulations are due to be published alongside the New CP Law in due course, but until then the executive regulations issued alongside the previous law, Federal Cabinet Resolution No. 12 of 2007, will remain in force (to the extent that they do not contradict the New CP Law). The New CP Law and the current associated regulations state that a supplier of goods must immediately report any harmful defect discovered in the goods to the relevant UAE authorities and consumers. The Cabinet Resolution contains more detailed provisions regarding the notification and other procedures that must be followed by a supplier where a defect is found in goods. In practice, the notification is made to the UAE MOE Consumer Protection Department, and an advertisement of the recall is published in UAE newspapers to notify consumers. The notification to the Consumer Protection Department must be made within 14 days of the commencement of any product recall. It should be in Arabic (but can be accompanied by the home language of the supplier) and it must:

- state the name of the goods, the supplier and the country of origin;
- contain a colour photograph of the goods and the defective part;

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- contain a detailed description of the defect and its causes;
- indicate the number of products sold and the quantity to be recalled;
- suggest the type and nature of probable damage to consumers;
- indicate procedures adopted by the supplier to recall the goods;
- provide the manner of announcing the recall (such as a newspaper advertisement), together with the duration and timing of such announcements;
- provide procedures to be adopted by the supplier in relation to the defective goods; and
- estimate the time frame expected to remedy the defect.

The supplier has a further obligation to notify the Consumer Protection Department with a report within 30 days of initiation of the recall, which must set out the following information:

- the quantity of the goods recalled in the UAE;
- the number of recalled goods either repaired (in which case providing details of the defective parts repaired), replaced or returned for a full refund; and
- the procedures to be adopted to avoid the defect arising, where possible.

The advertisement in local UAE newspapers is also quite prescriptive in that it must not be less than 15cm by 15cm in size and must contain the following information:

- the name and address of the supplier;
- the name of the goods and the country of origin;
- a description of the defect;
- the trademark of the goods;
- instructions that consumers should follow to avoid harm; and
- instructions that consumers should follow to have the goods repaired or replaced or to have the price of the goods refunded.

The responsibility to notify the authorities and consumers lie with both the manufacturer and the distributor, but it is the distributor that will be found liable for failure to notify. Penalties for non-compliance in connection with product recall rules include a fine of a minimum of 1,000 dirhams (with no maximum financial penalty stipulated) and referral to the Public Prosecutor for possible prosecution for commercial fraud, which may result in a prison sentence of up to two years, presumably for the manager of the establishment being prosecuted.

Product liability and recall

- 8** Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

There are no specific product liability laws or regulations that exclusively apply to the automotive industry in the UAE. Below are the general principles that apply in relation to consumer litigation in product liability and product recalls.

A consumer can make a claim against a manufacturer or an importer under the UAE Civil Code if any products are defective and such defects are not covered by a warranty, or if

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the products do not fit their descriptions. Distributors can also be sued for misrepresentation in such cases. Additionally, consumers can bring claims for breach of contract against distributors under the Commercial Transactions Law No. 18 of 1993 if any vehicles are not fit for purpose.

In cases of 'gross cheating', the consumer can have the entire contract with the distributor invalidated. As a general rule, courts in the UAE only award damages for direct losses. Class actions do not yet exist in the UAE, and are unlikely to be introduced in the near future.

When claims are brought by consumers against distributors or importers, vehicle manufacturers may be required under the supply contract to indemnify such parties for the cost of remedying the defects in vehicles or spare parts.

DISPUTES

Competition enforcement

9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

General principles of competition law under UAE Federal Competition Law No. 4 of 2012 are applicable to the automotive industry. For example, geographic division of markets and agreements between competitors to avoid soliciting each other's customers are considered to be anticompetitive. It is therefore unlawful, for example, for automotive distributors to allocate territories between them and agree not to market products in the territories allocated to the other distributor.

Similarly, abuse of a dominant position by a distributor or manufacturer, or any agreements between competitors aimed at reducing competition in the market, such as collusion in bids and tenders or agreements on the terms and conditions for goods and services, will likely be prohibited under the UAE Competition Law.

Consumers who are affected by anticompetitive agreements or conduct can complain to the Competition Regulation Committee at the Ministry of Economy. The potential for follow-on litigation is currently unclear on the basis that it is largely untested, but a finding of anticompetitive behaviour will have a negative impact on the business of both the manufacturer and the distributor, in addition to resulting in potential criminal sanctions and fines ranging between 50,000 and 5 million dirhams for either abusing a dominant position or entering into an agreement that restricts competition in the UAE.

Notwithstanding the information above, the Federal Competition Law No. 4 of 2012 is stated to be subject to further regulations, some of which have not yet been published. The competition law of the UAE has therefore not been completely implemented, and it is uncertain and unclear how the courts will enforce competition law principles in the UAE.

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Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

According to an article published in August 2016, 73 per cent of the disputes related to non-compliance with the terms of sales or service agreements, refunds or defective products, making it the third most complained about sector after services and electronics. The terms and conditions of vehicle warranty, insurance and sales and service agreements constitute most of the disputes. In 2021, according to the Commercial Compliance and Consumer Protection (CCCP) sector in the Department of Economy and Tourism as reported by *Khaleej Times*, the automotive sector dropped to the sixth most common subject of customer complaints in Dubai, after services, electronics, e-commerce, clothing and shipping.

Several manufacturers and distributors are in the process of setting up bilingual customer care counters in their showrooms to comply with the standards set by the Department of Economic Development, to offer solutions and accelerate the customer satisfaction process and resolve disputes with customers prior to the commencement of litigation.

Disputes between automotive manufacturers and their distributors have historically been quite rare in the UAE because of the difficulty a manufacturer would have in terminating such a relationship. Disputes between principals and their registered agents are heard by a specifically constituted Commercial Agencies Committee, which convenes to adjudicate on whether the distributor has fulfilled its duties as an agent and has the power to strike an agency relationship from the register. If the Commercial Agencies Committee is unable to adjudicate the dispute, it has jurisdiction to refer the case to the UAE courts. Under the New Commercial Agency Law, however, parties are allowed to resolve their dispute by arbitration, which provides for more flexibility.

Registered agency relationships can be removed from the register either with the consent of the local agent, or by direction of the Commercial Agencies Committee. It is therefore in the manufacturer's interests to resolve any problems with the distributor amicably as the manufacturer will find the termination process difficult and time-consuming. The New Commercial Agency Law will allow a manufacturer to terminate the distribution agreement prior to the end of its term (or by expiry of the agreed term, without renewal), provided certain conditions are met, which will make it much easier for a manufacturer to change agents. Any purported early termination will be open to challenge by the agent; however, in contrast to the old law (and provided the Minister of Economy approves the arrangement), the automotive manufacturer will be able to sell its products in the UAE via other exclusive channels during the period in which it is in dispute with its extant distributor, rather than experience the sale paralysis of the previous regime.

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Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

In practice, the distributor and the automotive manufacturer may seek to reach an agreement to extend the supply period by offering discounts to the distributor or shipping certain products free of charge to reduce damage caused to the distributor and to avoid complaints from customers.

Ultimately, the parties are reliant upon each other to the extent that neither the automotive manufacturer nor the distributor is capable of selling products in the UAE without the other party's support. It is, therefore, in each of their best interests to support the other party during periods of distress.

Intellectual property disputes

12 | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

Intellectual property disputes between automotive manufacturers tend to commence in international markets and are simply reflected in the UAE, rather than originating in the UAE. Disputes between distributors in the country are rare and have not historically related to intellectual property.

The principal intellectual property issues for automotive manufacturers and distributors in the UAE typically relate to branded counterfeit spare parts being imported or exported by non-authorised distributors and sold to consumers, which can potentially lead to safety concerns in addition to causing losses to the authorised distributors, which sell genuine but often more expensive spare parts.

To resolve this issue, a key consideration for automotive manufacturers and distributors will be how to efficiently implement anti-counterfeiting measures in the UAE. This process is likely to require extensive communication with customs authorities and the police to effectively implement such measures.

EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

Employment law in the UAE is relatively basic compared to other jurisdictions. By way of example, trade unions and works councils are not permitted in the UAE. Employment agreements (with the exception of those for employees within the Dubai International Financial Centre and the Abu Dhabi Global Market, each of which has its own employment regulations)

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must comply with Federal Law No. 33 of 2021 (the New Labour Law) and associated regulations and ministerial decisions. In accordance with the New Labour Law, employment agreements in the UAE are required to be of a fixed duration. Most employment contracts can be terminated on one month's notice unless otherwise agreed between the employer and the employee. On termination of an employment contract, an end of service gratuity may be payable to the employee.

Under the New Labour Law, any employee who has completed at least one year of continuous service is entitled to an end of service gratuity payment that amounts to 21 days' remuneration for each year of service for his or her first five years of service and 30 days' remuneration for each additional year of service, provided that the aggregate amount of the end of service does not exceed two years' remuneration.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

The Emirates Authority for Standardization and Metrology (ESMA) has prepared draft standards applicable to electric and hybrid vehicles being imported into the UAE, and these standards have been provided to the Gulf Standardization Organization (GSO) for consideration as the GSO is also seeking to develop standards in connection with these vehicles. The standards are still in draft form at the time of writing. They address:

- the general requirements as to the performance and safety of electric vehicles;
- the responsibilities of manufacturers;
- the installation of charging ports and electricity supply; and
- how to deal with accidents.

It will be important for cooperation between the GSO and the local standards bodies in each Gulf Cooperation Council (GCC) country (such as the ESMA in the UAE) to ensure that the final standards produced by each authority are aligned and automotive manufacturers are not required to make modifications to vehicles for each of the GCC countries.

It will also be important for these standards to be substantially similar to those used in other significant markets (such as the United States) to incentivise manufacturers to export their electric and hybrid vehicles to GCC countries in mass quantities. Uncertainty in the standards could potentially cause problems in the licensing of such vehicles as well as inconsistency of product quality, therefore frustrating the objectives of standardisation and objective to create a sustainable electric and hybrid market in the UAE.

The Dubai Green Mobility Initiative was established in 2015 by the Supreme Council of Energy as a strategy to achieve sustainable development and to create a low-carbon economy by promoting the use of hybrid cars and electric vehicles in Dubai. In addition, Vision 2021 was launched by His Highness Sheikh Mohammed bin Rashid Al Maktoum, the country's prime minister and the ruler of Dubai. One of the pillars of the Vision 2021 project was to create

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a sustainable environment and infrastructure, measured by a number of key performance indicators. The Vision 2021 site reports that many of the targets were achieved, including an air quality index of 91.4 per cent and a 10.64 per cent share of clean energy contribution.

Shared transportation services continue to be a growing trend in the UAE; car-sharing service Udrive launched in Abu Dhabi in 2018 after finding popularity in Dubai the previous year. Users rely on an app to find cars in their vicinity, which can then be driven to a location and left behind.

Regulations and standards in relation to connected and automated driving vehicles are still under development at the time of writing, but it is expected that the UAE will continue to be progressive with its legal framework to enable such vehicles to enter the country's market. Following the launch of the Dubai Self-driving Transport Strategy in 2016, it is anticipated that 25 per cent of all Dubai's journeys will be self-driving by 2030. Dubai began flight testing the world's first electronic autonomous passenger drones (autonomous air taxis) in 2017, with services planned to launch in 2023. Legislative and operational guidelines continue to be developed and are expected to be the first of their kind worldwide.

UPDATE AND TRENDS

Trends and new legislation

15 Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

There are no updates at this time, except for the potential changes to the foreign direct investment landscape in the UAE due to the removal of 51 per cent local to 49 per cent foreign ownership requirements in many sectors. There may also be changes to the product recall process once the executive regulations in connection with Federal Law No. 15 of 2020 on consumer protection are issued.



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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

The automotive industry is a significant contributor to the UK economy, generating an annual manufacturing turnover of £67 billion in 2021 (an increase on the 2020 figure of £60.2

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billion) and employing 781,800 people in 2021. However, due to the instability of the global economy, production continued to decline in 2022, with 775,014 cars being built in the UK (compared to 859,575 in 2021). In 2021, the UK automotive manufacturing industry invested £3 billion in automotive research and development, displaying the importance of this field to the industry. In 2022, car exports decreased by 14 per cent and only 606,838 cars were shipped worldwide. Notably, 78.3 per cent of total production in the automotive industry in 2022 was exported to more than 150 markets, with over half of those exports to the EU (57.6 per cent), followed by the US (13.3 per cent) and China (8.7 per cent).

In terms of consumer behaviour, 1.61 million new car registrations were recorded in 2022. This was a decrease of 2 per cent from 2021, and a much larger decrease from the 2.3 million new car registrations in 2019. In 2021, 49.3 per cent of new car registrations were fleet registrations and, although there has been a continuing decrease in fleet registrations, it remained the most common sales type in 2021. With an increasing focus on car emissions affecting both climate change and air quality, the demand for electric and hybrid vehicles is ever increasing: in 2022, there were 14,433 registrations of battery electric vehicles, and 13,492 registrations of hybrid electric vehicles. In response, the decline in demand for new diesel cars continues. Consumers are also looking to online marketplaces for competitive deals, and in 2022 more than 6.8 million used cars were sold in the UK; this was down 8.5 per cent from 2021 figures; however, it is likely this decrease was (at least partially) due to supply chain restraints.

Brexit is still creating uncertainty in the UK's automotive industry, particularly as the EU and UK automotive industries have historically been deeply integrated. This trend of integration continues, as illustrated by the export statistics above. The figures demonstrate that the maintenance of trade flows between the UK and the EU will be critical to support the continued success of the UK automotive sector, and the EU-UK Trade and Cooperation Agreement – signed on 30 December 2020, and presented to Parliament in April 2021 – will be central for managing the UK's trade relationship with the EU moving forward.

The figures used above are from the [Society of Motor Manufacturers and Traders](#).

COMMERCIAL OPERATIONS

Regulation

- 2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

Generally, to operate a vehicle on public roads, the vehicle must be registered and type-approved in the UK. The Vehicle Certification Agency (VCA), an executive agency of the Department for Transport, is responsible for issuing vehicle type approvals.

