


EFTA SURVEILLANCE AUTHORITY

Doc. No: 02-1216-I
Ref. No: SAM 030.01.001
Dec. No: 32/02/COL

EFTA SURVEILLANCE AUTHORITY DECISION
of 20 February 2002
regarding support to film production and film related activities
(NORWAY)

THE EFTA SURVEILLANCE AUTHORITY,

HAVING REGARD TO the Agreement on the European Economic Area¹, in particular to Articles 61 to 63 thereof,

HAVING REGARD TO the Agreement between the EFTA States on the establishment of a Surveillance Authority and a Court of Justice², in particular Article 24 and Article 1 of Protocol 3 thereof,

HAVING REGARD TO the Procedural and Substantive Rules in the Field of State Aid³,

WHEREAS:

I. FACTS

Procedure

By letter dated 12 October 1999 (*Doc. No:* 99-7559-D), the Authority initiated a review of existing aid schemes in support of film production in Norway. The schemes subject to this review covered aid for film production administered by the Audiovisual Production Funds, which was approved by the Authority by decision of 11 May 1995⁴, aid awarded by the Norwegian Film Institute, which was communicated to the Authority in 1994 as an existing aid scheme⁵, as well as financial contributions to Norsk Film A/S in relation to its production activities.

¹ Hereinafter referred to as the EEA Agreement.

² Hereinafter referred to as the Surveillance and Court Agreement.

³ Guidelines on the application and interpretation of Articles 61 and 62 of the EEA Agreement and Article 1 of Protocol 3 to the Surveillance and Court Agreement, adopted and issued by the EFTA Surveillance Authority on 19 January 1994, published in OJ 1994 L 231, EEA Supplements 03.09.94 No. 32, last amended by the Authority's Decisions No. 368/01/COL to 370/01/COL of 28 November 2001, not yet published.

⁴ Dec. No. 49/95/COL, State aid No. SAM 030.95.001 – Norway.

⁵ State aid No. SAM 030.94.194 - Norway.

In accordance with point 7.4.1 of Chapter 7 of the Authority's State Aid Guidelines⁶, the Authority requested the Norwegian Government to submit the relevant information enabling the Authority to assess the existing aid schemes in light of recent EC Commission practice concerning film funding⁷.

The Norwegian Government responded by letter from the Ministry of Culture dated 5 November 1999, received and registered by the Authority on 3 December 1999 (Doc. No. 99-9301-A). This information was supplemented by general observations regarding the application of State aid rules to the schemes in question, by fax from the Ministry for Trade and Industry dated 22 November 1999, registered by the Authority on the same day (Doc. No. 99-8834-A). Further information was sought by the Authority in letters dated 16 February 2000 (*Doc. No. 00-1321-D*) and 27 July 2000 (*Doc. No. 00-5306-D*).

The relevant issues regarding the assessment of film support measures under EEA State aid rules were also discussed at bilateral meetings between the Authority and the Norwegian Government (on 23 February 2000 and 10 July 2000 in Brussels, as well as on 19 October 2000 in Oslo) as well as at a multilateral meeting with EFTA States (on 21 March 2000 in Brussels).

By letter dated 25 October 2000, received and registered by the Authority on 27 October 2000 (Doc. No. 00-7700-A), the Norwegian Ministry of Culture informed the Authority that it intended to submit a notification concerning the Norwegian film support system in January 2001. In a letter dated 31 October 2000 (Doc. No. 00-7790-D), the Authority indicated that it would not pursue the review procedure, given that the Norwegian Government was, at that time, working on a reform of the existing film support schemes and based on the understanding that the Norwegian Government would notify the amended film support schemes.

By letter dated 18 April 2001, received and registered by the Authority on 23 April 2001 (Doc. No. 01-3059-A), the Norwegian Government notified the Authority of a proposal for amended film support schemes.

The Authority acknowledged receipt of the notification by letter of 25 June 2001 (*Doc. No: 00-4888-D*) and requested additional information. By letter dated 13 November 2001, received and registered by the Authority on 16 November 2001 (Doc. No. 01-9143-A), the Norwegian Government submitted the requested information. Additional information and clarifications were provided in a letter dated 16 January 2002, received and registered by the Authority on 18 January 2002 (Doc. No. 02- 462-A). By letter from the Ministry of Culture dated 12 February 2002, received and registered by the Authority on 14 February 2002 (Doc. No. 02-1221-A), the Norwegian authorities submitted the final texts of the regulation for film support and confirmed that no aid would be granted under the new scheme before the EFTA Surveillance Authority has reached a decision.

⁶ Point 7.4.1 (1) of Chapter 7 of the Authority's State Aid Guidelines on the procedure in existing aid cases reads: "*Whenever the EFTA Surveillance Authority believes that existing aid may not be compatible with the progressive development or the functioning of the EEA Agreement, it begins a review by writing for information to the EFTA State concerned...*".

⁷ Reference was made to the "French" decision (State aid N 3/98) and the "Irish" decisions (State aid N 49/97 and N 357/99).

Description of aid measures

Financial parameters for film production in Norway

According to information submitted by the Norwegian Government, out of a total number of around 80 audiovisual production companies in Norway, only approximately 10 companies are engaged in continuous feature film production. According to information provided by the Norwegian Government, in the period 1997-1999, on average 13 Norwegian films were produced/released per year. According to the Norwegian authorities, production companies typically have few employees. The accumulated annual turnover of the companies engaged in continuous feature film production is estimated to be approximately NOK 200-300 million.

