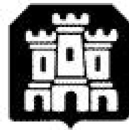

BRIEFING PAPER TO DTI CONCERNING THE DETRIMENT IMPLIED BY THE DRAFT DIRECTIVE CONCERNING PRECIOUS METAL ITEMS

April 2003

Introduction

This further briefing paper is provided by the British Hallmarking Council to the Department of Trade and Industry in response to a request for further clarification of the reasons for Councils opposition to the draft Directive concerning legal and administrative arrangements for precious metal items. It should be read in conjunction with the briefing paper on the same subject dated 8 January 2003, a copy of which is in Annex A.

Executive Summary

This further briefing paper has been researched and is based on such evidence as is available. In particular, it draws on policy statements on consumer protection from the European Parliament and Commission, it records the highly relevant judgment given under European Law by the Advocate General in the Houtwipper case, it gives graphic examples of the failure of unrestricted systems of marking in different countries, it makes comparisons in recent performance in jewellery manufacture between certain EU states and it draws attention to the pro-hallmarking policy of the UK consumer bodies, the retailers' organisation (the NAG) and Trading Standards. It also notes the substantial additional public resources that would be required effectively to police a manufacturers' marking system.

This evidence has served to reinforce the Council in its belief in the essential need, if at all possible, of retaining the UK practice of independent marking.

The experience of markets worldwide where regimes exist which are similar to that which would operate under Annex III of the Directive – marking by manufacturers under lax or ineffective disciplines – presents an almost conclusive case against Annex III: that is, unless we are prepared to lay open our consumers to the sort of exploitation, by chance or deliberate fraud, which is prevalent in those market places.

As the paper concludes, Council believes that, in theory, it should be possible to tighten up the controls on manufacturers' marking under Annex II so as to give consumers and the trade adequate protection. However, we doubt that delivery of and effective policing of such a regime could be ensured throughout the EU.

History and purpose of hallmarking

A system of compulsory hallmarking has existed in the UK since at least 1300.

The purpose of compulsory hallmarking has always been and continues to be to provide a guarantee of quality: that is to say, a guarantee of precious metal fineness to those concerned with an article. It provides a level playing field for manufacturers and importers, and provides a guarantee to the ultimate consumer.

Hallmarking has, incidentally, also provided a valuable marketing tool.

Hallmarking in EU countries

Hallmarking is not a system peculiar to Britain. In the EU France, Ireland, the Netherlands, Portugal and Spain have compulsory hallmarking systems. Nine of the ten countries due to join the EU in May 2004 also have such systems. Austria, Belgium, Denmark, Finland, and Sweden have voluntary hallmarking systems. Germany, Greece, Italy and Luxembourg have no independent systems. In these nine countries manufacturers regulate their own activities by self-certification, or there is no certification at all.

The Vienna Convention

The UK was a founder member of the Vienna Convention on hallmarking which has enabled the promotion of cross border trade in jewellery and silverware since 1972 by way of mutual recognition of the CCM hallmark. The eleven participating countries (eight being members of the EU) are Austria, Czech Republic, Denmark, Finland, Ireland, Netherlands, Norway, Portugal, Sweden, Switzerland and the UK. In 2002, 18 million articles were marked with the CCM mark in the UK enabling UK manufacturers to export with confidence.

The Houtwipper Judgment

The draft Directive is intended to "approximate" ie draw close together, the different systems in the EU, and it is driven by those countries who do not have a system. Their desire is to try to make their self-certification system equivalent to an independent hallmark. This results from the effect of the judgment of the European Court in the Houtwipper case, decided in 1994.

This vital ruling made permissible inter-Community trade, subject to certain strict criteria, without the need for visiting and marking by the importing member's state, and the Advocate General ruled it was legitimate under European law for a member state to protect its consumers through a system of independent marking. The draft Directive would effectively circumvent this ruling.