Following Brexit, there are now separate provisions for Great Britain and Northern Ireland as a consequence of the terms of the Northern Ireland Protocol, and Northern Ireland remains subject to EU type-approval regulations. These approvals are known as UK(NI), which distinguishes them from EU member states' approvals. The UK type-approval

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regulations cover both Great Britain and Northern Ireland, but apply differently in each area. On 27 February 2023, the UK government and the European Commission announced that they had (in principle) reached a political agreement to address various concerns raised by the situation in Northern Ireland. This agreement, known as the Windsor Framework, will operate within the Northern Ireland Protocol once it is formally adopted by all parties, and aims to simplify the movement of goods between Great Britain and Northern Ireland. For example, in the area of customs, 'trusted traders' will enjoy a smoother process consisting of reduced customs checks and controls when transporting goods from Great Britain for end use in Northern Ireland. This new trusted trader scheme is expected to be in place by September 2023. The regulations governing type approvals are:

- [the Road Vehicles \(Approval\) Regulations 2020](#) (Statutory Instrument 2020 No. 818 (as amended));
- [the Motorcycles \(Type-Approval\) Regulations 2018](#); and
- [the Agricultural and Forestry Vehicles \(Type-Approval\) Regulations 2018](#).

New type approvals are available for all categories of vehicles under these regulations, in conjunction with:

- retained EU legislation, in the case of UK approvals; or
- directly applicable EU Regulations, in the case of UK(NI) approvals.

When making an application for type approval, a manufacturer's production processes will be subject to a conformity of production assessment. This will ensure that all vehicles are manufactured in accordance with a particular approved specification. Pre-production vehicles will also undergo examinations to ensure that safety and environmental standards are met (including, where appropriate, destructive testing).

Where automobile parts are manufactured or sold separately, generally they must be tested for compliance with the vehicle to which they will be fitted. However, certain component parts can be tested for compliance in isolation (eg, seat belts).

According to the VCA, [the following rules currently apply for vehicle and component type approval in the UK as of 1 January 2021](#):

Existing vehicle and component type approvals

- Vehicle manufacturers need a provisional GB type approval before placing their products on the UK market. EC type approvals will no longer be valid for this purpose, unless the vehicle was in the UK on or before 31 December 2020.
- UK and EU technical standards were aligned on 1 January 2021. As such, the UK will issue provisional GB type approvals, upon application, to manufacturers that can prove they hold valid EC type approvals. This administrative conversion of EC type approvals into UK type approvals avoids costly retesting and redesign for manufacturers, and ensures that products can continue to be sold and registered in the UK.
- The provisional UK type approval will be valid for two years from the date of issue. It must be converted into a full GB type approval during this period, or it will become invalid.
- Until 1 January 2023, a valid EC type approval was acceptable for component, trailer and non-road mobile machinery (no provisional GB type approval was needed).

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- Since January 2021, EC type approvals issued in the UK have not been valid for sales or registrations in the EU market. Manufacturers should, therefore, have a new EC type approval from a type-approval authority in an EU country. This process is set out in [EU Regulation 2019/26](#).

New vehicle and component type approvals

- Manufacturers now need a UK type approval if they intend to place new vehicle models on the UK market. Manufacturers must follow the requirements of the provisional GB type-approval scheme if they intend to get a UK approval on the basis of their EC type approval.
- Manufacturers wishing to place new products on the EU market need to follow the existing procedure for obtaining a new EC type approval. Full testing and certification must be done by an EU type-approval authority and a technical service designated by that authority.

Registration

For use on UK roads or in UK public places, vehicles must be registered with the Driver and Vehicle Licensing Agency (the DVLA) and hold a V5C vehicle registration certificate. The person named on the V5C is responsible for the vehicle as the registered keeper of the vehicle, and has a number of registration and licensing obligations. Without type approval, a vehicle cannot be registered or licensed by a person in the UK. A V5C is not evidence of ownership of the vehicle, and the owner and registered keeper are not always the same.

Insurance

Under current legislation, the UK has a compulsory motor insurance policy, under which a person using a vehicle (or causing or permitting the vehicle to be used on public roads or in a public place in the UK) must have insurance cover against third-party damage, although there are some exceptions for motor traders. For example, if a vehicle is between registered keepers or registered as 'in trade' with the DVLA, it is excluded from continuous insurance enforcement. This contrasts with the EU approach where, generally, the vehicle itself must be insured, not the individual person.

The [Automated and Electric Vehicles Act 2018](#) (AEVA) contains new insurance measures in light of advances in vehicle technology, and came into force on 21 April 2021. In particular, a new form of direct liability has been imposed on the insurer of a self-driving vehicle that causes an accident while driving itself. The single, comprehensive motor insurance framework allows a person who suffers damage in an accident involving a self-driving vehicle with automated mode engaged to have a direct claim against an insurer. Unlike the current third-party motor insurance framework, insured persons in the automated vehicle at the time of the accident will also be covered.

Drivers taking a UK-registered vehicle outside the UK may need to carry a green card depending on the destination country. The green card is an international certificate of insurance currently issued by insurance providers in the UK, guaranteeing that the motorist has the necessary third-party motor insurance cover for travel in the destination country. All UK vehicle insurance provides the minimum third-party cover to drive in the EU, as well as

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other countries including Switzerland, Norway and Iceland. Drivers taking a UK-registered vehicle to an EU or EEA state require valid vehicle insurance, but are not required to carry a green card.

Development, manufacture and supply

3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

As automotive companies are global businesses, arrangements for the UK tend to mirror global or regional arrangements. OEMs generally have a supply chain structure of Tier 1 suppliers (supplying directly to OEMs) and Tier 2 suppliers (supplying to Tier 1 suppliers) and so on. For common parts, OEMs tend to source products pursuant to pan-European arrangements, but also often have specialist local suppliers located in close proximity to manufacturing sites. In the case of the UK, it is not uncommon to see parts move across the border between the UK and the EU multiple times as part of the manufacturing process.

Arrangements with suppliers tend to be pursuant to purchase orders, which are governed by general terms and conditions established by an OEM. Typically, commercial arrangements contemplate that the OEM will place orders for specific components supplied for particular vehicles over the life of a vehicle, but do not necessarily include minimum purchase quantities. Prices are negotiated with respect to each vehicle (often annually), and longer-term agreements may be subject to price adjustment mechanics. Larger suppliers and specialist suppliers for hard-to-source components often have more bespoke arrangements reflecting their bargaining power.

For major OEMs, design and engineering tend to be completed internally, although it is not uncommon to see licensing or collaboration arrangements between OEMs for the use of new technology.

The interconnectedness between UK and EU supply chains for parts and components, as well as finished goods, presents challenges in a post-Brexit world. The EU–UK Trade and Cooperation Agreement (the EU–UK TCA) goes some way to help mitigate these challenges by providing for tariff-free trade for UK and EU originating products under the ‘rules of origin’. However, even for products qualifying for preferential origin under the EU–UK TCA, there are now added steps and costs associated with trading between the UK and the EU (most notably border checks).

Electric vehicles are one of a number of products to benefit from a phase-in period for rules of origin requirements to apply. EVs can benefit from an exemption on the tariff for vehicles manufactured outside the UK or EU until 2026, rather than the tariff being introduced immediately or over a shorter timeframe. However, EV manufacturers in the UK will have to prove that at least 40 per cent of the value of parts in a finished EV that is exported to the EU were produced in the UK or the EU (with no diagonal cumulation). The threshold for this originating content will increase to 50 per cent from 2023 until the end of 2026, and to 55 per cent from the start of 2027. The tariff exemption came about in part because batteries form a large proportion of the value inherent in an EV, and imposing tariffs on imported batteries (which are mainly imported from Asia or the US) would therefore stifle EV trade. The new

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rules of origin requirements further increase the need for domestic UK battery production, which will likely shape the cost-benefit analysis for EV manufacturers with plants in the UK. To maintain its position as an attractive market for manufacturers of EVs, a material increase in the UK's domestic production of batteries will be required; this goal suffered a blow when Britishvolt, which had planned a gigafactory in Northumberland, went into administration in early 2023.

Distribution

4 | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

In the UK, new vehicles are sold through selective distribution networks, usually in the form of car dealerships. As such, manufacturers can control branding and sales processes, including aftersales relations. Owing to the nature of selective distribution networks, manufacturers can sell directly to consumer or fleet companies, but generally not to other dealerships outside their selected network.

Competition law imposes particular requirements on selective distribution networks, especially with regard to the criteria for being an authorised dealer, and restrictions on trading within or outside the authorised network. Following Brexit, UK competition rules are of primary relevance for businesses operating in the UK or importing into the UK, and EU competition rules remain relevant for UK-based exporters into the EU. Both the EU and UK rules on vertical arrangements have been revised within the last year, with some divergence now that the UK is no longer part of the EU. However, the rules applicable to selective distribution arrangements remain largely aligned and unchanged between the two regimes.

Relationships between manufacturers and approved dealerships in practice tend to be long-term arrangements (although typically they will be subject to termination on two years' notice), and the dealership will usually undertake warranty repairs as well as general vehicle sales services. Vehicle financing is increasingly common in the UK and takes a variety of forms, from manufacturers offering dealer financing for the dealership's purchase of vehicles for onward sale, to consumer car financing for purchase of new vehicles by individual consumers.

Fundamental issues across the distribution network (such as changes to a standard dealership contract) are usually handled by the manufacturer dealer association, while localised issues with a specific dealer are addressed on an individual basis. In recent years, there has been a consolidation of dealerships, creating larger dealers who have greater individual negotiating power outside a dealer association.

The UK's Motor Ombudsman (an automotive dispute resolution body) self-regulates the UK's motor industry through a number of Codes of Practice approved by the Chartered Trading Standards Institute. The Codes of Practice cover accreditations for vehicle manufacturers, warranty product providers, franchised dealers and independent garages. While voluntary, compliance with relevant codes is frequently an obligation in contractual arrangements between manufacturers and dealerships or garages.

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Traditional distribution models are, however, starting to be challenged by the development of alternative forms of access to vehicles, such as car subscription and car sharing schemes. This is an area that OEMs are exploring to be able to sell directly to consumers, and subsequently bypassing dealerships.

This is supported by consumers' increasing confidence in buying or hiring online, without using the traditional car showroom.

Mergers, acquisitions and joint ventures

5 | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

At the time of writing, there are no issues particular to the UK automotive industry that need to be considered in the negotiation of an M&A transaction. However, the covid-19 pandemic and semiconductor shortage have caused supply chain disruption, driven up costs and impacted manufacturing and global demand for new vehicles. For this reason, the number of M&As, joint ventures and strategic partnerships are expected to increase for companies requiring new capability (as with electrical vehicles) in a short amount of time or needing to maintain their market position. In addition, over time there may be increased divergence between the EU and UK legal regimes that could impact M&A transactions, for example, with respect to competition law.

Incentives and barriers to entry

6 | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

There are a number of significant UK tax incentives that apply to the automotive sector (although not exclusively) to encourage investment in capital and research-intensive activities, and in specific geographical locations.

As introduced in the Spring Budget on 15 March 2023, from 1 April 2023 to 31 March 2026, companies can benefit from 'full expensing' on qualifying capital expenditure on 'main rate' plant and machinery, which allows a 100 per cent deduction of the cost of permitted plant and machinery from profits before tax in the year it was incurred. For qualifying expenditure on 'special rate' plant and machinery, a 50 per cent first-year allowance is available with the balance being deducted at 6 per cent a year on a writing down basis. Disposals of plant and machinery for which 'full expensing' or a 50 per cent first-year allowance has been claimed are subject to immediate balancing charges. While these new rules are currently only in place until 31 March 2026, the government has indicated an intention to make them permanent. The existing writing down allowances (at 18 per cent for 'main rate' expenditure and at 6 per cent for 'special rate' expenditure) will continue to apply where the new rules do not.

Furthermore, the UK government has granted the following areas freeport status: East Midlands Airport, Felixstowe and Harwich, Humber, Liverpool City Region, Plymouth and South Devon, Solent, Teesside and Thames. In December 2022, Plymouth, Solent and

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Teesside became the first operational freeports. Two sites have also been confirmed for freeports in Scotland (Forth Green and the Inverness and Cromarty Firth), and a site in Wales is expected to be confirmed in early spring 2023. In addition to some freeports being (1) a customs duty and import VAT-free zone (until the goods enter the UK market); (2) benefitting from preferential treatment in respect of employer National Insurance contributions; and (3) simplified planning processes, freeports are expected to benefit until 30 September 2026 from:

- an increased (10 per cent instead of the usual 3 per cent) rate of Structures and Buildings Allowance on constructing or renovating non-residential structures and buildings;
- enhanced capital allowance of 100 per cent for companies investing in plant and machinery for use in the freeport. Unlike the 'super deduction', the enhanced allowance applies to both main and special rate assets;
- full relief against stamp duty land tax on the acquisition of land or property purchased and used within the freeport for a qualifying commercial purpose; and
- full business rates relief on qualifying new properties and partial relief for expanded properties within the freeport sites.

In addition, in the Spring Budget 2023, the UK government confirmed its intention to create 12 'investment zones' with 'special tax sites'. This concept is an iteration of the above freeports concept. While the detailed legislation is yet to be drafted, the benefits afforded will be similar to those afforded to freeports (noting that only freeports shall enjoy the special customs status).

Other tax incentives applicable to the automotive sector include research and development (R&D) expenditure credit and R&D tax relief, to support companies that work on innovative projects in science and technology. Both incentives are available for large companies to reduce their taxable profits if they carry out qualifying R&D work. The Spring Budget 2023 also introduced a new enhanced R&D tax credit payable at 14.5 per cent to loss making SMEs whose R&D expenditure makes up at least 40 per cent of their total expenditure for an accounting period. On 13 January 2023, the government published a consultation paper proposing to merge R&D expenditure credit and R&D tax relief into one scheme – which would apply both to SMEs and large companies – from 1 April 2024, with the aim to simplify the tax system and prevent fraud. This consultation concluded on 13 March 2023 and the results will be announced in due course.

