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CRITERIA FOR THE ADMISSIBILITY OF "PURE ECONOMIC LOSS" AND "PREVENTIVE MEASURES" TAKEN TO PREVENT OR MINIMIZE "PURE ECONOMIC LOSS"

Note by the French delegation

1 The criteria for the admissibility of "pure economic loss" and "preventive measures" relating thereto should be considered in the light of decisions already taken by the Executive Committee of the IOPC Fund. However, because the Fund's practice is recent, and because of the context in which some specific decisions were taken, reference to this practice should not preclude the Working Group from establishing new principles which, if they had been applied in the past, might have led to the rejection of some of the claims that were allowed.

2 National law is clearly a useful source of reference, but should not prevent the IOPC Fund from determining its own criteria for admissibility, regardless of any solutions evolved in the jurisprudence of the courts of Member States. One of the Fund's major objectives under the founding conventions is to arrive at out-of-court settlement of claims for compensation. The compensation awarded in national courts should therefore be the exception in marine oil pollution cases. Indeed, because of that exceptional nature, it is clear that any decisions in litigation will be influenced by the rules that the Working Group has been asked to establish.

3 To achieve this result, the rules must be clear and flexible enough to adapt to each case. Moreover, account must be taken of the rather different approaches to "pure economic loss" in civil law and in common law so as to avoid rejection by either system. Such a rejection might come from the courts in legal proceedings, or even from the victims if the Fund's compensation proposal was too far removed from national legal concepts.

PURE ECONOMIC LOSS

4 Definition of the concept

4.1 Issues involved in definition

The first question that arises is whether there is a need to define the concept of pure economic loss.

The reply to this question is important, because it will necessarily affect the way in which the problem as a whole is perceived.

If a definition of the concept is given, the criteria for admissibility will be determined in accordance with that definition and will therefore be abstract and general.

This theoretical approach to the question will allow major principles to be identified and subsequently adapted to the situations facing the IOPC Fund, and perhaps to be interpreted by national courts in the light of the applicable laws. However, the need to make Fund practice uniform and to have pre-established rules known to all would not be fully met.

The second possible approach would be to exclude any definition of the concept of pure economic loss and to identify technical criteria for each category of claim. The Intersessional Working Group, in this case, would establish criteria for admissibility on the basis of the list of claims already submitted to the IOPC Fund. Subsequent application of the criteria to claims of a new kind would be made by the Director when analogy was possible and by the Executive Committee when it was not.

This pragmatic approach would keep the IOPC Fund's decisions purely technical, away from any legal debate. All the interests concerned - victims, P & I Clubs, contributors, even national courts - would know precisely what were the criteria for the admissibility of claims. It would, however, probably be necessary for the Secretariat to update the "compensation guide" periodically for approval by the Assembly or the Executive Committee.

4.2 Status of the question

4.2.1 The concept of pure economic loss does not seem to be specifically defined in the various national laws. In **French law**, economic loss ("préjudice économique") is defined in legal writings as loss or damage existing independently of any injury to persons or physical property. This theoretical definition has little effect in compensation practice, since jurisprudence does not stop at the nature of the loss or damage but rather at the traditional criteria for admissibility (direct, actual and certain damage) which, if met, give rise to full compensation, the discretion of the judge playing an important part in determining the amount.

4.2.2 At the international level, the 1969 Civil Liability Convention does not refer to "pure economic loss" in its definition of "pollution damage".

The Protocol of 1992 amending that definition indirectly confirms the principle of compensation for "loss of profit", but does not give a comprehensive definition of "pure economic loss".

4.2.3 However, in a draft working document for the 1994 Sydney conference on the assessment of claims for pollution damage, the CMI gives the following definition:

1°) *For the purpose of these Guidelines the following definitions are used:*

(a) *"Consequential loss" means any reasonable financial loss sustained by a claimant as a result of physical loss of or damage to his property through contamination by oil;*

(b) *"Pure economic loss" means any reasonable financial loss sustained otherwise than as a result of such physical loss or damage."*

[Draft CMI Guidelines on assessment of claims for oil pollution damage, Annex to draft document dated 10 August 1993].

4.2.4 International insurance practice seems to follow similar lines. Within "non-material loss" (i.e. monetary loss suffered by a victim as the result of an accident), it distinguishes "non-material loss or damage consecutive upon material damage or bodily injury" and "pure non-material loss or damage".

For instance, the ASSURPOL standard contract, which is increasingly being used for pollution risks in France and elsewhere in Europe, defines *"pure non-material loss"* as *"any monetary loss resulting from deprivation of the use of a right, from the suspension of a service by a person or by a movable or immovable item of property"*. (Standard ASSURPOL contract, general conditions, Article 1.9).

