A LEGAL/ECONOMIC ASSESSMENT OF THE DEVELOPMENT OF THE BLOCK EXEMPTION SYSTEM IN THE EUROPEAN UNION

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Abstract

This thesis assesses the development of block exemptions in order to investigate the economic benefits and drawbacks of using this legal technique to regulate competition in the European Union. It examines the provisions of Article 81, the legal basis of block exemptions, and demonstrates that they do take into account economic considerations even if few shortcomings exist due to the way in which they have been interpreted. This thesis also discusses the main characteristics of block exemptions as a legal technique and the procedural rules which govern their implementation. It demonstrates that over time the importance of economic considerations has increased, which is a strong positive aspect in favor of block exemptions. Finally, the thesis looks al all past and present block exemptions issued in the different sectors of the economy. It shows that the evolution of block exemptions was a difficult process and that their content changed over time, sometimes significantly. This is why a simplification of their structure would be welcome in order to provide more flexibility so that the legal rules can adapt to changing economic circumstances without the need for them to be amended frequently. The thesis concludes that overall the benefits created by block exemptions outweigh their shortcomings and thus they are an effective legal technique for regulating competition law in the European Union.

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INTRODUCTION

Competition policy is one of the major areas of European Union law and one of the areas regulated even from the establishment of the European Communities. The EC Treaty provides three standards in this area: "the principle of an open market economy with free competition"[1], "a system ensuring that competition in the internal market is not distorted"[2] and that "developments in conditions of competition within the Community [should be encouraged] in so far as they lead to an improvement in the competitive capacity of undertakings"[3]. Thus, even from the original legislative document, a double perception on competition existed: a competition free from regulatory intervention and a competition overseen by regulatory bodies in order to prevent inefficiencies. This double view corresponds with that according to which competition is beneficial in a free market economy but there are circumstances in which some limits to competition should exist.[4] In this situation, a line must be drawn between when regulation should be used by the European Union institutions and when it should not.

One of the main parts of European Union competition law is collusion. It is regulated by Article 81 in the EC Treaty which has been the subject of an abundance of European Union secondary legislation and case law. This article imposes a prohibition for entering into certain types of agreements by undertakings and declares that these agreements, if concluded, are void. However, the same article provides an exemption according to which some agreements are permitted if certain conditions are met. The Commission has issued a series of block exemptions in different sectors of the economy and has set the rules under which certain types of agreements are exempted from the application of the prohibition provided by Article 81(1).

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[1] Article 4(1) and (2) of the EC Treaty
[2] Article 3(1)(g) of the EC Treaty
[3] Article 27(b) of the EC Treaty
[4] Alison Jones and Brenda Sufrin, *EC Competition Law: Text, Cases, and Materials*, 2nd ed. New York: Oxford University Press, 2004, 41

This thesis will assess the evolution of block exemptions in the European Union from both an economic and a legal point of view. The importance of this topic is given by the fact that many undertakings from the European Union are affected by these competition rules, which consequently also affect a great proportion of consumers. Previous research has been conducted in this area by both lawyers and economists. From the lawyers' perspective, the most important issues are behavioral ones.[5] Their work starts from the legal provisions and continues by adding to those legal provisions thorough the many existing cases. Lawyers like Whish[6], Goyder[7] and Toth[8] have written on Article 81 and block exemptions using this model. On the other hand, from the economists' perspective, the most important issue is economic impact.[9] Their work concentrates on the economics of competition law in the European Union and includes only a general view of block exemptions accompanied by a smaller number of cases. Authors like Van den Bergh[10], Bishop and Walker[11] have analyzed the economic effects of certain legal provisions adopted by the European Union. Thus, the work done so far is divided between lawyers, who view block exemptions as a regulatory technique meant to maintain competition in the internal market, and economists, who criticize the European Union institutions for often disregarding economic arguments. However, no work has combined these two approaches by applying them to all past and present block exemptions and expressing an opinion about their economic impact. This is important because behavioural and economic impact issues should be considered together in order to improve the provisions of competition law.

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[5] Torok, Lecture on April 15, 2009
[6] E.g. Richard Whish, *Competition Law*, 6th ed. Oxford: Oxford University Press, 2009
[7] E.g. D.G. Goyder, *EC Competition Law,* 4th ed. New York: Oxford University Press, 2003
[8] E.g. A.G.Toth, *The Oxford Encyclopedia of European Community Law*, 3 vols: Competition Law and Policy, Oxford: Oxford University Press, 2008
[9] Torok, Lecture on April 15, 2009
[10] E.g. Roger J. Van den Bergh and Peter D. Camesasca, *European Competition Law and Economics: A Comparative Perspective*, Antwerpen: Intersebtia, 2001
[11] E.g. Simon Bishop and Michael Walker, *Economics of E.C. Competition Law: Concepts, Application and Measurement,* London: Sweet and Maxwell, 1999

In an attempt to contribute to the scholarity of this field, the thesis will investigate the economic benefits and drawbacks of regulating competition in the common market by the issuance of block exemptions by examining both behavioural and economic impact issues. Due to space limitations, this thesis will provide an overview look of block exemptions and the principles employed by them without commenting every legal aspect of the block exemptions. Furthermore, the thesis will concentrate only on the main economic effects of these block exemptions and not on assessing the economic impact of each legal right or obligation. The main method used is the analysis of legal documents, including all block exemptions issued by the Council and the Commission, the Guidelines issued by the Commission in this field and several related decisions of the European Court of Justice. The analysis of these legal documents will be done using arguments from economic theory and arguments specific for the economic analysis of law. It will be shown that the overall benefits of block exemptions outweigh their shortcomings and thus they are an effective legal technique for regulating competition law in the European Union.

The thesis is of practical value because its findings can be used by undertakings while defending themselves in front of the Commission or the European Court of Justice or even by the institutions of the European Union when drafting new legislation in this field or while evaluating the circumstances of a particular agreement which falls under Article 81.

In order to answer the research question, Chapter 1 looks at the conditions set out in Article 81 of the E.C. Treaty and evaluates whether these legal provisions are acceptable from an economic point of view. Chapter 2 examines the structure of block exemptions and considers whether this is an efficient legal technique to regulate competition in the common market. The final chapter looks at all past and present block exemptions and examines how they have developed over time.

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CHAPTER 1 – THE ELEMENTS OF ARTICLE 81

Article 81 from the EC Treaty is the legal basis for the issuance of block exemptions. Consequently, before analyzing the elements of block exemptions and their development, it is essential to examine the provisions of Article 81. The analysis will be based on the evaluation of the economic impact of these provisions and on the interpretations given to them by the Commission and the European Court of Justice. In order to achieve this, the chapter first looks at the structure of Article 81 and then analyses the conditions imposed by the prohibition and the ones required by the exemption contained in Article 81.

1.1. The structure of Article 81

Article 81 is the first article of the chapter on competition rules from the EC Treaty. Its provisions are applicable to undertakings, and more specifically to agreements between undertakings. The structure of Article 81 consists of three parts. The first one prohibits certain agreements as being incompatible with the common market, the second paragraph declares these agreements void if concluded and the third one describes the conditions under which these agreements are nevertheless acceptable.

1.1.1. The Prohibition

The prohibition set out in Article 81(1) refers to all agreements which may affect trade between the Member States and which may, by their object or their effects, distort competition within the common market. The article enumerates the most obvious such agreements and they are those which fix prices and trading conditions, those which limit production, markets, technical development or investment, those which share markets or suppliers, those which apply different conditions to comparable transactions and those which

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impose unrelated conditions into contracts. This list is not exhaustive[12] but it offers some useful guidance regarding the intention of the drafters of the EC Treaty.

The types of agreements prohibited by this paragraph are considered to be the most harmful to competition for two reasons. First, economic theory suggests that prices and quantities produced should be freely determined by the market through the supply and demand.[13] Agreements which fix prices, limit production or markets and share markets or suppliers would greatly distort this equilibrium. This is because a limited number of undertakings could partially decide on the most important elements of a market with a view of maximizing their own profit and not with a view of bringing more efficiency into the market. Secondly, economic theory suggests that each undertaking should be allowed to freely adapt to the market in order to maximize its profits.[14] However, the bargaining power between undertakings is unequal and thus, a bigger undertaking could impose unfair trading conditions on a smaller one. Agreements which contain these types of provisions will also significantly distort competition because the gap between powerful and less powerful undertakings will increase. Furthermore, these agreements intend to maximize the profit of the undertakings which are part of the agreement even if this has a greater negative impact on the market.

1.1.2. Nullity

According to Article 81(2), all agreements which fall under the prohibition of Article 81(1) are automatically void. Even if this provision seems to be straightforward, it has also given raise to interpretations by the European Court of Justice. The provision indicates that agreements which fall within the scope of Article 81(1) are void and thus, produce no effect between the parties and the parties cannot use them as a defense against the claims of a third party.[15] However, the European Court of Justice has said that "this provision applies only to

[12] D.G. Goyder, *EC Competition Law,* 4th ed. New York: Oxford University Press, 2003, 27
[13] Gerald W. Stone, *Core Microeconomics,* Worth Publishers: New York, 2008, 64
[14] Ibid., 172
[15] Goyder, op. cit., 38

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those parts of the agreements which are subject to the prohibition, or to the agreement as a whole if those parts do not appear to be severable from the agreement itself."[16] In practice, this interpretation is beneficial because it means that if such an agreement could have a positive economic impact but unfortunately contains an unlawful provision which could distort competition, the positive effects will be allowed to occur while the application of the unlawful provision will be blocked.

1.1.3. The Exemption

The exemption contained by Article 81(3) provides that the prohibition set out in Article 81(1) does not apply to agreements which are economically efficient, allow consumers a fair share of the benefit, do not impose unnecessary conditions and do not eliminate competition. The economic rationale behind this exemption is the fact that the overall effect of an agreement which falls under Article 81(1) should be taken into account and if the agreement produces more benefits, it should be allowed. However, this exemption should be narrowly applied and thus not be allowed if the provisions of the agreement which fall under Article 81(1) eliminate competition. This is because, no matter the positive economic impact of the effects, in this situation the negative economic impact will be higher for sure. Furthermore, if there is a less restrictive way to achieve the same benefits, that method should be chosen in order for competition to be restricted as little as possible. This is beneficial because it ensures that the method which restricts competition the least will be employed in order to achieve the efficiencies.

The application of this article suffered three major changes as a result of the adoption of Regulation 1/2003. First, this article was used initially by the Commission to issue two types of exemptions, individual and in block. However, at the present time, only block exemptions

[16] Joined cases 56 and 58/1964, Consten and Grunding, 344

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are still available and individual exemptions were replaced by self-assessment.[17] Secondly, the application of the exemption had initially to be expressly granted while now undertakings have to conduct a self-assessment and decide whether their agreement falls within the scope of the exemption or not. Thirdly, this article could initially be applied only by the Commission and reviewed by the European Court of Justice but after 2004, the national competent authorities gain the power to apply this article and the national courts gain the power to review those decisions. However, the Commission retains the sole power to adopt block exemptions.[18]

1.2. Conditions for Article 81(1)

The European Court of Justice in the Metro[19] case interpreted the provisions in the EC Treaty as meaning that workable competition should be maintained on the market. This means that European Union institutions should maintain a degree of competition necessary to ensure the attainment of the objectives of the Treaty and in particular the creation of the single market. In a later case, in Glaxo[20], the same concept was renamed by the European Court of Justice as being effective competition. Furthermore, in the same case, the European Court of Justice recognized that price competition is not the only form of competition which is a positive aspect from an economic point of view. Thus, the role of Article 81(1) is to prohibit all agreements which might prevent effective competition on the market. In order to achieve this, Article 81(1) prohibits agreements which affect trade between Member States and which restrict competition in two ways, by their object or their effect. When analyzing whether an agreement falls within the scope of this paragraph, the European Court of Justice has stated

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[17] Stucky, Lecture on October 2, 2009
[18] Jones and Sufrin, op. cit., 103
[19] C-26/1976, Metro, 20
[20] T-168/2001, Glaxo, 9

that the object of the agreement has to be taken into account first and only after that its effects should be considered. [21]

1.2.1. Restriction of Competition by Object

Of the two conditions imposed by Article 81(1), the restriction of competition by object is the most limiting one because it prohibits an agreement without considering its economic impact but just its object. From this strict limitation it can be concluded that the provisions covered by this condition are hardcore restrictions which will certainly prevent effective competition and thus it is not necessary to analyze its effects. In practice, only agreements which contain a hardcore restriction are considered to restrict competition by their object.[22]

Many block exemptions provide that the exemption granted is not applicable if certain hardcore provisions are contained by the agreement. For example, Regulation 2658/2000 on specialization agreements provides that the exemption does not apply if prices are fixed, if outputs or sales are limited and if the markets or customers are allocated.[23] The economic impact of these provisions can only be negative because if prices are fixed, price competition is eliminated, if outputs or sales are limited, the demand will not be satisfied in order for a monopolist profit to be gained and if markets or customers are allocated, there will be no competition to attract new customers and new markets which creates a disincentive for undertakings to become more efficient. In other regulations, for example in Regulation 772/2004 on technology transfer agreements, a distinction is made between competing undertakings and non-competing undertakings. For the first category the previous restrictions apply.[24] For the second category, the previous restrictions are relaxed and thus the parties may impose maximum or recommended sale prices and they may restrict territories or consumers

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[21] Goyder, op. cit., 96
[22] Stucky, Lecture on October 1, 2008
[23] Article 5(1) of Regulation 2658/2000
[24] Article 4(1) of Regulation 772/2004

to which the licensee may actively sell.[25] These relaxations of the restrictions are caused by the nature of the distribution system required by a technology transfer agreement. Thus, the licensor has certain rights among which the right to impose maximum prices in order to control the image of its patent products. Recommended prices are also acceptable as long as they are not binding for the licensees. On the other hand, this type of agreement should not limit the freedom of the licensee in such a manner that it would not be allowed to passively sell into other territories. Thus, the agreement should only prohibit a licensee from actively selling in other territories due to the specific structure of the distribution system.