Where intellectual property is developed and exploited, a preferential Patent Box regime might apply. Although it has been amended to bring it into line with Organisation for Economic Co-operation and Development multinational requirements, the Patent Box offers an optional lower rate of corporation tax on eligible profits attributable to intellectual property. At the time of writing, the optional rate is 10 per cent.

Demand-side tax advantages are also available for ultra-low emission vehicles, to support demand in this sector. Fully electric, zero-emission cars are exempt from Vehicle Excise Duty or road tax, and also benefit from a plug-in grant of up to £1,500, deducted from the cost of a new EV. The UK government has also committed to significant expenditure to support ultra-low emission vehicles (including in developing charging infrastructure), renewable fuels and connected and autonomous vehicles through the National Productivity Investment Fund.

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While a number of incumbent OEMs are embedded in the UK market, new challengers are continuing to disrupt the UK market, from technology companies to mobility service providers. With the rise of self-driving vehicles, EVs and alternatively fuelled vehicles, we expect this trend will continue. The current state of flux of the UK automotive sector is exemplified by the recent collapse of Britishvolt and the upcoming announcements of possible investments in battery and EV manufacturing by Jaguar Land Rover and Nissan, respectively. Online purchases have already challenged traditional dealerships in the UK, as consumers spend more time researching and analysing information online. In response, many dealerships and retailers have adopted digital strategies to ensure consistency between online and offline consumer experiences.

PRODUCT SAFETY AND LIABILITY

Safety and environmental

7 | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

The UK regime for the type approval of vehicles is set out in the UK Framework Regulation ([Regulation \(EU\) 2018/858 of the European Parliament and of the Council of 30 May 2018 on the approval and market surveillance of motor vehicles and their trailers, and of systems, components and separate technical units intended for such vehicles, amending Regulations \(EC\) No. 715/2007 and \(EC\) No. 595/2009 and repealing Directive 2007/46/EC \(Text with EEA relevance\)](#)) and the [Road Vehicles \(Approval\) Regulations 2020](#) (SI 2020/818).

The UK Framework Regulation prescribes a series of technical standards (including requirements relating to vehicle emissions) for road vehicles and their component parts, systems and separate technical units intended for such vehicles, which must be met before type approval can be obtained. The UK type-approval authority has powers to withdraw or suspend type approvals where vehicles are found not to conform to the approved type, or where the vehicle is found to present a serious risk to health, safety, the environment or other public interests. It can also refuse to recognise type approvals where it finds that a type approval does not comply with the UK Framework Regulation.

Product recalls and other corrective actions are an important concern for the automotive industry in the UK. The competent authority, the Driver and Vehicle Standards Agency, is an active regulator, and manufacturers carrying out corrective actions are often subject to ongoing reporting obligations. Recalls can be required under the [General Product Safety Regulations 2005](#) (where the product is unsafe or dangerous) or under the UK Framework Regulation (where the recall is due to a non-conformity with the Regulation, including emissions requirements, or a serious risk to the health or safety of persons, the environment or other aspects of the protection of public interests). UK authorities have also published a Code of Practice on vehicle safety defects and recalls and a manufacturer's guide to recalls in the automotive sector, which (while not strictly mandatory) are generally regarded as authoritative. A separate Code of Practice, and a guide, exist for recalls in the vehicle aftermarket.

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Despite the UK's withdrawal from the EU, UK authorities continue to work closely with EU member state authorities in relation to type approvals and recalls. The UK Framework Regulation continues to require UK authorities to make notifications to other member states and to the European Commission (all references to member states in the UK Framework Regulation are defined to include the UK). The scope of the UK's continued cooperation with EU authorities on safety and standards is set out in the Annex on Motor Vehicles to the EU-UK Trade and Cooperation Agreement.

Once a vehicle has been authorised for use on public roads in the UK, drivers must also comply with various vehicle safety provisions to ensure that the vehicle is operated in a manner that does not pose a danger to the general public (including the requirement for a driver to always be in a position to have full control of the vehicle, a full view of the road and traffic ahead, and a motor vehicle to be attended by a person who is licensed to drive it unless the engine is switched off and the parking brake is applied). Most vehicles are required to pass a Department for Transport test of vehicle safety, roadworthiness and emissions on a regular basis.

Product liability and recall

- 8** Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

Product liability cases in the UK automotive industry are generally brought by consumers under the [Consumer Protection Act 1987](#), which implemented the [EU Product Liability Directive 85/374/EEC](#).

Group litigation is also highly relevant and topical for the automotive industry, particularly in the context of consumer claims in respect of diesel vehicles that are alleged to have 'defeat devices'. Claims have been brought and are ongoing against a number of manufacturers, dealers and automotive finance companies.

The UK has an opt-in collective actions system for product litigation (rather than a US-style opt-out class action) and punitive damages are not available. However, group actions are still a considerable threat (and claimant firms are very active in the automotive sector, particularly around diesel emissions claims and other product claims), so companies operating in the sector should be aware of this risk.

Developments in the automotive industry, such as the increasing prominence of hybrid, electric and connected vehicles, and the emergence of autonomous driving systems, will also impact the liability landscape in the UK.

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DISPUTES

Competition enforcement

9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

Following Brexit, distribution systems in the UK automotive industry are governed by the [Vertical Agreements Block Exemption Order](#), which came into force on 1 June 2022. However, this block exemption does not cover agreements relating to the purchase, sale or resale of spare parts for motor vehicles, or the provision of repair and maintenance services for motor vehicles, as these activities are covered by a separate block exemption, which came into force on 1 June 2010 and has been retained in UK law post-Brexit (the [Motor Vehicle Block Exemption Regulation \(461/2010/EU\)](#)).

The Motor Vehicle Block Exemption Regulation is up for renewal or reform on its expiry on 31 May 2023, presenting an obvious point at which the UK may adopt a different approach from the EU. The UK's Competition and Markets Authority (CMA) carried out a consultation and, in October 2022, recommended to the UK government that the retained Regulation be replaced on expiry with a UK Motor Vehicle Block Exemption Order, updated to reflect market developments.

In recent times, the CMA has imposed significant fines on an OEM and five of its commercial vehicles dealers for anticompetitive behaviour, including market sharing, price coordination and the exchange of commercially sensitive information. Following this, the authority issued an open letter to the motor industry warning against unlawful contact between competitors.

The CMA and, separately, the European Commission have also launched investigations into suspected anticompetitive behaviour in the recycling of end-of-life vehicles.

In addition, the [Supply of New Cars Order 2000](#) (as amended) prevents new car suppliers from:

- discriminating on price between dealers and fleet buyers;
- providing bonuses and discounts to dealers on pre-registered cars; and
- imposing restrictions on price advertising on dealers.

The UK is currently a popular forum for private follow-on damages actions based on competition authorities' infringement decisions, including in the automotive sector. For example, there was recently a claim for damages before the UK Competition Appeal Tribunal (which is a specialist judicial body with cross-disciplinary expertise in law, economics, business and accountancy, that hears and decides cases involving competition or economic regulatory issues) against automotive bearings suppliers.

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Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

The most common disputes in the automotive industry are supply chain disputes and disputes with dealers. These are usually settled out of court. The most common forum for resolving disputes with dealers and suppliers located in the UK is the English courts. The English courts have power to grant interim relief, including injunctions to compel performance. Where disputes concern international suppliers or joint ventures, it is common for the relevant contracts or joint venture agreements to provide for such disputes to be resolved through arbitration. Where arbitrations are seated in England and Wales, the English courts have the power to grant interim relief, including injunctions, in cases of urgency when the arbitral tribunal is unable to act.

There has also been an increasing number of technology licensing disputes as more technology companies enter the market.

There are procedures for group litigation in the UK, and there is the potential for increased use of these procedures for collective redress, particularly in relation to claims by groups of consumers or distributors, or both.

Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

OEMs and their suppliers enter into long-term and highly symbiotic relationships. Tier 1 suppliers contract directly with the relevant OEM. Tier 2 suppliers' contractual relationships lie with the Tier 1 suppliers. In some cases, there will be additional links in the chain (for example, Tier 3 suppliers contracting with the Tier 2 suppliers, and so on). These relationships are complex and interdependent on account of the high level of investment needed in new car models. Additionally, car models may be in production for a decade or more. Every model invariably requires bespoke tooling even though some aspects (for example, vehicle platforms) may be common among a number of models.

OEMs and their suppliers usually work together on the development of new models and their respective key components. Tooling and car parts are very often difficult to transfer between particular models and the supplier market. The result is that, if a supplier encounters financial difficulty, it may take an OEM months (and occasionally a year or more) to re-tool and re-source from one supplier to another.

Production interruptions or delays may cause an OEM (and other supply chain members) daily and weekly losses wholly out of proportion to the financial worth or turnover of an individual distressed supplier. Those losses can quickly and easily run into significant sums of money. For that reason, major OEMs manage supply relationships closely. Where possible, they will dual-source (and on occasion even multi-source) components. In all cases, OEMs are likely to monitor the creditworthiness and ongoing financial viability of suppliers. OEMs'

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terms and conditions almost invariably lay down approval procedures where suppliers change hands or, on a worst-case basis, encounter financial difficulties. Where problems arise, OEMs are therefore often willing to provide ongoing finance to suppliers, negotiating priority arrangements with their bankers or other creditors. Such negotiations are likely to be combined with rights of access and inspection. In our experience, OEMs tend to seek to secure access to intellectual property rights and the ability to remove tooling and finished parts, where a supplier gets into financial difficulty.

The relationship between the OEM's rights and insolvency practitioners can also be complex. Where a supplier goes into liquidation or administration, the supplier's administrator or liquidator will always seek to maximise recoveries from key OEM clients. In our experience, OEMs are frequently willing to fund production during an administration or liquidation in exchange for rights of inspection and the ability to influence (as a means of securing ongoing production) the identity of the purchaser of the business or assets of an insolvent supplier.

Intellectual property disputes

12 | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

Intellectual property disputes are significant in the automotive industry, and we anticipate this area of litigation to grow as technology from diversified fields is incorporated into vehicles.

IP disputes arise in the automotive industry in a variety of contexts. Automotive manufacturers have previously brought proceedings for infringement of the design rights they hold over the appearance of their parts. These disputes typically occur between two parties within the automotive industry. A well-known example is in the context of car wheels, where the European Court of Justice (ECJ) held that the manufacture and sale of replica car wheels by a third party was permissible in certain circumstances, where the products are visually identical and the purpose is for repairs.

Patent disputes in the automotive industry are also expected to become more commonplace owing to the increasing connectivity incorporated into vehicles, which in turn has caught the attention of (commonly litigious) patentholders of cellular telecommunications patents. Unlike designs disputes, this will bring parties from different industries together in court. Patent litigation of cellular patents necessary to operate certain cellular standards (such as 4G or 5G, and known as standard essential patents (SEPs)) is already very common for mobile phone manufacturers. As vehicles begin to incorporate the same technology, the owners of large SEP portfolios are now approaching manufacturers for substantial licensing royalties to use their technology. Where licence fees cannot be agreed, litigation (and with it the risk of an injunction preventing the use of the standard) can follow. A well-known example was between Nokia and Daimler, although this case resulted in settlement.

As to how well-protected IP is, and how easy it is to resolve disputes, it is too early to reach a definitive conclusion. Design manufacturers may have been disappointed by the decision of the ECJ to permit the sale of replica components that do not contribute to a technical function of a vehicle under repair exemptions. As to how easy it will be to resolve disputes:

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SEP litigation, for example, can be complicated and expensive, and if history from mobile phone company disputes teaches us anything, they can last for several years and require multiple trials to determine different issues. Conclusion of licensing agreements is not always straightforward, given the high royalty fees SEP holders can command, many of whom are non-practising entities that have acquired their patents from other companies (commonly referred to as 'patent trolls').

EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

There are no specific automotive sector employment regulations or laws in the UK. All basic UK employment laws and regulations essentially apply to employers in every industry or sector. Although the UK is arguably one of the larger economies when compared with the economies of the EU member states, it is the jurisdiction with the lightest-touch employment laws. The UK still has far more employee-friendly legislation, for example, when compared to the US.

The automotive sector is heavily unionised. The trade unions are strong, and usually represent a significant part of the workforce. There can often be more than one trade union recognised by a company. In the UK, there are no national, sector-specific or employer-association negotiated collective bargaining agreements (CBAs) of general application. Locally negotiated CBAs may apply within particular unionised UK employers. These are commonplace in the automotive sector.

A CBA will usually cover certain groups of employees, or bargaining units, at the workplace. In the automotive industry, a CBA typically covers, among other things, remuneration, working time (including overtime and overtime payments), disputes in the workplace (such as disciplinary matters) and security of employment. It is not uncommon to see restrictions regarding compulsory redundancies and agreed enhanced redundancy payments.

In addition to UK trade unions, large employers in the automotive industry are often part of multinational groups with EU works councils. This creates different levels of information and consultation obligations about issues affecting not just the UK workforce, but also those in other EU jurisdictions. Post-Brexit, whether UK employees continue to participate in EU works councils will depend on the wording of the relevant agreement, and any agreement reached between the employer and employee representatives.

Strong trade union presence can be coupled with political interest (and sometimes pressure) when there are perceived, and actual, threats to jobs.

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NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

Electric vehicles

The UK government is under increasing pressure to put in place measures to reduce air pollution, including pollution caused by vehicles. In response to this pressure, and in connection with the UK government's wider climate change strategy, the government intends to ban all sales of new petrol and diesel cars by 2030. The sale of some hybrid cars and vans will continue until 2035. Various respondents to the government's consultation on the ban felt that the revised date was unfeasible, but the government's view is that setting a clear and accelerated target would act to stimulate industry development.

Data published by the Society of Motor Manufacturers and Traders shows that, for the first time, there were more electric car sales than diesel sales in 2022. Although, with the energy crisis continuing in to 2023, the gap between the cost of petrol and the cost of running an EV is narrowing.