5 IOPC Fund practice

5.1 If the concept of loss or damage existing independently of any damage to physical property belonging to the victim is adopted as a general criterion (and not strictly as a definition), it is possible to find in the IOPC Fund's previous practice a relatively large number of claims that have been accepted on such grounds.

Most of the claims were submitted in recent cases (HAVEN, AEGEAN SEA and BRAER). Others were made in less recent accidents (TANIO).

To obtain a full picture of the decisions taken by the IOPC Fund, it would be useful if the Secretariat could establish a basic document detailing each claim, wherever possible spelling out the terms in which they were accepted.

5.2 On the basis of an introductory analysis by the French delegation which, it must be stressed, is probably of a relative nature, a preliminary classification of this type of damage can be made, and eight categories of claim corresponding to three types of activity can be identified.

5.2.1 Activities related to the living resources of the sea

[1] Fishing

- sea fishing (excluding damage to equipment)
- shellfish gathering

[2] Farming of marine products (excluding damage to plant)

- fish farming
- shellfish farming
- cultivation of algae

[3] Related activities

- processing plants

- handling (unloading of fish)
- supply of specialist equipment (nets, pallets, ice, etc.)
- marketing of produce

5.2.2 Activities connected with seaside tourism

[4] Restaurants, beach facilities, hotels (excluding damage to installations).

[5] Related activities

- suppliers of tourist services (accommodation and travel agents)
- retail trades

[6] Local authority tax revenue

5.2.3 General maritime activities

[7] Use of seawater

- electricity power stations
- purification plants
- desalination plants (this theory to be checked).

[8] Use of the sea

- boat hire - cargo inspection
- leisure activities

5.3 In addition to this type of claim, which corresponds to specific economic activities, the IOPC Fund has had to deal with other claims of a more general nature:

- claims by employees under contract, because of lay-offs or reduction in activity;
- claims for reimbursement of legal expenses involved in submitting compensation claims;
- claims for compensation for exceptional cash expenditure.

5.4 One point relating to criteria for the admissibility of claims arises from this preliminary classification. The 1969 Civil Liability Convention and the Protocol of 1992 thereto refer only to loss or damage caused by contamination.

This general criterion is hard to apply to "pure economic loss", whether alleged by victims with a "primary" activity connected with the sea (fishing, breeding, hotels), or by those with a related activity (processors, retailers, etc).

For fishermen and breeders, the IOPC Fund has several times used the concept of exclusion zone to solve the question of the link of causation with the physical pollution. When the victim exercises his activity within this zone, the existence of loss or damage "caused by contamination" seems to be assumed. However, the claimant has to prove contamination and its effects on activity outside the exclusion zone (BRAER FUND/EXC.35/10, paragraph 3.4.12).

This criterion, which on the face of it seems reasonable, is in fact problematical (at least as far as fishing is concerned).

Without providing any certainty as to the real connection between the alleged loss or damage and the physical pollution, it involves a decision by the public authorities (the establishment of an exclusion zone) which could legally be considered as breaking the link of causation in the same way as the measures to destroy produce for reasons of health or the measures to create a safety barrier on land around the polluted areas.

Generally speaking, direct recourse to the criterion of loss or damage by contamination has proved empirical, and this has led the IOPC Fund to seek other criteria that correspond better to the nature of the loss or damage, while retaining physical pollution as a reference.

5.5 This development may be compared with the "bright line rule" in some common-law countries (the loss must result from damage to property belonging to the victim). In Canada and Australia the requirement of a link with damage to property belonging to a victim has been relaxed in recent years by the criterion of "proximity". The concept of reasonable proximity is one of the alternatives adopted by the IOPC Fund on several occasions in different forms:

- **the damage was foreseeable** (BRAER - fish processors - FUND/EXC.34/9, paragraph 3.3.19)
- **dependence on fishing** (AEGEAN SEA - unloading of fish - FUND/EXC.35/10, paragraph 3.3.18)
- **geographical proximity** (HAVEN - retailers - FUND/EXC.35/10, paragraph 3.2.7).

6 Definition of new criteria of admissibility

The definition of new criteria of admissibility for pure economic loss will depend on the method of work adopted (see point 4.1). Some major lines of thought may already be suggested.

6.1 First, the practical use of the criterion of "loss or damage by contamination", which leads to unclear solutions, should be abandoned. In many cases, attempts to include a loss under the definition of loss or damage by contamination are artificial and do not reveal the legal elements that have led to the decision.

Other criteria of a legal nature can give a better idea of the actual consequences of an incident of pollution by contamination.

6.2 The **"reasonable proximity"** criterion is one of the most promising lines of research, since it can be transposed to civil-law countries as well as to some common-law countries. A study could be made to create a set of sub-criteria to establish the existence of such "reasonable proximity" between the alleged loss and the pollution (e.g. geographical proximity, proximity in activities, etc.).

6.3 The concept of **economic dependence** (whether or not there are substitute activities, the percentage of the activity affected within the claimant's overall activity) might also play a useful part, either as a principal or as a supplementary criterion.

