

**Testimony of
W. Neal Menefee
President and CEO of Rockingham Group**

**on behalf of
National Association of Mutual Insurance Companies (NAMIC)
and
Property Casualty Insurers Association of America (PCI)
and
Quality Parts Coalition (QPC)**

**House Judiciary Subcommittee on Intellectual Property
Hearing on
H.R. 3889, the “Promoting Automotive Repair, Trade, and Sales Act”**

August 1, 2012

Introduction:

Chairman Goodlatte, Ranking Member Watt, and other esteemed Subcommittee members, I am Neal Menefee, the President and CEO of the Rockingham Group of insurance companies, whose home office is in Harrisonburg, Virginia. The parent company of the group is Rockingham Mutual Insurance Company, whose oldest predecessor company has been in business since 1869. The group currently underwrites and markets property and casualty insurance products, including auto, in Virginia and Pennsylvania with annual revenues in excess of \$40 million.

Our company is proud to be a member of both the National Association of Mutual Insurance Companies (NAMIC) and the Property Casualty Insurers Association of America (PCI), and I am pleased to be here to testify on their behalf.

The National Association of Mutual Insurance Companies (NAMIC), is the largest and most diverse national property/casualty insurance trade and political advocacy association in the United States. Its 1,400 member companies write all lines of property/casualty insurance business and include small, single-state, regional, and national carriers accounting for 50 percent of the automobile/ homeowners market and 31 percent of the business insurance market.

PCI is composed of more than 1,000 member companies, representing a broad cross-section of insurers. PCI members write over \$175 billion in annual premium and 37.4 percent of the nation’s property casualty insurance. PCI represents 43.5 percent of the US automobile insurance market, 30.6 percent of the homeowners market, 35.3 percent of the commercial property and liability market, and 41.8 percent of the private workers compensation market.

NAMIC and PCI are both members of the Quality Parts Coalition (QPC), which represents the interests of the automotive collision parts industry, the insurance industry, seniors, and consumers.

We commend you for holding this important hearing and thank you and your staff for this opportunity to testify in strong support of H.R. 3889, the Promoting Automotive Repair, Trade, and Sales Act, the PARTS Act. Also, we applaud Representatives Issa and Lofgren for their bipartisan leadership in sponsoring the PARTS Act.

Background and Benefits of Competition in the Automotive Collision Repair Parts Market:

By way of background, I would start by asking you to consider whether you or a family member has ever been in an auto accident, perhaps a fender bender? Most of us have been and while I hate to see anyone experience an auto accident, if you have then whether you knew it or not, you benefitted from competition in the collision repair parts marketplace; competition that has existed for decades between car companies and alternative suppliers of such parts.

To be clear, we are talking about collision repair parts, which are the cosmetic, exterior parts of an automobile that typically can be damaged in fender bender types of auto accidents. This might include fenders, quarter panels, bumper covers, grilles, and other similar parts. Generally speaking, these parts are not structural or safety-related parts designed to be part of a vehicle's collision management system, like reinforcement bars or bumper brackets.¹

It is worth noting that the car companies already have captured two-thirds of the market for collision repair parts, while alternative suppliers have about fourteen percent.² However, despite the alternative suppliers' relatively small market share, the competition they provide is still very important to consumers. That's because alternatively-supplied collision repair parts typically are 26% to 50% less expensive than the car company parts. But even if a more expensive car company part is used, the existence of competition has been shown to cause car companies to lower their collision part prices by an average of about 8%.³ The estimated total benefit to consumers from the availability of competitive alternatives is approximately \$1.5 billion⁴ to \$2.4 billion⁵ per year. It's a great example of the free market at work for the benefit of consumers.

Design Patents Are Being Used to Eliminate Competition:

¹ "Status Report," Insurance Institute for Highway Safety, Vol. 35, No. 2, Feb. 19, 2000. See also, Insurance Institute of Highway Safety, Statement Before the Property-Casualty Insurance Committee of the National Conference of State Legislators, "Institute Research on Cosmetic Crash Parts," July 7, 2005. In fact, the Insurance Institute for Highway Safety ("Institute"), through crash testing and crashworthiness evaluations, consistently has found that, generally speaking, cosmetic, exterior parts "serve no safety or structural function . . . [t]hey merely cover a car like a skin." Moreover, the Institute has found that whether a cosmetic collision repair part is a car company part or an alternatively supplied part "is irrelevant to crashworthiness." Id.