The development of charging infrastructure across the UK is a particular focus for the government given rapidly increasing demand for EVs. The Automated and Electric Vehicles Act 2018 (AEVA) granted the Secretary of State powers to implement secondary legislation to improve the infrastructure in place for EVs (including to ensure provision of EV charging points at key strategic locations, such as motorway service areas and large fuel retailers), and require that charging points have 'smart' capability.

Various grant schemes exist to promote the development of this infrastructure, both through rapid chargers and on-street connections (eg, lamp posts) for charging of vehicles at home. Additionally, recently the UK government has come under pressure to cut the 20 per cent VAT chargeable on electricity supplied by public charge points (which is considerably higher than the 5 per cent VAT chargeable on domestic electricity).

Autonomous vehicles

The emergence of autonomous vehicles presents a number of critical legal challenges for the UK government, car manufacturers and drivers.

At present, the majority of road traffic laws in the UK assume that a vehicle will be controlled by a human driver who is engaged at all times and remains ready to resume control of the vehicle. One of the challenges – being insurance – was addressed in the AEVA. But questions remain of how to allocate liability, which was one of the focuses of a joint report published by the Law Commission of England and Wales and the Scottish Law Commission. This was taken forward by the government in August 2022 through the announcement of a report setting out its vision for Connected and Automated Mobility (CAM), which it hopes will materialise by 2025. The government has explained the first pillar of CAM is creation of a comprehensive set of policies and regulations to enable safe development and deployment

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of automated vehicles in the UK. The government has committed to dedicating £60 million towards research and development in this field. The CAM report also recognises that there will be varying levels of automation developed incrementally over a number of years; the report therefore proposes a regime that will authorise individual automation features, rather than catering only for whole-vehicle automation.

Another challenge involves the collection and use of personal data. Collection and use of data through sensors and cameras in cars (to enable vehicles to make their own hypothetical driving decisions) is necessary for the development of autonomous vehicles. However, gaining consent for collection and use of that data, or relying on another legal basis, is a major challenge facing the car industry. The UK data protection regime includes a range of obligations that apply to any data collected from vehicles that can be linked to an identifiable living person. When designing vehicles, automotive manufacturers must abide by the principle of 'privacy by design and by default', which requires that privacy issues be addressed throughout the design process. The Law Commissions' report recommends that the regulator for automated vehicles should have responsibility for regulation relating to cybersecurity and data privacy.

UPDATE AND TRENDS

Trends and new legislation

15 Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

SMMT action plan

The unstable political climate in 2022 contributed to the continuing decline in UK production of, and demand for, automotive vehicles (which was initially triggered by the impact of Brexit and the covid-19 pandemic). This was exacerbated by the impact of rising energy costs on consumer confidence. As such, the Society of Motor Manufacturers and Traders (SMMT) has called for an urgent action plan, emphasising that the industry is estimated to contribute £14 billion of growth towards the UK's economic recovery in 2023. SMMT's action plan suggests various government-backed initiatives, including:

- support for energy costs available to cash-flow constrained SMEs;
- more lenient business rates to incentivise investment; and
- Apprenticeship Levy reforms.

At the date of this article, the SMMT is corresponding with the government to ensure continued profitability and flexibility within the automotive industry.

M&A

Due to changing demands (most notably the push for electric vehicles), an increased use of software in vehicles and requirements of decarbonisation throughout the supply chain,

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many automakers are seeking M&A solutions (particularly through joint ventures and other partnerships) to gain access to new and developing technologies.

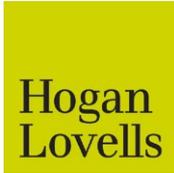
Changes to the Highway Code

The Highway Code has been updated to include new rules to protect the most vulnerable road users. The new rules create safer roads for cyclists by introducing a Hierarchy of Users, which places high-risk road users at the top of the hierarchy. Furthermore, the new Highway Code places responsibility on cyclists cycling in shared spaces, prioritising the safety of pedestrians. Other additions include rules as to the positioning of cyclists on roads, overtaking, passing stationary traffic and cycling in junctions. However, these do not pose significant changes to the UK road safety landscape.

CAM

The introduction of the government's Connected and Automated Mobility proposals will be more extensive than the Automated and Electric Vehicles Act 2018, and will require additional primary legislation. A draft of this legislation is expected in the coming year.

* *The authors gratefully acknowledge the assistance of Jo Broadbent, Margaret Kemp, Penelope Thornton, Lookman Rawat, Juliette Parkinson, James Gray, Gaspare Chirillo, Abraham Warraich, Simi Malhi and Celine Al Asadi in writing this chapter.*



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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

The US automotive industry is massive. The US auto market is the world's second largest by number of vehicles produced. Over 250 million vehicles populate US roads.

Covid-19 delivered a vigorous economic shock to the US auto industry as it did on a global basis. Russia's war on Ukraine delivered another shock by extending challenges with supply lines. New vehicle sales that were around 17 million for each of the few years before the pandemic dropped precipitously. In 2022, light duty vehicle sales were around 13.75 million units. While sales volumes were lower than any year since 2011, automakers did well at improving profitability. As supply lines are expected to improve, greater production capacity and vehicle availability to consumers are expected. There is much discussion of manufacturers seeking to 'maintain discipline' to focus more on profitability than market share. The range of issues and challenges involved on a global scale make reliable predictions on sales and profitability difficult this year.

Given the magnitude of the US automotive industry, it has obvious significance to the US economy as a whole and that is not expected to change. The industry's share of US GDP is often estimated to range between 3 and 3.5 per cent. Approximately 1.5 million people are directly employed in the industry. Projections indicate that around 7.25 million US jobs – about 3.8 per cent of total private sector employment – are to some extent dependent on the auto industry.

The scale needed to cost-effectively produce vehicles is large and resource intensive. Major suppliers often locate facilities near OEM plants and manufacturing hubs of substantial size tend to develop. As a result, the industry is typically an engine for local and regional economies where major production plants are located.

The impact of the industry extends to nearly every community in the nation as a host of businesses are required to sell new and used vehicles and to maintain and fuel those vehicles already on the road.

The transition to electric vehicles (EVs) is significantly impacting the US market with government policy being the primary driver of the pace at which manufacturers are expected to shift production to EVs. Emissions stringency is increasing dramatically, and these rules effectively force a very rapid transition to EVs, even though EVs are not specifically mandated by US emission rules. A quest to address global climate change is far from the only motivating factor for this policy stance, geopolitical concerns are also a primary concern. Geopolitical competition between the United States and China continues to accelerate, while cross-border trade volume still hits new records. As the United States seeks to reindustrialise, auto production – especially EV batteries and related supply lines – is deemed by both nations as a critical industry. President Biden's Administration is using a 'whole of government' approach to encourage this transformation. Legislation passed in 2022 marks

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a fulsome entry by the United States into industrial policy that seeks to significantly transform various industries in the country, among them, the automotive market.

COMMERCIAL OPERATIONS

Regulation

- 2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

In the United States, new automobiles must be certified to both emissions and safety standards.

Emissions certifications are granted by the US Environmental Protection Agency (EPA) on an annual basis for all models sold in a given model year. The emissions certification is based on an application submitted by the manufacturer to EPA and supporting emissions test results. The state of California has developed its own emissions certification and enforcement programme for new vehicles sold in the state, which requires the submission of a separate application and test results to the California Air Resources Board (CARB). In recent years, a number of states, representing nearly one-third of vehicle sales, have adopted the California emissions programme, which historically has imposed more stringent emissions standards for certain pollutants including greenhouse gases as well as targets for zero-emission vehicles. New automobiles can only be sold in the United States after the receipt of certificates of conformity from EPA or approving executive orders from CARB.

In the United States, safety certification is done by the manufacturer through a self-certification system. In this system, the National Highway Traffic Safety Administration (NHTSA) sets performance-based safety standards for a wide range of vehicle functions (from occupant crash protection to headlight performance), and manufacturers are required to self-certify, under penalty of law, that the vehicle meets all of the federal safety standards. Falsely certifying a vehicle subjects the manufacturer to substantial civil penalties and mandatory recalls at the manufacturer's expense for any and all non-compliances with safety standards. In addition to self-certification to safety standards, manufacturers are required to recall vehicles at no cost to the customer where defects that cause an unreasonable risk to motor vehicle safety are identified by either the manufacturer or NHTSA.

Development, manufacture and supply

- 3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

Globally and in the United States, the commercial terms with respect to distribution and supply arrangements for production and non-production parts and components tend to vary depending on whether the transaction involves an OEM or aftermarket customer.

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For OEMs, products generally are supplied through purchase orders that are governed by terms and conditions established by an OEM. Typically, commercial arrangements contemplate that an OEM will place orders for specific parts and components supplied for particular vehicles over the life of the vehicle, but do not include minimum purchase commitments. Prices are commonly negotiated with respect to each vehicle but may be subject to adjustment for various reasons, including commodity or foreign exchange escalation or de-escalation clauses and cost reductions achieved because of productivity improvements. Individual purchase orders are terminable for cause or non-performance and, in most cases, upon the supplier's insolvency and certain change of control events.

Suppliers manufacture and ship parts and components based on OEM customer release schedules, normally provided on a weekly basis, subject to variance based on cyclical automobile production or dealer inventory levels. Suppliers generally ship directly from a manufacturing location to the customer for use in vehicle production and assembly.

The OEM's general terms and conditions for purchase will cover issues such as intellectual property, technical information and data licences and access; compliance with law obligations; environmental, social and governance commitments; payment provisions and audit rights; indemnification obligations; warranty and recall terms; and other customary terms.

Distribution

4 | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

The US legal environment is a challenging one for manufacturers and distributors. The distribution of motor vehicles is principally governed by 50 different state franchise protection statutes. Of the 50 states, 46 expressly prohibit most OEMs from selling vehicles directly to retail consumers, and the remaining four place potentially onerous restrictions on direct sales. Notably, however, a growing number of states are granting statutory exceptions to new market entrants that do not have existing dealer networks and only sell electric vehicles (EVs). Several of these states extend exceptions only to select OEMs with existing sales and service operations in the state. At the request of dealer groups, other states are pursuing legislation to strengthen prohibitions and prevent competition to dealers from new brands with direct-to-consumer distribution models. Accordingly, vehicles are generally distributed to retail customers by independent dealers, with the exception of EV-only OEMs such as Tesla. While, as noted, the relationship between OEMs and their dealers is governed by statutes that vary from state to state, those statutes include some common elements. Chief among them are the following.

- The statutes are intended to redress an alleged 'imbalance in bargaining power' between 'large' manufacturers and 'small' retail dealers. As a result, each statute offers significant protection to the latter as against the former.
- Initially, the principal form of protection was against 'unreasonable' terminations and various forms of manufacturer 'coercion' (eg, against requiring dealers to accept product not ordered and not wanted).

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- Most statutes have been amended multiple times over the years to add a host of additional protections and requirements. Among these are protections against ‘unreasonable’ refusals to recognise proposed transfers; restrictions on ‘add-points’ (ie, the addition of new dealer locations); regulations governing incentive programmes; regulations governing certain kinds of facility standards (eg, chiefly restrictions on the ability of manufacturers to insist that dealers sell exclusively one make of vehicle from a dealership location); mandates that franchisors pay ‘retail’ rates and prices for labour and parts used in warranty repairs; protection against unfair allocation of products; and restrictions on a franchisor’s right to modify its standard form of dealer agreement.
- In addition to passing laws that are highly favourable to franchisees, many states have special administrative agencies (dealer boards) to enforce the statutes and to hear and decide disputes between manufacturers and dealers.

Due to the substantial protections granted to dealers by these state laws, it is very difficult to terminate a dealer for poor performance and for most breaches of the franchise agreement. Dealers usually contest manufacturer attempts to terminate; the statutes provide for an ‘automatic stay’ of termination until the termination protest is fully litigated; and termination litigation can take years to complete. Restructuring a dealer network is extremely expensive. A manufacturer’s need to restructure does not constitute good cause to terminate a dealer or to require a dealer to relocate under most state statutes, and, consequently, substantial settlement payments must typically be made to dealers to effectuate a restructuring.

Mergers, acquisitions and joint ventures

5 | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

The US automotive industry has traditionally been highly regulated and increasingly so in recent years because of surges in disruptive technology and innovation driving change, as well as governmental policies such as the Inflation Reduction Act (IRA) designed to encourage domestic investment and sourcing for critical technologies. Consequently, US automotive industry participants must carefully consider national, state and local legal requirements as strategic plans are formulated. While traditional automotive M&A and joint venture transactions involve due diligence and structuring issues with respect to competition, safety and environmental matters, the advent and adoption of ACES – vehicles that are automated, connected, electric and shared – and related technologies, as well as a competitive and dynamic environment for supply and sourcing those technologies, have resulted in new and expanded regulatory and business frameworks.

Technology-driven investments, new product entrants and growth in partnerships among industry participants (including between competitors), fuelled largely by a shift toward ACES and away from established supply chain sourcing practices, continue to challenge and reshape traditional US automotive industry models. OEMs and suppliers alike seek to transform their technological capabilities and manage risk associated with supply chain disruption (including the supply and sourcing of battery components) from the fallout of the Covid-19 pandemic and governmental priorities for technologies deemed critical, through a variety of legal arrangements including licences, investments, direct-supply arrangements, partnerships and full acquisitions of technology-focused companies and talent. While

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emerging technologies, evolving business models and governmental incentives provide deal-making opportunities globally, the United States is uniquely positioned as a home to traditional automotive industry participants such as the Big Three OEMs in Detroit, centres of innovation and new market entrants such as Silicon Valley, and investment incentives under well-funded IRA programmes to support strategic developments. Furthermore, the disruptive forces of new technology add additional complexities in the transaction context within the United States, given that regulatory regimes developed over many decades need to be flexible to take new changes into account.

As an example of the evolving regulatory environment, while government regulation of autonomous vehicles remains a work in process, there is surging interest and investment in the application of autonomous vehicle technology, including to support supply chain logistics and specifically in last-mile delivery as the most expensive and time-consuming portion of deliveries to consumers. Consequently, from a transaction perspective, potential investors in targets developing and utilising autonomous vehicle technology must develop a sophisticated understanding (and diligence) of the current federal and state regulatory environment as well as the target's compliance plans.