6.4 If the Intersessional Working Group takes this course (already taken in practice by the IOPC Fund), there will be a need to re-examine all the cases in which there is a contract between the claimant and the act causing the damage.

At the moment there is a certain inconsistency in the matter. For example, the IOPC Fund has excluded compensation for workers laid off or put on part-time work because of the existence of a contract of work which breaks the direct link of causation between their drop in income and the pollution.

However, although there was absolutely no doubt that the salmon processors had a contract for the supply of goods with the breeders, they were compensated for the consequences of the slaughter of salmon in the exclusion zone. Legally, however, contracts for the supply of goods are also grounds for breaking the link of causation between the loss of earnings of the processors and the pollution.

In the matter of contractual link, a distinction might be drawn between "long-term" contracts (for the supply of goods) and ad hoc contracts (e.g. for transport).

By application of the criterion of dependence, contracts in the former category would be neutral, i.e. they would not entail a break in the link of causation regarding compensation for possible loss suffered (to the extent, of course, that reasonable proximity is established), whereas the "ad hoc" contractor would have to prove the importance of the contract within his entire business activity as well as the fact that there were no substitute activities.

6.5 The classification of "pure economic loss" made on the basis of IOPC Fund practice shows that the claims refer either to activities open to all or to **rights protected by law.** In the latter case, which concerns beach facilities, fishing and shellfish gathering, in a great many States parties to the Fund Convention the possession of a valid permit would be a determinant criterion for admissibility.

6.6 One of the essential criteria for admissibility of claims remains the **economically quantifiable nature** of the loss.

For claims relating to "pure economic loss" the IOPC Fund has already developed a satisfactory practice. The claimant generally has to substantiate his turnover for the last few years and produce certified accounts which are compared whenever possible with the results of operators in the neighbourhood who have not been affected by the pollution.

In order to allow satisfactory examination of certain claims that are hard to check, the production of tax returns for the last two or three years might be required systematically.

6.7 It seems inevitable that the direct link of causation (which might be assimilated to the "bright line rule" in common law) as the main criterion in matters of "pure economic loss" must be abandoned if satisfactory and lasting solutions are to be found. However, this does not mean opening the door to all claims, thus going beyond the framework of the initial conventions. On the contrary, only by identifying new criteria corresponding more closely to economic reality will it be possible to restore to its true dimensions the concept of "loss or damage by contamination" and to retain the technical character of the IOPC Fund's financial intervention.

6.8 The application of new criteria for admissibility will probably involve the rejection of some claims that might previously have been met and acceptance of others that might have been rejected.

In order to measure the precise financial impact of the decisions to be taken by the Intersessional Working Group, the Secretariat might make a simulation on the basis of a case that has already been settled (the BRAER would probably be a good example).

6.9 In addition to all these criteria, the "reasonable nature" of claims in respect of pure economic loss would have to be verified systematically when their admissibility is considered.

This general criterion has traditionally been adopted by the IOPC Fund, in particular for the reimbursement of clean-up operations at sea or on shore, and it was recalled at the 35th session of the Executive Committee in connection with publicity campaigns. It should make it possible to reduce the amount of compensation when the claim is admissible in principle, by application of the other criteria, but when the amount is clearly excessive.

PREVENTIVE MEASURES

7 Once the principle of compensation for "pure economic loss" is admitted under the Conventions of 1969 and 1971, the question of taking account of possible "preventive measures" relating to such loss has to be considered. The concept of such preventive measures is easy to understand, since recent Fund practice has demonstrated some of its practical applications, but it is essential to define its limits very clearly in order to maintain a compensation system that is economically viable.

8 At recent sessions of the Executive Committee, three kinds of measure that can be considered as preventive measures were referred to either directly or implicity, namely:

- publicity campaigns;
- lay-off of employees;
- destruction of produce.

In view of the limited number of possible cases - probably few other than the three examples above - a case-by-case study could be made, following a reference to the relevant instruments.

Status of the question

9 According to the 1969 Civil Liability Convention, *"preventive measures"* means *"any reasonable measures (1) taken (2) by any person (3) after an incident has occurred to prevent or minimize pollution damage".*

Furthermore, the cost of such measures, as well as loss or damage caused by them, constitute pollution damage within the meaning of that Convention.

10 On the basis of the IOPC Fund's classic "jurisprudence" (i.e. by referring to the preventive measures relating to physical damage from pollution) some general remarks may be made with respect to the criteria for admissibility.

10.1 The measure must be **reasonable**

This first criterion does not mean that the claimant is obliged to get results. A preventive measure may still be reasonable even if it was not as effective as expected.

For the IOPC Fund the reasonable nature must be assessed on the basis, first, of the circumstances of the incident (and not a posteriori when the claim is made), and second, in the light of the technical know-how reasonably available to the entity that took the decision.