² Recycled parts comprise the remainder of the market.

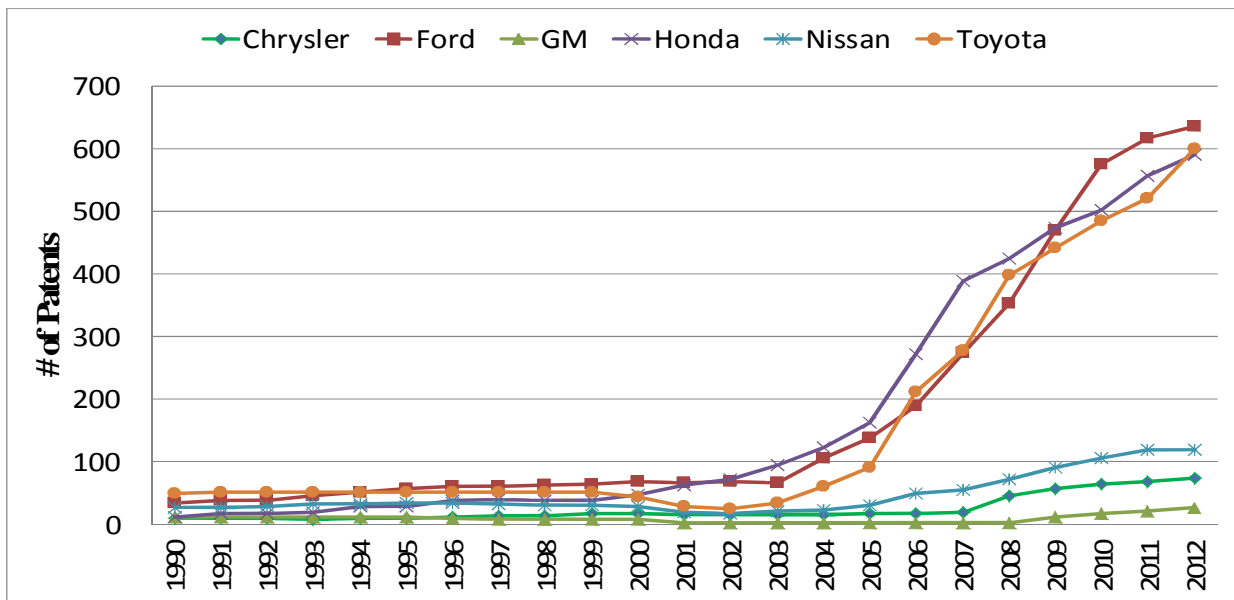
³ Consumer Benefits from a Competitive Aftermarket for Crash Parts., R.W. Boulten, MiCRA Consulting & Research Associates, Inc., 2008.

⁴ Id.

⁵ Analysis of the Impact of Banning Aftermarket Parts, Property and Casualty Insurers Association of America, January 19, 2010.

Clearly, consumers benefit from the lower costs created by the competition provided by alternative suppliers of collision repair parts. However, some car companies appear to have formulated a new business strategy to eliminate competition and expand their already dominant share of the market by obtaining 14-year design patents on their collision parts and enforcing them against alternative suppliers. Beginning around 2003, several car companies began to dramatically increase the number of design patents they were obtaining on individual component collision parts of the automobiles they manufacture. Obtaining design patents on these individual parts is a significant departure from the car companies' past behavior, when they may have obtained 14-year design patents on the overall design of their cars, but did not place much, if any, emphasis on the interchangeable component collision parts. Below is a chart on the cumulative number of crash part design patents owned by a number of the major car companies. As you will see, some of the companies now have hundreds and hundreds of such 14-year design patents on a wide variety of collision parts.