Incentives and barriers to entry

6 | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

There are no significant incentives targeted specifically at generalised manufacturing in the US auto market.

Legislation passed in 2022, however, particularly the Inflation Reduction Act (IRA), does have various programmes that significantly incentivise battery production. This Act, and other previously existing programmes, also provide incentives for other types of alternatively fuelled vehicles.

The IRA significantly revises the tax incentive for the purchase of qualified electric vehicles. While the maximum potential credit remains at US\$7,500 and there is no longer a limit on the number of credits assigned per original equipment manufacturer, the qualification for a credit is now quite complex and few vehicles are expected to fully meet those parameters in the next couple years. To qualify for a credit, there can be no involvement of an 'entity of concern', final assembly must be in North America, prices must not exceed the manufacturer's recommended retail price and consumers must not have an income over a certain level. If these terms and rules about critical minerals are met, a sale is eligible for a US\$3,750 credit. Another US\$3,750 is available if certain battery component rules are met. These rules are complex and, as the programme is new, regulations and interpretations are still evolving.

The IRA includes other programmes that can incentivise EV sales. A commercial lease programme for 'clean vehicles' can be used without the many restrictions in the EV purchase programme to benefit consumers who lease a vehicle.

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As this statutory structure is a significant new endeavour and the regulations are complex and evolving, experienced counsel should be sought to further understand the application of these programmes. The political context for these programmes is also complex, and future legislation or revised regulations may bring additional changes.

Various federal and state incentive programmes are in place that a manufacturer may take advantage of but are not focused exclusively on the auto industry. For instance, those building manufacturing facilities may try to generate competition among states and local governments regarding the incentives offered to encourage them to build a plant in a given location.

Material practical barriers remain in effect for new OEMs entering the US auto market. Automobiles are highly regulated goods. The emission and safety rules are complex and challenging and becoming more so. State statutes effectively prohibit manufacturers from selling directly to retail customers, so building a network of dealers adds additional complexity in entering the market.

The most significant barriers to entering the US market are the depth and competitiveness of the market. While entering the US market requires careful planning and compliance with complex rules, staying in the market is even more challenging. A successful new OEM requires the resources to build a brand with a good reputation, as well as cars that capture the public's imagination and praise from specialist reviewers. Those cars must remain serviceable over time and maintain value in the used market. A solid distribution network is crucial for success, as well as a good media team with a large budget to advertise the vehicles. Given the competitiveness of the market, profit margins can be small. A new entrant will need sufficient financial resources and resolve to stick with the investment when positive returns are unlikely for several years.

The most likely opportunity for new entrants in the US market comes from the prospect of EVs and autonomous-drive vehicles. Large and well-known technology companies with significant access to capital and established brand names have explored these new markets, in addition to a host of companies interested in developing novel technology and production capacity. Various EV manufacturers have entered the market and more are expected to evaluate entrance into the US market, but none since Tesla have had a significant impact on the overall market. Mobility services using a fleet of vehicles would constitute a challenge of sorts to the business model of sales to individuals that has dominated the industry for decades. While it is difficult to evaluate exactly how such developments would impact market dynamics, many automotive manufacturers have explored these service options themselves and many of those programmes have ended. Ride-hailing and vehicle-sharing services have not yet posed a challenge to incumbent manufactures.

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PRODUCT SAFETY AND LIABILITY

Safety and environmental

- 7 | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

Environmental regulations

Pursuant to the Clean Air Act (CAA), the Environmental Protection Agency (EPA) and California Air Resources Board (CARB) have comprehensive regulations for passenger vehicles and light duty trucks that apply throughout the full useful life of the vehicle. Since the 1970s, EPA has established mandatory emissions standards for criteria pollutants (eg, NO_x, PM, CO and HC) that have become progressively more stringent. Through a grant of a CAA waiver of pre-emption, the state of California can develop and enforce its own separate emissions requirements for vehicles sold in the state. Over time, California has developed additional requirements for criteria pollutants and other emissions, and a number of other states, representing nearly one-third of all vehicle sales, have chosen to adopt California's emissions standards. Since the 1980s, EPA and the National Highway Traffic Safety Administration (NHTSA) have implemented and enforced fleet-wide standards for fuel economy. More recently, EPA and CARB have been regulating greenhouse gases (GHG) through progressively more rigorous mandatory fleet-wide standards. Currently, California's GHG regulations are more stringent than EPA's, which gives rise to a market for California GHG credits to facilitate compliance in California and the other states that have adopted California's GHG programme. In addition, California has established a zero-emission vehicle (ZEV) programme requiring manufactures' annual sales to include a certain fraction of electric or hybrid vehicles. Both EPA and CARB have warranty requirements for emission-related components and require reporting and potential penalties or recalls for emission-related defects. EPA recently enacted new, more stringent GHG emission requirements for Model Year 2023–2026 and proposed new multipollutant emissions requirements for Model Year 2027 and beyond. Its proposed rule for Model Year 2027 would be the most stringent vehicle emissions requirements ever proposed and include requirements for electric vehicle and plug-in hybrid vehicles. Similarly, NHTSA recently enacted new, more stringent fuel economy requirements for Model Year 2024–2026 and is expected to propose new requirements for Model Year 2027 and beyond later this year. Last year, California also enacted new requirements for Model Year 2026–2035, including more stringent ZEV mandates with the goal of 100 per cent new vehicles to be ZEVs by 2035. These upcoming, NHTSA, EPA and California requirements will likely influence the credit market for GHG, ZEV and CAFE credits.

Safety regulations

NHTSA maintains more than 70 federal motor vehicle safety standards covering the full range of safety-relevant vehicle performance parameters, from occupant protection to headlight illumination levels. Following the Ford-Firestone tire safety crisis in the United States, NHTSA developed mandatory reporting requirements for potentially relevant safety information from in-use vehicles both in the United States and in foreign markets – pursuant to the Transportation Recall Enhancement, Accountability and Documentation (TREAD) Act

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enacted in 2000. The TREAD Act requires manufacturers to actively monitor warranty claims, customer complaints, death and injury claims, property damage claims, field reports and service measures, and report relevant data to NHTSA on a periodic basis. In July 2021, NHTSA issued a new Standing General Order requiring OEMs and operators to promptly report incidents and accidents that occur while their vehicles are operating with Level 2 advanced driver assistance systems and Level 3 to Level 5 automated driving systems. This reflects NHTSA's increased efforts to regulate autonomous vehicles, and semi-autonomous vehicles, using its existing authority to mandate that manufacturers recall safety-defective vehicles and equipment at the manufacturer's expense. NHTSA has ramped up enforcement of all of its regulations and requirements aggressively in recent years, following major safety issues by a number of manufacturers. NHTSA has collected hundreds of millions of dollars in civil penalties for a wide variety of violations, including failure to recall safety-defective vehicles and failure to comply with the TREAD Act reporting requirements. In recent years, NHTSA has shifted its enforcement focus to corporate conduct and process, and the bulk of civil penalties have been associated with gaps in corporate compliance structures and processes.

Product liability and recall

- 8** Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

Product liability and class action litigation play a significant role in the US automotive market. Each year, consumers file numerous individual product liability lawsuits alleging that purported automotive defects resulted in injury, death or other damages. Consumers also frequently file individual lawsuits seeking reimbursement for certain repair costs. (These are often referred to as 'lemon law' cases.) Consumers also file several class actions alleging that purported automotive defects (or alleged unfair business practices) resulted in economic damages, such as unreimbursed repair costs.

In some of these class actions, the consumer filing suit will not have incurred any repair costs or experienced the alleged vehicle malfunction. This type of class action is frequently referred to as a 'no injury' class action. In such class actions, a consumer frequently alleges that the automotive company concealed a supposed defect in the vehicle or its components and that, as a result, the consumer either paid more to purchase or lease the vehicle than intended or will recoup a lesser amount than expected upon resale. (This is also frequently referred to as a diminution in value claim.) Generally, a class action cannot be premised on the basis of bodily injury as there would be too many individual variations in class member claims.

A few trends are apparent in automotive companies' efforts to defend against individual and class action product liability claims. First, when facing class action allegations that a particular component is supposedly susceptible to malfunction (but has not yet actually malfunctioned), automotive companies have argued that consumers have no standing to litigate, either individually or as part of a class action, because they have not in fact been injured. Second, US Supreme Court decisions issued in recent years have enabled more corporate defendants to raise personal jurisdiction defences. In limited circumstances,

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these decisions permit automotive companies (particularly foreign ones) to argue that courts have no authority to exercise personal jurisdiction over them. Third, automotive companies have investigated strategies for diverting consumer claims from the US court system to arbitration, which can often be a more efficient mechanism for resolving disputes. However, thus far, automotive companies have enjoyed only limited success in compelling the arbitration of claims by vehicle purchasers against automotive companies.

The advancement of autonomous vehicle technology also has implications for US litigation, including potentially reapportioning the liability of certain actors and the burdens of proof associated with particular claims. However, until new legislative and regulatory frameworks to address autonomous vehicles are developed, consumers are likely to continue to rely on traditional common law and statutory claims in lawsuits involving autonomous vehicles.

DISPUTES

Competition enforcement

9 | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

While no special competition laws apply exclusively to the automobile industry, antitrust issues are pervasive in the sector. First, the Hart–Scott–Rodino Antitrust Improvements Act, 15 USC section 18a, requires parties to certain mergers, asset acquisitions and joint ventures to notify government enforcement agencies before closing. If notification is necessary, then the parties may not close the transaction until the statutory waiting periods expire. These statutes allow government enforcement agencies to review mergers, acquisitions and joint ventures for competition-law concerns before consummation of the deal. If the transaction may substantially lessen competition, the government may sue to prevent it under section 18 of the Clayton Act, 15 USC. Even transactions that are not subject to pre-closure review, however, may be challenged retrospectively under US antitrust law. In the past few years, government review of mergers in all industries has become more aggressive, and the number of government challenges to mergers has increased.

Second, automotive sector companies must comply with generally applicable antitrust laws. The Sherman Act prohibits agreements among two or more entities that unreasonably restrain trade, such as agreements among competitors to fix prices, rig bids, allocate customers or territories and boycott suppliers, customers or competitors. Other agreements are judged under a fact-bound inquiry into their competitive effects. Under that analysis, if, on balance, the anticompetitive effects of an agreement outweigh its pro-competitive benefits, the agreement is unlawful. The Sherman Act also prohibits certain unilateral conduct permitting or threatening to permit a firm to obtain or maintain monopoly power.

The Robinson–Patman Act in certain circumstances prohibits differential pricing of commodities, which includes automobiles and automobile parts, and many states have special statutes protecting automobile dealers.

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In the United States, antitrust violations carry both criminal and civil penalties. In addition, private parties injured by antitrust violations may recover triple their actual damage and obtain injunctions against future violations. An active plaintiffs' bar regularly brings private actions. Antitrust actions are common in the automotive industry. In recent years, the US Department of Justice obtained guilty pleas to criminal violations from a number of automotive parts suppliers, who paid substantial fines. Individual employees also pleaded guilty and received prison sentences. Those investigations spawned substantial private civil litigation by automobile dealers and consumers. The Department of Justice also recently investigated whether four automobile manufacturers improperly entered an agreement concerning emission of greenhouse gases with the State of California. That investigation closed without action.

The Department of Justice has also recently been aggressive in investigating non-compete and non-solicitation agreements in the employment area. Although no investigation that has been made public directly implicates the automobile industry, contract covenants related to the solicitation or hiring of employees have become more common in asset sale or joint venture agreements in the automotive industry, particularly as manufacturers enter arrangements with non-traditional suppliers and partners for the development of electric vehicles and autonomous driving systems. These covenants should be reviewed carefully to ensure compliance with US antitrust law.

Dispute resolution mechanisms

10 | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

OEMs rarely have disputes with each other. Consequently, litigation among OEMs is rare.

Disputes are more likely along the extended supply chain in the auto sector. Even there, however, litigation between an OEM and a supplier is uncommon. The nature of the economic relationship between the parties means disagreements are typically worked out through other methods of dispute resolution.

Disputes are not uncommon between manufacturers and auto dealers.

Disputes regarding intellectual property are a somewhat different situation.

Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

Traditionally, financial distress may arise from:

- internal sources (eg, weak quality control, financial mismanagement or strategic missteps);
- sources close to the supplier (eg, a defaulting upstream raw materials or sub-component supplier and a lender unwilling to renew or extend a line of credit); or

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- market-wide influences (eg, government regulation, technological change and commodity supply or pricing).

Today, a perfect storm is hitting the automotive industry and its supply chain. The automobile sector is undergoing a once-in-a-century transformation, as the industry evolves rapidly from the internal combustion engine to electric vehicles. Software and sensors are becoming increasingly important, as are connectivity and related interfaces, and driver assistance functions are developing quickly.

This massive transformation is dramatically realigning the supply chain for this significant global industry, and some companies are struggling to adapt.

In addition, the following factors are causing significant incremental stress on the supply chain:

- a gradual return to normalcy from the pandemic that has led to the withdrawal of government aid;
- shortages and price increases for raw materials or components like semiconductors, steel and other metals and minerals, as well as energy cost increases, affecting both input costs and consumer demand;
- logistics bottlenecks and tensions;
- effects stemming from Russia's war on Ukraine;
- growing geopolitical tensions between China and the United States; and
- macroeconomic factors – a one-two punch of inflation, interest rate increases and fears of economic recession – impacting both manufacturers and their customers.

The resulting stresses on the supply chain are varied, significant and ongoing.

While some manufacturers reported relatively strong sales in the fourth quarter of 2022, as supply chain pressures eased, continued inflationary pressures (eg, the high cost of living and higher gas prices) and higher interest rates may dampen consumer demand. In addition, wages and freight costs continue to increase, while commodity prices (including raw materials for electric vehicle batteries) have become more volatile. Many manufacturers and suppliers are also finding it challenging to pass on these increased costs, and not all suppliers will be able to equally navigate the shifting landscape.