10.2 The preventive measure must have been **"taken"** when its reimbursement is claimed from the IOPC Fund. For preventive measures relating to pure economic loss, this apparently simple criterion may well be hard to apply. Recent experience shows that the persons likely to decide on such measures try to have the IOPC Fund meet their financial cost directly. The interpretation of the word "taken" must therefore be examined: does it refer to the decision or to the financial commitment?

10.3 The preventive measure may be taken by **any person**, that is, within the meaning of the 1969 Convention, *"any individual or partnership of any public or private body, whether corporate or not, including a State or any of its constituent subdivisions"*.

This latter general criterion must be carefully considered, especially as regards the question of destroying produce. When such a measure is decided upon by the public authorities, should it not be considered as a preventive measure taken by those authorities, who would be the only person qualified to claim compensation for that measure?

11 In addition to its traditional "jurisprudence" and the interpretation that may be made of the definition given in the founding instruments, the IOPC Fund has recently developed a specific practice with regard to preventive measures in respect of pure economic loss.

At the 35th session of the Executive Committee, new criteria introducing the further concept of "reasonable cost" were identified. There are four such specific criteria:

- *the cost of the measures proposed must be reasonable;*
- *the cost of the measures must not be disproportionate to the damage or loss that they are supposed to limit;*
- *the measures must be appropriate and offer a reasonable chance of success, and*
- *if a publicity campaign is carried out, the measures must be in relation to the reference markets that actually exist.*

Proposal concerning criteria for admissibility

12 Admissibility of claims relating to publicity campaigns

12.1 *Reasonable nature of the campaign*

Appropriate identification of objectives and reasonable chances of success (objectives in time: period after the incident and duration – and in space: local or regional campaign, etc.);

in relation to the markets actually involved (choice of media and public directly concerned);

data on the actual risk of damage to the activity concerned (production specific to the polluted region, date of pollution in relation to the tourist season).

12.2 Reasonable nature of the cost

Overall the claimant must be able to prove that he has made use of competition and has chosen the least costly solution (estimates to be produced).

In order to assess the reasonable nature of the campaign in relation to the damage it is supposed to limit, a detailed estimate of the damage, backed up by reliable documents, must be submitted in support of the claim.

Subject to all these criteria, and if, because of special circumstances, individuals (with the exclusion of public bodies) have had to take urgent measures, the IOPC Fund might meet the cost directly on the basis of a written agreement.

Otherwise there should be no compensation for publicity campaigns if the claimant is unable to produce a receipted invoice.

However, the fact that a campaign was financed from an item of the budget that is generally used for that purpose should have no effect on the right to compensation.

13 Admissibility of claims relating to lay-off of employees

The decision to lay-off or put on part-time working some or all the staff of an undertaking whose activity is directly affected by the pollution can be considered as a preventive measure to diminish the operating losses of that company.

In considering the criterion of proportionality of the measure to the damage to which it relates, several elements might be taken into account, including:

- the proportion of the activity affected by the pollution in the general activity of the undertaking;
- the characteristics of the jobs involved (level of skills);
- the state of the local labour market for such jobs (possibility of being taken on again when the activity starts up again).

The attention of the Intersessional Working Group should be drawn to the fact that any claims which may be submitted by the employees concerned who have not received satisfactory compensation from social welfare bodies, or claims by such bodies themselves, should be accepted as loss or damage caused by the preventive measures taken by the employer (see 6.4 above).

14 Admissibility of claims relating to the destruction of produce

IOPC Fund practice shows that the claims relating to loss or damage of this type arise from situations of several different kinds. The slaughter of the fish-breeders' intake can be justified by direct contamination. In such cases there is loss or damage to property and the claim must be dealt with accordingly.

However, the destruction may be justified not because of large-scale contamination but because of public health considerations or market reaction. In such cases, the pollution has indeed had an effect but it is difficult to assess its extent early enough to avoid an adverse effect on future cycles of production, which might have large-scale economic effects.

Thus the decision to destroy produce must be considered as a preventive measure and examined in the light of the relevant criteria. These criteria would of course be in addition to the technical criteria identified (reference samples, etc.).

This analysis would have the advantage of clarifying a situation which, in practice, has proved confusing.

If the destruction is the result of a decision by the public authorities, they must claim reimbursement and take the risk of their claim being rejected by the IOPC Fund after application of the criteria for admissibility. This would allow the claim to be examined objectively and would protect the IOPC Fund from the very strong pressure of the professions concerned.

If the destruction is the result of the personal choice of the undertaking, the identification of pre-established criteria will allow it to gauge the precise consequences of its decision.

The IOPC Fund will consider claims of this type but will no longer have to intervene in the decision-taking, which will be the sole responsibility of the director of the undertaking.