According to statistical data submitted by the Norwegian authorities, in the period between 1997 and 1999, Norwegian films had market shares in Norway of around 8%. This percentage is below the average share of domestic films within the EEA area (which is around 14%). It is also lower than in other Nordic countries which can be regarded as comparable in terms of the size of population, national film production, admissions and box office revenues (in particular Denmark and Finland), where the average market share of domestic films was around 16% within the same period; and significantly lower than in the five major film producing countries (Germany, Spain, Italy, France and the UK), where the market share of domestic films was around 20% in the same period.⁸

Norwegian films shown on the domestic market reached, on average, an audience of 40 000 – 80 000. However, a significant proportion of Norwegian films reached audiences of only around 10 000. In addition, the export market for films in the Norwegian language is marginal. A total number of 15 Norwegian films were shown in cinemas in Denmark and Sweden in the three-year-period between 1997 and 1999. Based on statistics presented by the Norwegian authorities, in the period between 1990 and 2000, the 23 Norwegian films that were distributed within the European Union reached on average 35 000 admissions per film.⁹ This situation implies, according to the Norwegian authorities, that Norwegian films do not reach an audience sufficient to achieve economies of scale necessary to sustain profitable national film production.

According to information submitted by the Norwegian authorities, average production costs for Norwegian feature films amounted to around NOK 15 million. Total box office revenues for a Norwegian feature film averaged, according to the Norwegian authorities, around NOK 3 million. The Norwegian authorities have further explained that, in general, a production company's share of total gross box office revenues amounts to only around 25%.¹⁰ This means that box office revenues paid out to the film producers covered on average only 5% of production costs.

⁸ The comparison is based on figures presented in the European Cinema Yearbook 2000.

⁹ Reference is made to statistical information provided by the European Audiovisual Observatory. It is noted that the audience figure is significantly smaller when disregarding one film which alone achieved more than 500 000 admissions: the average would be as low as 13 000 admissions per Norwegian film distributed in the European Union.

¹⁰ This figure may vary depending upon the particular financing arrangement for each individual film.

Production costs were only to a limited extent financed by the producer's own capital contributions. In the period 1997-1999, the film producer's own capital contribution amounted on average to 25% of the production budget. As results from the figures provided by the Norwegian authorities, on average, box office revenues did not cover the film producer's own capital/investment. Therefore, and even though there are also other sources of income (mainly licensing of television rights, and video rental and sales), total revenues generated by Norwegian films are, according to the Norwegian authorities, not sufficient to financially sustain the current level of feature film productions.

Due to the weak capital contributions by film producers, film production support covered the remaining production costs. In the period 1997-1999, film production support represented on average above 60% of the production budget. In addition, public support granted in the form of box office returns in the same period was on average above 10% of the production budget. Total public support amounted therefore in the period 1997-1999 to around 75% of production costs.

Description of proposal for new system of film support measures

Pursuant to § 1-1 of the regulation for film support ("*Forskrift for tilskudd til filmformål*"), the revised film support mechanisms will be administered by one single public body, the Norwegian Film Fund ("*Norsk filmfond*"), replacing the various institutions involved in the promotion of cinema production and culture in Norway which had been established in the past. In addition to the film support mechanisms notified to the Authority, this newly established body would also be responsible for the administration of the existing aid scheme for screenplay development¹¹ as well as a new scheme for "business development loans" which will, according to the Norwegian Government, be notified to the Authority separately.

The Norwegian Film Fund was established on 1 July 2001 and will replace the Audiovisual Production Fund and the Norwegian Film Institute, previously responsible for the administration of the film production support schemes (ref. existing aid schemes registered under SAM 030.95.001 and SAM 030.94.194). The former institution will be discontinued and its personnel and funds subsumed under the newly created Norwegian Film Fund. This new body will manage the budgetary allocations previously made to the Audiovisual Production Fund and the Norwegian Film Institute.

The Norwegian Film Institute will retain tasks related to the promotion of film culture and preservation and dissemination for non-commercial purposes. The Institute's services will be directed primarily towards the general public.

Finally, the new film support system entailed that Norsk Film A/S, a formerly publicly owned company, which in the past had owned film production facilities, offered film related activities and was also engaged in film production, was split into a film production division and an infrastructure division. Following the separation of the various activities, the Norwegian Government sold its shares in the production

¹¹ This scheme is not subject to the present notification.

division. This process was finalised in January 2002 by the privatisation of Norsk Film AS. As of that time, Norsk Film AS has been a private limited liability company which no longer enjoys specific rights or privileges granted by the Norwegian State. Consequently, the new company will need to apply for State aid under the film support mechanisms as any other film production company.

Pursuant to § 1-2 of the regulation for film support, the various film support mechanisms have as an objective to promote films as a vehicle for the expression of culture and to contribute to the promotion of Norwegian quality films, and in particular films for children and adolescents. The support mechanisms should also contribute to Norwegian films reaching the widest possible audience, as well as to cost efficiency and continuity in the Norwegian film production environment.