An important aspect of this first condition of Article 81(1) is revealed by the European Court of Justice in its reasoning of the Consten and Grunding.[26] In this case, it is generally considered that the European Court of Justice "sent out a clear message: agreements which divide up the common market and preclude all cross-border trade in the contract product will not be tolerated."[27] Thus, the application of this condition is also related to the achievement of the single market objective and agreements whose aim is to preserve the national markets will automatically infringe Article 81(1). This approach discloses the fact that not only the economic impact of these agreements is important but also political aspects. This perspective is faulty from an economic point of view because political objectives should not be achieved at the expense of economic efficiency. The vast majority of economists support the idea that non-economic goals should be pursued by other public policies and not by competition law. [28] The main shortcoming of European Union competition law is the fact that its goals are not only economic but also political. Thus, the achievement of market integration is and

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[25] Article 4(2) of Regulation 772/2004
[26] Joined cases 56 and 58/1964
[27] Jones and Sufrin, op. cit., 198
[28] Roger J. Van den Bergh, and Peter D. Camesasca, *European Competition Law and Economics: A Comparative Perspective*, Antwerpen: Intersebtia, 2001, 6

important political goal which it is taken into account even if it can cause inefficiencies in the market.[29]

1.2.2. Restriction of Competition by Effect

The second condition imposed by Article 81(1) is less restrictive than the first one because it takes into account the effects of certain agreements. Since it is more practical-oriented, this approach is probably favored by economists. The previous approach was more formalistic because it prohibited an agreement only because of its object. This second condition allows the Commission and the European Court of Justice to assess the economic impact of the agreement while the condition regarding the restriction of competition by object does not allow for this possibility.

This condition excludes from the prohibition imposed by Article 81(1) certain agreements which are incapable of restricting competition by their effect. Thus, if undertakings have a small aggregate market share there is a presumption that their agreement will not restrict competition in the common market as long as it does not contain hardcore restrictions. The *de minimis* threshold imposed to actual or potential competitors is that the aggregate market share does not exceed 10% and the one between actual or potential non-competitors does not exceed 15%.[30] Moreover, if competition is restricted by the cumulative foreclosure effect of parallel networks, these thresholds are reduced to 5%.[31] The market share thresholds are an important element of modern block exemptions and thus they will be analysed in detail in Chapter 2.

Under the restriction of competition by effect condition, an important aspect is the extraterritorial effect of the European Union legislation. For example, block exemptions in the

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[29] Van den Bergh and Camesasca, op. cit., 1-2
[30] Commission Notice on agreements of minor importance which do not appreciably restrict competition under Article 81(1) of the Treaty establishing the European Community, 2001, 7
[31] Ibid, 8

air service industry were initially limited to air transport between Community airports[32] but in 2004 this changed and the scope of these block exemption was extended to include air transport between Community airports and third countries.[33] Extraterritoriality means basically that "a law [is] being applied beyond the territorial ambit of its sovereign legitimacy."[34] Due to this principle, the Commission was able to initiate proceedings against undertakings whose registered office is outside the European Union[35] and to fine them when their actions restricted competition in the common market. For example, in the Wood pulp[36] case, the European Court of Justice applied the effects doctrine and decided that it was competent because the Canadian company was present on the European Union market and thus affected this market.[37] This approach is in concordance with the group economic unit doctrine which attributes to foreign parents the anticompetitive effects caused by subsidiaries.[38] However, these decisions are also likely to cause conflicts between the European Union and other legal systems. This is because, due to the extraterritorial application of competition laws, the same behavior will be evaluated under different standards which may cause conflicting decisions to be adopted by the two national authorities.[39] These frictions also negatively affect the undertakings by increasing the costs of compliance with the competition laws of two different countries. This is why, in such situations, one appropriate solution would be for the authorities of the two countries to work together and reach a mutually satisfactory decision.

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[32] Article 1 of Regulation 3975/1987 and of Regulation 3976/1987
[33] Article 2 Regulation 411/2004
[34] Goyder, op. cit., 498
[35] A.G. Toth, *The Oxford Encyclopedia of European Community Law*, 3 vols: Competition Law and Policy, Oxford: Oxford University Press, 2008, 388
[36] Joined cases C-89/85, C-104/85, C-114/85, C-116/85, C-117/85 and C-125/85 to C-129/85, Ahlström Osakeyhtiö
[37] Stucky, Lecture on October 1, 2008
[38] Goyder, op. cit., 499
[39] William E. Kovacic, "Extraterritoriality, Institutions, and Convergence International Competition Policy", *American Society of International Law Proceedings*, April 2-5, 2003, 2

1.3. Conditions for Article 81(3)

Article 81(3) makes it possible for an agreement which falls within the scope of Article 81(1) to escape nullity. The European Court of Justice in the Glaxo case has reaffirmed that "any agreement which restricts competition […] may in principle benefit from an exemption".[40] However, in order for the exemption provided by Article 81(3) to be applicable, an agreement must satisfy two positive conditions and two negative conditions. The first two consist of creating efficiency and providing consumers a fair share of the benefit while the second ones prohibit the introduction of unnecessary provisions contrary to Article 81(1) and the elimination of competition. Because these conditions may receive a wide variety of interpretations and, especially since from 2004, undertakings are responsible for conducting their own self-assessment, the Commission has published Guidelines[41] for the application of Article 81(3). These Guidelines reaffirm the fact that these conditions are cumulative and exhaustive.[42]

1.3.1. Efficiency

The official text refers to agreements which "contribute to improving the production or distribution of goods or to promoting technical or economic progress".[43] In a more simple form, this condition refers to agreements which create efficiencies. The Commission has broadly interpreted this provision as referring to efficiency gains which cover both cost efficiencies and qualitative efficiencies. According to the Commission, cost efficiency may be attained by saving costs due to new technologies, integrating complementary assets and technologies, economies of scale, obtaining different outputs based on the same input, allowing for a better planning of production and better utilization of the capacity as well as

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[40] T-168/2001, Glaxo, 233
[41] Communication from the Commission – Notice – Guidelines on the application of Article 81(3) of the Treaty
[42] Ibid., 34, 42
[43] Article 81(3) of the EC Treaty

reducing the need to hold expensive inventory.[44] On the other hand, the Commission specifies that qualitative efficiencies may be attained by improving the quality of products or by improving the technology used through cooperation, combination of complementary assets or specialization of distribution.[45] These methods are appropriate ways of creating efficiencies from an economic point of view. The broad interpretation provided by the Commission is supported by the European Court of Justice. In the Metro[46] case, this condition was considered satisfied by the fact that the agreement provided for a more regular and stable distribution system, the manufacture had to compensate wholesalers for services performed under guarantee and supply spare parts and the fact that supply forecasts were established. Thus, efficiency gains cover a wide range of situations[47] which is a positive aspect for the interpretation of this condition from an economic point of view.

The freedom awarded to undertakings to decide how they could improve their activity is an incentive for them to enter into agreements by which they could become more efficient. On the other hand, the incentive for undertakings to become more efficient also exists due to the prospect that, by becoming more efficient, they will enjoy more market power.[48] Consequently, this condition adds merely the obligation for an agreement to become more efficient if the parties would like their agreement to be exempted from the application of Article 81(1) since the incentive to become more efficient already existed. The positive significant aspect of the introduction of this obligation is that it eliminates from the application of the exemption those situations in which undertakings enter into agreements only to maximize their own profits and not to become more efficient.

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[44] Guidelines on the application of Article 81(3) of the Treaty, 64-68
[45] Ibid., 69-72
[46] C-26/1976, Metro
[47] Goyder, op. cit., 121
[48] Massimo Motta, *Competition Policy: Theory and Practice*, Cambridge: Cambridge University Press, 2004, 64

The method according to which the European Union institutions decide whether an agreement creates efficiencies is also important. In the Glaxo[49] case, the European Court of Justice analyzed in great detail the gains in efficiency and the losses associated with parallel trade in medicines and balanced them. This technique is hard to apply in practice because many facts and circumstances have to be taken into account. However, from an abstract point of view, this is the correct approach because it calculates the net efficiency of each agreement and only if the net efficiency is positive, is the exemption applicable.

1.3.2. Fair Share of the Benefit to Consumers

The European Union places a great emphasis on consumer welfare. First, in competition law the emphasis on consumer welfare is bigger than the one on global economic welfare.[50] Second, the European Union has developed significant legislation regarding consumer protection. This is why this condition for the application of the exemption provided by Article 81(3) is not unusual or unexpected. The economic argument which can be raised against this approach is the fact that passing on the benefits of an agreement to consumers is a redistribution of wealth which does not increase overall welfare. However, social considerations override this economic argument in the European Union. From the point of view of overall welfare, it would be more appropriate to evaluate the tradeoff between the loss of undertakings negatively affected by the restriction of competition and the gain of consumers and undertakings which are part to the agreement. Only if the sum of the losses would be lower than the sum of the gains, should the exemption be applicable.

The concepts of "consumers" and "benefit" have been broadly interpreted.[51] For example, in Regulation 1475/1995 the mere existence of an effective competition is considered to allow consumers to take an equitable share in the benefit from the operation of

[49] T-168/2001, Glaxo
[50] Van den Bergh and Camesasca, op. cit. 1-2
[51] Goyder, op. cit, 123

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such competition.[52] This is accurate because one of the reasons for which effective competition is desirable is the fact that consumers benefit from competitive prices, a wider range of products and from the efforts of undertakings to improve their market share. This approach was also followed by the European Court of Justice in Metro when it considered that the pressure of competition forces Saba to pass on benefits from rationalization of production and distribution system to the consumers.[53] However, the fact that consumers benefit from effective competition achieved through competition law was not treated as an implied presumption by the EC Treaty means that, in some situations, this benefit might not be sufficient for the exemption to be applicable.

According to the Commission, the concept of "fair share" is used to describe the situation in which the benefits passed on to the consumers must at least compensate consumers for any negative impact caused to them by the restriction of competition. This amounts to a Kaldor-Hicks test[54] according to which there is a welfare improvement if the gainers, the undertakings which concluded the exempted agreement, are still better off after compensating the losers, the consumers. However, there is no fair share of the benefit passed on to other undertakings from the market which might have suffered from the restriction of competition. Because of this, the Commission should also check whether there are such undertakings and whether their losses are lower than the welfare improvement or not.

The Commission provides three important interpretations for Article 81(3). First, the Commission states that the second condition of Article 81(3) does not require for consumers to receive a share of each efficiency gain but to obtain a fair share of the overall benefits and to be compensated for the negative effects of the restrictive agreement. [55] This interpretation is to be expected and reasonable because it would be very hard in practice to pass on a benefit to

[52] Recital 30 of Regulation 1475/1995
[53] C-26/1976, Metro, 48
[54] Anthony W. Dnes, *The Economics Analysis of Law: Property, Contracts and Obligations*, Manson, Ohio: International Thomson Business Press, 2005, 8
[55] Guidelines on the application of Article 81(3) of the Treaty, 86

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consumers for every efficiency gain. Second, the Commission allows for the passing on of the benefits to take place at a later time.[56] In this situation, the Commission is right in taking into account the fact that the value of a gain for consumers in the future is lower than the same gain in the present and thus it is necessary to make adjustments. Third, the Commission affirmed that undertakings are not obliged to pass the entire benefit to consumers but just a portion of them in order to allow consumers to be as better off as if the agreement would not have been entered into or a little better off.[57] Because not all benefits are passed on to consumers and some of the benefits are retained by the parties to the agreement, the undertakings have an incentive to achieve efficiency which is a positive aspect from an economic point of view.

1.3.3. Indispensability

This negative condition imposed by Article 81(3) is hard to assess in practice. The Guidelines issued by the Commission provide two important interpretations regarding this condition. First, the Commission considers that this condition requires the determination of whether the agreement and the restrictions of competition caused by the agreement are each reasonably necessary and proportionate in order to obtain the efficiencies.[58] Second, the Commission affirms that in order for this condition to be fulfilled, there must not be any other economically practicable and less restrictive way of achieving the same level efficiencies.[59] The first interpretation proposed by the Commission provides a welcome flexibility since a more precise test cannot be imposed. Thus, the reasonable necessity and the proportionality standards, specific to common law countries, have been used by European Union law in a variety of situations, including the assessment of the indispensability condition. However, the second interpretation provided by the Commission limits this flexibility by excluding all those

[56] Guidelines on the application of Article 81(3) of the Treaty, 87
[57] Ibid., 99
[58] Ibid., 73
[59] Ibid., 75

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agreements which could have opted for a less restrictive method for achieving the same efficiencies. By combining these two interpretations, the fact that hardcore restrictions cannot be exempted under the indispensability condition can be implied. This is because a hardcore restriction cannot be determined to be reasonably necessary and proportionate nor can it constitute the least restrictive means of obtaining certain benefits. This is an essential aspect because it recognizes the fact that hardcore restrictions can never be considered indispensable to an agreement and should never be exempted due to their significant negative effects.

The approach used by the Commission for interpreting this situation is more specific to common law because of the reasonably necessary and proportionality standard. Thus, according to the Commission, the assessment of the indispensability condition is done based on the structure of the market, the economic risks related to the agreement and the incentives facing the parties which might face substantial sunk investments.[60] This approach is appropriate because each case will be decided according to its own facts and not according to a predetermined test which hardly ever takes into account specific circumstances.

To the approach adopted by the Commission, the Court of First Instance added a new requirement in the Metropole television case. Thus, the indispensability condition also requires for the exempted agreement to impose objective and sufficiently determinate rules which can be applied uniformly and in a non-discriminatory manner.[61] This add-on of the Court of First Instance is based on equal treatment considerations. Under the reasonable necessity and the proportionality standard, the Commission had more freedom to decide and give different weights to economic and social considerations. However, the Court of First Instance considered that the non-discrimination principle is a fundamental principle which should be applied no matter what the economic considerations are. This approach could be

[60] Guidelines on the application of Article 81(3) of the Treaty, 80
[61] Joined cases T-528/93, T-542/93, T-543/93 and T-546/93, Metropole télévision, 95

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explained by the existence of unequal bargaining power between undertakings and by the fact that opportunities should be provided to all undertakings.

1.3.4. Non-elimination of Competition

This last negative condition imposed by Article 81(3) is probably the most important one. This is because if competition is eliminated, the efficiency gains and the passing on of benefits to consumers lose their value since in the long run the undertakings will start behaving like monopolists. Due to this condition, agreements which restrict competition by their object are unlikely to be exempted because usually those agreements contain hardcore restrictions which aim at eliminating competition.