Cumulative Numbers of Collision Repair Part Design Patents Owned By Major Car Companies



The number of design patents awarded to the major car companies on collision repair parts has increased dramatically since the 1990s, after Congress said NO to their strategy to enact legislation providing copyright protection for repair parts. **Note 1:** The term "collision repair parts" includes bezels, bumper covers, deck lids, door shells, fenders, fascias, front/rear grilles, header panels, headlamps, high-mounted brake lights, hoods, pickup beds, pickup box sides, quarter panels, radiator supports, side markers, side mouldings, tailgates, taillamps, and wheel houses as defined by the Certified Automotive Parts Association at <http://www.capacertified.org/whatparts.asp>. **Note 2:** Figures shown are cumulative. For 2012, those figures have been "annualized" and are based on the number of design patents granted through July 20, 2012.

In December 2005, Ford Global Technologies (Ford) took the unprecedented action of filing a Section 337 case at the International Trade Commission (ITC) against companies in the alternative parts industry for allegedly infringing design patents held by Ford on fourteen exterior component parts for the Ford F-150 (model years 2004-2007). On December 4, 2006, the Administrative Law Judge held that seven of the design patents were valid, judged them to have been infringed, and issued an exclusion order on those parts.⁶ The exclusion order went into place on August 6, 2007, and – until a legal settlement was reached in April of 2009 – competition was effectively eliminated in the United States for seven Ford F-150 exterior collision repair parts. Therefore, for almost 2 years, the car company was the one and only source for the purchase of those seven parts.

We would point out that the purpose of such parts is only to restore the vehicle’s original, pre-accident appearance. Naturally, that is what consumers demand and what insurance policies provide; therefore, these are “must match” parts. There is no room for innovation by alternative suppliers so as to avoid allegations of infringement. In fact, many state insurance laws require that alternatively supplied collision repair parts be of “like kind and quality” in “form, fit, and finish” to car company parts. But after Ford’s unprecedented actions at the ITC, alternative suppliers are in the untenable position of complying with state law and meeting consumer demand while, simultaneously, facing allegations of design patent infringement by the car companies. Fourteen-year design patents, when applied to these parts in the aftermarket, serve only to restrict or eliminate competition and facilitate a monopoly on cosmetic replacement parts.

In addition, on May 2, 2008, Ford filed yet another Section 337 complaint at the ITC, alleging design patent infringement for eight parts for the Ford Mustang (model year 2005). Not insignificantly, the legal defense costs for alternative suppliers in both the F-150 and Mustang cases were enormous and mounting. While the ITC’s decision in the Ford F-150 case was pending on appeal at the Federal Circuit, and the ITC ALJ hearings were about to commence in the Ford Mustang case, Ford reached a settlement with one alternative supplier.

While many of the settlement’s details remain confidential, publicly available information suggests that the settlement is very limited in nature. It’s only between Ford and one alternative parts distributor, and it only lasts until March 2015. As such, nothing in the settlement prevents any of the other car companies from filing a complaint at the ITC today and continuing to eliminate competition. Nothing in the settlement prevents Ford from marching right back to the ITC as soon as the settlement expires in 2015 and continuing its effort to eliminate competition. Therefore, despite the temporary settlement between Ford and one alternative supplier, we cannot sit and simply cross our fingers that the car companies will simply ignore future opportunities to exploit new design patents on component parts and wipe out competition. Faced with these realities, Congress must act now, before it is too late.

The Harmful Effects of Eliminating Competition on Collision Repair Parts:

The impact of eliminating competition in the collision repair parts market would fall directly on consumers. If competition is eliminated, the insurance industry estimates that \$2.4 billion would

⁶ Lower bumper valance (2WD), lower bumper valance (4WD), side view mirror (LH/RH), honey comb grille, head lamp (LH/RH), tail lamp styleside ((LH/RH), and tail lamp flareside (LH/RH).

be added to insured automobile repair costs every year. Ultimately, the higher costs of those repairs would be passed on to consumers in the form of higher insurance premiums.⁷ Nor would the effect of eliminating competition on collision repair parts be limited to consumers' auto insurance costs. Consumers that pay for their own repairs out of pocket would bear these costs directly, or might choose to forgo repairs, leading to more rapid deterioration and depreciation of their vehicles. Higher repair costs also means that there is an increased likelihood of a vehicle being declared a total loss, compelling consumers to replace the vehicle, pay off a loan that may exceed the value of the vehicle, and seek financing for the purchase of a replacement vehicle, all of which depletes savings. In tough economic times like these, these kinds of added costs hurt consumers that much more, especially as autos age and depreciate. The impact of all of these factors would be much greater on those low- or fixed-income consumers who can least afford it.

