

**COMPETITION IN EUROPEAN UNION- ARTICLE 101 OF THE TREATY ON THE FUNCTIONING OF THE EUROPEAN UNION, EXEMPTIONS AND STATE AID.**

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**ABSTRACT:** *Doing ‘the right thing’ in a profitable way seems to be a trend that is increasingly gaining field among business. This triggers undertakings to innovate, create new technologies and adapt the supply chain management of their production and distribution processes, which often turns out to require costly investments. Moreover, market parties often are forced to operate together with like-minded undertakings. This cooperation has instigated a lot of discussion in the framework to the current European competition law under which the behavior of market parties is scrutinized. Researches show that undertakings attach great importance to the competition policies, however, these are not always as clear and predictable. In this framework this paper, aims to identify the criteria that agreements between undertakings should fulfill in order to be considered as an exemption under Article 101(3) TFEU. In this perspective importance takes also the state-funded aid granted directly by Member States, in cases when it distorts or is likely to distort competition and adversely affects trade between Member States. Results will shed light on the so called grey area, in which these undertakings operates and unsure whether their collective actions are qualified as permissible under Article 101.*

**KEYWORDS:** Antitrust Laws, Block Exemption, Competition, Market Liberalization, State Aid, Trade, Vertical Restraints.

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## **INTRODUCTION**

Infringement of competition is not an easily remedied action. The consumers would be satisfied if legal problems between undertakings would be able to be resolved among themselves instead of by spending a lot of time tied up in the courtrooms. The reconciliation is more worthy than the conflict and all is in the consumers benefit. There is nothing entertaining in lawyers filling their pockets with the tax payer’s money.

The main purpose of competition policies is to protect the process of competition as a process and not the competitors, because their interests are not the same. Competitors want to maximize their profits and not to extend competition.

The consumer interest should be always the first priority and not the interest of big undertakings. And because of this the purpose of competition laws is to restrict the economic and decision making strength of these undertakings, in order that the last ones could not block the access into the market of the new and innovative forces, improvement of quality and techniques or competition in favor of the consumers. The competition laws should always try to achieve these objectives.

## **Competition, Reason of the Law**

Competition is a mechanism of disciplined pluralism, which assessed the success and punished the failure. The purpose of the competition rules is the protection of this mechanism. A clear and right competition policy is very important not only for undertakings but also for the European citizens. They want a clear view how competition laws can improve their everyday life through influencing in the ways and forms of doing trade. One of the most important roles of competition is to promote innovation and to secure the consumers that goods and services are being produced in the most possible efficient way. And from all this, they profit in lower prices, higher quality of goods and services and more possibilities of choices. An example is the reduction with 40% of all phone charges during the period 1997-2003 in all Member States. Competition in this sector reduced the prices, supplied the subscribers by means of a higher technology, greater investments in various studies over the phone as well as providing a higher number of free phone services [10].

Another role of competition is to ensure competitive markets in accordance with the new globalization policies and improve employment. For example, state aid, which operates in base of competition laws, helps the structural change of conceptual ways of production and helps in developing an innovative and competitive industry, which brings the final result of opening new positions. It is very important that competition laws should be clear, transparent and continuously reinforced with new politics. But on the other hand, these rules have to walk alongside the economic and technological progress of the 21-st century [18].

Continuously we should consider the main purpose of these rules, especially in the antitrust policies, where is more possible that actions undertaken by undertakings can distort competition also in the staid aid sector, where state actions can bring the same negative effects.

### **Antitrust laws: revising and reasons behind the process**

After the publication of “White Paper” (for the modernization of the procedural rules included in Article 81 and 82 of EC Treaty) by the European Commission (the Commission) in 1999, there was a big debate for the reforms in the procedural law. This paper proposed a revision of rules and was a fundamental reform in that time, because it deemed certain rules unsuitable (these rules especially regulation 17 were in force since 1962) [4] [11]. After enormous debates with interest groups, the European Parliament (the Parliament) published a resolution on 18 January 2000. The most important point was the need for modernization of the process in order to respond to the questions raised by the modern economy. The resolution welcomed the regulatory suggestions and decentralized the competences. It gave more competences to the national courts and Member States authorities, because this could help in the improvement of the European “competition culture” [14].

In order to achieve the desired outcome the resolution asked to the Commission of Economy to implement some points included in it. Two of them were:

- a. To remove some tasks to the Commission that was not giving the proper contribution for the improvement of competition laws.
- b. Bringing the decision making power closer to citizens.