The Commission interprets this condition as depending on the degree of competition existing before the agreement and the impact of the agreement on that competition.[62] This approach is consistent with economic theory because it takes into account the economic impact of a certain agreement. Furthermore, the Commission is in accordance with economic principles when asserting that market shares are relevant but not sufficient and thus factors like the degree of substitutability and the competitive relationship between the products sold by the parties should be taken into account.[63] Furthermore, the Commission also recognizes that, besides actual competition, potential competition should also be taken into account in the form of entry barriers.[64] Thus, in assessing if this condition is met, the Commission is willing to take into consideration various arguments supported by economic theory which is a positive aspect for the Commission's attitude towards competition.

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The function of this chapter was to evaluate the role of economic considerations in the provisions of Article 81 and in the interpretations given by the Commission and the European

[62] Guidelines on the application of Article 81(3) of the Treaty, 107
[63] Guidelines on the application of Article 81(3) of the Treaty, 109
[64] Ibid., 114

Court of Justice. In the great majority of circumstances, economic considerations are taken into account and the economic impact of potential agreements is assessed by the European Union institutions. However, there is one economic aspect which is not taken into consideration and this is the fact that third party undertakings may be negatively affected by the agreement. This is because, from an overall welfare point of view, loses suffered by third party undertakings and consequently also by consumers can be higher than the gains acquired by the parties and consequently by consumers. This is not an argument for protecting the weak and inefficient third parties undertakings but just for ensuring that the market conditions in which third party undertakings operate are not distorted so as to cause more overall loses than overall gains.

Furthermore, there are some circumstances in which social and political considerations are more important than economic considerations. Social considerations like consumer welfare and non-discriminatory treatment are not necessarily bad. They are to be expected because the European Union opted for a social market economy approach.[65] However, political considerations like the achievement of the single market objective cause economic inefficiencies. They are not justifiable because the single market is impossible to achieve due to significant customary differences which cause different populations to use dissimilar types of the same product.[66] Furthemore, as the existing literature has pointed out, political objectives should be achieved by other means than competition law.

After analyzing the legal basis for block exemption and the conditions imposed by the prohibition and the exemptions contained in Article 81, this thesis continues by analyzing the main characteristics of block exemptions by looking at their main substantive and procedural elements.

[65] Torok, Lecture on May 7, 2009
[66] Torok, Lecture on April 15, 2009

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CHAPTER 2 – CHARACTERISTICS OF BLOCK EXEMPTIONS

Block exemptions are an important legal instrument used by the Commission and the Council to regulate competition law in the European Union. The first such regulation was issued in 1968 and since then their defining characteristics have changed significantly. The aim of this chapter is to assess whether block exemptions are an efficient legal technique to regulate competition in the common market. The efficiency standard is based on the way in which economic principles of assessing anti-competitive behavior are taken into consideration. In order to achieve this, the chapter first looks at the definition of block exemptions, their general development over time, their essential common elements, the procedural rules on which they are based and finally it considers several current trends and two legal techniques employed by other legal systems.

2.1. Definition

Block exemptions are regulations which exempt certain categories of agreements between undertakings from the application of Article 81(1) for a limited period of time if certain conditions are met. The legal basis for these exemptions is Article 81(3) which allows for agreements which fall under the scope of Article 81(1) to be exempted if they provide efficiency gains, allow the consumers a fair share of the benefits, do not eliminate competition and do not impose unnecessary conditions. The policy reason for these exemptions is stated in many block exemptions recitals as being the fact that the categories of agreements exempted have more pro-competitive effects than anti-competitive ones.

Block exemptions may be adopted directly by the Council or by the Commission on the basis of an enabling regulation issued by the Council.[67] Very few block exemptions are adopted directly by the Council, most of them being adopted using the second procedure

[67] Toth, op. cit, 123

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because the Commission is the European Union institution most actively involved in regulating competition law. From the standpoint of their coverage, some block exemptions are general, like the ones on vertical agreements, while others regulate specific sectors, like the one on motor vehicle distribution.[68]

2.2. Early Development

Block exemptions began being used as a legal technique to exempt certain categories of agreements due to practical circumstances related to the application of Article 81(3) by the Commission. Regulation 17/1962, the first regulation on procedural rules for the application of Article 81, provided that all agreements which fell under Article 81(1) but were considered to meet the conditions of exemption provided by Article 81(3) had to be notified to the Commission. Toth argues that this procedural requirement led to a significant number of notifications and that many of them did not raise actual competition issues.[69] As a result, he maintains that the workload of the Commission increased significantly.[70] The first solution adopted was the usage of informal settlements but they were not favored by undertakings since, from a strictly legal point of view, the agreement remained un-exempted.[71] In these circumstances, Toth argues that the solution adopted was to dispose of these cases by the issuance of block exemptions.[72] They were an attractive option because they implied less costs than individual exemptions and they created an incentive for undertakings to draft their agreement in order to comply with the block exemption.[73] Bishop and Walker deny the effectiveness of this incentive because they consider that block exemptions cause parties to

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[68] Jones and Sufrin, op. cit, 96
[69] Toth, op. cit., 122
[70] Ibid.
[71] Ibid
[72] Ibid, 121
[73] Ibid, 123

concentrate more on the structure of the agreement than on its impact.[74] This view is not justified because undertakings are primarily interested in the economic impact of their agreement and mechanically drafting an agreement to comply with a block exemption is of no value to them as long as certain economic effects are not achieved.

Thus, the emergence of block exemptions was more due to practical requirements than to legal technique considerations. However, the appearance of block exemptions is unlikely to have occurred in another manner because of the initial lack of experience of the Commission in dealing with agreements between undertakings which fell under Article 81. In time, while dealing with individual exemptions, the Commission acquired experience which permitted it to draft block exemptions. Furthermore, the experience gained during the life of the earlier block exemptions was used by the Commission to replace these block exemptions by improved ones, as it is acknowledged in the recitals of the modern block exemptions.[75] Many of these modifications, especially those in the late 1990s and in the 2000s, were part of a modernization process which took more into consideration economic principles.

2.3. Economic Justifications for the Modernization Process

The modernization process started with Regulation 2790/1999 and had two directions: the modernization of substantive rules by the renewal of block exemptions on vertical and horizontal agreements and the modernization of procedural rules through the adoption of Regulation 1/2003.[76] This section deals only with the modernization of substantive rules and the four major changes they suffered while the modernization of procedural rules is dealt with by a later section.

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[74] Simon Bishop and Michael Walker, *Economics of E.C. Competition Law: Concepts, Application and Measurement*, London: Sweet and Maxwell, 1999, 77
[75] E.g. Recital 2 of Regulation 2790/1999
[76] Philip Brentford and Tony Reeves, A New Competition Policy for a New Milennium, *International Company and Commercial Law Review* 2000, 11(3), 75

The first most important aspect of the modernization system was that the Commission's intention, as stated in the recitals of the block exemption adopted as a result, was to move to a more economic based approach.[77] Thus, while earlier block exemptions were narrow in scope and were strongly prescriptive of the content of agreements, modern block exemptions tend to have a broader scope and to lay down a less rigid framework.[78] One essential step was to eliminate white lists[79] because, as the Commission acknowledges in the recitals of these block exemptions, the intention was to move from an approach of listing exemptions to placing greater emphasis on defining categories of agreements exempted.[80] In order to define the categories of agreements exempted, the Commission made use of market share thresholds, which will be analyzed in the next section, and of hardcore restrictions, which were analyzed in the first chapter. This modernized approach is more consistent with economic theory because it affords undertakings more flexibility in concluding an agreement while at the same time providing legal certainty. Thus, undertakings are free to draft an agreement in a way which favors them the most and not in the way dictated by the Commission which is an important aspect of market economies.

The second significant improvement employed by the Commission during the modernization process was that the block exemptions made an important distinction between competitors and non-competitors[81] and employed different rules applicable to each category. This division is also welcome because situations in which the parties are competitors and those in which parties are not competitors give rise to different economic consequences and thus they should be treated differently. The dissimilar treatment should take into account the fact that agreements between competitors are more likely to restrict competition and thus stricter rules should be applicable to them than to agreements between non-competitors. On

[77] E.g. Recital 4 of Regulation 772/2004
[78] Toth, op. cit., 123
[79] Richard Whish, *Competition Law*, 6th ed. Oxford: Oxford University Press, 2009, 167
[80] E.g. Recital 4 of Regulation 772/2004
[81] E.g. Regulation 772/2004

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the other hand, agreements between non-competitors also have the power to restrict competition and thus they also should be subject to certain competition law provisions.

A third change imposed by the modernization system was for the Commission to adopt a more functional approach. According to this approach, the exemptions provided by the earlier regulations were extended to also include agreements which do not have as their primary objective the type of activities regulated by the block exemption but to which this type of activities are directly related to and necessary for their implementation. For example, the modern block exemption on research and development is applicable to both agreements whose primary object is research and development activities and to agreements to which research and development activities are directly related and necessary for their implementation.[82] This change is useful because the Commission recognizes that, in order for certain provisions to have pro-competitive effects and benefit from an exemption, it is not necessary for a separate agreement to be concluded but those provisions may be included in a broader agreement. The abandonment of the formalistic approach by the Commission affords undertakings more freedom in drafting their agreements which is an important aspect of a market economy as has been previously mentioned.

A fourth tendency imposed by the modernization process was the consolidation of existing block exemptions.[83] For example, the two regulations covering know-how licensing and patent licensing were combined.[84] Even if this change appears significant only from a regulatory point of view, it is a welcome adjustment because it makes it easier for undertakings to become familiar with the legislation applicable to their agreements. Fewer block exemptions reduce the costs of compliance by reducing the number of provisions that have to be studied and by grouping the rules applicable to the same undertakings.

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[82] Article 1(2) of Regulation 2659/2000
[83] Toth, op. cit., 123
[84] Ibid.

Thus, the four major changes imposed by the modernization process of the substantive rules employed by block exemption are based on economic rationales. These changes also had an influence on the structure of block exemptions, by eliminating some of the elements found in the earlier block exemptions and introducing new elements in the modern ones.

2.4. The Elements of Block Exemptions

The main elements of past and present block exemptions are the market share and maximum annual turnover thresholds and the relevant market according to which they are calculated. They will be analyzed first because their introduction in block exemptions was subject to many debates. White, grey and black lists were present differently in past and present block exemptions and they also compose an essential element of block exemptions. The non-application of the exemption in certain situations, the rights of the Commission to start the opposition procedure and to withdraw the benefit of the exemption are also important because they describe situations in which the benefit of the exemption is eliminated. Finally, the duration and the amendment of block exemptions are analyzed because they are a source of legal certainty.

2.4.1. The Relevant Market

The relevant market is a key element in the application of modern block exemption because, according to it, the market power of the undertakings is measured. This is an important aspect since the role of competition law is to prevent the exploitation of market power.[85] The Commission defines the relevant market in its Guidelines as the market on which the undertakings operate both from the product and the geographic dimension.[86] According to the Guidelines, the relevant product market comprises all products considered

[85] Van den Bergh and Camesasca, op. cit., 5
[86] Commission Notice on the definition of relevant market for the purposes of Community competition law, 2

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substitutable by the consumer[87] and the relevant geographic market refers to a distinct area with homogeneous competition conditions.[88]

In order to find the relevant market in real situations, the Commission examines certain competitive constraints: demand substitutability, supply substitutability and potential competition.[89] First, the Commission defines demand substitution as the range of products viewed as substitutes by consumers.[90] This definition resembles more a principle than a practical approach because there are many situations in reality in which products viewed as substitutes by some consumers are not viewed the same way by others. Furthermore, if the price difference is high, consumers might be more willing to substitute the product while if the price difference is low, consumers might be more reluctant to do so. The Commission should also take into account these elements while examining demand substitutability. Second, the Commission regards supply substitution as the ability to switch production in short term without incurring significant additional costs or risks[91] which is in accordance to economic theory. Third, the Commission states that potential competition is not usually taken into account.[92] This is a reasonable approach because it is hard to know when potential competition will become effective competition. Furthermore, the Commission analyses the present market on which the undertakings operate and not future markets. Nonetheless, the Commission should at least glance at potential competition when there are insignificant sunk costs for entering the market because, in this situation, potential competition can turn into actual competition easily, especially if certain incentives exist. This is not to say that potential competition should be included as such in the relevant market but just that it should be

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[87] Commission Notice on the definition of relevant market for the purposes of Community competition law, 7
[88] Ibid., 8
[89] Ibid., 13
[90] Ibid., 15
[91] Ibid., 20
[92] Ibid., 24

decided in each individual case whether potential competition is worth taken into consideration or not.

As a regulatory authority, the Commission faces the situation of informational asymmetries between itself and the regulated firms.[93] The Commission usually relies on information gathered from the parties, consumers, competitors and others.[94] The problem is that the parties have an incentive to distort the data in order for the Commission to define a bigger relevant market in which their market power is smaller and thus the agreement could be exempted.[95] On the other hand, their competitors have an incentive to misrepresent the data in order for the Commission to define a smaller relevant market in which the market power of the parties is bigger and thus the agreement may not be exempted. These effects may cancel each other out but, the important aspect is that the Commission will probably receive truthful information only from independent sources and that it should double check the data received from the undertakings. A solution for this problem might be the decentralized enforcement of competition rules which has been partially achieved by Regulation 1/2003.[96]

2.4.2. Market Share Thresholds and Maximum Annual Turnover

Effective competition, the goal of the Commission, occurs in the absence of market power.[97] Market shares are used as a proxy for market power in order to provide legal certainty[98] and they became a common feature of modern block exemptions. They have been strongly opposed by the industries but the Commission persisted with its proposed approach arguing that other practical tests of market power had not been put forward.[99] Market shares thresholds are generally set according to the relevant market and only one regulation, from

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[93] Van den Bergh and Camesasca, op. cit., 131
[94] Commission Notice on the definition of relevant market, 33, 40
[95] Torok, Lecture on May 26, 2009
[96] Van den Bergh and Camesasca, op. cit., 140
[97] Bishop and Walker, op. cit., 4
[98] Toth, op. cit, 124
[99] Brentford and Reeves, op. cit., 78

1972[100], set a market share threshold of 10% of each national market which seems only a mistake given the political goal of achieving the single common market.