In his summing up of the Houtwipper judgment, the Advocate General gave the following opinion. "There is no doubt that controls and hallmarking carried out by an independent body have a more significant preventative effect and better protect consumers than when the hallmarking is carried out by the manufacturer himself. In this field frauds constitute a foreseeable risk and the member state must be free to refuse to accept that criminal liability a posteriori is sufficient assurance against such a risk".

The effect of Houtwipper was to make it legitimate for hallmarking countries to ban sales of imported precious metal goods unless those goods were marked in accordance with the standards applicable in hallmarking countries; despite the challenge, the Court decided that it was perfectly right for member states to safeguard their consumers via a compulsory independent hallmarking system, whether the system was operative in that or another EU country.

So, the purpose of the draft Directive is to circumvent the Houtwipper decision, and allow all three types of system to apply across the EU, for the benefit of manufacturers and importers in non hallmarking countries, so they can attempt to increase their market share in hallmarking countries, to the detriment of " local " consumers, traders and manufacturers. The hallmarking countries have two routes for mutual trading by which goods can move freely within the EU, the Vienna Convention and the Houtwipper judgment. The problem exists for those countries without any hallmarking system.

Consumer Interests Paramount

Council is charged with advising the Secretary of State for Trade and Industry in relation to the adequacy of facilities for the assaying and hallmarking of articles of precious metal in the UK, the primary purpose of hallmarking being, of course, to safeguard consumers.

A primary purpose of any Directive to "harmonise" legal systems in the EU should also be to safeguard consumers. This principle is to be found in Article 100a of the EEC Treaty, which in turn has been discussed and adopted as a principle on many occasions since then. Particular reference is made to the European Press Release dated 6 May 2002 entitled "Commission to adopt new Consumer Policy Strategy". That document begins by stating that the new consumer policy strategy which the Commission was due to adopt on 7 May would be based on three objectives - a high common level of consumer protection, effective enforcement of consumer protection rules and the involvement of consumer organisations in EU policies. Further, reference is made to the adoption by the European Parliament of the Commission Green Paper on the future of EU Consumer Protection - debate and vote on 13 March 2003 - Doc.A5-0423/2002. Importantly, it is stated in that report that "harmonisation should not result in the lowering of the protection to consumers achieved under certain national arrangements". Further that "MEPS also emphasise the need to enable the consumer to make an informed choice…."

The proposed Directive fails to meet any of these requirements.

Hallmarking Best For Consumer Protection

Council contends that it is self-evident that consumers can better be protected by a compulsory independent system of assay and marking, than by any other means. A self-monitoring system run by manufacturers (whether under the auspices of a system such as ISO or otherwise), cannot provide the same level of protection. In this respect Council accepts and agrees with the Houtwipper judgment.

Confirmation can be found in a study by Eindhoven University of Technology entitled "Qualitative Assessment of Draft Procedures for Declaration of Conformity d.d. 93.10.14 Concerning Fineness of precious metals", a copy of which is in Annex B.

It is also possible to demonstrate the relative effectiveness of hallmarking by comparing the available statistics and evidence relating to undercarating found in compulsory hallmarking countries, countries with voluntary hallmarking and countries with no independent systems.

In a report by the Holland Assay Office, based on official statistics provided by Denmark, Norway and Dubai, a posteriori testing on the market showed the following 'reject undercarated items of jewellery'.

Year	Denmark	Norway % of rejected articles	Dubai
1996	2.9	-	-
1997	4.5	8.7	34.0
1998	4.5	7.3	8.0
1999	2.5	5.8	18.0
2000	3.1	-	7.0

Source: Waarborg Holland

Extrapolation from these statistics for the UK market in 2002 when 34,170,255 articles were hallmarked, would mean that at the lowest percentage of 2.5% (in Denmark in 1999) there would have been 854,256 undercarated articles, and at the highest percentage of 34% (in Dubai in 1997) there would have been 11,617,886 undercarated articles on the UK market and the same number of cheated members of the public.