### **Single state market and state aid**

The state aid given to different undertakings can lead to unacceptable destabilizing effects in a common market economy. State aid policies may contribute in the improvement of an only one market (Italian, French, etc.). We must pay a lot of attention in the process of application and monitoring if we want a market that can bring employment and economic growth. Transparency is also a key element in the process. In order to increase the efficiency of the market and not to lead to an arbitrary process, the whole “state aid process” should be controlled by a monitoring group [15].

### **Effects of Article 101/1 on the Member States trade and market liberalization**

European Union (EU) competition policies are always based in the written legislation and especially in the Article 101 of the Treaty on the Functioning of the European Union (TFEU) (ex-Article 81/1 of the Treaty Establishing the European Community (TEC)).

Article 101/1 is applicable against an undertaking, if its infringement affects competition between Member States, otherwise it remains competence of national authorities of the Member States. It has not been difficult for the Commission to bypass this part of the law because it adopted a broad interpretation of it. If there is the possibility, that agreements between undertakings may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market, the Commission does not impose itself the problem of jurisdiction. The fact that the agreement had affected other Member States does not matter as long as these effects have or have had the opportunity to happen. Even the fact that all parties in agreement are under the jurisdiction of one state, did not stop to work Article 101/1 with the justification that the agreement between them, potentially has banned access in the market of the other possible undertakings by other countries. The Commission does not take into account agreements between undertakings that only have a small share of the market (*de minimis doctrine*) [12] [17].

### **Competition in market liberalization**

Services like transport, energy, postal and telecommunication services, have not been markets open to competition. The Commission played an important role to open these markets to competition (the process is known as “liberalization”). Before these kind of services were offered only by state operators, which had exclusive rights in the market. With the liberalization and the introduction of international undertakings, consumers could choose between different offerings and services.

How did all of this begin? It has been years since the Commission was confronted with this and the facts have since changed. In 1993, Denmark was asked to bring down the state monopoly on rail transport undertakings DSB. The Commission said that Denmark should decide if it wanted to open this sector for international competitors or build a new relief system. Soon was noticed that the opening of these markets to competition was not necessarily profitable for the parties, especially when the market or product was spread over the whole country, because large investments were required and economically was not efficient [6]. Because of this the Commission created the so called “legal separation” between the service creation and its commercial use. In the field of railway, electricity and gas the system operators are obliged to allow competitors the entrance into the market. Monitoring

this possibility is the main task of the Commission by allowing consumers to choose better services and offerings [21].

In the markets where this liberalization was done first (air transport and telecommunication) the average prices decreased significantly. This did not happen in those markets when their liberalization was done late or is not done yet (like gas, electricity and postal services). In the last ones prices remained unchanged or increased [9]. Though there is still debate for the reason (the price of gas is closely associated with the oil price), seems like consumers have had the possibility to profit more in those sectors, which have been opened to the new competitors.

Opening new markets requires new rules to ensure that a public service will continue to be provided and consumers should not pay more to have it. European Commission takes into account the specific obligations imposed on any undertaking that profits from monopoly rights. This provides a right competition without damaging the services offered by the state, which is obligated to offer services in public interest even when they provide no benefits [16]. An example is the German postal services (financed by the state), which is obliged to keep a large postal network and has greater costs than its competitors and was allowed by the Commission to keep prices slightly higher than its competitors, because of this reason [7].

Based on Article 101 of TFEU the Commission has these tasks [22]:

- 1) To undertake all the needed measures against undertakings that have infringed the law.
- 2) Examination of the mergers and activities (contracts) between undertakings, if they are in conformity with the competition law or limit it.
- 3) How infringement of Article 101/1 may effect trade between Member States and the expansion of competition in those areas previously controlled by state monopolies.
- 4) Exemptions on competition practices under Article 101/3 and supervision of the aid granted by Member States to undertakings.
- 5) Reinforcement and application of competition laws and cooperation with the competition authorities of the Member States.

The focus of this paper will be the analysing of what are the exemptions under Article 101/3 and under what circumstances state aid granted by Member States to undertakings does not constitute an infringement of Article 101/1.

### **Article 101/3 exemption and state aid**

It is very important for competitors to compete in equal conditions for all. Faced with the free trade between EU Member States and the opening of the public services sector to competition, national authorities want and may use public funds to promote certain economic activities or to protect their national industries. The use of these funds is known as “public assistance” or “state aid”.