Alternative analysis of preventive measures

15 The three kinds of measure just considered in relation to the concept of "preventive measures" might also be considered as **"preventive measures"** taken by the victim to minimize his losses.

This approach, corresponding to a general principle of the law of liability found in all legal systems, has practical consequences on the solutions considered previously.

Unlike the "preventive measures" that can be taken by any person, this one has to be taken by the victim himself.

As far as the admissibility of claims relating to the destruction of produce is concerned (point 14), the assumption that it is for the public authority that took the decision to claim compensation would no longer be valid.

Similarly, employees laid off or put on part-time work (point 13) would no longer have the right to submit a claim for compensation on the basis of a loss caused by a preventive measure.

This would also apply to social welfare bodies.

ANNEX

ECONOMIC LOSS IN FRENCH LAW

By way of introduction, it should be explained that the notion of *"pure economic loss"* as such does not exist in French law.

We do however encounter the notion of economic loss, definable as a loss which exists irrespective of any damage to physical assets or to persons, although the concept is difficult to pin down in precise terms.

Traditionally, legal theory (B. Starck, HLJ Mazeaud, J. Carbonnier) and jurisprudence agree that the lucrum cessans, or loss of profit, and the damnum emergens, i.e. the losses actually incurred, are to be treated as a loss to be compensated. Loss of profit covers all the profits which have been forfeited by the actions of the third party liable. The losses incurred represent the degree of impoverishment occasioned by the act which inflicted the damage.

Accordingly, loss of profit, or even the unavoidable need to bear certain exceptional expenditure, is regarded as a form of damage which may give rise to a claim for compensation. The jurisprudence of the ordinary and the administrative courts is similar in this respect.

Although the application of the rule of French law as described above does not give rise to any objections unlike in some foreign legal systems, such as the jurisprudence developed from common law which only awards damages for *"pure economic loss"* where the loss results from the deterioration of physical objects (the bright line rule), its interpretation by the courts has however been somewhat restrictive.

We also find clauses in insurance policies which offer cover for pure economic loss. It is therefore appropriate to consider the present scope of such cover, since this may have a direct influence on the way the courts handle the concept.

I ECONOMIC LOSS IN THE FRENCH CASE LAW

There are two kinds of pure economic loss: loss of profit and additional operating costs.

A LOSS OF PROFIT

Economic loss is primarily a loss of profit, which may be experienced in different ways.

The extent to which it is reflected in court decisions depends on two fundamental criteria: the **degree of certainty** involved and the **direct connection** with the facts to which it is attributed.

1 A certain and direct loss of profit

This refers to losses which are certain and have been sustained or are bound to be sustained.

a) The administrative jurisprudence

- *"operating losses caused by the forced cancellation of a number of crossings"* when a passenger vessel was put out of action by an accident attributable to the port authorities (CE, 23 April 1986, Armement naval SMCF Sealink);

- loss of income suffered by a maritime freight company when the port was barricaded by fishermen, the port authorities making no attempt to prevent them (CE, 15 June 1987, Société Navale des chargeurs Delmas Vieljeux and others;

- operating losses suffered by a business owing to a delayed start-up caused by the cancellation of a building permit (CE, 23 December 1981, M. Stinco);

- loss of the intangible assets of a business forced to cease activity owing to the execution of public works (CE, 6 February 1981, SA des Comptoirs Français);

- loss by a hotel of some of its customers due to the building work involved in laying out a car park (CE 26 February 1986, Entreprise Blondet; also CE 11 October 1985, Bouillon);

- loss of sales by a fishmonger who was illegally refused a permit to buy at auction (CAA Nantes, 18 December 1989, Mme Méléard).

Traditionally, therefore, the administrative jurisprudence recognizes that compensation may be awarded for all types of loss, including loss of property which includes pure economic loss.

The principle of awarding compensation for such losses is explicitly upheld in two opinions of 6 April 1990, *"Société nationale des chemins de fer français"* and *"Société Compagnie financière et industrielle des autoroutes (Cofiroute)"*. In these opinions, the Conseil d'Etat finally dispelled uncertainty in the matter as regards State liability arising from unlawful assembly.

Until then, the courts had taken the position that purely commercial losses should be taken as uncertain, at least in this field, according to legal provisions. However, the Conseil d'Etat held that the State might incur liability *"when the losses claimed were of the nature of a commercial loss, consisting in particular in an increase in operating costs or a loss of operating revenue"*.

The fact that the Conseil d'Etat has adjusted its position in respect of state liability to the common regime of administrative liability shows that the administrative courts are willing to award compensation for a wider range of losses.

However, these opinions do not mean that the victims of such losses will always be able to obtain compensation. They will still have to furnish proof of a link of causation between their loss and the fact to which they attribute it.

b) Jurisprudence of the ordinary courts

The ordinary courts also take account of commercial loss without too much difficulty:

- Cass. Civ. 3, 4 November 1971 Texier.