With few exceptions, all major US automakers reported 2022 as their worst sales year in a decade, with US auto sales totalling 13.7 million vehicles in 2022, the lowest since 2011 and a reduction of 8 per cent compared to 2021.

Unsurprisingly, the foregoing signs of financial distress and declining sales figures have manifested themselves in 2023 with the first significant automotive industry Chapter 11 cases in several years, for example, Bolta US (injection moulding, chrome plating and component assembly for OEMs and Tier 1 suppliers), IEH Auto Parts (Auto Plus auto parts stores) and Stanadyne (fluid and air injection and management system products for OEMs and aftermarket sales).

This dynamic industry backdrop provides a more complex environment for assessing both financial viability and points of distress for suppliers, customers and other counterparties.

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Ideally, an OEM or top-tier supplier will identify a distressed supplier before the first delivery is missed or the supplier requests payment in advance to cover insufficient working capital. Obvious signs of supplier distress include, without limitation, failed refinancing, increasing leverage ratios, impending debt maturities, divestitures or sale-leaseback transactions, sharp drops in debt or equity security prices, management resignations, employment of advisers and deteriorating accounts receivable. While these signs of distress need to be monitored closely, the investigation of each of these criteria needs to be evaluated in terms of overall liquidity and strategic assessment within the currently changing industry environment.

When these signs emerge, customers must assess, through a close and open dialogue, how long it may be before a supplier's distress may affect them, and whether the supplier has the talent, ability, resources and time to cure its distress. These factors will inform a decision on whether to merely work with and monitor the supplier as it addresses a problem, or to move more aggressively to replace the supplier or consider other options, including:

- entering into accommodation agreements, under which the customer provides the supplier with commitments to continue sourcing parts balanced with customer protections, such as collateral grants (including intellectual property rights) and facility access agreements;
- extending the financing;
- providing operational support or facilitating changes in management; and
- acquiring the supplier.

The last option would not necessarily change the source of distress, but would provide the OEM or top-tier supplier with greater control to assess and fix its problems, and make necessary adjustments.

The US Bankruptcy Code permits the assets of bankrupt companies to be sold 'free and clear' of all liens and other liabilities, which could allow an OEM or top-tier supplier to obtain key unencumbered assets from the distressed business. An OEM or top-tier supplier may therefore find that an acquisition of a distressed supplier (or key assets) is best accomplished within a formal bankruptcy proceeding, where the transaction is approved by a court and the chances of a post-closing challenge to the transaction terms are greatly diminished.

A distressed supplier may materially disrupt the complex and potentially fragile just-in-time inventory system upon which the automotive industry depends. OEMs and top-tier suppliers examine the financial health of prospective suppliers, but one that fails to continue to monitor its suppliers, competitors or trends in its sector or region does so at its peril. It will be prudent for all stakeholders to frequently review potential signs of distress and associated risk mitigation strategies as these largely unprecedented matters unfold.

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Intellectual property disputes

12 | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

Intellectual property disputes, and in particular patent infringement actions, remain a significant issue in the automotive industry. Over the past several years there have been hundreds of automotive-related patent litigation cases, filed in US district courts and the International Trade Commission. Most of these suits have been filed by non-practicing entities (NPEs or patent trolls), often against multiple OEMs, and sometimes against suppliers. This patent litigation continues to trend towards global disputes with high risk.

Many of these patent cases, however, do not focus on vehicle-specific technologies, but rather on such aspects as communication protocols in the infotainment, mapping and navigation systems, semiconductor or integrated circuit technologies used in auto parts, such as battery power packs and radar systems, and software algorithms used in autonomous vehicles and connected car networking technologies incorporated into the vehicles. There also continues to be a clear trend towards disputes involving standard essential patents (SEPs), particularly in the connected car space. Connected cars need to rely on existing infrastructure owned by telecommunication entities and others to access the internet, communicate with other devices, receive traffic information, provide in-vehicle entertainment and enable control of vehicle systems via smartphones (eg, climate control and turning the car on and off). Using the existing telecoms infrastructure, however, requires using certain protocols, procedures and data formats that are subject to industry standards set by standard-setting organisations whose members are telecoms companies, national administrations, universities and research groups. Existing patents that cover these standards, such as WiFi, LTE, 5G, 4G, 3G, UMTS, GSM, GPRS and WLAN, are referred to as SEPs. There is also an increase in SEP enforcement related to wireless charging standards. The owners of these SEPs are often the telecom or chip companies, although NPEs (including Nokia and Ericsson) are obtaining an increasing share often by purchasing patents from innovators. SEP owners are also forming patent pools together (eg, Avanci) to attempt to license large patent portfolios relating to telecom standards. As vehicles implement more connected car technologies, including in 5G, the owners of SEPs in this space will continue their licensing campaigns and file suits against automotive makers and suppliers when those licensing negotiations fail. These litigations will likely be on a global level and carry significant risk.

Resolution of intellectual property disputes varies and may depend on whether the plaintiff is an NPE or an automotive company or supplier. When the plaintiff is an NPE or SEP holder, it is more likely that the dispute may be resolved for a licence fee, although the threat of an injunction still looms in jurisdictions such as Germany and the International Trade Commission, to create leverage in licensing pricing. Resolution of automotive patent litigation (and the amount and nature of such litigation) has also been impacted by inter partes review (IPR) proceedings filed by defendants in the US Patent and Trademark Office (USPTO) to challenge the validity of patents asserted in litigation. Defendants are having success invalidating patents or forcing the patent owners to settle or drop lawsuits by filing or threatening to file IPRs. The trend of filing IPRs in response to most patent lawsuits is expected to continue. There is also a recent trend to ensure that IPRs are filed in advance

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of or early at the start of lawsuits, as the institution of an IPR can be denied by the USPTO if the final decision in the IPR would come after trial or claim construction of the same issues.

EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

Any company interested in getting a deal done in the automotive industry must understand both US labour law and the state of labour relations in the industry, especially in 2023. Two major developments in the auto industry will happen in 2023:

- the announcement of the first President of the United Automobile, Aerospace and Agricultural Implement Workers of America (UAW) elected by the general membership; and
- the expiration of the collective bargaining agreement covering the three domestic auto makers – Ford, GM and Stellantis. Negotiations for a new contract will be very difficult this year, with significant implications for electric vehicles and battery production.

US law does not provide for works councils and, in fact, severely discourages their existence by making dealing with employee groups that do not represent a majority of the employer's employees unlawful except for very limited purposes. Thus, works councils as formulated in Europe are non-existent. The way unions come to represent employees in the United States is to demonstrate majority support among a group of employees, usually through a secret ballot election conducted by the National Labor Relations Board (NLRB), a federal government agency responsible for regulating labour relations, or a request for voluntary recognition.

Although unions represent less than 7 per cent of the US private sector workforce, they have been making gains in organising certain sectors. The UAW is the union that has traditionally represented American automotive workers. It has been very strong in the Midwest, representing workers at Ford, GM and Stellantis for decades, as well as a number of their suppliers. But it has struggled in the US South, where it has largely been unable to organise the foreign transplant OEMs, due to, among other things, the fact that these are mostly right-to-work states that preclude union security agreements requiring all members of a collective bargaining unit to become members of a union.

An employer making a major investment, particularly a controlling interest, in an automotive manufacturer or supplier in the United States must consider dealing with a number of key questions:

- is the target unionised;
- if so, is there a collective bargaining agreement in place;
- does that collective bargaining agreement obligate the target to require a purchaser to assume the collective bargaining agreement; and
- is the transaction structured as an asset or stock deal?

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If an acquirer purchases the majority of the stock of a corporation, the corporation remains subject to the terms of the collective bargaining agreement. If it simply purchases the assets, it will have to bargain with the union if a majority of the employees it employs come from the predecessor target. (The purchaser is not bound by law to hire the employees of a unionised target, but if it does not hire those employees because of their union affiliation, this would be an unfair labour practice.) Even if it hires the unionised workforce, the law requires the acquirer only to bargain with the union; it is not required to assume the collective bargaining agreement. However, many collective bargaining agreements require the employer signatory for a business to oblige an acquirer to assume the contract. If so, the seller will likely require contract assumption; otherwise, it faces a damage claim by the union and the possibility of the sale being enjoined altogether. The bottom line is that a company considering buying a unionised operation must undertake careful due diligence. Issues to consider include whether the target is unionised, what kind of relations it has with the union, what are the provisions of the collective bargaining agreement, if it is possible to operate successfully under the agreement and whether it will be required to assume the collective bargaining agreement. Mistakes can result in expensive litigation and strikes.

A major investment in a unionised OEM would be particularly complex. The UAW would carefully scrutinise a major investor and if it concluded that the investor would jeopardise its relationship with the OEM or have a negative impact in any way, the UAW would likely engage in significant efforts to block the deal. Again, a buyer should not consider such an investment without the most scrupulous due diligence and without a full understanding of the impact of the union.

An investment in a non-union company will not guarantee that the company will remain non-union. The UAW is aggressively seeking neutrality and card check agreements at new facilities as a method of organising companies without the need for an NLRB-conducted election.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

The most important legal developments all revolve around the vast amount of technology coming into vehicles. Connectivity and accident-avoidance technologies have made the prospect of driverless cars a matter of extensive research and development not only by incumbent OEMs, but also by large global technology companies. These developments extend throughout an evolving supply chain.

Significant legal questions are developing around safety regulation. Federal safety rules are traditionally oriented around crash survivability, but cars in the future will seek to avoid accidents. Safety rules also mandate certain structures such as mirrors that may be replaced by screens, or a steering wheel and brake pedal that would obviously not be needed where the vehicle is entirely autonomously driven. A host of rules will need re-evaluation as technology

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increasingly enters vehicles. The injection of advanced technology will also reshape the intellectual foundation for safety rules and lead to extensive changes over time.

The US Department of Transportation (DOT) continues to indicate the desire to facilitate these new developments and not over-regulate the industry in a way that inhibits development while still fostering safety. Guidelines issued by the Obama administration in September 2016 attempted to strike a balance between safety and technological development in a manner to encourage development and foster different solution pathways. The Trump administration issued in September 2017 its revision of these guidelines: A Vision for Safety 2.0. These guidelines made clear that the safety assessments are 'voluntary assessments' that do not have to be submitted. Nevertheless, DOT officials note they have extensive authority to address safety concerns and have stated that if those testing autonomous vehicles do not submit their assessments, the DOT will ultimately revise the guides in a more restrictive fashion. In October 2018, the Trump administration's DOT issued Preparing for the Future of Transportation: Automated Vehicles 3.0 (AV 3.0). This document further updated the administration's policy guidance and took a multi-modal approach (applies not just to cars but to other modes of surface transportation). In general, AV 3.0 affirmed the desire to use existing authority to advance and enable the technological development of the transportation sector. AV 3.0 provided updates on various initiatives related to autonomous vehicles and outlined a rulemaking agenda. Similarly, Ensuring American Leadership in Automated Vehicle Technologies: Automated Vehicles 4.0 (AV 4.0) was issued in January 2020 and continues to reiterate the administration's desire to revise existing regulations to remove barriers to automated vehicle technology, while remaining technology-neutral and maintaining safety goals. In addition to DOT's four rounds of voluntary automated vehicle guidance, the National Highway Traffic Safety Administration (NHTSA) under the former Trump administration had undertaken numerous efforts to evaluate changes to the regulations needed to remove barriers against the growth of automated vehicle technology, including initiating advanced notices of proposed rulemaking as well as a new rulemaking for Occupant Protection for Automated Driving Systems (the FMVSS 200 series). Under the Biden administration, NHTSA has recently finalised new rules amending the occupant protection-related FMVSS 200 series to account for automated driving system-equipped vehicles that do not have traditional manual controls associated with a human driver. We expect the Biden administration to continue developing a framework to address automated driving systems as well as similar efforts to incorporate safety standards for battery electric vehicles into the federal motor vehicle safety standards. Against this backdrop of required compliance with federal safety rules that do not yet accommodate automated technology, states continue to take varying approaches to the regulation of autonomous vehicles operating on their public roads.

With vehicles generating increasing amounts of data coupled with connectivity, privacy issues are of paramount concern. Automakers have issued industry privacy principles to follow for the protection of consumer interests in privacy. In addition, the California Consumer Privacy Act (CCPA), which became effective in January 2020, has a significant impact on OEMs' and technology companies' handling of California consumer data. For example, while personal information shared between dealers and OEMs for recalls and vehicle repairs covered by warranties are excepted, other sharing arrangements between such entities that have been occurring for decades have been significantly affected by the CCPA because of its broad definition of 'sale' and corresponding consumer right to opt-out of the sale of personal information. In addition, a new ballot initiative that California voters

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considered in November 2020, the California Privacy Rights and Enforcement Act of 2020 (the Initiative), could further impact the industry. The Initiative added new additional privacy protections that began on 1 January 2023 that expand the CCPA, including through greater regulation of geolocation information, data that is frequently collected by today's vehicle technologies. Policymakers remain keenly interested in this area and additional laws or regulations could significantly impact how the industry handles data.

The extensive use of computer coding in vehicles (estimates indicate modern vehicles already have over 100 million lines of code) and connectivity dictate that vehicle cyber resilience is a significant concern. The DOT recently issued guidelines in this area as well.