Austria, which moved to voluntary hallmarking in 2002 (the most recent country), has found that in its first year the frequency of inspection will be once only in 18 months to cover 5,000 premises. Indeed, factory and market surveillance after this first year found non-compliance with the law at a staggering rate of 14.8% of articles! Based on this experience, Friedrich Kahr, the Assay Master in Vienna both before and after the amendments to the regulations, said: "Summarised we dropped a strict and reasonable system with high protection for consumer and trade, and settled for a liberal one with advantages especially for producers and importers. My recommendation for the UK, try to keep your system!"

The situation in the United States which has weak laws and weak enforcement further illustrates the problems of an a posteriori system. The 'National Jeweller' magazine from July 1 2002 prints " The Jewellers Vigilance Committee has targeted mall retailers across the country, looking for undercarating violators. The violators, found in 74 malls from California to New York, sold charms, bracelets and earrings mostly stamped as 1o-karat gold but without registered trademarks, the JVC contends. JVC investigators purchased 173 suspected counterfeit items. Of these untrademarked products, 128 were found to be undercarated. The culprits were mall retailers in Arizona, California, Florida, Indiana, Louisiana, Michigan, Missouri, New Jersey, New York, North Carolina, Pennsylvania, Texas and Virginia".

Just prior to Christmas 2003, the Jewellers Vigilance Committee had to draw the widespread problem of undercarating to the attention of the US public through national TV on the Dan Rather 'Eye on America' news report, and through the national newspapers.

An article from the internet magazine "Business Line" shows that of the 8,000 consumers in India that had their jewellery checked, 4,800 had jewellery of a substandard fineness (60%).

Detriment to the UK consumer

Council draws the attention of DTI to the fact that as compulsory independent hallmarking is the best consumer protection system concerning precious metal items the absence of such hallmarking can only be detrimental to the interests of consumers.

There is no evidence of any demand from consumers for compulsory hallmarking to be abolished.

Independent market research evidence, undertaken by NOP in 1999 shows that in the UK buyers of the majority of precious metal items sold (ie less sophisticated buyers) rely on the presence of hallmarks as the only guarantee of quality they need before buying an article.

According to the World Gold Council, one third of all the gold jewellery sold in the EU is sold in the UK.

Statistics demonstrating the relative growth or decline of the size of markets for precious metal items in EU countries reveal that there is a trend of market growth in compulsory hallmarking countries and decline in others. The table below shows the fine gold jewellery consumption for Italy, UK, France, and Germany for the ten years from 1992 to 2001. It is noticeable that in the UK and France where hallmarking is compulsory jewellery purchasing has been strong while in Italy and Germany it has been in significant decline.

Jewellery Consumption in tonnes of fine gold

				Germany
1992	167	44	44	68
1993	133	40	46	68
1994	121	42	45	67
1995	114	41	48	61
1996	105	43	49	57
1997	111	54	50	54
1998	108	64	56	50
1999	101	65	57	48
2000	92	82	52	34
2001	92	82	52	34

Source: GFMS Gold Survey 2002

The statistics support the view of Council that compulsory hallmarking serves to boost consumer confidence and hence the reputation and attraction of the precious metal items market in the UK. It is Council's strong belief (confirmed by the market research evidence as above) that the abolition of compulsory hallmarking will have the converse effect, and that consumers in the UK faced with marks on items they cannot recognise or interpret, coupled with increased reports of growing levels of undercarating will shun jewellery and silverware.

Council's belief that undercarating will increase is not just based on the evidence referred to above but also on the reject statistics of the Assay Offices for 2002. In that year ,approximately 34,000,000 items were marked, and 66,000 items (0.19%) were rejected by Assay Offices for failing to achieve the minimum fineness. Those items were submitted by manufacturers and importers in the belief that they were as described on the documentation relating to them, and so it is reasonable to expect that all those items would be released to the market if self-certification was allowed.

Detriment to the UK retailer/wholesaler

Although consumer protection is of paramount importance Council draws attention to the fact that dealers in the UK will suffer as a consequence of the detriment to the UK consumer as mentioned above.