  "There is no contradiction in finding that the constant drop in a trader's turnover before work begins on the construction of a building next door is an indication that the business was in serious trouble, while fixing the amount of compensation due for the loss arising from the commercial disruption caused by the works".

Although the Cour de Cassation does not define the concept of *"commercial disruption"*, it must probably be understood in the sense of operating losses. In general terms, the ordinary courts are prepared to award compensation for economic loss.

It is however necessary to emphasize one basic rule of non contractual liability: the entire loss, but only the loss, is to be compensated. This means that different heads of damage are not to be duplicated.

This rule was referred to in a judgement of the Cour de Cassation of 30 January 1990:

"In the light of Articles 1137, 1147 and 1382 of the Civil Code;

Whereas, in defining the heads of damage which give right to compensation, the judgement has included an economic loss equivalent to a loss of profit for a period of 16 months, as well as the commercial loss associated with a loss of customers, and the judgement has also taken account of a so-called financial loss corresponding to the monthly instalments paid to the leasing company before the machine was replaced;

Whereas in so finding, despite the fact that the compensation awarded may not exceed the actual loss suffered, which was already made good by taking account of the loss of customers and the loss of profit, the Appeal Court acted in defiance of the above-mentioned texts";

2 Aleatory and direct loss of profit

a) Administrative jurisprudence

In some cases, the administrative courts award compensation for economic losses in which the elements of certainty and directness are open to question:

- CE, 26 October 1988, Ministre de l'Equipement v SCI "Les Moulins d'Hyeres" and others.

- compensation for the loss arising from the fact that a builder had paid the owner of a site a sum which was tied up for the period of years during which a building project was deferred owing to the refusal of a building permit;

- compensation to the owner of a site for the loss of the rents which he could have been paid for the flats which he should have received as payment for the balance due on the price of the site.

An interesting feature of this judgement is that the administrative court awarded compensation for the loss of the income which the builder could have received from reinvesting the profits of the sale. Normally, the loss of anticipated profit from a construction project which has been illegally prevented is regarded as not constituting a certain loss, and is not compensated. In this judgement the loss is compensated, the anticipated profit being treated as "*in part aleatory*" and hence to some degree certain.

Moreover, the fact that this judgement takes account of the loss suffered by the owner of the site as a result of not receiving rent income, despite the reluctance of the courts hitherto to treat this as a certain loss, is a strong indication that in future the administrative courts will be making greater allowance for pure economic loss.

- Compensation for the damage arising from the expected loss of profit where an entrepreneur has been wrongly excluded from tendering or where a contract already entered into was null and void because of an administrative error (CAA of Paris, 6 June 1991, OPHLM of Villeneuve St-Georges (CE, 13 May Ronti, 10 January 1986 Société des Travaux du Midi, 23 May 1979 Commune de Fontenay-le-Fleury).

These judgements, awarding compensation for losses which at first sight are potential rather than real, are based on the fact that in the first two cases the firm which was ousted had a real chance of tendering successfully, and consequently the profits which might have resulted were sufficiently certain. In the third case, the firm was definitively engaged to perform the contract, and was therefore bound to earn the resulting profits.

Hence the damage arising from the loss of profit consisting in the non-receipt of anticipated profits can be regarded as certain, and will therefore be compensated only if it is based on a previously existing contract, or on one which would certainly have existed if there had not been an administrative error.

Thus the loss of profit will only be a certainty if the source of the income anticipated but not received is certain.

b) Jurisprudence of the ordinary courts

In this respect, the jurisprudence of the ordinary courts resembles that of the administrative courts, as we see from the following judgement of the Cour de Cassation (Cass. Civ. 2, 12 June 1987):

> *"In the case where a company, following an accident which prevented its chairman and managing director from carrying out his functions, claimed compensation for the damage it had suffered, which it argued was the result of the non-completion of transactions which were in progress at the time of the accident, the court in refusing compensation did not err by failing to investigate whether the company had forfeited a genuine prospect of concluding these contracts owing to the unavailability of its chairman, since the Court of Appeal found that the non-conclusion of these contracts could not be described as certain loss".*

So if no allowance is made for the loss which may result from the non-conclusion of the contracts, this is because it is most uncertain whether the contracts would actually be concluded.

B OPERATING EXPENSES

1 Jurisprudence of the administrative courts

The administrative courts award compensation for various heads of loss corresponding to operating costs. Such operating costs, representing financial outlays following upon a fact which has been causative of damage, are somewhat abstract in nature. We note here that the jurisprudence has developed to take account of losses the definition of which is left unprecised, thus giving an entitlement to compensation in undefined terms.

a) Pure economic loss, reflecting a specific reality

Such losses vary considerably. They include:

- financial outlays resulting from the attitude of the authorities, who illegally prevented a builder from completing his project (CE, 28 October 1987, SCI Résidence Neptune);
- amortization charges for the period during which a quarry was illegally closed (CE, 20 March 1985, Ministry of Industry v Marques);
- an increase in operating costs for a fishmonger due to his removal from the list of approved auction purchasers (CAA of Nantes, 18 December 1989, Mme Méléard);
- "*commercial loss represented by an increase in operating expenditure*" (opinion no. 112485 of the Conseil d'Etat, Assemblée du contentieux, 6 April 1990).