Market shares are generally considered to be part of an economic approach because if the parties do not have a certain level of market power, their agreement is unlikely to negatively affect competition on the market.[101] However, economic theory does not provide a certain market share threshold under which anti-competitive effects are not significant and this has caused problems in practice. The specialization and research and development block exemptions suffered the most changes with regard to market share thresholds. The various regulations provided in 1982 for a market share threshold of 15%, in 1985 this threshold was increased to 20% and in 2000 the market share threshold set in the research and development block exemption was of 25%. This pattern was followed by other regulations as well. The highest market share threshold of 40% was set for the motor vehicle block exemption in case of quantitative selective distribution systems.[102] Later regulations also make a distinction between competitors and non-competitors and the maximum market share thresholds imposed to the first ones are always lower. The various increases in the market share thresholds over time and the different thresholds used by block exemptions in different sectors is explained by the fact that the size of these thresholds is not based on a mathematical calculation but rather on the intuition and experience of the Commission. This is not necessarily a bad thing but it reveals the fact that other elements should also be taken into account when assessing the market power of certain undertakings. Economic theory suggests three indicators of market power: first, the number of competing suppliers of the same product, market shares and concentration, second, the availability of substitutes and product differentiation and third, barriers to entry and potential competition.[103] Surprisingly, when certain individual cases are

[100] Article 3(1)(a) of Regulation 2779/1972
[101] Toth, op. cit., 124
[102] Article 3(1) of Regulation 1400/2002
[103] Bishop and Walker, op. cit., 34

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being investigated by the Commission, some of these factors are taken into account but they are not included in block exemptions.[104] An explanation for this might be the fact that there has not been found an appropriate way in which these indicators could be introduced in block exemptions.

The only other tool chosen to be used by the Commission in block exemptions in order to assess market power was maximum total annual turnover. The first regulation which instituted a maximum total annual turnover was the same as the one which instituted the first market share threshold and its level was of 150 million units of account in 1972. This threshold was doubled in 1982 and then set to 500 million units of account in 1985 and to 1.000 million units of account in 1993. These frequent and significant changes show that it is very hard to set a maximum total annual turnover threshold since the industries are always growing and this economic indicator is increasing year after year. The last such threshold was set in 2002 for vertical agreements on motor vehicle at the amount of 50 million euro and it will expire in 2010. The conclusion is that this is not an adequate measurement of market power unless the actual threshold is linked to an economic indicator which reflects the changes in the economy.

2.4.3. White, Grey and Black Lists

Because earlier block exemptions were narrow in scope and strongly prescriptive of the content of agreements, many times they gave birth to a compulsory model contract which caused companies to adopt commercially and economically less than optimal agreements in order to benefit from automatic exemption.[105] These lists of prescriptive provisions were called white lists and they contained provisions exempted from the application of Article 81(1). In order to award undertakings more freedom, these lists are not used anymore. This

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[104] E.g. Guidelines on the application of Article 81 of the EC Treaty to technology transfer agreements, some of these factors are taken into account for individual assessments
[105] Toth, op. cit., 123-124

change is useful because each undertaking should be able to decide what to include into an agreement and what not to include in order to optimize its activity.

Grey lists were used in earlier block exemptions to name the clauses subject to the opposition procedure.[106] Thus, the parties could include in an agreement clauses which restrained competition but were not included neither in the white nor in the black lists and consequently they were named grey.[107] Since the opposition procedure is not used anymore, neither are the grey lists. The main disadvanatage of this list was the fact that legal certainty was not provided for since the Commission could decide, upon notification according to the opposition procedure, not to exempt the agreement.

Black lists were included in earlier block exemptions and were composed of prohibited clauses.[108] In modern block exemptions, two types of black lists are used: hardcore restrictions and excluded restrictions. The first ones cause the entire agreement to be void while the second ones cause the voidance of only that clause.[109] This difference clarifies the interpretation given to the nullity provision of Article 81(2) which was discussed in the first chapter. Its main role is to provide legal certainty regarding the provisions which cause an entire agreement to be void and those which cause the voidance only of a particular provision.

2.4.4. Non-application to a Particular Market

The Commission has the right to declare the exemption non-applicable to a particular market or to specific restraints within a market, especially when the parallel networks cover more than 50% of the relevant market.[110] This is an important aspect for European Union competition law because, as the European Court of Justice stated in the Glaxo case, the object of prohibiting parallel trade is to prevent competition.[111] Even if the Commission has not

[106] Toth, op. cit. 24
[107] Goyder, op. cit., 116
[108] Toth, op. cit., 124
[109] Goyder, op. cit., 116
[110] Toth, op. cit., 125
[111] T-168/2001, Glaxo, 115

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exercised this right so far,[112] it is beneficial that this right exists and when competition on a particular market is restricted, it can be exercised.

2.4.5. Opposition Procedure

The opposition procedure was introduced in some of the block exemptions issued before Regulation 2790/1999. According to the procedure described in those regulations, the exemption applied to certain agreements which did not entirely respect the conditions set out in the block exemption as long as those agreements were notified to the Commission and the Commission did not oppose the exemption within a certain period of time.[113] This procedure is no longer appropriate after the entry into force of Regulation 1/2003 because the possibility or the obligation to notify agreements in order to be granted the exemption under Article 81(3) is no longer available.[114] The main disadvantage of this procedure was that it provided for no legal certainty since the Commission had the power of decision on a case to case basis.

2.4.6. The Right to Withdraw the Benefit of the Exemption

The right to withdraw the benefit of a block exemption is available to the Commission with regard to certain agreements which fall within the scope of a block exemption but which are considered not to fulfill the conditions of Article 81(3). This right has been used only once[115] but it is important because, if the benefit of an exemption is withdrawn, the undertakings concerned would be put in the difficult situation of readjusting their market behavior in order not to infringe Article 81(1).

In the past, this right of the Commission was included in each block exemption and it could be exercised whenever the agreement had effects incompatible with Article 81(3). However, due to the specificity of each economic sector, more explicit reasons were used as well. Among the reasons formulated by the Commission, two of them are more interesting.

[112] Toth, op. cit., 125
[113] E.g. Article 7 of Regulation 418/1985
[114] Toth, op. cit., 124
[115] Whish, op. cit., 167

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First, the benefit of the research and development block exemption could have been withdrawn if the parties did not exploit the results of the research and development activity without an objective reason.[116] This is reasonable because, if an agreement is exempted, the undertakings should use the advantages gained in order for consumers to also benefit from the exemption. Second, in the case of air service block exemptions, if the system vendor refused to enter into a contract with a subscriber without objective reason, the benefit of the exemption could have been withdrawn.[117] This is also appropriate since an undertaking which had become more powerful because it benefited from a block exemption should not be permitted to behave abusively.

Regulation 1/2003 brought changes to the Commission's right to withdraw the benefit of a block exemption. First, this right is now available in connection with all block exemptions without needing an explicit mentioned in each block exemption, although this still happens. Second, the benefit of a block exemption could have been withdrawn only by the Commission until 1 May 2004, but Regulation 1/2003 also granted, under certain conditions, the right of withdrawal to the competent national authorities.[118] The question which arises is whether the system used before 1 May 2004 was better or the one provided in Regulation 1/2003. From the perspective of drafting a regulation, the second system is better because it is easier to include the right of the Commission in one regulation and not have to restate it in each block exemption. However, from the point of view of legal certainty, the first system was better and maybe this is why certain modern block exemptions do include some specific reasons for which the benefit of the exemption can be withdrawn. The undertakings receive more guidance by the specific reasons stated in the block exemptions and they benefit from this, especially since now competent national authorities can also exercise this right.

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[116] Article 10(c) of Regulation 418/1985 and Article 7(c) of Regulation 2659/2000
[117] Article 11(iv) of Regulation 2672/1988 and Article 12 (iv) of Regulation 83/1991
[118] Article 29(2) of Regulation 1/2003

2.4.7 Duration and Amendment

Block exemptions are valid only for a certain period of time, which is subject to modification. At the end of that period, the Commission usually amends the block exemption. The duration of a block exemption is essential because it makes the undertakings aware about the period of time for which their agreement will be exempted, providing legal certainty and allowing them to plan their future market behavior based on existing legal provisions. However, there were also situations in which block exemptions were amended before they expired. Thus, a negative aspect is that in practice it is hard to identify a rule regarding the usual duration of block exemptions. This is because, for example, the block exemption for transport by rail, road and inland waterway is in force since 1968 while Regulation 3604/1982 on specialization agreements was amended after only three years.

The amendment of a block exemption usually takes place when the Commission gains experience in that particular field by seeing how the undertakings react to the block exemption. On one hand, if certain legal provisions are not functioning as they should and the undertakings have an anti-competitive behavior, those provisions should be amended. On the other hand, undertakings would benefit more from block exemptions which are not frequently amended because the costs of redrafting their agreement, and rethinking their market behavior would be avoided. The solution used by the Commission is to provide a transitional period allowing the undertakings to adjust their agreements in order to continue to benefit from the block exemption. This solution is appropriate because it eliminates the anti-competitive effects from the market without causing extensive harm to undertakings. However, the Commission should be careful in not abusing its power of amendment by frequent modifications.

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2.5. Procedural Rules

After anayzing the main substantive elements of block exemptions, it is important to also examine the two prodedural phases on their application, the one imposed by Regulation 17/1962 and the one imposed by Regulation 1/2003. The first provided a centralized system while the second instituted a more decentralized system. Thus, Regulation 1/2003 improved the position of competent national authorities and national courts but the Commission and the European Court of Justice still retain certain exclusive rights.

Once Regulation 1/2003 entered into force, block exemptions could have been repealed because their rationale for existence, the increase workload for the Commission, disappeared by the elimination of the notification system.[119] Nevertheless, they were maintained and continue to be replaced because they provide legal certainty[120] which is of significant importance to undertakings.

2.5.1. Council Regulation 17/1962

Regulation 17/1962 was the first regulation to implement Articles 81 and it opted for a centralized system controlled by the Commission. The powers of the Commission were broad and they include the power to adopt recommendation and decisions, to make inquires into sectors of the economies, to conduct investigations, to impose fines and periodic penalty payments and to accept commitments from the undertakings and make them binding.[121] The role of the competent national authorities was only to assist the Commission in exercising its powers by sharing information and by conducting investigations and they could apply Article 81(1) only if the Commission had not acted in that particular case.[122] Thus, the Commission clearly played the central role of European Union competition law and this was needed in order to achieve a uniform application of these provisions in the conditions of the common

[119] Toth, op. cit., 126
[120] Ibid.
[121] Article 3, 12, 13, 15 and 16 of Regulation 17/1962
[122] Article 13 of Regulation 17/1962

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market. For the first period in which competition law was applicable in the European Union, this was the most appropriate solution.

In the relationship between the Commission and the undertakings, clearly the undertakings had the subordinate position. They had to provide information to the Commission and to notify the Commission if they sought exemption under Article 81(3).[123] The Commission would take a decision but that decision was subject to retroactive or non-retroactive revocation and amendment[124] and these provisions were capable of putting undertakings into difficult positions. Economic theory suggests that only as long as the costs imposed by an investigation are lower than the deadweight loss created by the restriction of competition, the authority should take action which is not the case in the European Union.[125] Furthermore, the Commission should act only if there are concrete reasons to suspect unlawful behavior and not to conduct habitual investigations which impose unnecessary costs on the undertakings. On the other hand, the rights of undertakings in front of the Commission included the right to address their concerns, the right for their business secrecy to be protected and the right to make commitments[126] which are the usual basic rights of any respondent.

2.5.2. Council Regulation 1/2003

Regulation 1/2003 was part of the modernization process. Regulation 17/1962 helped disseminate a competition policy but it was generally considered necessary to adopt a new regulation in order to prepare the future enlargements of the Community.[127] The new regulation creates a more decentralized system but the chief position is still occupied by the Commission. Three main changes were implemented by this regulation. First, no decision from the Commission is needed regarding the exemption under Article 81(3)[128] which

[123] Article 4 and 11 of Regulation 17/1962
[124] Article 8 of Regulation 17/1962
[125] Torok, Lecture on April 28, 2009
[126] Article 19 and 20 of Regulation 17/1962
[127] Recital 1 of Regulation 1/2003
[128] Article 1 of Regulation 1/2003

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simplifies the burecracy process and thus is a welcome change. Secondly, the competent national authorities and national courts have now the power to apply Article 81(3)[129] which was a needed change in the context of the enlargement since the number of undertakings in the European Union would increase significantly, unlike the staff of the Commission. Thirdly, the Commission has the sole power to adopt block exemptions[130] but now the competent national authorities are also given the power to withdraw this benefit in individual cases.[131] This means that even if a more descentralized system is created, the policy is still made by the Commission.

The relationship between the Commission and the competent national authorities is now more balanced, but the Commission still retains powers which are not available to the competent national authorities. The term used by the new regulation is "close cooperation"[132] as opposed to the term "cooperation"[133] used by the old regulation. Among the powers which are now shared there are the powers to apply Article 81(3), to require an infringement to be brought to an end, to order interim measures, to accept commitments, to impose fines and periodic penalty payments and to carry on inspections.[134] However, the competent national authorities still have an inferior position in their relationship with the Commission because, when the Commission initiates a procedure, the competent national authorities have to refrain from initiating or continuing their own procedures.[135] Another limitation of the competent national authorities powers is the fact that they cannot take decisions which run counter to a decision already taken by the Commission[136] in order to avoid inconsistencies. However, the reverse is not true which confirms the fact that policies are still determined by the

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[129] Article 3 of Regulation 1/2003
[130] Jones and Sufrin, 103
[131] Article 29(2) of Regulation 1/2003
[132] Recital 15 of Regulation 1/2003
[133] Recitals of Regulation 17/1962
[134] Article 5 of Regulation 1/2003
[135] Artile 11(6) of Regulation 1/2003
[136] Article 16(2) of Regulation 1/2003

Commission. In the European Union this is to be expected because the competition policies of the national states are harmonized at the supranational level.

Some of the powers of the Commission regarding undertakings are more detailed and broader. Under the new regulation, the Commission may in addition interview all persons who might have relevant information and not only the representatives of the undertakings, may affix seals and may enter all premises in which business records might be kept, including private homes, as long as the Commission has judicial authorization.[137] These increased powers of the Commission make undertakings more vulnerable. The reason stated in the recital is that it is getting harder and harder to detect infringements.[138] However, the Commission should impose some limits on its activity and not overburden undertakings against which there is no proof of unlawful behavior. This limitation would have been more powerful if included in the actual regulation but it may still be employed since the Commission does not have any interest in overburdening undertakings and creating resentment. The power to impose fines and periodic penalty payments has also been amended in a beneficial way because now they cannot exceed certain limits correlated to the size of the undertakings,[139] which eliminates the risk of under-punishment and over-punishment. Furthermore, undertakings can now be sanctioned for past infringements[140] and this is a welcome change. Under this regulation, the undertakings also gain some well deserved rights which improve their defensive perspective like the right to access their file.