Norwegian film is defined in § 1-3 of the regulation as a film produced by a Norwegian independent audiovisual producer and shot in Norwegian or in Sami. Under special circumstances, the Norwegian Film Fund may grant support to films shot in another language, provided that the film has a Norwegian producer as the main producer (i.e. a producer whose share in total production budget exceeds 33,33%) and that the film has a special artistic or technical input, which contributes to the promotion of cinematographic art and culture in Norway. A film will be regarded as contributing to the promotion of cinematographic art and culture in Norway depending on the share of Norwegian contribution to the film (participation of Norwegian directors, screenplay, leading actors, etc.).

A Norwegian independent audiovisual producer is defined as a production undertaking, which

- has audiovisual production as its main objective;
- is either a company registered in the (Norwegian) register of business enterprises as a producer or a foreign company with a registered branch (in Norway), provided that the head of the branch is a Norwegian citizen or is domiciled in Norway; and which
- is not, to any considerable degree, connected to a private or public broadcasting company, either in commercial or financial terms.

Independent production companies registered in another country which is a Party to the EEA Agreement shall be regarded as a Norwegian producer for the purpose of this regulation.

The proposed new film support mechanisms came into effect on 8 February 2002 and will be applied for a period of 5 years.

The regulation covers five different film support mechanisms, of which some may be used cumulatively, while others are mutually exclusive:

- Production support for feature films, including support for project development;
- Support for the Norwegian part in international co-productions;
- Production support based on market potential (so-called “50/50 grants”);
- Production support for short films, including support for project development;
- Support in the form of box office returns.

In addition, the Norwegian Film Fund may grant support for copies, marketing and cinema distribution in Norway and abroad as well as support for special marketing and promotional activities and /or presentation at film festivals abroad.

Support for feature film productions

According to the Norwegian authorities, support for feature film productions¹² is directed towards films with restricted market potential and budgets¹³. Grants are given to independent audiovisual producers for the production of feature films, feature-length documentaries or animation films intended for cinema showing as well as international co-productions with a Norwegian co-producer. In addition to costs relating to the production of films, producers may apply for support to project development, marketing and promotion. The projects are evaluated on an individual basis and monitored closely by a professional film consultant. The level of aid will be determined on the basis of the project's artistic, production-related, economical, technical and marketing merits. This so-called "selective aid"¹⁴ will be granted on the basis of a thorough examination of projects and continuous supervision of the project throughout the production process. Grants are made in several instalments at given, identifiable milestones of the film production. The regulation gives detailed instructions on criteria that must be met before the payment of the various instalments, on supervision and control measures as well as on sanctions that take effect in case of non-fulfilment of the regulation.

Aid intensity is capped by the requirement that the producer must provide at least 25% of the budget ("own financing"). It is for the Norwegian Film Fund to verify and approve the means of "own financing" provided by the producer. For documentaries or films suitable for children, a lower percentage may be accepted under special circumstances. When submitting the application for public support, the applicant must inform the Norwegian Film Fund about possible State support granted in relation to screenplay¹⁵ and/or project development. As the Norwegian authorities have clarified, possible public support in the pre-production phase will be taken into account when determining the permissible support for each film production. Such aid will also be taken into account when determining the amount of repayment. According to a simulation carried out by the Norwegian authorities, public support intensity for films released between 1996 and 1999 would have been 55% if the proposed new regulation had been applied and all other figures remaining unchanged.

¹² Chapter 2 of the regulation "*Forskrift for tilskudd til filmformål*".

¹³ In this respect, it is noted that film production budgets for Norwegian films remain on average below the average investment in film production within the EU, which in 1996 amounted to about € 2.7 million (approximately NOK 21 million), and far below investment in film production in the UK as one of the major film production countries where film production budgets were around € 5.5 million, approximately NOK 44 million (see *The European Film Industry under Analysis*, second Interim Report 1997).

¹⁴ "Selective aid" is to be understood as aid which is granted to individual film projects at the discretion of the responsible authority based on an individual evaluation of the project in particular based on artistic criteria.

¹⁵ Public support for screenplay development ("*tilskudd til manuskriptutvikling*") has not been notified to the Authority.

Public support for international co-productions

The regulation also provides for public support for Norwegian contributions in international co-productions.¹⁶ Such aid is subject to the requirement that a Norwegian producer is responsible for the Norwegian share in the production (regarding artistic and/or technical and financial aspects) and that there is a reasonable relationship between the Norwegian and foreign influence on production, artistic and technical input and investment in the production.

Public support for international co-productions is only available under the feature film production support mechanism and not under the support mechanism “50/50 grants”.

“50/50 grants”

Under the support mechanism called “50/50 grants”¹⁷, independent producers of feature films, feature-length documentaries or animation films primarily intended for cinema showing may receive so-called “semi-automatic”¹⁸ support up to 50% of the approved production budget, provided that the producer contributes with own capital of at least 50% of total production costs. The aid takes the form of grants. According to the Norwegian authorities, the quality of the project in market terms is ensured by the project’s ability to raise capital. Individual projects will not be scrutinised in detail for cultural content. However, the producer and key personnel will be required to prove considerable prior experience in film production. Furthermore, the funding body will examine the projects financially, technically and artistically before a decision to grant aid is taken in order to avoid sprinkling on a large number of sub-standard projects.