An undertaking that receives this kind of aid, profits also advantages in front of other competitors. Therefore the EU Treaty normally prohibits state aid, except in the cases when it is justified by reasons of an overall economic development. The Commission is tasked to ensure the legality and the progress of this process, in order to make sure that this cause is

recognized and applied in the same way in all the EU Member States [19]. The first step is to find out whether an undertaking has obtained the aid and the aid given has fulfilled the following criteria [23] [32]:

- a. If there was an intervention by the state or through it with various funds (which can be money, tax relief regime, bank guarantees, the purchase of some or all shares of undertaking by the state or other public institutions, the purchase or sale by the state of products produced in base of preferences etc.).
- b. The intervention may influence the trade between Member States.
- c. The intervention gives advantage to the profiteer on selective bases (for example: The state helps some specific undertakings, the aid is given to undertaking located in a particular area).
- d. There is the risk of infringing the competition or this has happened now.

On the other hand, the general measures taken are not considered state aid, because are not taken on selective bases for undertakings or other industrial sectors, regardless of size, location or sector.

A list of cases where state aid can be given is included in the EU Treaty. In these past few years, the Commission made clear that state aid is permitted when it is in the interest of its own citizens. This includes: a.) development of backward areas; b.) promotion of SMA's; c.) technical and scientific research and development (R&D); d.) environmental protection; e.) different trainings; f.) employment and culture [16].

### **Exemption from Article 101/1 as stated in Article 101/3**

Article 101/1 of the TFEU prohibits all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between EU countries and which have as their object or effect the prevention, restriction or distortion of competition. As an exception to this rule, Article 101/3 of the TFEU (ex-Article 81(3) TEC) provides that the prohibition contained in Article 101/1 of the TFEU may be declared inapplicable in case of agreements which contribute to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefits, and which do not impose restrictions which are not indispensable to the attainment of these objectives and do not afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products concerned.

The assessment under Article 101 of the TFEU thus consists of two parts. The first step is to assess whether an agreement between undertakings that is capable of affecting trade between EU countries has an anti-competitive object or actual or potential anti-competitive effects. Article 101/3 of the TFEU becomes relevant only when an agreement between undertakings restricts competition within the meaning of Article 101/1 TFEU. In the case of non-restrictive agreements there is no need to examine any benefits resulting from the agreement. The second step, which becomes relevant only when an agreement is found to be restrictive of competition, is to determine the pro-competitive benefits produced by that agreement and to assess whether these pro-competitive effects outweigh the anti-competitive effects. The

balancing of anti-competitive and pro-competitive effects is conducted exclusively within the framework laid down by Article 101/3 TFEU.

The exemptions for the non-application of Article 101/1 can be general (for each undertaking that is active with one or some products and services listed below) or individual (where the possibility for exemption is seen case after case). Exemption based on Article 101/3 can be given only by the Commission and national courts of Member States cannot do that. Article 101/3 of TFEU consist of four cumulative criteria that needs to be fulfilled for the pro-competitive effects of an agreement to outweigh its anti-competitive under, which are [5]:

1. *Cost and qualitative efficiencies*: Efficiency can take the form of reduced production costs because of the improved production method, higher quality of products etc. In each case the Commission requires facts to prove this benefit as well as cause –effect coherence with the reached agreement.
2. *Fair share for consumers*: The consumers should profit from these improvements and be compensated for each possible negative effect, created or strengthened by the agreement to restrict competition.
3. *Indispensability of the restriction*: The agreement to restrict competition should be active only to achieve the above mentioned points (so there are no other possible ways to increase efficiency if not by restricting competition).
4. *No elimination of competition*: The agreement cannot eliminate competition completely, even if production is more efficient. This because for the Commission preservation of the right competition is more important than increase efficiency. The agreement to restrict competition is more likely accepted in those markets where competition for a product or service is already low.

Even if the condition for the application of Article 101/3 are clear, the debate is on vertical restraints. The debate is held in two plans, economic and legal [8] [20].

### **Economic Debate**

There is no evidence yet, if vertical restraints poses a threat to competition or not. Some have the idea that these kind of restriction are harmless others think that in one way or another they may cause different anticompetitive behaviors, which are illegal.