Fuel economy and vehicle emissions are aggressively regulated under a trifurcated and overlapping regulatory system with NHTSA regulating fuel economy and US Environmental Protection Agency (EPA) and California both regulating vehicle emissions, including greenhouse gasses (GHGs). The current regulatory structure covers fuel economy and GHG emissions requirements, including four potential credit systems for electric vehicles and other low emission technologies, through Model Year 2026: NHTSA Corporate Average Fuel Economy (CAFE); EPA GHG; California GHG; and (4) California zero-emission vehicle credits. Last year, the Biden administration repealed and replaced the former Trump administration fuel economy and GHG emissions standards, effective for Model Year 2024 and Model Year 2023, respectively. In particular, EPA's Model Year 2023–2026 GHG emissions standards will be the most stringent GHG standards finalised to date and will continue to increase in stringency year-over-year by 5 per cent in Model Year 2024, 6.6 per cent in Model Year 2025, and more than 10 per cent in Model Year 2026 (compared to 1.5 per cent year-on-year under the Trump rules). EPA's recently proposed emissions requirements for Model Year 2027 and beyond would be even more stringent and will likely force deep electrification within the nationwide fleet. In addition, CAFE civil penalty amounts have been increased from US\$5.50 to US\$15 per 0.1mpg by Model Year 2022. The increases in regulatory stringency as well as penalty amounts will undoubtedly impact the market for credits generated by electric vehicles and plug-in hybrid vehicles.

UPDATE AND TRENDS

Trends and new legislation

15 Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

The trend towards a mobility system defined by autonomous, connected, electric and shared vehicles is technology driven and continues vigorously.

Public policy developments are having a significant impact on the industry. The administration of President Biden has environmental, labour and foreign policy goals that have led it to aggressively seek the development of a robust electric vehicle (EV) market with production of the vehicles and the batteries located in the United States.

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New and proposed rules on vehicle emissions are, as expected, dramatically more stringent and will essentially force a rapid shift to EVs by vehicle manufacturers. The Biden Administration previously revoked a rule issued by the administration of President Trump that eliminated a waiver under the Clean Air Act that allowed California and states that follow its lead (the section 177 states) to have their own rules on vehicle emissions. California has long sought to be at the vanguard of environmental stringency in the United States, so the return of its regulatory capacity will further force OEMs to aggressively bring forward EVs.

Governmental regulation does not, however, automatically lead to consumer acceptance. EV sales are a relatively small percentage of total vehicle sales in the United States and a very dramatic change in consumer demand is needed for the desired transformation to EVs to occur as contemplated by recent regulatory developments. The sale of electric vehicles is, however, increasing and consumers show a greater willingness to consider an EV purchase. To facilitate this transition, EV infrastructure and supply lines will also have to evolve. Government policy will certainly impact that development in complex and evolving ways.

The National Highway Traffic Safety Administration has taken tentative but significant steps to update regulations in anticipation of highly advanced vehicles. This nascent effort has a long way to go, but the formal start of the rulemaking process establishes an important process of regulatory change.

Legislation to advance a mobility future, and autonomous vehicles in particular, has been introduced in each of the past few years. While legislation has led to Congressional hearings and negotiations, nothing has found Congressional approval and no legislation in this area is expected to become law in 2023.

The accelerating geopolitical competition between the United States, the Global West and China and Russia will impact significantly the automotive industry given the industry's global scale and supply lines and its strategic and economic importance. This geopolitical competition will be expressed in government policy in major markets in complex and evolving ways that may force difficult trade-offs onto manufacturers and their suppliers.

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OVERVIEW

Market

- 1 | For the automotive and mobility industry, describe the market's significance and identify major trends.

Vietnam's automotive industry continued to flourish in 2022 with the second-fastest growth among countries in Southeast Asia [according to the ASEAN Automotive Federation](#). In the

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same year, the Vietnam Automobile Manufacturers' Association [recorded a 33 per cent year-on-year increase in automobile sales](#), with more than 404,000 units sold.

Despite the increasing local demand for cars, Vietnam is largely an automobile-assembling, rather than automobile-producing, country. There are few local parts suppliers, meaning the vast majority of automobile parts used by in-country manufacturers are imported. Imports of completely built units are also experiencing faster growth than domestically assembled units, and in recent years have represented approximately 30 per cent of total sales within the country. Vietnam's tariff reduction commitments under the ASEAN Trade in Goods Agreement, the EU-Vietnam Free Trade Agreement (EVFTA) and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) have opened the market to imports from regional car-producing countries such as Thailand and Indonesia, as well as from member countries of EVFTA and CPTPP.

Real estate giant Vingroup JSC debuted locally manufactured cars under the VinFast brand in 2019, and its models have quickly become among the most popular in their markets. In March 2021, VinFast officially launched sales of its first electric car, with limited deliveries to consumers starting on 25 December 2021. On 15 July 2022, VinFast announced the end of its production of gasoline-powered cars as its focus shifted to exclusively developing electric vehicles. VinFast also has ambitions to enter the highly competitive US market, and recently exported 999 electric cars to the United States, including a delivery of 45 units to US customers on 1 March 2023. Vingroup has plans to establish an electric vehicle rental company with a focus on car and taxi rentals.

COMMERCIAL OPERATIONS

Regulation

2 | What is the regulatory framework for manufacture and distribution of automobiles and automobile parts, such as the homologation process as well as vehicle registration and insurance requirements?

The Vietnamese automotive industry is regulated and supervised by both the Vietnam Register, under the supervision of the Ministry of Transport, and the Ministry of Industry and Trade. The Ministry of Transport has oversight over technical and environmental standards for automobiles, while the Ministry of Industry and Trade is responsible for regulating imports of automobiles and automobile parts, as well as their manufacture and assembly.

Local assemblers of completely knocked-down (CKD) vehicles (ie, those that are imported for assembly in Vietnam) must ensure that assembled units satisfy technical and environmental standards set by the Vietnam Ministry of Transport. For that purpose, Circular No. 30/2011/TT-BGTVT, as amended by Circular No. 54/2014/TT-BGTVT and Circular No. 26/2020/TT-BGTVT, and Circular No. 25/2019/TT-BGTVT of the Ministry of Transport require automotive designs to be evaluated and approved (as evidenced by a certificate of design appraisal) and the final product to be tested for satisfaction of relevant technical standards (as evidenced by a certificate of quality, technical safety and environmental protection) before being permitted into circulation. Final products are also subject to ongoing annual and ad hoc inspection under the Ministry of Transport. In May 2020, the Vietnamese government

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issued Decree No. 57/2020/ND-CP amending Decree No. 122/2016/ND-CP on the tax incentives applying to the importation of CKD. Accordingly, a preferential import tariff of zero per cent will be applied to CKD parts from 2020 to 2024.

Completely built-up (CBU) vehicles (ie, those that are imported fully assembled) must undergo a homologation process and receive a certificate of homologation issued by the Vietnam Register. Vehicles exempt from homologation requirements must obtain a notice of exemption from the Vietnam Register. To be exempt from homologation requirements, Circular No. 31/2011/TT-BGTVT amended by Circular No. 55/2014/TT-BGTVT requires the following conditions to be satisfied:

- the vehicle must be completely new;
- the vehicle must have been manufactured within three years prior to the date of import; and
- the vehicle must be either examined in accordance with a treaty or agreement on mutual recognition of technological standards to which Vietnam is a signatory, or manufactured by a foreign vehicle manufacturer that has obtained conformity of production clearance from the Vietnam Register.

Decree No. 116/2017/ND-CP, which took effect on 1 January 2018 and was recently amended by Decree No. 17/2020/ND-CP, requires automobile importers to obtain a licence from the Ministry of Industry and Trade. Decree No. 116/2017/ND-CP also imposes rigorous quality inspection requirements and a list of business conditions regarding facilities and environmental protection, among others. Automobile manufacturers and assemblers must obtain a certificate of compliance with these conditions from the Ministry of Industry and Trade, and are required to fulfil these conditions throughout the course of their operations.

Individual vehicle owners must register the vehicle with the competent police department, and purchase and maintain automobile insurance as well as pay road maintenance fees throughout the period of use. Vehicle owners must also undergo periodic inspections and obtain an inspection certificate issued by the Vietnam Register.

Development, manufacture and supply

3 | How do automotive companies operating in your country generally structure their development, manufacture and supply issues? What are the usual contractual arrangements?

Most foreign automobile manufacturers operate in Vietnam through manufacturing joint ventures entered into with local (often state-owned) companies. Automobile parts are often imported, although there is a small local supplier market as well.

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Distribution

- 4** | How are vehicles usually distributed? Are there any special rules for importers, distributors, dealers (including dealer networks) or other distribution partners? How do automotive companies normally resolve restructuring or termination issues with their distribution partners?

Because the distribution sector is not completely open to foreign investors (in other words, foreign investors and certain foreign-invested companies established in Vietnam engaging in distribution activities are subject to legal requirements not applicable to purely domestic companies), foreign-invested manufacturing companies typically work with local networks and agents to distribute fully assembled vehicles into the market. Local distributors and qualified importers also engage in the import and distribution of CBU vehicles from outside Vietnam.

Decree No. 116/2017/ND-CP, as amended by Decree No. 17/2020/ND-CP, requires automobile importers to obtain a licence from the Ministry of Industry and Trade. One of the licensing conditions is that the importers have warranty and maintenance shops, and are authorised by the relevant foreign automobile manufacturers to recall defective imports. Currently, importers no longer need to provide vehicle type approval certificates issued in the country of origin, and imported cars are not required to undergo rigorous quality control tests if they are identical to previously imported cars tested in the past 36 months.

Restructuring or termination issues with distributors are typically resolved in accordance with the relevant distribution or agency agreement between the manufacturer and the distributor. If the distribution relationship is structured as a principal-agent relationship, the Vietnam Commercial Law provides for compensation upon termination equal to the average monthly remuneration of the distributor for each year of acting as agent for the manufacturer, unless otherwise expressly agreed by the parties. No compensation upon termination is payable in the case of a distribution agreement unless agreed by the parties.

Mergers, acquisitions and joint ventures

- 5** | Are there any particularities for M&A or JV transactions that companies should consider when preparing, negotiating or entering into a deal in the automotive industry?

Foreign investment activities in Vietnam, including M&A and joint venture transactions, are subject to completion of a licensing process that can be time-consuming and appear, at times, unpredictable and arbitrary. Acquisition of shares or other equity in an existing company is usually more straightforward than the establishment of a new company, but relevant licensing formalities must still be followed.

To establish a new company in Vietnam, a foreign investor must first obtain an investment registration certificate (IRC) from the provincial Department of Planning and Investment or the management board of special zones (eg, an industrial zone, export-processing zone, high-tech zone or economic zone) where the new company will be located. Certain special or large-scale projects also require approval from the prime minister, the National Assembly or local People's Committee. After obtaining the IRC, the next step is the application for an

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enterprise registration certificate, which serves as the business licence of the company and signifies the completion of its establishment.

An IRC is not required in the case of acquisition of shares or other equity in an existing company in Vietnam. However, consent from the provincial Department of Planning and Investment is required if:

- the foreign investor is acquiring shares in a company that operates a conditional business;
- the acquisition increases foreign ownership of the target company (unless the total foreign ownership following the acquisition remains below 50 per cent); or
- the target company holds land in certain strategic locations.

In addition to the investment-related licensing processes, Vietnam's merger control regime stipulates that economic concentrations meeting certain thresholds must be notified to the Vietnam Competition and Consumer Authority, and closing may not occur before clearance is granted. This regime applies to transactions occurring both within and outside of Vietnam, so long as any of the following thresholds are met:

- either party (together with its affiliates) had assets or revenues in Vietnam in the preceding financial year of at least 3 trillion Vietnamese dong;
- the value of the transaction is at least 1 trillion Vietnamese dong for transactions occurring within Vietnam; or
- the combined market share of the parties and their affiliates in the relevant market is at least 20 per cent.

Some business sectors or activities are also restricted or subject to additional conditions if the company has foreign investment capital, so a potential foreign investor should carefully consider any impact the investment may have on the existing or contemplated operations of the target company.

Incentives and barriers to entry

6 | Are there any incentives for investment in the automotive market? Are there barriers to entry into the market? What impact may new entrants into the market have on incumbents?

In February 2016, the prime minister issued Decision No. 229/QĐ-TTg specifying incentives relating to finance, trade promotion, land and taxation for the automotive industry. Accordingly, automotive companies engaged in the manufacture, purchase and use of certain types of priority vehicles (eg, small vans used in agriculture with a capacity of 3 tonnes, medium- and short-distance passenger vehicles, cars with nine or fewer seats and cylinder capacity of 1500 cubic centimetres and certain other specialised vehicles) are entitled to certain incentives. Specific key incentives include:

- projects relating to auto parts production and car assembly of local companies are eligible for loans from the Vietnam Development Bank;
- companies that are part of a global supply chain for production of parts or vehicle exports are eligible for export credit from the Vietnam Development Bank;

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- financial support is available from the government for government procurement, development investment credits and projects using priority vehicles;
- goods imported to create fixed assets for auto and auto parts production, or assembly projects located in industrial zones, economic zones and high-tech zones enjoy preferential import tariffs;
- most-favoured-nation import duties will be applied to priority and locally made vehicles;
- preferential corporate income tax rates will be set for projects relating to the manufacture of priority vehicles with a capacity of 50,000 units a year and manufacture of certain types of auto parts;
- auto parts production projects may enjoy certain land incentives (eg, exemption or reduction of land rent); and
- in addition to the aforementioned specific incentives, the government may provide support for large-scale automotive projects on a case-by-case basis.

Generally, barriers to entry into the market are more commercial than legal. For example, Vietnam's underdeveloped road infrastructure and cultural preference for motorbikes act as a check on the further development of the domestic automotive industry. Substantial taxes imposed on automobiles in Vietnam, including import taxes, value-added taxes on both new and used vehicles and special consumption taxes (which can be as high as 150 per cent and apply to both imported and locally produced vehicles) also make them unaffordable to the vast majority of the local population.

In November 2020, the government instructed the Ministry of Finance, in collaboration with the State Bank of Vietnam and the Ministry of Industry and Trade, to propose policies on taxation and preferential credit to create favourable conditions for the development of Vietnam's domestic automotive industry. The government further instructed the Ministry of Industry and Trade to propose policies promoting the development of the country's leading automotive manufacturers.