The aid intensity is limited to 50% of the film production budget, as approved by the Norwegian Film Fund. The aid intensity per production under this mechanism is further limited by setting an absolute aid ceiling of NOK 10 million. Possible public support for screenplay and/or project development will be deducted from the first instalment (§ 4-1 of regulation). The aid intensity may be further reduced, depending on the film’s commercial success, by possible repayments (for further details, please see below).

Production support for short films

Production support for short films is granted under similar conditions as those for feature film production, with the exception that no minimum requirement exists regarding the producer’s contribution with own capital¹⁹. According to the Norwegian authorities, short films have little or no commercial value and are primarily employed as a means of training and development of talent and are primarily distributed on the festival circuit. Beneficiaries of this support measure are independent producers/production companies. There is no absolute aid ceiling. Estimates provided by the Norwegian authorities regarding public support for short films in the past

¹⁶ Chapter 3 of regulation “*Forskrift for tilskudd til filmformål*”.

¹⁷ Chapter 4 of regulation “*Forskrift for tilskudd til filmformål*”.

¹⁸ “Semi-automatic aid” is to be understood as aid which is granted partly based on objective criteria and partly based on an individual evaluation of the film project in question.

¹⁹ Chapter 5 of regulation “*Forskrift for tilskudd til filmformål*”.

indicate that own capital in short films lie in the region of 50-75% of the production budget. On the basis of the most recent 18 short films which received State funding own capital contributions averaged 63%. Furthermore and according to the Norwegian authorities, support per project remained normally well below the *de minimis* ceiling.

“Box office returns”

Under the support mechanism “box office returns”²⁰, so-called “automatic support”²¹ will be provided with the aim of increasing the number of films with market potential, of stimulating the production of films for children and of attracting more private capital to be invested in film production. Box office returns motivate private investors to contribute private finance to film production by making feature films more profitable. This form of aid is offered to independent producers of Norwegian films.

The aid amounts to 55% of the film’s gross box office receipts from screening in Norway. For children’s feature films, support amounts to up to 100% of the film’s gross box office receipts from screenings in Norway. The box office returns will only be awarded if the film reached a minimum audience of 15 000. For films which have received State support in the form of the “50/50 grants”, the minimum audience to be reached is increased to 30 000.

Support may not exceed the sum of the producer’s own capital (as approved by the Norwegian Film Fund) and common costs minus the film producer’s share of gross box office revenues. The box office return mechanism allows producers to recover common costs, which under Norwegian film production support mechanisms (i.e. feature film production support mechanism and 50/50 grants) may not be included in the production budget when determining the admissible State support. Common costs are fixed, for this purpose, at 20% of the approved own capital.

Co-productions may also benefit from box office returns, provided that the project had received production support from the Norwegian Film Fund.

In principle, and given that the mechanism provides for automatic State support, there is no aid ceiling expressed as a percentage of production costs. Information submitted by the Norwegian authorities shows that box office returns amounted on average (in the period between 1997 and 1999) to above 10% of production costs. State support in the form of box office returns will be limited to the producer’s own capital contributions (plus common costs and after having deducted the producer’s share of the box office revenues).

Aid for marketing and promotional activities

As regards aid for marketing and promotional activities, the Norwegian authorities explained that, until recently, marketing and promotion-related costs were normally included in the production budget and therefore formed an integral part of the film

²⁰ Chapter 6 of regulation “*Forskrift for tilskudd til filmformål*”.

²¹ “Automatic support” is understood to be aid which is granted to a film simply on the basis of certain objective criteria without discretion of the responsible authority and without individual evaluation of the film in question.

production grant. Under recent practice, a certain amount (lump sum) was granted at the production stage, allowing the producer to plan and prepare the basic marketing and promotion material. An additional grant may be given for such activities if the producer can demonstrate that admissions will increase as a result of the planned (additional) promotional activities.

Furthermore, in cases where Norwegian films are nominated to the official programme of sales-promoting festivals (e.g. Cannes, Berlin, Venice, San Sebastian), the producer may apply for additional support. In 2000, a total sum of NOK 1.9 million was awarded to Norwegian producers for this purpose.

The Norwegian Government explained that, in the future, the Norwegian Film Fund would award production support and marketing support separately on the basis of a thorough individual assessment of each project. The Norwegian authorities further explained that marketing support would be granted in exceptional circumstances and provided that the producer covers 50% of the marketing costs with own capital.

Cumulation

The Norwegian Government confirmed that all aid from Government-financed sources other than the funding mechanisms administered by the Norwegian Film Fund, including any support given by regional bodies, would be considered aid for the purpose of assessing the permissible aid intensity.

Support for feature film productions, support in the form of “50/50 grants” and support for the production of short films are mutually exclusive and may not be awarded to the same project. However, a project that has received support for feature film production or aid in the form of “50/50 grants” may also receive support in the form of “box office returns”.

Cumulated public support is subject to an absolute aid ceiling of NOK 30 million. The Norwegian authorities have presented simulations, based on film productions in the past, according to which the cumulated aid intensity for film production support and box office returns would be around 63% of total production costs, if the new provisions regarding the absolute aid ceiling and the repayment obligation were applied.

Repayment Obligation

According to § 1-6 of the regulation, production support for feature films and support granted as “50/50 grants” will be repayable when a film generates net revenues.