- a) The first view is supported by those who are convinced that somehow the market regulates itself and we should limit as much as possible interference in it. Everything should be left in the hands of producers to find the best way to sell its own products or services. They are the only ones that can do this in the best ways, for their own interest. Also the seller will not tighten the qualities of the product (price, quantity, quality) more or less than he already does (because is in oligopoly position). So there will be no need to create anticompetitive policies because he is interested to have competition. To support this line of thought, we must say that is more important to launch a new and innovator product than the minimal restriction of competition.
- b) The second view is supported by those who are convinced that directly or indirectly this kind of restriction will bring consequences for competition. In support of their theses they brought some excuses as solid as for example closing the market. If the producer has

exclusive contracts with another producer, it will be very difficult for others to reach the market. Another one is keeping sale prices high in an artificial way, although there are conflicting ideas on this point. Vertical restraints may be a way to hide a cartel between producers and sellers, by eliminating transparency. The last argument is that EU is not based only on efficiency principle. Creating a unique market is also an important principle and creating restraints that have mainly local character and are a barrier for the creation of this market.

### **Legal Debate**

From all sides came criticism for the Commission's policies on vertical restraints, because it uses widely many concepts and strictly the measures envisaged by Article 101/1 without doing an economic analysis of the last ones. A lot of debates are also based on the fact if the Commission measures are persuasive and did not take into account the opinions of the Community Courts.

In 1996, with the Green Paper Report on vertical restraints, the Commission began to revise its own practices, because to the large number of critics against it. The Commission agreed in its reports that should be taken into account the economic effects on vertical restrictions and the most important principle was to safeguard the market structure in all the cases. The report made it clear that vertical restriction with a local character were prohibited by Article 101/1 and 101/3. Commission saved the previous line, that will not do economic evaluation in cases related with Article 101/1 but will use this kind of evaluation by using Article 101/3 [3]. The new rules entered into force on 01 of June 2000. Below we will present different types of vertical restraints, which are under competence of Article 101/1:

#### **Exclusive Distribution Agreement (EDA)**

Exclusive distribution agreement is between the producer and the seller, where the producer is obligated to supply only one seller in a specific area, with mutual benefit for the parties. The main problem is if this kind of agreement is forbidden from Article 101/1 and is allowed from 101/3. Absolutely, this kind of agreement is an infringement of Article 101/1 and as such is accepted by the European Court of Justice (ECJ) and European Commission with same differences from each other. Usually, these kind of cases are forbidden and do not exceed the review under Article 101/3 [13].

#### **Selective Distribution Agreement (SDA)**

Selective distribution agreement is a little bit different from the exclusive one, and the Commission has maintained a different line. The system is based on the seller's supply by the producer only in base of competences and after meeting certain criteria. If these criteria are properly fulfilled the agreement does not infringe Article 101/1. They are [2]:

1) **The nature of the product:** It must be to justify the competition in prices and may operate under a regime of selective distribution. Similar products can be those that require a staff specialized in their selling or products brand of a particular importance.

2) **The seller quality:** Sellers can be selected on point of sale quality, staff etc. But in reality is very difficult to create a set of rules, when a seller is more qualified than the other one.

3) **No territorial distribution:** As we mentioned before each exclusive or selective distribution agreement, which have as a principle exclusive distribution based on a certain geographical area, will infringe Article 101/1.

### **Franchising**

Franchising is different than the other two (EDA and SDA) mentioned before. The producer gives to the seller the right to use his intellectual property rights (marks, production and marketing way, logo etc.) against a payment. So we have a mutual profit for the both parties, the seller uses intellectual property rights beyond his reach to gain profits and the producer is paid for giving his property rights [16]. This kind of agreement usually does not infringe Article 101/1, but in each case should not be on territorial bases [13].

### **Exclusive Purchase Agreement (EPA)**

Exclusive purchase agreement is that when one party agrees to purchase the total amount of a product from a particular producer. We can mention the example of different points of hydrocarbons which buy only from a producer. To the question if these kind of agreement do infringe Article 101/1, we can answered only after a detailed analyze of the market. If the agreement legally, actually and in an economic context has as an effect the distortion, restriction or prevention of competition, than it infringe Article 101/1 [13].

### **State Aid**

The most controversial and detailed investigated state aid is that for the rescue and restructuring of public undertaking and work in certain sensitive sectors such as steel processing, shipbuilding and motor vehicles [1]. In particular, aid for saving from bankruptcy and the reorganization of the undertakings in financial difficulties, may allow to these undertakings to continue their activities at the expenses of competitors and workers. These undertakings, helped with state aids, are not safe [9]. Usually such undertakings are very large and the aid received has a significant negative impact on competition. With the new rules put into force, which are stricter, these undertakings are obligated to cover at least 50% their costs of reorganization [16].