Currently, the UK retailers and wholesalers are protected by a UK hallmark, or Convention mark, or a national mark recognised as equivalent under the Houtwipper judgment. All of these can be readily traced back to the manufacturer or importer. Under the proposed Directive this protection will be sidelined. Retailers will be in line for potential prosecution under trade description legislation if jewellery is found to be undercarated.

Detriment will also follow from the fact that dealers will be less certain of the quality of the items which they are describing and selling. As a result, and as a consequence of the rise in claims and returns, their own confidence will be affected. The level of undercarating already highlighted for Denmark, Norway and Dubai supports this. Further, as a result of damage to consumer confidence and willingness to buy, the market will shrink to the detriment of dealers revenues, and profits, and very importantly levels of employment in the jewellery industry. Confirmation that dealers share this view is to be found in the support by the dealers association, the National Association of Goldsmiths, for the position taken by Council concerning the Directive, and in the sample letters from dealers copied herewith in Annex C.

There will also be practical issues for retailers especially relating to traceability and responsibility of imported products. For example, new manufacturers or importers with the same type of product could start doing business on the same day in say Athens or Aberdeen. There is no explanation in the Directive about an eye line for differentiation and recognition of marks. A central database containing thousands of registrations appears unrealistic, incapable of being financed and unlikely.

The detriment suffered in the UK in these respects will be greater than that suffered elsewhere in the EU, for the reasons already given.

Detriment to the UK Manufacturer

The UK manufacturer will face competition from overseas from jewellery landed in say Finland (where enforcement is not strong), which will come legally onto the UK market unchecked. There may also be a temptation for EU manufacturers, unable to compete with cheap labour from abroad, to try to compete by undercarating.

It is well known from other industries that inspections a posteriori tend in the main to be carried out with more frequency and diligence on 'friendly' organisations. Those who are more hostile to inspections get visited less, if at all. It's human nature. This means that open, bona fide businesses tend to get far more attention than the less scrupulous organisations, thwarting the intentions of the Directive.

From time to time in the past it has been claimed on behalf of some manufacturers that they would benefit by the abolition of compulsory hallmarking as associated costs would be saved. That claim was disproved by DTI's own researchers recently in their conclusion that from the economic point of view of manufacture hallmarking was "broadly neutral".

Nevertheless Council is reinforced in its believe that its objection to the Directive is also in the interests of manufacturers (because of the prospect of all the causes of detriment to retailers also affecting them and the prospect of floods of imports of untested items from large manufacturers in Italy and elsewhere) by the broad agreement reached about the Directive between Council and the BJA.

Detriment to the UK taxpayer

Council also takes the view that the costs of marking and enforcement systems should be taken into account by DTI. There is no cost to the State of assaying or marking goods, and as a result of the efficiency of the Assay Offices the enforcement authorities, Trading Standards Departments, can treat precious metal standards as low priority, and as requiring little resource.

Under the present system all assay charges are passed on from manufacturer or importer to the retailer, and then on to the final consumer. This means that only those people who are buying jewellery, i.e. are in market, pay for hallmarking. Taxpayers who are not buying jewellery are paying nothing.

On the other hand under the Directive, the presumption is that the cost of supervising the market will have to be paid by all taxpayers whether they are in market or not, under an increased a posteriori market surveillance system with more central registers and administration, more beauracracy, and at increased cost to all taxpayers.

The London Assay office has undertaken an exercise that indicates it would need to increase its staff by over 50% to carry out inspection visits to its 3856 customers at a level similar to its current frequency of testing.