Net revenues are defined as gross revenues minus the producer’s own capital and common costs fixed as being 30% of the approved own capital. When determining gross revenues, all revenues in Norway and abroad are to be taken into account, including income from cinema distribution, video rental and sales, sale of rights for television broadcasting or income from distribution agreements with other media as well as State support received in the form of box office returns. According to the

Norwegian authorities, common costs determined as constituting 30% of own capital was in line with the going rate for common costs in film productions internationally.

The producer will be obliged to repay an amount that equals 30% of the net revenues multiplied by the State support share of the overall production budget (taking into account production support). This percentage was considered by the Norwegian authorities as striking the balance between concerns for giving film producers an incentive to market and exploit the film on the one hand, and concerns of limiting excessive State support on the other. The Norwegian authorities have further indicated that this percentage will be reviewed after a certain time.

The repayment formula implies that producers with a low amount of State support are allowed to keep a higher proportion of net revenues. According to the Norwegian Government, the repayment obligation is expected to generate relatively modest income, since only productions with a high degree of economic success will be subject to it.

Budgetary allocations

According to the Budget for 2002, a total amount of approximately NOK 217 million (approximately € 27 million) will be allocated for the purpose of the film support mechanisms notified to the Authority (*St. prp. nr. 1 (2001-2002), Chapter 0334 regarding Film and Media, post 50*).

Budgetary allocations for the individual film support mechanisms will be decided on an annual basis by the Ministry of Cultural Affairs on the basis of a proposal from the Norwegian Film Fund's board of management.

Budgetary allocations for the 50/50 grants would, according to the Norwegian authorities, amount to some 30-40% of the current total annual budget for feature film production. Based on budgetary allocations for feature film production for 2002 (approximately NOK 217 million), this mechanism will have an initial budget of approximately NOK 76 million.

II. APPRECIATION

State aid within the meaning of Article 61 of the EEA Agreement and notification requirement

Article 61 of the EEA Agreement stipulates: "*Save as otherwise provided in this Agreement, any aid granted by EC Member States, EFTA States or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, insofar as it affects trade between the Contracting Parties, be incompatible with the functioning of the Agreement.*"

The concept of aid applies to any advantage, financed out of State resources and granted directly by the State itself or by an intermediary body acting by virtue of powers conferred on it. According to the reform proposal from the Norwegian Government, there are several film support mechanisms, which are administered by one, newly created fund. This fund will receive State budgetary allocations for the purpose of granting subsidies in relation to film production and film-related activities (cf. State Budget for 2002, Chapter 334, post 50). It can therefore be concluded that film support is granted by the State.

The aid gives undertakings eligible under the mechanisms, i.e. independent film producers, a financial benefit they would not have enjoyed in the normal course of business. It thus strengthens the financial position of the eligible film production company compared with other undertakings engaged in film production within the EEA.

State aid to specific undertakings is regarded to affect competition and trade between the Contracting Parties, if the recipient firm carries on an economic activity involving trade between the Contracting Parties. [Cinema productions may be shot in different alternative locations within the EEA. The films are subsequently traded between the Contracting Parties to the EEA Agreement and may compete to attract audience. Production aid \(including pre-production aid for project development and post-production aid for marketing and promotional activities\) may therefore alter the competition existing between different locations for the realisation of a film as well as it may influence the trading conditions for their commercialisation. Therefore, the proposed aid can be considered as distorting competition and affecting trade between the Contracting Parties.](#)²²

The financing of the Fund's own administrative costs does not constitute aid within the said meaning, as the Norwegian Film Fund is not an undertaking but just an aid distribution agency that does not bear any business risk.

Against this background, the State support under the film support mechanisms (including, in certain instances, support at the pre-production stage and certain forms of support in the post-production stage) constitutes aid within the meaning of Article 61 (1) of the EEA Agreement.

Pursuant to Article 1 (3) of Protocol 3 to the Surveillance and Court Agreement, “[t]he EFTA Surveillance Authority shall be informed, in sufficient time to enable it to submit its comments, of any plans to grant or alter aid... The State concerned shall not put its proposed measures into effect until the procedure has resulted in a final decision”.

The Norwegian Government notified the planned changes to the existing film support schemes in April 2001. The new regulation took effect on 8 February 2002. The Norwegian authorities have, however, confirmed that no aid would be granted before the Authority has given its approval. The Authority therefore concluded that the

²² See Judgment of the European Court of Justice, Case 730/79, *Philip Morris Holland BV v Commission*, [1980] ECR 2671, para. 11.

Norwegian Government complied with its obligations pursuant to Article 1 (3) of Protocol 3 to the EEA Agreement.

Compatibility of Aid Measures

Introduction to the legal framework conditions

With the Maastricht Treaty, a cultural derogation was added to the State aid rules of the EC Treaty. This cultural exemption under Article 92 (3)(d) of the EC Treaty (now Article 87 (3)(d) EC) provides that the EC Commission may consider compatible with the common market “*aid to promote culture and heritage conservation, where such aid does not affect trading conditions and competition in the Community to an extent that is contrary to the common interest*”.

It is on this legal basis that the EC Commission has assessed and approved film support schemes in the EC Member States. In its decision of 3.6.1998 on the French film support programme, the EC Commission set out a series of specific criteria on the basis of which it intended to assess State aid to film and TV production under the culture derogation of Article 87 (3)(d) EC. Following the adoption of this decision, the EC Commission launched an inquiry requesting information from all EC Member States about their aid schemes in support of the film industry²³.