State aids that do not contribute in the realization of the EU community objectives are prohibited. Examples of illegal aids are those granted to undertakings which are away from areas known as backward, aids in helping the exports of undertakings or their operational costs [25].

Usually, the EU Member States are obliged to inform the Commission in advance about the planned help before it becomes effective [17]. Only after the aid is approved by the Commission, it could be delivered and be effective. In certain cases the warning is not mandatory and just a simple notification about the aid is enough. This relief is applies in those areas where the Commission has more experience and where it contributes significantly to the general development of EU economy. This relief allows to the Commission to focus on more important issues [26][27].

Commission approves the majority of all aids announced by Member States after a first review [24]. Only in the cases when are presented conflicts or resentment by the parties it makes formal investigations, and all the acts are published in the Official Journal or in the competition website [26]. This procedure allows other “actors” to comment the decision

made and imposes to the Commission the task to see the issue in question in every aspect before it can take the final decision. The Commission investigates also on aid granted and not announced. It can be informed by the competitors of these undertakings, complaints of individuals and from the media. By informing the Commission in this way, different undertakings can stop this illegal aid before the National Courts can take a decision. If the Commission decides that the aid granted is illegal based on competition law, it asks to the Member States to withdraw the aid in its entirety and to restore the situation existing before it [26][27].

The Commission is also tasked to recognize the amount and the nature of the overall state aids. The analysis shows that EU Member States have consistently reduced the amounts and instead have used the money to stimulate commercial activities of general interest to EU. This new development makes the European economy more competitive and improves the position of EU market compared to world market [31].

In many cases, the Council of Europe has highlighted the need for these aids to be in amount as smaller as possible and to be well administered to improve the European economy. In response to these statements the Commission responded by adopting a number of measures to accelerate and facilitate granting of aids, which are in conformity with EU objectives. As an example we can bring the reduction of bureaucratic procedures for all those aid that are in conformity with EU objectives and usually the institutions do not reveal problems for these. In this case after granting the aid Member States should inform the Commission, in order to have more transparency. Forms are available on warning and information. Their advantage is that forms include only the amount of information about the amount and the content of the aid granted, in which the Commission is interested [28]. In case of illegal aids the Commission provides a more strict control.

Public services are in the focus of the Commission because this kind of service is for both the economy and the society. So it is very important that these services should be offered and continues to be in the future, although at a minimum [29]. Many of them as postal services, transport services (see the previous section) have seen a substantial change in the last years, and are facing difficult situations in a competitive market. In order to make sure that these services can continue to be offered, undertakings that are active in these sectors should be compensated for costs they have to assume such a responsibility. There are also risks that these undertakings may use the aid in other sectors. In its 2003 Altmark judgement the ECJ held that public service compensation does not constitute State aid when four cumulative conditions are met [30]:

- The recipient undertaking must have public service obligations and the obligations must be clearly defined;
- The parameters for calculating the compensation must be objective, transparent and established in advance
- The compensation cannot exceed what is necessary to cover all or part of the costs incurred in the discharge of the public service obligations, taking into account the relevant receipts and a reasonable profit;
- Where the undertaking which is to discharge public service obligations is not chosen pursuant to a public procurement procedure which would allow for the selection of the tenderer capable of providing those services at the least cost to the community, the

level of compensation needed must be determined on the basis of an analysis of the costs of a typical well-run company.

Where at least one of the Altmark conditions is not fulfilled, the public service compensation will be examined under State aid rules.

## CONCLUSION

Competition itself is a huge concept and laws are not enough to protect a system. The prime objective for undertakings is to maximize their profits, not to pay attention to competition. So the coordination of the actions between the national and central authorities is very important in the process of maintaining and establishing a fair competition system.

A right competition brings goods for all EU members under the form of technical and scientific innovation, efficiency in production and brings a decrease in prices and improves the quality. A right implementation of competition generates an increment in employment. In recent years, the position and ways of applying the provision of this law have changed. As a result of the globalization of the economy, the rules of game have changed. But the primary objective of the competition laws remains the protection of the consumers' interests.

The Commission has its own methods to preserve competition and could exempt some infringements based on Article 101/3. The reasons for exemption could be: promoting technical innovation, benefits for the consumers etc. These kinds of reasons could stand as long as there were no serious violations of the law. The Commission controlled also the state aids granted by the Member States to undertakings, because could affect not only the Member States competition but also to the other ones in EU.

Competition law has changed during these past couple years. This happened because changed the way of doing business, globalization etc. But the main and final purpose of these laws remains that of protecting the consumer rights and the economic and social development of EU Member States.

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