By this regulation, the national courts are now able to apply Article 81(3) but are at the same time subject to certain limitations. For example, they cannot take decisions which run counter to a decision already adopted by the Commission[141] which means that the competence of the national courts is limited to areas in which the Commission has not issued a decision

[137] Article 17-21 of Regulation 1/2003
[138] Recital 25 of Regulation 1/2003
[139] Article 23-24 of Regulation 1/2003
[140] Article 7 of Regulation 1/2003
[141] Article 16(1) of Regulation 1/2003

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which infringes the freedom of the courts. This limitation is somewhat justified by the need for uniform jurisprudence and it is acceptable because the European Court of Justice still has unlimited jurisdiction to review the decisions of the Commission. On the other hand, a particular limitation is not acceptable. The power of the Commission to enter private homes is subject to judicial authorization of the national courts.[142] However, in giving such an authorization, the national courts cannot call into question the necessity for the inspection nor demand that it be provided with information in the Commission's file.[143] In such a context, it does not seem that the national courts have other option than to grant the judicial authorization which is a negative aspect that cannot be justified.

In sum, the introduction of a more decentralized system was needed due to the enlargement process. However, even if the adoption of Regulation 1/2003 resulted in some welcome changes, this modernized system is not free from fault. Thus, the powers of the Commission should have been more limited in its relationship with the undertakings and the national courts.

2.6. Current trends

The first major current trend in the European Union competition law is that economic arguments are gaining more and more weight. This is true for both the Commission, which implemented the modernized system, and for the European Court of Justice. This change was partially due to the increase use of economic principles in the undertakings' submissions.[144]

Two other more targeted current trends are also of importance. The first is more strictly related to block exemptions while the second one affects all areas of European Union competition law. First, block exemptions were originally and most frequently used to exempt certain categories of agreements from the prohibition contained in Article 81 but more

[142] Article 20(7) of Regulation 1/2003
[143] Article 20(8) of Regulation 1/2003
[144] Bishop and Walker, op. cit., 2

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recently they have also been used to exempt certain categories of state aid from the prohibition in Article 87 of the EC Treaty.[145] Even if state aid is generally prohibited, certain exceptions which promote a well-functioning and equitable economy are permitted.[146] Thus, the Commission has adopted Regulation 800/2008 which declared certain categories of aid compatible with the common market. The state aid may be directed, for example, to employment, training, small and medium size enterprises, research and development, environment and investments.[147] The second trend refers to damages in case of breach of competition law and it is marked by the White Paper from 2008. The aim of the White Paper is "to improve the legal conditions and victims' access to full compensation for breaches of Articles 81 and 82".[148] However, no actual steps were taken in this direction.[149]

2.7. Alternatives to the Block Exemptions System

After analyzing the evolution of block exemptions and the effects of the modernization process on substantive and procedural rules, it is interesting to observe how other legal system regulate collusion issues and whether they use block exemptions or not. The approaches employed by two legal systems are considered: the United States perspective, as the first country to implement a competition policy, and the South Africa approach, as a country which implemented its competition policy more recently.

The United States competition law is one of the major models of competition law in the world. In this legal system, economic arguments always win when competition law is applied[150] and this is the main feature that the European Union competition law lacks. The modernization process of the European Union competition law tried to eliminate this

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[145] Toth, op. cit., 121
[146] Archer Clive, *The European Union*, Routledge: London, 2008, 68
[147] http://europa.eu/rapid/pressReleasesAction.do?reference=IP/08/1110&format=HTML&aged=0&language=EN&guiLanguage=en
[148] http://europa.eu/scadplus/leg/en/lvb/l26124.htm
[149] Torok, Lecture on 26 May, 2009
[150] Van den Bergh and Camesasca, op. cit., 7

weakness by the introduction of market share thresholds. This proxy for market power was first used in the United States during the Reagan administration.[151] The term used by the United States legislation for the exemption of agreements below a certain market share thresholds is "safety zones". Furthermore, by the modernization process, the European Union moved to a more functional approach which is closer to the rule of reason approach employed by the United States. The hardcore restrictions maintained by the European Union correspond with *per se* restrictions in the United States.[152] The one notable difference is price fixing. If from the 1900s until 2007 it was illegal for United States manufactures to fix minimum prices, in 2007 the Supreme Court said that minimum prices are not automatically illegal. [153] The difference between the two systems is that the European Union treats price fixing as hardcore restrictions while the United States now analyzes price fixing under the rule of reason.

Torok has examined competition law in South Africa, a legal system which does not make use of block exemptions but grants individual exemptions.[154] The two main rules used by this legal system in collusion issues are *per se* and the rule of reason.[155] Under the first rule certain practices, like price fixing and partitioning of markets, are prohibited without needing an assessment of the effects.[156] The remaining majority of restrictive practices are prohibited only if they pass the substantial lessening of competition test.[157] This system resembles more the United States system than the European Union system. This is a suprinsing outcome because South Africa was a European colony which means the natural tendency would have been to follow the legal models from Europe. However, at the time its first competition law

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[151] Abbott, Lecture on May 19, 2009
[152] Ibid.
[153] Ibid.
[154] Torok, op. cit., 36
[155] Ibid.
[156] Ibid.
[157] Ibid.

was adopted, in 1955[158], the United States had the most experience in competition law which might explain the choice made by South Africa in drafting its competition law.

Thus, block exemptions as such seem to be the creation of European Union competition law although certain elements are similar to the ones from the United States. The United States and South Africa make use of the *per se* and the rule of reason, regulating this competition law area differently. This may be explained by the fact that the appereance of block exemptions was due to practical circumstances which probably arose because the European Union is a unique supranational organization.

In concluding this chapter, it is important to observe that block exemptions are a well developed legal technique which is frequently used by the Council and the Commission to regulate competition law. Until the late 1990s, their content was not sufficiently based on economic considerations, as was frequently pointed out in the literature. They contained certain important shortcomings like the fact that they were too prescriptive which limited the freedom of undertakings. However, the modernization process succeeded in giving more weight to economic considerations and employing a more functional approach. Nevertheless, some difficulties remained like the fact that only market shares are used as a proxy for market power and the fact that some of the Commission's powers are too broad. However, the positive aspects are more significant than the negative ones and, although some improvements would be welcome, overall block exemptions seem to be an efficient legal instrument in the European Union. After establishing that block exemptions are a viable way of regulating competition law, the next chapter is going to look at their actual content and their development over time.

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[158] Torok, op. cit., 7

CHAPTER 3 – MAJOR BLOCK EXEMPTIONS

Over time, the Commission and the Council have issued numerous consecutive block exemptions in different sectors of the economy. After examining in the first chapter their legal basis and establishing that the provisions of Article 81 do take into account economic considerations and concluding in chapter two that block exemptions are an adequate legal technique for regulating competition law, this chapter looks at all past and present block exemptions and examines how they developed over time. This is the most important step of the analysis of the development of block exemptions since it cannot be decided whether they bring more benefits or more drawbacks without looking at their actual content. Since their content is specific for each field regulated, it is appropriate to look jointly at the block exemptions for the same types of agreements, namely those regarding vertical agreements, those regarding horizontal agreements, those regarding transport agreements and those regarding insurance agreements.

3.1. Block exemptions under Council Regulation 19/1965

Regulation 19/1965 allows the Commission to declare Article 81(1) inapplicable to bilateral exclusive distribution or purchase agreements and to agreements which include restrictions regarding industrial property rights.[159] This regulation was amended by Regulation 1215/1999 in order for the Commission to be able to grant an exemption for the first category of agreements even if they are multilateral ones but for the second category the bilateral condition was maintained.[160] The agreements covered by these regulations are vertical ones. The Commission chose to issue both general block exemptions on vertical agreements and also more targeted block exemptions, on technology transfer, franchise and motor vehicle agreements. The analysis will start with technology agreements since these are

[159] Article 1(1) of Regulation 19/1965
[160] Article 1(1) of Regulation 1215/1999

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not covered and have never been covered by the general block exemptions on vertical agreements. The section will continue with franchise agreements because they are capable of falling either in the scope of technology transfer block exemptions or in that of the general block exemptions, the second one being the solution ultimately adopted by the Commission. The analysis will then continue with the general block exemptions on vertical agreements and will finally be concluded by analyzing the block exemptions on motor vehicle agreements which derogate from the general block exemptions.

3.1.1. Technology Transfer Agreements

From the standpoint of competition law, the granting of a patent or a copyright creates a monopoly for the holder[161] to exploit the invention for a limited period of time. The awarding of this right is necessary in order to create incentives for undertakings to invest in research and development. In addition to this, the Commission created a new incentive for undertakings to enter into technology transfer agreements by adopting block exemptions in this field. The Commission initially issued two separate block exemptions: Regulation 2349/1984 for bilateral patent licensing and Regulation 556/1989 for bilateral know-how licensing and bilateral mixed know-how and patent licensing. These two block exemptions had a very similar structure and were both amended by Regulation 151/1993. In 1996, the two separate block exemptions were combined by Regulation 240/1996 which was furthermore amended by Regulation 772/2004, in force until 2014.

Regulation 2349/84 and Regulation 556/1989 contained very similar white lists which included provisions that limited the freedom of the licensee, for example, the obligation to use the patent only for the period of the agreement, to confide its activities only in the contracted territory and in the predefined field, to observe minimum standards and confidentiality obligations, to mutually communicate any gained experience and to grant one another a non-

[161] Torok, Lecture on May 26, 2009

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exclusive license.[162] The rationale behind the second obligation, which is of great importance to competition law, is that if each licensee is assigned an exclusive territory, it will concentrate its efforts in that territory and thus the efficiency of the distribution system will consequently increase. All these obligations are typical for technology transfer agreements in which the licensor wants to protect its intellectual property rights and to ensure an effective distribution system. However, in these early block exemptions the strong prescriptive character criticized in the previous chapter is evident. In addition, these two block exemptions also contained very similar black lists which prohibited the determination of quantities, prices, discounts or consumers, the imposition of unwanted licenses to the licensee or the subjective refusal of demand from resellers.[163] These provisions were beneficial because they prevented an abusive behavior of the licensor. The main difference between these two early block exemptions was that the second limited certain obligations in time. They were later amended by Regulation 151/1993 which introduced separate market share thresholds for productions licenses, on one hand, and for production and distribution licenses, on the other hand.[164] This distinction can be explained by the fact that an agreement which covers both production and distribution is more likely to restrict competition than one which covers only production and thus it has to observe a lower threshold. In 2004, this distinction was replaced by a more economic distinction, between agreements entered into by competitors and those entered into by non-competitors which were analyzed in the previous chapter.

Regulation 240/1996 combined the two early block exemptions, maintaining the same basic exemptions. This was a welcome change because the two regulations were very similar and grouping their provisions into one block exemption and reducing the number of regulations and legal provisions is many times desirable as was pointed out in the previous chapter. The new regulation assumed a significant part of the provisions of the regulations it

[162] Article 1 and 2 of Regulation 2349/1984 and of Regulation 556/1989
[163] Article 3 of Regulation 2349/1984 and of Regulation 556/1989
[164] Article 3 of Regulation 151/1993

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replaced but it also brought several changes. The two most notable ones were the fact that the licensee was not even allowed to passively sell outside the contracted territory for a certain period of time and it could only supply a limited quantity of the licensed product to a particular customer.[165] Because these restrictions are likely to restrict competition and are not indispensable, they should not be exempted. Even if active selling outside the contracted territory is prohibited, passively selling outside that territory can still prevent the licensee from not adequately exploiting the technology since its customers can chose to purchase the product from other licensees. These provisions were detailed more in Regulation 772/2004, which replaced Regulation 240/1996, but unfortunately they were not eliminated in all situations. This new regulation was part of the modernization process employed by the Commission and thus it contains provisions in line with this process which were discussed in the previous chapter.

By exempting technology transfer agreements, the Commission validates the fact that competition law is applicable to intellectual property rights. However, by the issuance of the block exemptions, the Commission also confirms the fact that these agreements comply with the conditions of Article 81(3) and this is why they should be encouraged and not prohibited. The main benefit of these block exemption is the creation of incentives which increase the chances of a technology being exploited. First, since licensors can collect royalties without investing in the production and distribution of the products, they have an incentive to enter into these agreements. Second, since licensees will not face intra-brand competition in a certain territory, they have an incentive to invest in marketing the patented products. The creation of these incentives aims at benefiting consumers because it will increase the quantity of products available on the market. This is because usually the licensor cannot afford to market the same quantity of products as can several licensees. However, there is a harmful

[165] Article 1(6) and Article 2(13) of Regulation 240/1996

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aspect of these block exemptions and that is the possibility to prohibit passive sales in certain situations. This is because the licensee is afforded the possibility to not adequate exploit the technology if this is more profitable. In order to avoid this situation, the early regulations provided that the Commission could withdraw the benefit of the exemption if the licensor did not have the power to terminate the agreement when the licensee failed to adequately exploit the patent.[166] However, it was unlikely that this provision would achieve its purpose in reality since the licensor is mainly interested in receiving its royalty which is in many cases fixed and not in the well-being of the consumers. Probably this is why a later regulation amended this right in the sense that the Commission could withdraw the benefit if the patent was not adequately exploited[167] without the need for the licensor to take action.

The exemption of technology transfer agreements is needed for two main reasons. First, the undertaking which develops a technology might not be the most suitable one to also exploit it. By permitting the licensing of that technology, the licensor still retains some control of the exploitation of its technology which would not be possible if a sale was concluded. Second, by exempted these agreements, potential licensees will benefit from legal certainty which will create an incentive for them to enter into such agreements. The conclusion of these agreements is desirable because they help disseminate knowledge[168] which makes consumers better off.