The EEA Agreement does not contain a “cultural exemption” similar to Article 87 (3)(d) EC. Nevertheless, the Authority considers that, in line with its previous practice²⁴, film support measures may be approved on cultural grounds on the basis of Article 61 (3)(c) of the EEA Agreement. In its assessment, the Authority will apply criteria similar to those applied by the EC Commission on the basis of Article 92 (3)(d) of the EC Treaty (now Article 87 (3)(d) EC) and provided that this approach does not deviate from its previous practice under Article 92 (3)(c) of the EC Treaty (now Article 87 (3)(c) EC) and provided that the criteria developed by the EC Commission under Article 87 (3)(d) EC are sufficiently taken into consideration.

Against this background, the Authority has carried out a review, requesting the Norwegian Government to submit all relevant information which would enable the Authority to verify that the schemes in place in Norway were compatible with the EEA State aid rules as interpreted in the light of the EC Commission’s decision in the “French” case.²⁵

²³ So far, the EC Commission approved film support schemes in France (State aid N 3/98), Ireland (State aid NN 49/97 and N 357/99), Germany (State aid N 4/98 and film support measures by various German *Länder*: e.g. N 439/2001, N 440/2001, N 693/2001, N 701/2001, N 727/2001 and N 782/01), The Netherlands (State aid N 486/97), Sweden (State aid N 748/99), Denmark (N 486/2001), Finland (N 777/2001) and regional film support measures in Spain (N 698/2001).

²⁴ Authority’s Decision of 18 December 2000 regarding the Act on Temporary Reimbursements in respect of Film Making in Iceland (Act No. 43/1999), SAM 030.99.002 – Iceland.

²⁵ The same examination was carried out with respect to film support measures Iceland (SAM 030.99.002 – Iceland, Authority’s Decision of 18 December 2000 and SAM 090.300.003 regarding the Icelandic Film Fund.

Article 61 (3)(c) EEA Agreement

The Authority examined whether the proposed film support mechanisms can be approved under Article 61 (3)(c) of the EEA Agreement.

According to Article 61(3)(c) of the EEA Agreement “...aid to facilitate the development of certain economic activities or of certain economic areas...may be considered compatible with the functioning of this Agreement...where such aid does not adversely affect trading conditions to an extent contrary to the common interest”.

Operating aid which relieves a company of costs, which should normally be borne by it, is, in principle, incompatible with the functioning of the EEA Agreement²⁶. Such aid may, exceptionally, be regarded as compatible with the functioning of the EEA Agreement according to Article 61 (3)(c) of the EEA Agreement provided that the aid pursues objectives which are in the common interest of the Contracting Parties and that the aid is necessary for and proportionate to the objectives pursued.

According to the EC Commission’s recent communication on cinema, when assessing aid to cinema and TV production, it must be examined

- “...Whether the aid scheme respects the ‘general legality’ principle” (i.e. it must be verified “that the scheme does not contain clauses that would be contrary to provisions of the EC Treaty in fields other than State aid (including fiscal provisions)”);
- “...whether the scheme fulfils the specific compatibility criteria for aid, set out by the Commission in its 1998 decision on the French automatic aid scheme”.²⁷

Respect of the general legality criterion

In the recent Commission’s communication on cinema, the EC Commission stated that it would need to verify that “...the eligibility conditions of the State aid schemes do not contain clauses contrary to the EC Treaty provisions in fields other than State aids. The Commission must ensure, *inter alia*, that the EC Treaty principles prohibiting discrimination on the grounds of nationality, freedom of establishment, free movement of goods and freedom to provide services have been respected (Articles 12, 28, 30, 39, 43, 48 and 49 EC)...”

Against this background, the Authority had to ascertain that the film support mechanisms foreseen in the regulation as notified did not contain clauses contrary to the basic principles and freedoms as enshrined in the EEA Agreement (in particular Articles 4, 11, 28, 31, 34 and 36). Compliance with these principles requires, *inter alia*, that aid schemes must not reserve the aid for nationals exclusively; require beneficiaries to have the status of national undertaking established under national commercial law (undertakings established in one country within the EEA and operating in another by means of a permanent branch or agency must be eligible for aid).

²⁶ Judgment of the Court of First Instance, Case T-459/93 *Siemens SA v. Commission* [1995] ECR II-1675.

²⁷ COM (2001) 534 final, 26.09.2001, p. 6;

The Authority was satisfied that the regulation contains a provision that clarifies that foreign production companies established in a country which is a Contracting Party to the EEA Agreement are regarded/treated as Norwegian film producers for the purpose of this regulation. This means that foreign producers may apply for support under the Norwegian film support mechanisms, provided the film is shot in Norwegian or Sami. This condition is not in conflict with the basic principles of the EEA Agreement, but reflects a justified linguistic and cultural concern.

Therefore, the Authority concluded that the film support mechanisms respected the general legality criterion.

Specific compatibility criteria

In the “French” decision, the EC Commission developed a number of requirements which need to be fulfilled in order for the aid to be permissible under the cultural exemption:

1. The cultural content of eligible films must be ensured, in order to avoid that certain audiovisual productions and which do not contribute to culture, such as commercials, receive State support;
2. The aid intensity must be limited to 50%, with the exception of difficult and low budget films, with an aim to stimulating normal commercial initiatives inherent to a market economy and to avoiding a bidding contest between Member States;
3. Aid supplements for certain specific activities must be avoided to ensure that the aid has a neutral incentive effect; and
4. The producer must be free to spend at least 20% of the film budget in other Member States, which favours exchanges within the European Union; in other words, the full aid must still be available if only 80% of the budget is spent within the Member State that awards the aid.