More generally, these losses comprise all the financial costs, irrespective of damage to property, which result from the abnormal functioning of an enterprise for reasons attributable to some outside person.

b) Pure economic loss, in undefined terms

- Disruption of business as a result of the trader holding only a public sector licence to occupy, not the commercial lease which the authorities had wrongly made him believe he had been given (CE, 6 December 1985 BOIN-FAVRE).

For the Conseil d'Etat, although the point is not specifically mentioned, the damage here consists of the loss of the right to automatic renewal of the lease which the trader believed he held by virtue of his commercial leasing contract, by contrast with a public sector licence to occupy, which was a somewhat unreliable arrangement. Hence it is the precariousness of the trader's position which is compensated in this case.

However, by deliberately refraining from spelling out which loss is being compensated, the Conseil d'Etat apparently intends to leave itself the option of taking other heads of damage into account; while admitting that damage has been caused, it avoids the necessity of querying the extent of the damage, and this gives it more room for manoeuvre in calculating the amount of damages to be awarded.

- Problems experienced by the management of an enterprise in which the head of the firm believed the firm was secure for the next ten years, having been awarded a public sector contract; this was not in fact the case, the error being partly attributable to the public authorities (Submissions to Paris CAA, 1st Chamber, 6 June 1991, OPHLM de Villeneuve Saint Georges, see above).

2 Jurisprudence of the ordinary courts

A similar distinction is drawn by the ordinary courts. One example is a judgement of the Court of Appeal in Paris of 18 December 1986, dealing with the two kinds of damage:

> *"a computer firm which supplied a faulty computer and software must make good the losses suffered by the customer: these will include staff costs (the need to engage extra temporary staff) arising from the fact that the system produced invoicing documents which were unusable and had to be redone; the resulting confusion in customer accounts, which was a major problem for the financial management of the company, since it impeded the process of sending out invoices and obtaining payment; and the commercial loss suffered by the customer".*

This judgement must also be compared with a judgement of the Cour de Cassation (Cass. Civ. 2, 9 July 1990, SA Citroen). The comparison brings out a key factor in the compensation of economic loss: the requirement of a link of causation between the loss and the fact to which it is attributed.

The Cour de Cassation takes the view that the damage sustained by a company, in the form of the wages it had to pay to workers unable to work because access to the factory was barred by certain persons, cannot be imputed to the State as part of its responsibility for the fact of unlawful assembly. This is because the company's obligation to pay the wages does not arise from the criminal offences whose consequences the State is bound to make good, but from the contractual relationship between itself and its employees.

In this instance, there is no direct link of causation. By contrast, in the Court of Appeal judgement the wages to be paid to the temporary staff members who were engaged in addition to the

regular staff are the consequence of the faulty goods supplied, and therefore represent a head of loss for which compensation is payable.

II PURE ECONOMIC LOSS AND INSURANCE

The concept of pure economic loss is a familiar one to the insurance industry. Insurance brokers use the term *"non-material damage"* in respect of pecuniary losses sustained by a victim as the result of an accident. They also draw a distinction between *"non-material damage consequent upon secured material or physical damage"* and *"pure non-material damage"*. Hence the concept of *"pure non-material damage"* seems to be the same as that of pure economic loss.

We also find the concept reflected in two kinds of damage which are covered by insurance policies: *"indirect loss"* and *"additional costs"* covered in contracts for insuring operating losses.

A brief study of these three concepts will give us a reasonably clear idea of the scope of pure economic loss in insurance contracts.

1 Insurance cover for operating losses (OL)

The purpose of insuring operating losses is to provide cover, following a major incident, for losses arising from the decline in turnover which is normally reflected in the disappearance of the gross operating profit margin, and for the additional costs involved in meeting the most pressing outstanding commitments.

The additional costs represent all the extra expenditure which would not have arisen if the incident had not occurred, but which makes it possible to maintain a certain level of turnover. The standard terms in (OL) policies specify that *"damage represented by additional operating costs is made up of all the expenditure incurred by the insured or on his behalf, by agreement between the parties,* **with a view to avoiding or limiting, during the period of cover, the loss of gross profit margin** *due to the drop in turnover attributable to the incident".*

Here it should be explained that a loss which follows from a drop in turnover (T) is reflected in a loss of gross profit margin. This is because turnover is equal to the total of variable costs (VC), fixed costs (FC) and operating profits (OP):

$$T = FC + VC + OP$$

If there is an incident, the variable costs can be saved, but the company continues to bear the fixed costs (losses sustained) and it loses its operating profit (loss of profit). The gross margin (GM) represents both losses combined:

$$GM = FC + OP$$

In this sense, the additional costs represent a very wide range of financial expenditure, provided of course that the purpose of incurring them is to limit the loss of gross profit margin. It is for the parties to decide what ceiling, if any, is to be placed on such costs.