3.1.2. Franchise Agreements

Franchise agreements benefited from only one block exemption. Regulation 4087/1988 declared Article 81(1) inapplicable to bilateral franchise and master franchise agreements. The white list provided for by this regulation covered a variety of obligations. First, the franchisee was granted an exclusive territory outside of which it could not exploit the

[166] E.g. Article 9(3) of Regulation 2349/1984
[167] Article 6(2) of Regulation 772/2004
[168] Recital 3 of Regulation 240/1996

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franchise and was prohibited to make use of competing products other than spare parts or accessories.[169] Second, the white list contained obligations typical for franchise agreements aimed at preserving the common identity and reputation of the network and at preventing the disclosure of the know-how. These are representative obligations in a franchise agreement and by their enumeration in the block exemption, the Commission confirms its early preference for a strong prescriptive effect which is considered the main drawback of earlier block exemptions. In addition, the regulation provided for a black list among which the most important was the prohibition to the franchisor to determine sale prices and to impose unreasonable obligations to the franchisee.[170] These provisions are an adaptation of the list with prohibited restrictions contained in Article 81(1).

The Commission considered bilateral franchise agreements beneficial because they created a uniform network, improved distribution and signaled a certain standard of quality[171] from which consumers benefit. In order to prevent the elimination of competition, parallel imports and cross deliveries between franchisees were permitted.[172] From an economic point of view, the franchise agreement is characterized by the fact that the franchisee makes a specific investment incurring sunk costs. Thus, "franchising increases the specificity of investment for the satellite business, compared with independent operation".[173] This characteristic protects the franchisor because the franchisee is unlikely to breach the agreement since this would mean that it will not recover its sunk costs. On the other hand, the franchisee must also be protected precisely because it has incurred sunk costs and it should be given the possibility to recover them. This is the main purpose of this block exemption, the guaranteeing of certain rights to the franchisee which will make it easier to recover the sunk costs.

[169] Article 2(c,d) of Regulation 4087/1988
[170] Article 5 of Regulation 4087/1988
[171] Recital 7 and 8 of Regulation 4087/1988
[172] Recital 12 of Regulation 4087/1988
[173] Dnes, op. cit., 93

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Franchise agreements posed a regulatory problem because they could have been included either in the technology transfer block exemptions or in the vertical agreement block exemptions. The initial solution chosen by the Commission was to issue a separate block exemption. However, due to the tendency of consolidating the block exemptions, franchises agreements had to be fitted in one of the other vertical block exemptions. Franchising is a little more than licensing know-how because many more business aspects are controlled in franchising agreements since the aim is to signal out a certain quality to the consumers. The differences between franchising agreements and vertical agreements are less obvious and this is probably why the Commission has chosen not to renew Regulation 4087/1988 and just include the exemption in the scope of Regulation 2790/1999, which is the general block exemption on vertical agreements currently in force.

3.1.3. Vertical Agreements

Vertical agreements are those concluded between undertakings operating at a different level of the distribution system. Regulation 67/1967 was the first regulation to exempt bilateral exclusive supply and/or purchase for resale agreements. This regulation was modified by Regulations 1983/1983 and 1984/1983 which were then replaced by Regulation 2790/1999. Special provisions were provided in Regulation 1984/1983 for beer, fuels and motor vehicles. While those for beer and fuel are no longer applicable and were included in only one regulation, agreements regarding the exclusive supply of motor vehicles benefited from three consecutive block exemptions which will be discussed in the next sub-section.

Regulation 67/1967 exempted provisions in vertical agreements which limited the freedom of the exclusive dealer by imposing a certain market behavior regarding quantities, stocks, sales network, product ranges, staff and advertising and by limiting its activities to the contracted territory.[174] These limitations were explained by the need to provide a coherent

[174] Article 2 of Regulation 67/1967

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distribution system which would benefit consumers. The regulation also contained provisions aimed at preventing the elimination of competition. Thus, the exemption was not applicable to reciprocal exclusive dealing obligations between competing manufactures and if intermediaries or consumers were worse off due to abusive behavior.[175] These provisions were needed in order for the block exemptions to comply with the conditions of Article 81(3). Regulation 1983/1983 and 1984/1983 maintained these exemptions, the first regulation for bilateral exclusive supply agreements and the second one for bilateral exclusive purchase for resale agreements. The new regulations introduced a new protection for the dealers, the supplier's obligation not to provide the contracted goods to users in the contracted territory,[176] and a new protection for the suppliers, the dealer's or reseller's obligation to obtain the contracted goods only from the other party.[177] These provisions only increase the prescriptive character of these block exemptions, which is a negative aspect, as was discussed in the previous chapter. This is because these are typical provisions for vertical agreements and the parties would probably choose to include them in the agreement voluntarily.

Regulation 1984/1983 also contained special provisions for beer supply and services station agreements, the first ones referring to the distribution of beers and/or other drinks in the contract premises and the second ones referring to fuels and other petroleum based motor vehicle. According to the regulation, the agreement could contain a ban on the reseller to sell competing products or a different type of products unless certain conditions were met.[178] These provisions do not seem to benefit consumers because they limit the choices the consumers can make in each establishment. The reason for these special provisions was the fact that the supplier provided the reseller with special commercial or financial advantages in

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[175] Article 3 of Regulation 67/1967
[176] E.g. Article 2(1) of Regulation 1983/1983
[177] E.g. Article 2(2)(b) of Regulation 1983/1983
[178] Article 8(b) of Regulation 1984/1983

the hope for a long term agreement[179] and thus the supplier had to be protected. However, in this situation, protecting the supplier was done at the expense of the consumers which is not in accordance with the conditions imposed by Article 81(3). There is no compeling reason for which agreements regarding these products should benefit from a special treatment and should not just be covered by the general block exemption on vertical agreements. This was also indirectly recognized by the Commission since these special provisions were not taken over by the new block exemptions.

Regulation 2790/1999 was the first regulation adopted by the Commission in its modernization process and contains provisions in accordance with this approach, which were discussed in the previous chapters. The regulation declared Article 81(1) inapplicable to agreements relating to purchase, sell or resell of certain products regardless of the number of parties involved as long as certain thresholds were not exceeded. Furthermore, the block exemption provided for a typical black list aimed at preventing the restriction of competition and abusive behavior.

The reason for adopting block exemptions on vertical agreements was the fact that these agreements are considered to improve the distribution system.[180] This is true because several dealers can maintain a much better and a more efficient distribution system than just one undertaking. Consumers are considered to benefit from the improvement in distribution but also from the fact that they have a closer relationship with their dealer. In order to respect the conditions of Article 81(3), the manufacture is permitted to retain the control of the distribution system by the imposition of certain minimum standards while the dealers are prevented from becoming over dependent on the manufacturer.

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[179] Recital 13 of Regulation 1984/1983
[180] Recital 6 of Regulation 2790/1999

3.1.4. Motor Vehicle Agreements

Regulation 123/1985 declared Article 81(1) inapplicable to bilateral exclusive supply of motor vehicles agreements. Its main provisions are the same as those which were included in the two regulations from 1983 discussed in the previous sub-section. Regulation 1475/1995 maintained the exemption but allowed more freedom to the dealers. Thus, under the new regulation, they were allowed to sell competing products if they used separate sales premises and separate management.[181] This was a welcome change because, under the former approach, it was possible for a supplier not to be able to find a dealer which was not already part of an exclusive supply motor vehicle agreement. On the other hand, these suppliers should not be allowed to free ride on the investment made by a previous partner and this is why the dealer had to use separate sales premises and separate management. These provisions constitute the main difference between the block exemption on motor vehicle and the block exemption on vertical agreements. Regulation 1400/2002 uses a different structure than these two earlier block exemptions but its provisions resemble in great part Regulation 2790/1999.

The Commission justified these very specific block exemptions by the fact that motor vehicles are consumer durables which require expert maintenance and repair.[182] This is true, but having a separate line of block exemptions on motor vehicle agreements seems a little too much. This is because the general block exemptions on vertical agreements could have included some special provisions for this sector without the need to issue separate block exemptions. This is why the simplification of the block exemption system would be a welcome change in the competition law in the European Union. Because Regulation 1400/2002 is due to expire in 2010, a round table[183] was held by the Commission in February

[181] Article 3(3) of Regulation 1475/1995
[182] Recital 4 of Regulation 1475/1995
[183] http://europa.eu/rapid/pressReleasesAction.do?reference=MEMO/09/57&format=HTML&aged=0&language=EN&guiLanguage=en

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2009 in order to discuss what it is best for the industry and what changes would changes are favored by the different parties of the industry.

In concluding this section, it is important to observe the fact that the issuance of block exemptions regarding vertical agreements is justified by the fact that an improved distribution system complies with the conditions imposed by Article 81(3). However, a welcome change would be the consolidation of these block exemptions. Even if there are enough special characteristics to justify the separate exemptions of technology transfer agreements, this is not true for the motor vehicle agreements.

3.2. Block Exemptions in the Transport Sector

The transport sector is characterized by extremely high fixed and operating costs. First, the infrastructure is expensive and this is why in most situations it is provided by states. Second, the means of transportation are also expensive but they are usually owned by the undertakings. Third, it is hard for the undertakings to adjust the amount of their services to the demand. This is why pooling is very important in this sector since it makes the transport activities more efficient. However, in order to maintain competition on the market, the Commission has issued block exemptions in which it permits pooling in certain circumstances. These block exemptions regulate all kinds of transport, by rail, road, inland waterway, maritime and air. First, the block exemption for rail, road and inland waterway will be analyzed because it is the oldest one and it served as a model for the latter ones. Second, the maritime transport block exemptions will be analyzed because, even if they resemble closely the previous block exemption, the Commission's perception on them changed significaltly over time. Third, air transport block exemptions will be examined finally because they contain more specific characteristics.

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3.2.1. Transport by Rail, Road and Inland Waterway

The transport by rail, road and inland waterway benefited from only one block exemption which has several distinctive features. Council Regulation 1017/1968 uses a different structure than the one used by all the other regulations issued by the Commission. First, this regulation prohibits certain restrictive agreements and then creates two exemptions and two situations in which Article 81(1) may be declared inapplicable. The Commission' regulations from the same period and until 1999 began by exempting certain agreements, continued by stating the allowed clauses and at the end provided the situations in which the exemption was not applicable.

The agreements prohibited by Regulation 1017/1968 are those which restrict competition and those which create competitive disadvantages for certain undertakings. Provisions which fall in the first category are those which fix transport rates and conditions, control the supply of transport or share the markets[184] while provisions which fall in the second category are those which apply dissimilar conditions to equivalent transactions and impose unrelated additional obligations.[185] These conditions resemble the ones listed in Article 81(1) and which were discussed in the first chapter. The only difference is that they are adapted to the transport by rail, road and inland waterway sector.

The two types of agreements exempted by this regulation regard technical agreements and the operation of groupings. First, the exemption regarding technical agreements permits undertakings to enter into agreements regarding standardization, pooling or exchange of equipment, installations or staff, organization of combined transport operations and coordination of transport timetables for connecting routes.[186] The reason for this exemption is the fact that the operation of transport services supposes the utilization of a large quantity of

[184] Article 2 of Regulation 1017/1968
[185] Ibid.
[186] Article 3 of Regulation 1017/1968

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resources and, if an undertaking does not have these resources, it should be allowed to borrow them from other undertakings in order to provide the services. This exemption provides an increase level of efficiency because, for example, installations not used at a particular moment by the owner can be put to use by another undertaking which needs them. If this is not possible, the undertaking which needs the installation would be forced either not to provide the service or to buy additional installations even if it knows they will not be frequently used. These last two are inefficient solutions and this is why this regulation makes it possible for the efficient solution to be employed. The second exemption follows the same reasoning but refers to the operation of groupings by small and medium size undertakings. This exemption allows smaller undertakings to carry on transport activities and joint financing or acquisition of transport equipment or supplies[187] and thus compete with larger undertakings. This exemption is also beneficial because it allows for more competitors to be present on the market which benefits consumers and prevents large transport undertakings to behave abusively.

Because the transport market is subject to considerable temporal fluctuation and disturbances,[188] the regulation provides two situations in which Article 81(1) may be declared inapplicable. These situations refer to agreements which contribute to improving the quality and the stability of transport services, increase productivity or furthering technical or economic progress and reduce disturbances as long as they do not impose unnecessary restrictions and do not eliminate competition.[189] This possibility is beneficial for consumers because it ensures that transport services will be available off season as well, even if it is not profitable for only one undertaking to provide them, by allowing the services to be provided through cooperation agreements.

[187] Article 4 of Regulation 1017/1968
[188] Recitals of Regulation 1017/1968
[189] Article 6 of Regulation 1017/1968

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Regulation 1017/1968 is the block exemption which was in force for the longest period of time and is still applicable today. Its principles have been used in the drafting of the other block exemptions regarding transportation. However, because the maritime and air transport have suffered more changes in this period than the transport by rail, road and inland waterway, those block exemptions were amended several times. Still, Regulation 1017/1968 remains a model of legal certainty which would be desirable to be achieved by the other block exemptions as well.

3.2.2. Maritime Transport

Maritime transportation is an important element of the Community's trade but it requires large capital infusions. Furthermore, this field is based on a complex structure and this is why two sets of block exemptions were issued, the first one regarding liner conferences and the second one regarding consortia operations. The first type of block exemptions expired in 2008 and was not renewed while the second one will expire in 2010. The common feature of all block exemptions was that they regulated international maritime transport services involving at least one Community port.

Regulation 4056/1986 was the first block exemption regarding liner conferences and declared Article 81(1) inapplicable to technical agreements regarding the application of standards, pooling of resources, the organization of successive maritime transport operations, the coordination of transport timetables for connecting routes and the consolidation of individual consignments.[190] This exemption was basically the same as the first exemption provided for by Regulation 1017/1968 in the transport sector. Furthermore, as did Regulation 1017/1968, Regulation 4056/1986 also provided that the exemption was not applicable if the agreement restricted competition. In addition, Regulation 4056/1986 also attached the obligation to seek solutions through consultations and the possibility of transport users to

[190] Article 2 of Regulation 4056/1986

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approach whichever undertakings they chose in respect of inland transport operations and dockside services.[191] Regulation 4056/1986 was repealed by Regulation 1419/2006 which provided that the exemptions continued to apply until 2008 except for that regarding technical agreements in respect of liner conferences.