1. Cultural content of eligible film projects

The Authority observes that the film support mechanisms as such pursue the objective of promoting Norwegian quality films and that under the conditions of the mechanisms, support is, in varying degrees, subject to appraisal by the Norwegian Film Fund based on artistic, economic, technical and market related criteria.

The Authority was therefore satisfied that the aid granted under the film support mechanisms is directed towards a cultural product.

2. Permissible aid intensity (necessity and proportionality of the aid)

It is commonplace in Europe that film production requires substantial state support in order to ensure that Europe’s own culture and creative capacity has the opportunity to be expressed. This support is required for ensuring the European presence in a market dominated by audiovisual products from outside the EEA. The fostering of audio-visual production by the individual Member States allows the promotion of cultural diversity that would not otherwise have been possible.

One of the major impediments to the development of the European film production can be seen in the difficulty of obtaining a sufficient level of up-front commercial backing to enable a financial package to be put together so that production can proceed. Furthermore, the fragmentation of the cinematographic market in Europe is a further reason for the poor financial situation of the European film industry. To a large extent, national films attract audience mostly in their home country. Distribution of national films outside their home countries is therefore often limited. As a consequence, domestic films do not normally reach a sufficiently wide audience to make it possible to recover the production costs of the films through box office revenues and the proceeds from video and television showing.

It results from these circumstances that, in the absence of State support, market forces alone would not make it possible to produce the desirable volume of films and consequently to ensure an adequate promotion of the culture through cinematographic works.

These general observations concerning the situation for European films are particularly true for the Norwegian film market and the conditions for Norwegian film production. Based on the information submitted by the Norwegian Government it is evident that neither the general structure for film production nor the market potential and expected revenues are sufficient in order to maintain film production without substantial State support.

On the other hand, and in order to strike a balance between the objectives of promoting film production and maintaining conditions of undistorted competition, aid must be limited to what is necessary and proportionate. In the “French” decision, an aid ceiling of, in principle, 50% was regarded as justified in order to stimulate normal commercial initiatives inherent in a market economy and to avoid a bidding contest between the Contracting Parties. This threshold applies only to national film support, allowing cumulation with aid from other public sources, such as aid provided through the new EC programme MEDIA Plus (2001-2005)²⁸, the Council of Europe Eurimage Programme or the Nordic Film Fund.

So-called “difficult and low budget films” are excluded from this limit. In addition to exceptions from the aid ceiling of 50% for “difficult and low budget films”, and in view of the comparatively limited geographic extension of certain languages and cultures and further given the limited circulation of those cultural products within the EEA and world markets, the Authority could, in accordance with the Commission policy, also “*accept aid intensities higher than 50% where proven to be necessary in cases other than for difficult and low budget films...*”²⁹.

Finally, it results from the approach taken by the EC Commission in the “Swedish” case that aid not subject to restrictions concerning the place of expenditure of the film budget (so-called “territorialisation requirement”) may be granted up to higher aid ceilings.

²⁸ Council Decision of 20 December 2000, OJ L 13, 17.1.2001, p. 34; according to the MEDIA Plus programme, funding may be authorised up to 60% when the project contributes to the enhancement of European linguistic and cultural diversity.

²⁹ See Commission communication on cinema, p. 9.

Financial data regarding film production in Norway in the past (1997-1999) revealed that box office revenues did not cover the producer's own capital contributions. Even if the information did not include revenues from other sources, it should be recalled that, according to the Norwegian authorities, film producers would receive, in general, only 25% of total gross box office revenues. It should also be recalled that other sources of income depend upon the predicted market potential and the films' commercial success. Information also showed that market shares of Norwegian films in Norway were very limited and well below the average market share of domestic films in the respective home markets within the EEA. Norwegian films had also a modest presence on markets abroad.

It can therefore be concluded that State support covering the part of the film production budget which could not be financed with private contributions, can be regarded as necessary in order to maintain a minimum number of film productions in Norway. The necessity for State intervention is further underlined by the fact that there is only a small number of production companies engaged in continuous film production and that the number of films produced in Norway is modest.

Relatively high aid intensities would seem to be result the of the limited market potential for Norwegian films. Against this background, the Authority can therefore agree to public support for film production exceeding the generally applicable ceiling of 50%, provided that mechanisms are in place which ensure that film support granted for a film project is limited to what is necessary and proportionate.

As regards the *feature film production support mechanism*, the Authority notes that the mechanism's aid intensity is limited to max. 75%, due to the film producer's obligation to provide at least 25% own financing. This aid intensity may be further reduced by the obligation to repay a certain part of public support received. The Norwegian authorities have shown that, based on new provisions in the film support mechanisms, the aid intensity for film production support is expected to be reduced to 55%. Depending on whether or not these films would generate sufficient revenues, the repayment obligation would further reduce the overall aid intensity.

As regards support in the form of *50/50 grants*, the Authority observes that this mechanism limits State support for film production to 50% of production costs. The Authority further notes that the aid intensity may be further reduced by both the absolute aid ceiling of NOK 10 million and the repayment obligation.