Council apprehends that if implemented, the Directive will necessarily have the effect of destroying the existing system in the UK, with all its advantages, as manufacturers are driven to the easiest and lowest cost option route for them of self-certification. It could be that hallmarking activities at all the assay offices become loss making and so unviable, so that Annex IV could cease to be an option because there is no service provider

Conclusion

Council, having carefully revisited the subject and assembled and reviewed the available evidence, concludes as follows:

- that, on the evidence, the interests of consumers, retailers, manufacturers and taxpayers in the UK would only be adversely affected by the introduction of the Directive as drafted and that its introduction would be to the advantage of other member states to the detriment of the UK, and should therefore be opposed as it stands; but

- that a Directive containing only Annex IV would be acceptable;

- that the draft Directive runs contrary to the judgment of the Advocate General given in the Houtwipper case under European law, and conflicts with the policy objectives of the European Parliament and the Commission in regard to consumer protection;

- that adequate procedures and controls on marking by manufacturers under a strengthened Annex II would be unlikely to be achievable or enforceable throughout the EU; but

- that if total opposition to the draft Directive has to be yielded a Directive containing the best obtainable Annex II [and IV but not III] should be negotiated.

Sir Adam Butler
Chairman
British Hallmarking Council
17 April 2003

ANNEX A

`HARMONISATION and the draft DIRECTIVE

Briefing Paper from the British Hallmarking Council

Background

This Paper should be read in conjunction with the BHC'S policy statement of September 10th, 2001 on Hallmarking within the European Union.

In essence, Council's policy is strongly to prefer the continuation of the current practice of compulsory assaying and marking by independent, third parties. It believes that the free and fair flow of goods in precious metals between member states can be achieved, either through an extension of the membership of the International Convention on Precious Metals to all member states [currently eight belong]; and /or by following the "mutual recognition" route charted by the Houtwipper judgement. [The UK recognises Irish, French, Portuguese, Danish, Finnish and some Spanish marks by this route]. There are therefore already two routes for free movement of goods between hallmarking states. It is the other five states which have the problem!

Further, the BHC policy is to accept a Directive containing only Annexe IV – with appropriate other amendments.

If marking by manufacturers is to be permitted under a Directive, the BHC policy is that this must be subject to strict provisos. These are that such marking is subject to proper quality assurance [QA] procedures and also to strict third party monitoring; further, that such procedures and monitoring should combine to ensure that the consumer – and the trade – receive the same level of protection and comfort as given by present UK practices.

The policy Declaration subscribed to by the BJA, the NAG, LACOTS and the UK Assay Offices, as well as the BHC, should also be read. Essentially, this Declaration as regards marking by manufacturers is virtually identical in its approach to the draft Directive as that of the BHC.

The Brief

The purpose of any form of marking articles in precious metals is to inform and protect the public, as well as to assure the trade that it is dealing in goods of guaranteed quality; indeed, to assist in the regulation of fair trading. One consequence of the practice of hallmarking in the UK has been the establishment of a market "brand", which is increasingly valued by the industry and trade.

The above principles should guide UK negotiators.

Independent marking –

The BHC urges HMG not to abandon – or give the impression of abandoning – prematurely its previous, stoutly defended position: that independent testing and

marking should continue in the UK and be the norm within the EU. The position is not lost.

There are many supporting arguments and factors:

- It is by no means clear that the "blocking minority" has ceased to exist. Internationally, there is evidence that interest in independent hallmarking is very much "alive" and increasing. It should be recalled that the UK was a major player in forming a blocking minority in 1993/4, although this never had to be deployed as such;
- All but one of the ten states due to accede to the EU in 2004 currently practise compulsory, independent hallmarking;
- Eight EU states subscribe to the International Convention, with its agreed standards, independent marking and common control mark which allows for free circulation of goods within participating member states. At the encouragement of DTI, accession to the Convention has been made easier, and many countries including China are pursuing membership;
- Within the EU, the principal states which are not members of the Convention are Germany, Italy, France and Spain, but the latter two are covered by Houtwipper. Italy has recently put forward proposals which require marking by its "assay offices" in such a way as to meet the legal requirements of other member states. These should be actively investigated and encouraged;
- In the United States, which is the biggest jewellery market in the world, manufacturers and importers currently self-mark and certify their jewellery. The US jewellery trade's own watchdog - the Jewellers Vigilance Committee - immediately prior to Christmas issued a series of warnings to the public concerning the high level of cheating through undercarating on the US market. This was sparked by tests which showed that 64% of items purchased at random were undercarated. Alarmed by this finding, the bona fide US jewellery industry is seeking to find a solution through a third-party accredited marking system;
- Support for a Directive and for independent testing and marking are not incompatible. A Directive containing only Annexe IV, with the exclusion of Annexes II and III, would provide the desired harmonisation. This would be a logical extension of the Houtwipper judgement, and – as a negotiating card – member states could be left free to pursue their own domestic regimes. It is important to note that it is the non-hallmarking states which have difficulty with a robust Directive;
- Concerns re the quality of imports also provide arguments for retaining the status quo. The import by manufacturers of finished or part-manufactured goods into the EU is a fact and most likely to increase. Some EU manufacturers actually have factories elsewhere which apply the marks before despatching to the "mother" EU company. Importers equally have no direct control over their merchandise. In the UK at present, about half of the articles tested by the Assay Offices [or parts of them] have been imported. It is very difficult to see how quality control and monitoring of such goods could effectively match up to the sort of procedures and disciplines referred to above as necessary for achieving adequate consumer and trade protection, if

independent marking was no longer compulsory. It is understood that there is a developing problem in Italy because of this growing practice.

Manufacturers' marking –

If it is clear that a sufficient, dominant majority in favour of a Directive containing provisions for marking by manufacturers really does exist, the BHC [obviously] accepts that more good can come from actively seeking to achieve improvements than from a negative stance on the sidelines. However, BHC recommends the development of a plan for the deployment of delaying tactics in conjunction with sympathetic states, if the preferred objective – the continuation of compulsory, independent marking – is achievable in that way.

Desirable improvements in any regime involving marking by manufacturers would include:

General:

- UK negotiators should seek to draw a distinction between the "Quality Assurance route" [for marking by manufacturers] and the more simple "manufactures' marking" .The search for achieving an acceptable Annexe II should be driven by the strict demands of QA as opposed to the laxer regime of Annexe III; Annexe II should be tightened so as to give to the consumer and the trade the same degree of protection and comfort as now.

Annexe II

- Manufacturers' approach to and methods for the control of quality must operate throughout manufacturing and handling processes as well as in marking – and assaying, if appropriate; they must conform to certain acceptable QA Standards ie. EN 29001. Manufacturers' testing laboratories must be accredited to ISO 17025 [as of course must an independent laboratory];
- These must be supported by monitoring by genuine independent, qualified third party bodies;
- As a strengthening of the above, one proposal could be that each batch should be sample-tested [but not marked] by such bodies;
- The Directive must make clear the frequency with which the monitoring of manufactures must be carried out. Standards for market surveillance at retail levels should also be set.

Annexe III

It is BHC policy that this Annexe should be removed from the Directive. We recognise, however, the UK negotiators may have to deal with the proposal that a less demanding regime under Annexe III should be permitted for those states who wish to apply it for domestic transactions only. At first sight, such a proposal might appear harmless. However, we believe that in a "single market" situation there is a very real -

and unacceptable – risk of such "domestic" articles leaking into general, EU circulation.
The proposal should therefore be firmly resisted, and Annexe III struck out of the Directive.

Traceability

Traceability is crucial to the success of any monitoring regime. Therefore, in the same way as any Certificate issued by a notified body or testing house would identify its source so should articles marked by a notified body, such as a UK Assay Office, carry its unique "hallmark" to allow traceability, and therefore accountability by that body. [Negotiators should also bear in mind the value of a UK hallmark as a brand/marketing aid].

Common identifying mark

A mark should be agreed for application to all goods meeting the requirements of the Directive and therefore permitted free circulation within the EU, similar in operation to the Common Control Mark of the Convention.

ACB
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