Although the overall registration fee reduction applied during the covid-19 pandemic has expired, industry associations have requested the prime minister to reinstate the reduced fees for all vehicles to foster the market, as it is predicted to face difficulties this year due to the likelihood of higher interest rates. However, for electric and battery-powered cars and environmentally friendly vehicles, exclusive tax incentives and registration fee reductions continue to apply in the next five years. Decree No. 10/2022/ND-CP, dated 15 January 2022, provides that registration fees will be waived for battery-powered cars until 1 March 2025, following which the registration fee applied to electric cars will be 50 per cent of the fee applicable to the same class of gasoline-powered cars. A new wave of electric vehicle usage is foreseeable in the near future.

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PRODUCT SAFETY AND LIABILITY

Safety and environmental

7 | What are the most relevant automotive-related product compliance safety and environmental regulations, and how are they enforced? Are there specific rules for product recalls?

The most relevant automotive-related product compliance safety and environmental regulations are set out in:

- Circular No. 30/2011/TT-BGTVT of the Ministry of Transport governing the production of completely knocked-down (CKD) vehicles, as amended by Circular No. 54/2014/TT-BGTVT, Circular 26/2020/TT-BGTVT and Circular No. 16/2022/TT-BGTVT (Circular 30);
- Circular No. 31/2011/TT-BGTVT of the Ministry of Transport governing the import of completely built-up vehicles, as amended by Circular No. 55/2014/TT-BGTVT and Circular No. 42/2018/TT-BGTVT and Circular No. 16/2022/TT-BGTVT;
- Circular No. 25/2019/TT-BGTVT of the Ministry of Transport governing the manufacture and assembly of CKD and semi-knocked-down vehicles that have some domestically produced parts, dated 5 July 2019, as amended by Circular No. 46/2019/TT-BGTVT, dated 12 November 2019; and
- Circular No. 16/2021/TT-BGTVT of the Ministry of Transport setting out duties applicable to car owners, dated 12 August 2021.

Non-compliance with these regulations can result in administrative penalties including monetary fines or revocation of relevant licences and certificates. The Vietnam Register also has the power to inspect the quality and standards of domestic automobile manufacturers on a regular or irregular basis to ensure compliance with relevant regulations.

Specific rules apply to product recalls in the automotive industry. According to Circular 30, an automobile manufacturer must recall its products if they fail to comply with any applicable technical standards or cause (or may cause) danger to humans or property as a result of technical errors. The manufacturer must recall its products within five days of discovering the technical error and must notify the Vietnam Register in writing to propose a recall plan. Within five days of the date of receipt of the notification, the Vietnam Register must approve the plan (or suggest changes to it) and the manufacturer must recall its products in accordance with the approved plan. The manufacturer must also report the results of the recall plan to the Vietnam Register. Failure to comply with the regulations on product recalls may result in the manufacturer's certificate of quality, technical safety and environmental protection for the affected class of automobile to be suspended or withdrawn.

Decision No. 49/2011/QĐ-TTg of the prime minister raised exhaust emission standards for newly manufactured or assembled or imported cars from a Euro 2 standard to Euro 4 as of 1 January 2017, with a further increase to Euro 5 from 1 January 2022. Cars already in use and imported used cars are covered by Decision No. 16/2019/QĐ-TTg of the prime minister, which raised emission standards to Euro 4 for imported used cars from 15 May 2019. Cars manufactured prior to 1999 and still in use remain subject to the lower Euro 1 standard. From 1 January 2020, cars manufactured between 1999 and 2008 are subject to Euro 2, and from 1 January 2021, cars manufactured after 2008 are subject to Euro 2.

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The concept of extended producer responsibility was introduced in the new Law on Environmental Protection and its implementing decree, Decree No. 08/2022/ND-CP, which came into effect from January 2022 and primarily focuses on recycling and waste treatment contribution requirements for certain types of products. For the automotive industry, starting from 1 January 2027, manufacturers and importers of automobiles sold in Vietnam will have an extended producer responsibility to recycle 0.5 per cent of the total annual production and import of automobiles according to the mandatory recycling standards, which will be increased every three years. Manufacturers and importers can choose to self-recycle automobiles subject to annual recycling plans registered with the Ministry of Natural Resources and Environment and must report results. Alternatively, they can opt for making monetary contributions to the Vietnam Environmental Protection Fund to support recycling activities following the prescribed timeline. There is a formula to calculate contribution amounts in this case, and such amounts must be declared to the Ministry of Natural Resources and Environment on an annual basis.

Product liability and recall

- 8** | Describe the significance of product liability law, and any key issues specifically relevant to the automotive industry. How relevant are class actions or other consumer litigation in product liability, product recall cases, or other contexts relating to the automotive industry?

The Vietnam Civil Code and the Law on Protection of Consumer Rights both provide a basis for liability for damage caused by manufactured or imported products, including automobiles and automobile parts. The Civil Code sets out the broad principle that individuals or legal entities engaged in production or other business activities are liable for damage caused to consumers as a result of the individual or legal entity's failure to ensure the quality of goods they manufacture or pass on to consumers. The Law on Protection of Consumer Rights addresses product liability more specifically and provides that manufacturers and importers (including organisations or individuals who affix a commercial name on the goods or use a trademark or commercial indication identifying such organisation or individual as the manufacturer or importer of the goods) are liable for any damage caused by defective products manufactured or imported by them. In addition, where the manufacturer or importer of a defective product is unidentifiable, the direct supplier of the defective goods will be liable for damage suffered by consumers because of the defect.

Notwithstanding the basis for liability set out in the law, it has not yet been a common practice in Vietnam for consumers to bring claims for compensation (either individually or as a class) against manufacturers or importers of automobiles, automobile parts or other products for damages caused by defective products. One reason for this is the relatively poor reputation of Vietnam's legal system – and in particular its courts – which is more often than not seen as time-consuming, costly, unpredictable and arbitrary in both proceedings and results.

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DISPUTES

Competition enforcement

- 9** | What competition and antitrust issues are specific to, or particularly relevant for, the automotive industry? Is follow-on litigation significant in competition cases?

Vietnam's Competition Law is aimed at preventing acts of unfair competition, acts in restraint of competition and economic concentrations that have or may have a competition-restraining impact on the country's market. Acts that can serve to restrict competition include those that reduce, distort or prevent competition in the market through economic concentration (eg, mergers, acquisitions or other types of business combination transactions), abuse of dominant market position or monopoly or agreements to restrict competition (eg, agreements to divide the market to minimise or eliminate competition). Acts of unfair competition are those that are contrary to general standards of business ethics and that cause or may cause damage to the interests of the state or to the legitimate rights and interests of other enterprises or consumers.

The authorities tasked with enforcing Vietnam's competition regulations have not historically taken an aggressive approach to enforcement, and we are not aware of any case in which the authorities have accused an automotive company of violating applicable Vietnamese competition or antitrust regulations. It is yet to be seen whether the authorities will take a more active approach to enforcement towards the automotive industry.

Dispute resolution mechanisms

- 10** | What kind of disputes have been experienced in the automotive industry, and how are they usually resolved? Are there any quick solutions along the supply chain available?

Because Vietnam's court system is relatively unsophisticated and is perceived as being both arbitrary and unpredictable, most disputes are resolved outside of the formal legal system through commercial negotiations or amicable settlement of claims. This is particularly true in the case of product manufacturers or distributors who may be concerned that adverse news coverage or other publicity could negatively impact their brand in the eyes of consumers. Because most claims are handled outside of formal legal channels, and because Vietnam does not have a system of binding case law or other legal precedents, it is difficult to say with any degree of certainty what kinds of disputes have been experienced in the automotive industry. We can speculate, however, that disputes would likely arise from issues such as product liability and warranty periods.

When a dispute arises, the aggrieved party may seek one or more remedies, including not only damages for loss but also interim or equitable remedies such as specific performance, temporary cessation of contractual performance or termination or rescission of contract. Injunctive relief may also be available upon petition to the competent court.

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Distressed suppliers

11 | What is the process for dealing with distressed suppliers in the automotive industry?

The process for dealing with a distressed supplier depends on the terms of the contract between the supplier and the manufacturer or customer, together with any remedy provisions included therein. However, where a supplier is, or is at risk of becoming, insolvent, a manufacturer or other customer of the supplier may also petition a court to initiate bankruptcy proceedings and join the list of creditors seeking recovery.

Intellectual property disputes

12 | Are intellectual property disputes significant in the automotive industry? If so, how effectively is industrial intellectual property protected? Are intellectual property disputes easily resolved?

The most significant disputes in the automobile industry in Vietnam relate to counterfeiting of automobile parts and fittings and domain name disputes.

As a member of the World Trade Organization, Vietnam has established a relatively comprehensive legal framework to register and protect intellectual property rights. In the case of infringement or other violation of existing intellectual property rights in the country, the owner of such rights may pursue relief through administrative, civil or, in some cases, criminal proceedings. In practice, administrative relief for infringement of intellectual property rights is more common (and easier to obtain) in Vietnam. However, although administrative relief is cost-effective to obtain and generally results in an immediate cessation of the infringement, it has proven to have a somewhat low deterrent effect overall. To date, civil and criminal causes of action have been limited to instances of deliberate counterfeiting.

Generally, intellectual property disputes are not easily resolved due to the intangible nature of the assets and, particularly in the case of patents or industrial designs, the highly technical knowledge that is often in question. This is especially the case in Vietnam, where courts and enforcement agencies are not experienced in handling highly complex or technical disputes.

EMPLOYMENT ISSUES

Trade unions and work councils

13 | Are there specific employment issues that automotive companies should be aware of, such as with trade unions and works councils?

Vietnamese employment regulations are extremely employee-friendly, and in disputes relating to employment Vietnamese courts and other administrative authorities generally sympathise with employees over employers. Even in cases of clear wrongdoing, it is extremely difficult to terminate an employee without his or her consent and willingness to cooperate.

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Companies are not obligated to establish a trade union for employees, but must recognise and support trade unions or other representative organisations established by employees.

Companies with 10 or more employees must enact and register with the authorities a written set of internal labour rules. An employee may only be disciplined in accordance with the internal labour rules enacted by the company or pursuant to the limited (and poorly defined) offences provided for in the Labour Code. The internal labour rules must be agreed with the company's in-house trade union or other organisation representing the employees. The relevant trade union or representative organisation must also participate in cases of employee discipline or where changes are being made to the rights or responsibilities of company employees.

NEW TECHNOLOGIES AND MOBILITY

Legal developments

14 | What are the most important legal developments relating to automotive technological and mobility advances?

Although Vietnam is not at the forefront of automotive technological and mobility advances, car-sharing applications such as Grab (and previously Uber) have experienced rapid growth in popularity since their relatively recent entry to the market. Vietnam's largest taxi firm, Vinasun, sued GrabTaxi Vietnam under Vietnam's competition law for 'unhealthy competition', but both passengers and drivers continue to flock to ride-hailing firms owing to widespread dissatisfaction over the service provided by traditional taxi companies. Although GrabTaxi claimed that it was operating as a technology firm rather than a taxi company, the court concluded otherwise and awarded damages to Vinasun. Both parties appealed the decision and, on 10 March 2020, the Supreme People's Court in Ho Chi Minh City officially rejected the appeals and upheld the first court's judgment against GrabTaxi.

In early 2020, the Vietnam government enacted Decree No. 10/2020/ND-CP dated 17 January 2020 as amended by Decree No. 47/2022/ND-CP dated 19 July 2022 (Decree 10) on automotive transportation business and conditions for automotive transportation business, and officially put an end to the pilot programme for ride-hailing services under Decision No. 24/QD-BGTVT. Accordingly, from 1 April 2020, Decree 10 requires that entities that participated in the pilot programme must choose a suitable form of business, either in the form of passenger transportation business by taxi, contract-based passenger transportation business or providing software application to assist with connection in transportation. Other requirements apply depending on the form of business selected.

The first autonomous car in Vietnam was introduced in 2017, using software developed by local company FPT Software. FPT Software subsequently experimented with a Level 3 autonomous car in 2019, while Phenikaa Group introduced Vietnam's first Level 4 smart self-driving vehicle in March 2021. Although there are currently no regulations in place governing autonomous vehicles in Vietnam, the Ministry of Transport supports the development of self-driving cars as they are considered to be in line with the government's strategy on the 'fourth industrial revolution'. The Ministry of Transport has also responded positively

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to FPT Software's proposal to allow it to operate its driverless cars on a trial basis on internal roads in a hi-tech park in Ho Chi Minh City.

UPDATE AND TRENDS

Trends and new legislation

15 Are there other current legal developments, emerging trends or pending legislation relevant to the automotive and mobility industry that should be noted?

Vietnam's entry into the EU–Vietnam Free Trade Agreement and other international trade agreements such as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership and the ASEAN Trade in Goods Agreement will help Vietnam's domestic automobile industry to join the global supply chain while increasing competition between domestic and imported vehicles in Vietnam. As a result, the country's domestic automobile manufacturers will need to focus on improving quality and lowering production costs to compete with imported vehicles.

The Ministry of Industry and Trade published the second draft of a proposed Law on Protection of Consumer Rights in February 2023 for public consultation. The draft proposals introduce new consumer protection regulations that may affect the automotive industry, especially in terms of consumer data privacy protection, requirements on warranty policies and recall of defective products. The estimated timeline for the new law's effectiveness is sometime in 2024.

On 17 April 2023, the Vietnamese government promulgated Decree No. 13/ND-CP on personal data protection (Decree 13), which will become effective on 1 July 2023. Decree 13 marks a significant development in personal data protection law in Vietnam, introducing a number of legal concepts and new requirements, including:

- a detailed definition of 'personal data' including 'basic personal data' and 'sensitive personal data';
- definitions of 'personal data controller', 'personal data processor', 'personal data controlling and processing entity' and 'third parties' as well as their respective legal obligations;
- several exceptions to the general rule of prior consent of data subjects;
- stricter rules in respect of 'sensitive personal data'; and
- significant restrictions on cross-border transfer of personal data, by requiring an impact assessment to be filed with the Ministry of Public Security prior to transferring personal data of Vietnamese citizens abroad (including driver licence numbers and licence plate numbers).

As automobiles increasingly rely on software and generate personal data, including location data, Decree 13 can be expected to have a material impact on the operation of automotive market participants with operations in Vietnam.

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