With respect to both support mechanisms, the Authority notes that common costs are not normally included in the film production budget³⁰. Thereby, production support is limited to costs directly incurred in relation to the production of each film. The Authority also notes that, production costs would also include costs incurred in the pre-production phase (such as screenplay and project development). Any possible aid received by the film producer in this respect, would be taken into account/deducted from the aid available under the film production support mechanisms.

As regards State support in the form of *box office returns*, the Authority observes that this form of support is not calculated in relation to the production costs of the

³⁰ A certain share of common costs may however be covered through box office returns.

individual film project but is designed in such a way that it is proportionate to the size of the producer's own capital contribution to the total budget of the film. In particular, the payment of the audience-related support takes place up to the point in which the producer's/private investor's outlay (plus a certain share of common costs) has been covered. This form of aid is intended to increase the films' profitability and thereby attracts private investors to provide financing for film production projects. This aid mechanism is therefore a means of contributing to continuous film production in Norway.

Box office returns may be cumulated with aid granted for film production (as film production support or as "50/50 grants"). However, cumulated aid under both support mechanisms is subject to certain restrictions. Cumulated aid shall not exceed NOK 30 million. Based on simulations carried out by the Norwegian authorities, it would seem that with the introduction of an absolute ceiling of cumulated aid as well as the repayment obligation³¹, the aid intensity for films released between 1996 and 1999 and resulting from total support measures (feature film production support and box office returns) would be reduced to 63% of total production costs if the new provisions were applied (and given that all other figures remained the same).

As regards *support for short films*, the Authority notes that, based on estimates provided by the Norwegian authorities which showed that, on average, public support did not exceed 50% of production costs, it can be expected that, in general, the aid intensity is limited to 50% of production costs. The Authority would also add that even where in individual cases, the aid intensity should exceed 50%, such higher aid intensities would be considered as justified by the very nature of short films being difficult and low-budget films. The Authority finally observes that, in general, aid is, based on the application of support schemes in the past, not expected to be above the *de minimis* ceiling.

As regards *aid granted for marketing and promotional activities*, the Authority takes note of the Norwegian Government's confirmation that such aid is limited to 50% of marketing costs. The Authority also notes that, in particular in connection with presentations of the films at film festivals, according to the EC Commission Regulation 70/2001 on State aid to SMEs (which is not yet incorporated into the EEA Agreement), are considered as compatible with the common market and exempted from the notification obligation aid to SMEs for participation in fairs and exhibitions up to 50% of the additional costs. Against this background, the Authority considers that these support measures can be regarded as necessary and proportional (not contrary to the common interest).

Finally, the Authority observes that under the new regulation one single public body will be responsible for granting film support. This organisational reform can be expected to contribute so that the film support granted to each film project would be proportionate to what is necessary to enable production and to the film's predicted market potential. In addition, the Authority considers that, given the small size of the few companies engaged in continuous film production in Norway (these companies

³¹ It should be noted that even though box office returns do not have to be repaid as such, the receipt of such aid would, according to the repayment formula, increase the amount of film production support to be repaid.

having few employees and on average a turnover of around NOK 20 million), an aid intensity above 50% can be regarded as justified.

In light of all the above considerations, the Authority has concluded that the proposed film support mechanisms are limited to what is necessary and proportionate to the achievement of the cultural objectives pursued.

3. Aid supplements

In this respect, the Authority notes that there are no aid supplements in the notified Norwegian film support mechanisms.

4. 20% requirement

The definition of eligible Norwegian film does not contain any territory-related criteria linked to the realisation in Norway of a particular proportion of the production work. Only in cases where the film is shot in a language other than Norwegian or Sami, State support will be available if, *inter alia*, the film contributes to cinematographic art and culture in Norway. As stated above, whether this is the case depends on the extent to which film producers have recourse to Norwegian film directors, screenplay writers, etc. In this respect, the Authority notes that this provision extends the scope of films eligible under the film support mechanisms and can therefore not be regarded as limiting State support depending on the place in which certain film production activities are carried out.

The Authority therefore concluded that the proposed film support mechanisms respect the condition that a minimum proportion of 20% of the film budget may be spent in other EEA States with the full availability of the aid.

Limitation in time

The Authority accepts the validity of the regulation as being limited to five years.

Conclusions

In view of the foregoing considerations, the Authority regards the various film support mechanisms covered by the regulation for film support, as notified to the Authority, as compatible with the functioning of the EEA Agreement, and in particular with Article 61 (3)(c) thereof.

Finally, the Authority reminds the Norwegian Government of its obligation to submit annual reports regarding the implementation of the film support scheme in accordance with Chapter 32 of and Annex IV to the Authority's State Aid Guidelines.

HAS ADOPTED THIS DECISION:

1. The Authority has decided not to raise objections to the aid granted under the various film support mechanisms covered by the regulation on film support as notified by the Norwegian Government, for the period of five years, starting on 8 February 2002.
2. The Norwegian Government is requested to submit simplified annual reports regarding the implementation of the scheme in accordance with Chapter 32 of the Authority's State Aid Guidelines.

Done at Brussels, 20 February 2002

For the EFTA Surveillance Authority

Einar M. Bull
President

Hannes Hafstein
College Member