

## Can non-compliance with applicable regulations lead to a distortion of competition?

**In a decision rendered on January 21, 2014<sup>[1]</sup>, the Commercial Chamber of the *Cour de Cassation* (French Supreme Court) has ruled that the operation, without prior authorization, of a business activity governed by the legislation on classified facilities for the protection of the environment<sup>[2]</sup> could be considered as an act of unfair competition.**

This decision provides another concrete example of the numerous case-law applications in matters of unfair competition.

In this specific case, a company specialized in the recovery of recyclable metal materials derived primarily from end-of-life vehicles operated a crushing business included in the list of classified facilities and for which a prior authorization was required.

Considering that its competitor had engaged in unfair competition practices for the two years during which it had been operating a similar business without any authorization, the company (the "Plaintiff") initiated legal proceedings and requested the Commercial Court to acknowledge the existence of unfair competition practices and to order the competitor to indemnify it for the damage it claimed to have suffered, i.e. a loss of gross margin over the relevant two-year period and a damage to its business reputation.

In first instance, the Commercial Court dismissed these claims and even ordered the Plaintiff to pay 15,000 Euros in damages for abusive proceedings.

On the contrary, the Court of Appeals found that *"the Defendant's non-compliance with administrative regulations applicable to a crushing business activity constitutes, for the Plaintiff, an act of illicit and unfair competition that generates a business disruption implying the existence of a damage"*.

This position was upheld by the *Cour de Cassation* that considered:

- On the one hand, that *“the appellate judgment noted that from September 2005 to October 2007, the company MARCHETTO had operated an end-of-life vehicle cruising and storage business activity without the authorization of the Préfet<sup>[3]</sup> and in breach of applicable regulations, and inferred that such a conduct had generated a distortion of competition in the end-of-business storage market”, and*
- On the other hand, that *“for unfair competition to be established, the contentious actions do not need to have provided their perpetrator with a benefit”.*

It is not the first time that the judge asserts that non-compliance with a regulation is likely to disrupt the market by placing a company in an unjustifiably more favorable position compared to its competitors that follow such regulation. It can indeed be considered that those who escape regulations are put in an unjustifiably more favorable position compared to their competitors that comply with such regulations. As clearly indicated by the Court of Appeals, non-compliance with the regulations applicable to a business activity constitutes an act of unfair competition vis-à-vis compliant competitors and freedom of trade requires that competitors competes on the merits, thereby excluding any unfair method that would grant them an unjustified benefit.

For some actions to be considered as unfair competition practices, it is not necessary to prove that these actions have delivered some benefits to their perpetrator. If this is the case, the unjustified benefit(s) enjoyed by the perpetrator will be taken into account in the assessment of the damage suffered.

Indeed, the action for unfair competition, governed by Articles 1382 and 1383 of the French Civil Code, implies not only the existence of a wrongful act but also the existence of a damage. It can be a material damage - most of the time a loss of customers or a loss of profits - or a non-material damage resulting from a damage to the brand or to the company's business reputation.

The challenge then lies in demonstrating the existence of the damage and in assessing such damage. In the commended decision, the Plaintiff sought the payment of 1,655,268 Euros in compensation for the loss of margin over the relevant period and 50,000 Euros in compensation for the damage to its business reputation.

Regarding the material damage, the Court of Appeals had noted that *“the loss of margin caused by the unfair competition practices undoubtedly represents a small part of the overall loss of margin that is primarily due to a competition on the merits between two competitors located in the same commercial and trading area”.*

According to the Court of Appeals, in order to assess the loss of margin exclusively due to the unfair competition practices, the Plaintiff would have had to assess the costs that would have been incurred to make the competitor's site compliant , as well as the other expenses that would have been deferred during the contentious period in which it carried out its business activity without authorization and the temporary savings of which would have enabled it to apply lower prices or to buy scrap metal items at higher prices.

However, and since the proof of a quantified damage is not a prerequisite for the success of the action for unfair competition, the Court of Appeals held that it had in its possession enough elements (i.e. the nature of the relevant market, the gross margin usually generated by this type of business activity and the period during

which the business activity had been carried out without authorization) to properly assess the damage suffered and, therefore, set the amount of damages at 50,000 Euros.

Regarding the non-material damage, the Plaintiff failed to produce any conclusive exhibits to support its claims and the Court of Appeals consequently did not award any damages in this respect.

This decision takes on its full meaning when one considers that companies must comply with increasingly complex and broad regulations and that the human and material resources available within competent monitoring administrative agencies are still too limited.

Administrative agencies are indeed responsible for sanctioning non-compliance with applicable regulations and imposing administrative penalties. When a classified facility for the protection of the environment is operated without proper authorization, the administration can temporarily suspend its operations (Article L. 171-8 of the French Environment Code). In practice, inspections are infrequent and sanctions/penalties remain insufficient.

The judgment of the Court of Appeals also specified that the Plaintiff had first unsuccessfully tried to put an end to the unfair competition practices by taking administrative steps with the competent authorities. Incidentally, it could perhaps have brought a liability action against the State for failure to exercise its powers.

From a criminal law perspective, the operation of a classified facility for the protection of the environment without authorization is an offense punished by a one-year prison term and a 75,000 Euros fine (Article L. 173-1, I of the French Environment Code). Criminal courts have already ruled that the unlawful operation of a classified facility for the protection of the environment was *"a highly prejudicial conduct insofar as it constitutes an act of unfair competition for operators that comply with applicable legislation and as it flouts the basic rules aimed at protecting the environment which is a common asset to all men"*<sup>[4]</sup>.

Finally, there is also the possibility to go before the civil court. The harmed competitor can ask the trial judges to order measures to stop the unfair competition practices (in the commented case, these practices had stopped when the trial judges issued the decision, as the requested authorization had been granted in the meantime) and, like in the commented case, to order compensation for the damage suffered as a result of these practices. He can also initiate summary proceedings and seek an injunctive relief to stop these practices to the extent, however, that it can prove that such practices constitute an obviously unlawful disruption.

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[1] Commercial Chamber of the *Cour de Cassation*, January 21, 2014, n°12-25443.

[2] A classified facility for the protection of the environment is an industrial or agricultural facility that is likely to present a risk or cause pollution or nuisance, especially for the safety or health of local residents. The activities covered by the legislation on classified facilities are set forth in a list that indicates whether they are



subject to the authorization or administrative declaration regime, depending on the level of risks or inconveniences they present.

[3] Local representative of the government.

[4] Court of Appeals of Rioms, April 19, 2006, n°06-00041, upheld by the Criminal Chamber of the *Cour de Cassation*, December 5, 2006, n°06-83527.

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