The PARTS Act is Good Public Policy, Carefully Balancing Intellectual Property Rights and Preservation of Competition:

In February of this year, Representatives Issa and Lofgren⁸ introduced the PARTS Act in order to address the clear and present danger posed by car companies' use of design patents to eliminate competitive choice in the aftermarket for collision repair parts. The PARTS Act carefully balances the car companies' intellectual property rights with the need to protect consumers by preserving competition.

Specifically, when a part is being used "for the purpose of repair of a motor vehicle so as to restore [it] to its appearance as originally manufactured" the PARTS Act would effectively reduce from 14 years to 2.5 years the monopoly period during which the *sale* of alternative collision repair parts or the *use* of such parts would constitute an act of infringement of a car company's 14-year design patent. That said, under the PARTS Act, it would never be an act of infringement to make, test, market, or engage in pre-sale distribution.

We recognize that the overall design of a car can play a significant role in a consumers' choice when buying a new car and, in the very competitive market for new car sales, car companies invest a lot in their overall design of a vehicle as a result. While protecting competition in the market for collision parts, the PARTS Act would do nothing to deter car companies from obtaining 14-year design patents on their collision parts and enforcing them for up to 14 years against other car companies to prevent them from copying each another's vehicle designs in the new car sales market. Therefore, the PARTS Act does nothing to change the incentive of the car companies to innovate as they continue to design their cars to compete against each other.

We respect the investment made by the car companies in intellectual property when designing their cars to create a distinctive owning and driving experience, but when a consumer buys a car for \$35,000 in the showroom, puts the title in his pocket, and drives it off the lot, it is his property, and he has compensated the car company for the overall design and manufacture of the

⁷ Analysis of the Impact of Banning Aftermarket Parts, Property and Casualty Insurers Association of America, January 19, 2010.

⁸ The PARTS Act is similar to legislation that Rep. Lofgren introduced in the 111th Congress, H.R. 3059, the "Access to Repair Parts Act."

car. American consumers should not be forced to pay a monopoly price on a part such as a fender or a quarter panel whenever it has been damaged in an unexpected accident and needs repair. Yet Americans will find themselves unknowingly in just this situation as car companies enforce their design patents on collision repair parts against alternative suppliers – unless Congress enacts the PARTS Act. The PARTS Act addresses the problem in a properly balanced manner that is similar to how Europe and Australia have confronted identical concerns regarding the preservation of competition for collision repair parts.

The cost of car ownership is already significant and Americans are increasingly dollar conscious in these tough economic times. We believe it is in the public interest to ensure that U.S. patent law does not eliminate a place in the market for less-expensive, but perfectly functional alternative collision repair parts. The PARTS Act does not mandate the use of alternative collision repair parts, nor does it have the government facilitating new entry in the marketplace. Rather, the legislation would simply preserve the traditional place in the market for competition in the sale of collision repair parts. Consumers deserve it.

Conclusion:

We are not here today to advocate for the use of one type of part over another, but we are here in support of a measure that we believe would clearly benefit consumers regardless of their choice. At its core, this is a consumer issue; the costs of auto body repair are borne by all consumers who drive, either reflected in their insurance costs, or directly when they pay for repairs themselves.

In short, we believe that the PARTS Act will preserve competition in the market for collision repair parts and benefit consumers by helping to keep the cost of car ownership as low as possible. We want to thank you again for holding this important hearing and thank Representatives Issa and Lofgren for their continued leadership on the PARTS Act.