Regulation 4056/1986 did not apply to consortia agreements and this is why Regulation 870/1995 was issued and declared Article 81(1) inapplicable to consortia operations within or outside a liner conference. The agreements exempted were those which contained mainly the same provisions as those exempted under Regulation 4056/1986. In addition to Regulation 4056/1986, the agreement could not include provisions regarding the non-utilization of existing capacity.[192] This is an important positive aspect of the regulation because it makes it impossible for the undertakings to agree to reduce the supply in order to obtain monopoly profits. Furthermore, its provisions were intended to maintain the freedom of the members since the right to withdraw from the consortium or to engage in independent marketing were included.[193] Regulation 823/2000 maintained exactly the same exemption as Regulation 870/1995 and was amended by two regulations. First, Regulation 463/2004 made minor modifications to the obligation regarding real and effective consultations and second, Regulation 611/2005 also made minor amendments regarding the right of a member to withdrawal and effective price competition between the members.

The usefulness of liner conferences and consortia operations was subject to many debates. In 1986, the Commission considered liner conferences useful because they ensured reliable services, provided for efficient scheduled maritime transport services, gave fair consideration to the interests of users and were facing effective competition from non-members, tramp vessels and other modes of transport.[194] However, in 2006 the Commission

[191] Article 3 and 5 of Regulation 4056/1986
[192] Article 4 of Regulation 870/1995
[193] Article 8(2) of Regulation 870/1985
[194] Recitals of Regulation 4056/1986

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concluded that liner conferences no longer fulfilled the conditions of Article 81(3) for four reasons. First, the same structure was used in other industries which were not exempted.[195] Second, the number of individual service agreements which achieved the same results and ensured price stability had increased considerably.[196] Third, transport users considered that conferences operated for the benefit of the least efficient members.[197] Fourth, there was hardly any price competition with respect to surcharges and ancillary charges in a conference.[198] This evolution shows that the economic circumstances can change in such a manner that a block exemption is not justified even if in the past it was reasonable. This is why these block exemptions expired in 2008 and were not renewed. At the same time, consortia operations were considered by transport users less restrictive because no price fixing was involved and because they provided efficient scheduled maritime services.[199] This development shows that it is very hard to assess a priori the impact of a certain block exemption and how that block exemption will function once the industry changes. It is important thus for the Commission to be able to review these block exemptions ex post and decide whether they were beneficial or not and if they should be maintained, amended or eliminated.

3.2.3. Air Services

The air services industry benefited from block exemptions for a period of eighteen years. After an impressive number of changes, the Commission concluded that after 2006 this industry should not benefit from block exemptions anymore. Even the Council regulations which conferred to the Commission the power to issue block exemptions in this industry were modified several times. Within the air transport industry, three main areas were affected by block exemptions: joint planning and coordination, computer reservation systems and ground handling services.

[195] Recital 3 of Regulation 1419/2006
[196] Recital 4 of Regulation 1419/2006
[197] Recital 5 of Regulation 1419/2006
[198] Recital 7 of Regulation 1419/2006
[199] Recital 6 of Regulation 1419/2006

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The first area was the most difficult one and, on average, changes were introduced every three years. The opening block exemption was Regulation 2671/1988 which declared Article 81(1) inapplicable to agreements whose purpose was joint planning and coordination of the capacity, sharing of revenue from scheduled air services, consultations for the joint preparation of proposal on tariffs for carriage, slot allocation and airport scheduling.[200] Regulation 84/1991 eliminated the exemption regarding the sharing of revenue and amended the exemptions regarding consultations and the one regarding slot allocation and airport scheduling. After only two years, Regulation 1617/1993 also amended these exemptions and provided detailed rules for each of them. After some minor amendments brought by Regulation 1523/1996, the exemption regarding joint planning and coordination and the one regarding a scheduled air service on a new or on a low-density route were eliminated. Furthermore, Regulation 1459/2006 restated the remaining two exemptions. The initial intention of the Commission was to ensure a satisfactory supply of services during less busy times and routes, to encourage the operation of flights on routes that were not in themselves profitable, to promote consultations between carriers and to ensure that discriminatory behavior is not possible.[201] In order to achieve this, the Commission provided detailed and special rules in an attempt to cover each situation. These rules provided little flexibility and thus could not be adjusted to the changes in the industry and to the anti-competitive behavior of the undertakings. This is why they were modified so many times and provided little legal certainty to the undertakings concerned.

Secondly, computer reservation systems benefited from three block exemptions. Regulation 2672/1988 declared Article 81(1) inapplicable to agreements regarding the joint development of a computer reservation system or a system vendor[202] as long as the undertakings' behavior was non-discriminatory. Regulation 83/1991 brought several changes

[200] Article 1 of Regulation 2671/1988
[201] Article 2 of Regulation 2671/1988
[202] Article 1 of Regulation 2672/1988

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in order to ensure the fact that the system vendor cannot treat the air carriers discriminatorily and that the participants provide comprehensive and accurate data.[203] On the other hand, the information had to be provided to interested parties upon request with the exception of personal information.[204] Regulation 3652/1993 maintained this exemption and brought about minor amendments regarding the termination of the agreement and the requirement for a non-discriminatory conduct for the manipulation of data and the availability of marketing, booking and sales data. The Commission considered these systems efficient because they ensured services like making reservations, printing tickets and issuing boarding passes to consumers based on up-to-date and detailed information.[205] These block exemptions were beneficial because only few undertakings could afford to have their own computer reservations systems. Thus, cooperation in this field should be permitted especially since consumers benefit if they do not need to use more computer reservation system but only one on which they can access all the information they need.

The third area exempted was more straightforward and benefited from only one block exemption. Regulation 2673/1988 declared Article 81(1) inapplicable to bilateral exclusive supply agreements regarding all technical and operational ground handling services. However, the exemption was not applicable if services were unreasonably bundled together, if the power of choice of the air carrier was limited and if unreasonable conditions were imposed.[206] The Commission justified this block exemption by the fact that these agreements help ensure that high standard quality services are provided at reasonable cost.[207] On the other hand, this exemption was valid only for four years which means that its expected benefits did not actually take place in practice.

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[203] Article 5 of Regulation 83/1991
[204] Article 6(2) of Regulation 83/1991
[205] Recital 3 of Regulation 83/1991
[206] Article 3 of Regulation 2673/1988
[207] Recital 3 of Regulation 2673/1988

In concluding this section, it is important to point out that air and maritime transport services pose many more drafting difficulties than the transport services exempted by Regulation 1017/1968. A reason for this might be the detail in which those block exemptions entered, which did not permit any adjustments or interpretations. This only emphasizes the fact that the structure of this industry is complex and the effects of a block exemption are difficult to foresee. The many changes caused the benefits of the block exemptions to be reduced significantly which might be the reason for which the Commission decided not to exempt agreements in this industry anymore.

3.3. Horizontal Block Exemptions

Horizontal agreements are those concluded by undertakings operating at the same level of the distribution system. The main risk posed to competition by horizontal agreements is the risk of foreclosing the market. However, there are two areas, specialization agreements and research and development agreements, in which the conditions of Article 81(3) are generally considered to be satisfied and their pro-competitive effects are considered to be greater than their anti-competitive effects. An interesting aspect is the fact that the Council also gave the Commission the power to adopt a standardization block exemption but it chose not to do so and it only included certain provisions on standards in other block exemptions. The specialization agreements will be analyzed first because they were adopted initially by the Commission and the research and development block exemptions adopted later were inspired from them.

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3.3.1. Specialization Agreements

Specialization agreements benefited from five consecutive block exemptions during a period of almost forty years: Regulation 2779/1972, Regulation 3604/1982, Regulation

417/1985, Regulation 151/1993 and Regulation 2658/2000, the last one being currently in force.

Regulation 2779/1972 declared Article 81(1) inapplicable to specialization agreements in which the parties mutually agreed not to manufacture certain products that the other party would manufacture. In order for each party to be protected, they were prohibited from concluding similar agreements for equivalent products and purchasing the contracted products from other undertakings.[208] Furthermore, certain minimum standards regarding quality, stocks and guarantee services had to be observed.[209] Regulation 3604/82 modified this exemption in order to cover specialization agreements in which the parties mutually undertake to only manufacture certain products jointly. This regulation had a shorter life span than initially thought and was repealed by Regulation 417/1985. The new regulation maintained the exemption provided by the former regulation and was amended by Regulation 151/1993. The new regulation extended the exemption to the obligation to grant the exclusive distribution rights to one of the parties, to a joint undertaking or to a third party under certain conditions.

After the expiration of Regulation 417/1985, Regulation 2658/2000 was applicable. The new regulation brings more clarity to the exemption and declares Article 81(1) inapplicable to unilateral specialization agreements, reciprocal specialization agreements and joint production agreements. The new regulation provides supply and purchase obligations in the actual exemption and permits even exclusive purchase and/or exclusive supply obligations and joint distribution. Furthermore, the exemption is applicable to agreements which do not have specialization as the primary object but to which specialization is directly related to and necessary[210] in accordance with the adoption of a more functional approach employed by the modernization process and discussed in the previous chapter. Furthermore, the new regulation

[208] Article 2(1) of Regulation 2279/1972
[209] Article 2(2) of Regulation 2779/1972
[210] Article 1(2) of Regulation 2658/2000

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also black listed certain provisions which would restrict competition and which are in accordance with the list contained in Article 81(1).

The Commission justifies the specialization block exemptions by the fact that they enable undertakings to work more rationally and improve production and distribution since each undertaking concentrates only on certain products.[211] Thus, such an exemption creates economic benefits in the form of economies of scale or scope or better production technologies. From an economic point of view, specialization agreements are desirable because they allow each undertaking to focus on what they are better at and thus inefficiencies are eliminated. In the evolution of these block exemptions it is interesting to point out that the exemption provided by the current block exemption was possible due to the adding and building upon done by the previous block exemptions.

3.3.2. Research and Development Agreements

The EC Treaty imposes the obligation on the Community to encourage research and development activities and cooperation between undertakings in the research and development field.[212] This is probably one of the reasons for which this field benefited from three block exemptions: Regulation 418/1985, Regulation 151/1993 and Regulation 2659/2000, in force until 2010. These block exemptions follow the structure and types of amendments introduced by the specialization block exemptions.

By Regulation 418/1985, Article 81(1) was declared inapplicable to joint research and development agreements which may contain or not joint exploitation provisions. This exemption was applicable only if the work was carried out within the framework of a program and all parties had access to the results which were protected by intellectual property rights.[213] Furthermore, the agreement could contain obligations which limited the freedom of the

[211] Recital 8 of Regulation 2658/2000
[212] Article 3(1)(n) of the EC Treaty
[213] Article 2 of Regulation 418/1985

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parties, ensured the efficiency of the research and development activity and equalized the efforts and benefits of each party. The exemption did not apply if the agreement restricted research and development activities in other fields and by third parties, restricted competition by its effects or did not put the products on the market for a specified period[214] which is in accordance with the conditions of Article 81(3).

Regulation 418/1985 was amended by Regulation 151/1991 which introduced different market share thresholds and extended the exemption in order to also cover the granting of the exclusive right to distribute the contract goods to one of the parties, to a joint undertaking or a third undertaking under certain conditions. Regulation 2659/2000 maintained this exemption but extended it further, to also cover agreements that do not have as their primary objective research and development activities but these activities are directly related to and necessary for their implementation,[215] exactly like the amendment to specialization agreements block exemption done in the same year. Furthermore, the new regulation provides that the exemption is not applicable if the results of the activity are not exploited.[216] The aim of this requirement is to ensure the proper exploitation of the results of the research and development activities because, since the undertakings part to the agreement have already benefited from the exemption, it is fair that the consumers should benefit as well.

The Commission justifies the research and development block exemptions by the fact that these agreements increase technical and economic progress by the dissemination of technical knowledge between the parties and the avoidance of duplicated work.[217] Furthermore, consumers are expected to benefit from new, improved or cheaper products.[218] However, economic theory justifies the fact that research and development activities should be exempted by the fact that the sharing of the costs increases the incentives of undertakings

[214] Article 6 of Regulation 418/1985
[215] Article 1(2) of Regulation 2659/2000
[216] Article 5 of Regulation 2659/2000
[217] Recital 2 and 10 of Regulation 2659/2000
[218] Recital 12 of Regulation 2659/2000

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to invest in research and development activities.[219] Economic theory does not regard the avoidance of duplicated work as a valid reason because "we do not regard competition between several gas stations as wasteful even when we know that only one will survive."[220] Furthermore, the duplication of work is not often a problem which arises in practice since there are more ways of solving the same problem and, as long as one solution is better than the others, the duplication of work should not be regarded as wasteful.

In concluding this section, it is important to observe that the development of the block exemptions for specialization and research and development activities was gradual, each block exemption broadening the scope of the previous exemption. Furthermore, these types of agreements are generally considered to comply with the conditions of Article 81(3) because the specialization agreements allow for complementary technologies to be integrated while the research and distribution agreements combine the researching efforts of more undertakings, making it more probably for the activity to be successful.

3.4. Insurance block exemptions

The insurance industry is characterized by the fact that undertakings will not survive in the market unless they cooperate.[221] However, this economy sector benefited from the first block exemptions long after other economic sectors. An explanation for this might be the fact that the need for cooperation was considered so obvious that a block exemption was not issued. Only in 1992 was the first block exemption issued in this field. Regulation 3932/1992 was then replaced by Regulation 358/2003 which will be applicable until 2010.

The first block exemption provided four main exceptions which were replaced by six exemptions by the second regulation. However, in reality, the exemptions remained the same

[219] Motta,op. cit., 204
[220] Dnes, op. cit., 36-37
[221] Torok, Lecture on May 22, 2009

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but formally the first exception from the old regulation was divided into three exceptions in the new regulation. The main changes brought about by Regulation 358/2003 were to include more protections for the consumer, to facilitate market entry for new undertakings and to create the conditions for the coverage of new risks. The new block exemption only builds on the old regulation and it does not end the benefits awarded by the old regulation.

The first exception refers to the calculation of common risks and tariffs based on statistical data collected from the parties regarding the frequency with which certain risks occur, the number of claims and the amounts paid, payable or insured for those situations.[222] On the basis of these statistics, premiums are calculated and, if more data is available, the calculation is more precise. The aim of the exemption was to improve the ratings of risks for undertakings without the parties being obliged to use this data. The new regulation brought two changes, one regarding the data and one regarding the users. First, the new block exemption provided for the statistical data to be gathered from all undertakings but be maintained as detailed and as differentiated as possible.[223] This improvement is beneficial because it allows for the more precise calculation of probabilities since data is available from all the undertakings on the market and not only from the parties to an agreement. Second, any undertaking may consult this data.[224] This change is also welcome because it reduces the costs of making their own studies for undertakings which would like to enter the market.