It should however be emphasized that, in addition to the standard exclusions which apply in insurance policies to certain types of damage (fines, damage caused by war or by nuclear weapons, damage intentionally caused by the insured), a special limit is also set in policies of this kind. For instance, operating losses resulting from the unavailability or the death of a manager or the staff of a company are not covered.

2 Indirect losses

"Indirect losses" is an imprecise term sometimes used by insurers to provide cover for additional losses found to have been incurred following an incident which forms the main object of an insurance contract. The contracts in question are commonly *"fire insurance"* contracts, the purpose of which is to cover damage caused by fire (destruction of equipment, etc.), in which a clause is inserted to refer to *"indirect losses"*.

Such a clause may also provide cover, for instance, for refurbishment costs, travel costs and various kinds of non-material loss. Pure economic loss is also covered.

However, a special feature of such clauses is that they provide a flat payment for indirect loss. In general, all the various inconveniences caused by the incident are taken into account, no useful distinction being drawn between the various heads of compensated loss. The insertion of an *"indirect losses"* clause therefore represents the intention of covering something more than the risk which is the chief object of the insurance contract, while placing a ceiling on the extra cover provided. Cover for economic loss is therefore a somewhat vague affair.

The immediate advantage is that the insured does not have to furnish proof of the existence of the indirect losses (CA Paris, 8 January 1986).

3 Pure non-material damage

A definition of this type of damage is found in the ASSURPOL standard contract: *"Any pecuniary loss which results from the loss of enjoyment of a right or from the interruption of a service by a person or by movable or immovable property"* (Standard Terms Art. 1.9).

This concept will be examined in the light of one particular insurance contract, the contract known as *"Withdrawal expenses"*, the object of this contract being to provide cover for pure non-material damage.

The purpose of the *"Withdrawal expenses"* contract of insurance is to reimburse the insured for certain expenditure consequent upon the withdrawal from the market of products designed, manufactured or sold by him. These, therefore, are costs which have to be borne by the insured, regardless of any liability on the part of third parties.

Among the various types of insurance contract known as *"Withdrawal expenses"*, the contract called *"criminal contamination of products"* is worthy of attention.

Here the situation is similar in some respects to the pure economic loss resulting from oil pollution.

Whereas in other contracts of this nature pure non-material damage originates in an accidental defect which is attributable to the insured person, in the contract known as *"criminal contamination of products"* its origin lies in the act of a third party. In essence, all the pure economic losses sustained by the victims of oil pollution are attributable to a third party.

This type of contract guarantees compensation for any loss of profit which is attributable:

- to additional advertising costs incurred for the purpose of restoring the brand image;
- to expenditure incurred in launching a new product on the market for the purpose of limiting the company's losses;
- to costs incurred in increasing sales of the other products manufactured by the undertaking.

On the other hand, cover is specifically excluded for falling sales caused by population changes, consumer preferences or seasonal economic factors.

Such policies are not much found in France, being confined mainly to the United States. However, a company forming part of an American consortium has introduced in France a product which guarantees the cost of withdrawal, replacement or rehabilitation, or lost profits consequent upon criminal or accidental contamination. Cover is therefore provided both for the actual procedures of withdrawal and for the restoration of the brand image. However, the standard amount of the cover is relatively modest (10 million francs, with an excess figure of 1% of the insured sum) and the cost of restoring the brand image may not exceed 25% of the principal sum insured.

Even though, by definition, the clauses in a contract are freely decided upon by the parties, they are nevertheless based on both practical and legal realities. Moreover, as this type of insurance contract evolves, what seems to be emerging is the recognition of a right to compensation for pure economic loss, in a very broad sense. If this phenomenon were to be extended to contracts for *"civil liability towards third parties"*, this would most probably lead to a development in the case law to take fuller account of this kind of damage.

But even without looking to the future, this practice of the insurance industry is making its own contribution to refining a concept which cannot be ignored.

To conclude this study, one point is clear: pure economic loss is now a regular feature both in French jurisprudence and in the insurance world itself. But when faced with a concept which, because of its wide-ranging character, may seem to be something of a *"monster"*, the case law limits the extent to which it is taken into account, relying on the vagueness of the concept to grant the right to compensation while setting a restriction on the amount. The same tendency is found among insurers.

Of necessity, however, the latter are gradually refining the concept by defining specific kinds of economic loss, which in turn will give the courts food for thought.