The second exception refers to the establishment of standard policy conditions. This exception covers cooperation agreements for designing illustrative standard policy conditions in order to facilitate comparisons and assure transparency.[225] However, the agreement cannot impose on the parties the obligation to use these conditions or other obligations that would distort competition or would negatively affect the position of the consumers. The new block

[222] Title II of Regulation 3932/1992
[223] Article 3(1)(b) of Regulation 358/2003
[224] Article 3(2)(c) of Regulation 358/2003
[225] Title III of Regulation 3932/1992

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exemption made these standard policy conditions generally available and awarded two types of new protections to the consumer. First, a requirement not to impose policies for more than three years and automatic renewal periods for more than one year were introduced.[226] Second, the requirements not to reinstate a policy without consent, not to impose cover from the same undertaking for different risks and not to require the transfer of the policy along with the transfer of the object insured were introduced.[227] These changes are beneficial for consumers because they have a lower bargaining power which makes it possible for undertakings to abuse their position.

The third exception refers to the common coverage of certain types of risks. This exception regards cooperation agreements that have as their object co-insurance and co-reinsurance.[228] The aim of this exception is to ensure a better coverage of difficult risks by permitting cooperation under certain conditions in this market segment. However, in order to ensure that competition is not eliminated, certain combined market share thresholds must not be exceeded. In fact, if these thresholds are exceeded, the exception does not even make sense because the undertakings are more able to cover these difficult risks. Thus, this exception creates competitors for the markets which cover difficult risks. The new regulation also exempts the formation of groups for the exclusive coverage of genuine new risks.[229]

The fourth exception refers to the establishment of common rules for the testing and acceptance of security devices. This exception regards agreements on harmonization and standardization of technical specifications.[230] This system of evaluation and certification of undertakings is based on well defined criteria. Its aim is to remove the need for repeated individual evaluation which makes it harder for consumers to make comparisons.[231] Also, this

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[226] Article 6 of Regulation 358/2003
[227] Ibid.
[228] Title IV of Regulation 3932/2003
[229] Article 7 of Regulation 358/2003
[230] Title V of Regulation 3932/1992
[231] Recital 17 of Regulation 3932/1992

system aims at promoting competition by creating transparency regarding the technical devices used by undertakings. However, each undertaking is free to use another system of evaluation and certification. The new block exemption limits this exemption to situations for which standards at the Community level are not available. They still have to be objective, non-binding and available in a non-discriminatory manner.

In the insurance sector the main concern of the regulatory authorities is the fact that consumers are in a much weaker position than the undertakings, which may allow for abusive behavior. However, these block exemptions do not only afford more protection to consumers by increase transparency and facilitation of making comparisons but they are also are beneficial for the undertakings. This is because undertakings gain from more precise calculation, the elimination of the need to repeat individual inspections regarding technical specifications and the cost savings regarding the communication to the public of the criteria applied while maintaining their freedom of decision regarding the usage of these advantages. Furthermore, smaller undertakings benefit from the elimination of an entry barrier for the insurance market and for the difficult risks insurance market. However, another reason for exempting insurance agreements was proposed by the literature and this is the fact that the Commission's goal is to break down the national insurance markets[232] since, in general, "the Commission has held that the geographic market for insurance products is national."[233] Given the importance of the single market for the political factors and the fact that risks are also country specific, this is an acceptable view.

The aim of this chapter was to trace the development of block exemptions in different sectors of the economy over time in order to decide whether they bring more benefits or drawbacks to the competition law system in the European Union. The main conclusion is that

[232] Wulf-Henning Roth, "European Competition Policy for the Insurance Market", *European Competition Law Review 2000*, 21(2), 107
[233] Toth, 184

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the content of the block exemptions has developed gradually, by the adding new provisions or eliminating old provisions. The second conclusion is that these block exemptions build upon the conditions of Article 81 but sometimes just restate these conditions in a different form. For example, the black lists in many regulations, especially the later ones, resemble closely the list provided for by Article 81(1). It is true that these block exemptions bring more legal certainty because they adapt the conditions of Article 81 to specific sectors of the economy. However, at the same time, by regulating in detail a certain sector of the economy, these block exemptions provide little flexibility. This is most obvious in the maritime transport sector. A solution for this would be that the block exemptions use a more simplified form and, instead of repeating the provisions of Article 81, just provide the specific rules applicable if this is necessary. The first step was made by the elimination of the white lists during the modernization process. Maybe the next step would be to eliminate other unnecessary provisions, like the ones which only restate the conditions of Article 81.

The most typical justifications identified for the use of regulations are the existence of natural monopolies, externalities, inadequate information, excessive competition and unequal bargaining power.[234] The side conclusion of this chapter is that in many cases the issuing of block exemptions is not based on these justifications and only information assymentry and unequal bargaining power have a certain role. In reality, these block exemptions have in common the fact that they were adopted based on the idea that the agreements exempted are likely to have more pro-competitive benefits than anti-competitive benefits. If no other solution is available, this might be a good one because it provides legal certainty. However, care must be taken by the regulatory authorities not to overburden undertakings unnecessarily.

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[234] Stepehn Breyer, *Regulation and Its Reform*, Harvard University Press, 1982, chapter 1

CONCLUSION

The main objective of competition law in the European Union is to ensure effective competition in the market. One of the legal techniques frequently used to achieve this are block exemptions. This thesis has assessed the development of block exemptions in order to investigate the economic benefits and drawbacks of using this legal technique to regulate competition law in the European Union.

As shown in chapter 1, Article 81, the legal basis of block exemptions, does take into account economic considerations which is a powerful positive aspect. In the beginning, the Commission's and the European Court of Justice's interpretations did not usually rely on economic arguments but this has changed over time which is again a positive element. Nevertheless, a few drawbacks continue to exist and they are caused by these interpretations and not by the provisions of Article 81. One important shortcoming is the fact that the economic damage caused to third parties is not taken into account when assessing the overall pro-competitive or anti-competitive effect of an agreement. The reason for this might be that the actual damages are hard to assess in reality. However, at least a prediction of these damages should be made in order to prohibit agreements which are likely to cause damages to third undertakings that would not be offset by the benefits gained by the consumers and by the undertakings party to the agreement. The second important drawback, as was shown by other scholars, is the fact that certain political considerations are more powerful than economic arguments in particular situations which should not be the case in competition law.

Block exemptions are a unique legal technique to regulate competition law as concluded by chapter 2. The most significant drawbacks from the past, for example the prescriptive character of these regulations, were eliminated. Over time, the importance of economic considerations has increased significantly, which is a positive aspect. However, certain drawbacks remain because the Commission relies too havely on market share thresholds.

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These difficulties are cause by the complexity of applying competition law. The procedural rules which govern the implementation of competition law become thus more important in this context. Even if on the whole these rules are appropriate, their main shortcomings steam from the greater powers of the Commission in comparison with national courts and undertakings. First, the limitation imposed on the national courts regarding the issuance of judicial authorizations for investigations is unjustifiable. Second, Regulation 1/2003 does not limit enough the powers granted to the Commission in its relationship with the undertakings which leaves open the possibility of abuse.

Chapter 3 has proven that the evolution of block exemptions over time in different sectors of the economy has not been straightforward. Only one block exemption was maintained in the same form for a long period of time. The other ones have suffered frequent and important modifications which dilute the main advantage of block exemptions, namely providing legal certainty. The main conclusion is that the content of the block exemptions has developed gradually, by adding or eliminating provisions from the earlier block exemptions, process made possible by the gain in experience. However, block exemptions also build on the provisions of Article 81 and sometimes only restate these provisions which is why the simplification of their structure would be welcome. This is because the provisions would be more flexible and would be possible to adapt to changing economic circumstances.

Overall, the benefits created by block exemptions outweigh their shortcomings and thus, they are an effective legal technique for regulating competition law in the European Union. However, improvements can be made by allowing economic arguments to always win, eliminating the risk for the Commission to behave abusively and simplifying the provisions of block exemptions and thus making them more flexible. These findings are useful both from a practical and theoretical point of view. First, both lawyers and economists want to ensure an effective competition policy in the European Union. By working together and combining

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behavioral issues with economic impact assessments, they can more easily identify the problem areas and find adequate solutions. From the theoretical point of view, even if these block exemptions are only partially based on the classical reasons for regulating, namely unequal bargaining power and information asymmetry, they do have an overall positive effect. This is because the reason for their existence is the fact that the agreements covered by them provide more pro-competitive benefits than anti-competitive effects.

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Commission Notice - Guidelines on the application of Article 81 of the EC Treaty to technology transfer agreements

Commission Notice - Guidelines on Vertical Restraints

Commission Notice on agreements of minor importance which do not appreciably restrict competition under Article 81(1) of the Treaty establishing the European Community, 2001

Commission Notice on the definition of relevant market for the purposes of Community competition law

Commission Regulation 123/1985 on the application of Article 85 (3) of the Treaty to certain categories of motor vehicle distribution and servicing agreements

Commission Regulation 1324/2001 amending Regulation 1617/93 as regards consultations on passenger tariffs and slot allocation at airports

Commission Regulation 1400/2002 on the application of Article 81(3) of the Treaty to categories of vertical agreements and concerted practices in the motor vehicle sector

Commission Regulation 1459/2006 on the application of Article 81(3) of the Treaty to certain categories of agreements and concerted practices concerning consultations on passenger tariffs on scheduled air services and slot allocation at airports

Commission Regulation 1475/95 on the application of Article 85 (3) of the Treaty to certain categories of motor vehicle distribution and servicing agreements

Commission Regulation 151/1993 amending Regulations 417/85, 418/85, 2349/84 and 556/89 on the application of Article 85 (3) of the Treaty to certain categories of specialization

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agreements, research and development agreements, patent licensing agreements and know-how licensing agreements

Commission Regulation 1523/96 amending Regulation 1617/93 on the application of Article 85 (3) of the Treaty to certain categories of agreements and concerted practices concerning joint planning and coordination of schedules, joint operations, consultations on passenger and cargo tariffs on scheduled air services and slot allocation at airports

Commission Regulation 1617/93 on the application of Article 85 (3) of the Treaty to certain categories of agreements and concerted practices concerning joint planning and coordination of schedules, joint operations, consultations on passenger and cargo tariffs on scheduled air services and slot allocation at airports

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Commission Regulation 1983/83 on the application of Article 85 (3) of the Treaty to categories of exclusive distribution agreements

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Commission Regulation 2236/97 amending Regulations 417/85 and 418/85 on the application of Article 85 (3) of the Treaty to categories respectively of specialization agreements and of research and development agreements

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Commission Regulation 358/2003 on the application of Article 81(3) of the Treaty to certain categories of agreements, decisions and concerted practices in the insurance sector

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Commission Regulation 823/2000 on the application of Article 81(3) of the Treaty to certain categories of agreements, decisions and concerted practices between liner shipping companies (consortia)

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Commission Regulation 84/91 on the application of Article 85 (3) of the Treaty to certain categories of Agreements, Decisions and concerted practices concerning joint planning and coordination of capacity, consultations on passenger and cargo tariffs rates on scheduled air services and slot allocation at airports

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Commission Regulation 870/95 on the application of Article 85 (3) of the Treaty to certain categories of agreements, decisions and concerted practices between liner shipping companies (consortia) pursuant to Council Regulation 479/92

Communication from the Commission — Notice — Guidelines on the application of Article 81(3) of the Treaty, 2004

Consolidated version of the Treaty Establising the European Community

Council Regulation 1/2003 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty

Council Regulation 1017/68 applying rules of competition to transport by rail, road and inland waterway

Council Regulation 1215/1999 amending Regulation 19/65/EEC on the application of Article 81(3) of the Treaty to certain categories of agreements and concerted practices

Council Regulation 1419/2006 repealing Regulation 4056/86 laying down detailed rules for the application of Articles 85 and 86 of the Treaty to maritime transport, and amending Regulation 1/2003 as regards the extension of its scope to include cabotage and international tramp services

Council Regulation 1534/91 on the application of Article 85 (3) of the Treaty to certain categories of agreements, decisions and concerted practices in the insurance sector

Council Regulation 17/1962 - First Regulation implementing Articles 85 and 86 of the Treaty

Council Regulation 2344/90 amending Regulation 3976/87 on the application of article 85 (3) of the treaty to certain categories of agreements and concerted practices in the air transport sector

Council Regulation 2411/92 amending Regulation 3976/87 on the application of Article 85 (3) of the Treaty to certain categories of agreements and concerted practices in the air transport sector

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Council Regulation 2743/72 amending Regulation 2821/71 on the application of Article 85 (3) of the Treaty to categories of agreements, decisions and concerted practices

Council Regulation 2821/71 on application of Article 85 (3) of the Treaty to categories of agreements, decisions and concerted practices

Council Regulation 3975/87 laying down the procedure for the application of the rules on competition to undertakings in the air transport sector

Council Regulation 3976/87 on the application of Article 85 (3) of the Treaty to certain categories of agreements and concerted practices in the air transport sector

Council Regulation 4056/86 laying down detailed rules for the application of Articles 85 and 86 of the Treaty to maritime transport

Council Regulation 411/2004 repealing Regulation 3975/87 and amending Regulations 3976/87 and 1/2003, in connection with air transport between the Community and third countries

Council Regulation 479/92 on the application of Article 85 (3) of the Treaty to certain categories of agreements, decisions and concerted practices between liner shipping companies (consortia)

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LIST OF CASES

C-26/1976 - Metro SB-Großmärkte GmbH & Co. KG v Commission of the European Communities

Joined cases 56 and 58/1964 - Établissements Consten S.à.R.L. and Grundig-Verkaufs-GmbH v Commission of the European Economic Community

Joined cases C-89/85, C-104/85, C-114/85, C-116/85, C-117/85 and C-125/85 to C-129/85 - A. Ahlström Osakeyhtiö and others v Commission of the European Communities (Wood Pulp Case)

Joined cases T-528/93, T-542/93, T-543/93 and T-546/93 - Metropole télévision SA and Reti Televisive Italiane SpA and Gestevisión Telecinco SA and Antena 3 de Televisión v Commission of the European Communities

T-168/2001 - GlaxoSmithKline Services Unlimited v Commission of the European Communities

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