Case No: 57325
Event No: 411266
Dec. No: 39/07/COL

EFTA SURVEILLANCE AUTHORITY DECISION

of 27 February 2007

on public financing of municipal day-care institutions in Norway
(NORWAY)

THE EFTA SURVEILLANCE AUTHORITY[1],

HAVING REGARD TO the Agreement on the European Economic Area[2], in particular to Articles 61 to 63 and Article 109 thereof, and to Protocol 26 thereof,

HAVING REGARD TO the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice[3],

HAVING REGARD TO Protocol 3 to the Surveillance and Court Agreement, in particular to Article 10 (1), Article 13 (1) and Article 4 (2) thereof,

WHEREAS:

I. FACTS

1 PROCEDURE

In August 2004, Private Barnehagers Landsforbund (hereinafter "PBL"[4]) contacted the Authority with a view to filing a complaint concerning public subsidising of municipal kindergartens in Norway. Some informal exchange of views between the Authority's Competition and State Aid Directorate (hereinafter "CSA") and PBL took place in the course of 2004, *inter alia* in a meeting on 16 September 2004.

By letter dated 23 February 2005, PBL submitted a formal complaint alleging that the system for public contributions to the operation of municipally owned day-care centres contained elements of state aid. The letter was received and registered by the Authority on the same day (Event No 311163).

[1] Hereinafter referred to as "the Authority".
[2] Hereinafter referred to as "the EEA Agreement".
[3] Hereinafter referred to as "the Surveillance and Court Agreement".
[4] PBL is an association of approximately 1400 privately owned kindergartens in Norway.

By e-mail dated 25 April 2005 and by letters dated 17 January 2006, 4 May 2006 and 6 June 2006 registered by the Authority respectively on 2 May 2005 (Event No 318214), 23 January 2006 (Event No 359482), 9 May 2006 (Event No 373350) and 8 June 2006 (Event No 377431), the complainant submitted further information concerning the case.

Representatives of the Authority held meetings with the complainant on 5 April 2005 and 16 February 2006.

By letter dated 13 July 2006 (Event No 381204), the Authority requested clarifications from the Norwegian authorities.

By letter dated 29 September 2006 from the Norwegian Mission to the European Union, forwarding a letter from the Ministry of Government Administration and Reform dated 25 September 2006, both received and registered by the Authority on 2 October 2006 (Event No 390534), the Norwegian authorities replied to the information request.

By letters dated 2 October 2006 and 11 October 2006, registered by the Authority respectively on 2 October 2006 (Event No 390471) and 31 October 2006 (Event No 396210), the complainant provided further comments.

On 13 December 2006 (Event No 403505), CSA held a meeting with the complainant, who formally called upon the Authority to act under Article 37 of the Surveillance and Court Agreement. The invitation to act was registered on 13 December 2006 (Event No 403227).

By letter dated 5 January 2007, registered by the Authority on 9 January 2007 (Event No 405652), the complainant supplied further information.

On 26 January 2007 (Event No 407924), CSA held a meeting with the complainant.

By e-mail dated 9 February 2007, received and registered by the Authority on the same day (Event No 409387), the complainant informed the Authority that it maintained the complaint. The Authority acknowledged the receipt of the complainant's e-mail by response dated 9 February 2007 (Event No 409439).

By fax dated 12 February 2007, received and registered by the Authority on the same day (Event No 409616), the complainant submitted further observations.

2 NORWEGIAN LAW

2.1 Development of day-care for children in Norway

Kindergartens (*barnehager*) for children under compulsory school age (i.e. between 0 and 6 years) have been available in Norway for many years.

Since 1953, a system of publicly funded municipal kindergartens has existed. Since 1963, establishments other than municipalities have also been allowed to establish kindergartens. Currently, kindergartens in Norway are run either by the municipalities (hereinafter "municipal") or by public institutions (e.g. hospitals), private companies or private organizations under the supervision of the municipalities (hereinafter "non-municipal") or as family day-care institutions under the supervision of an educated pre-school teacher. In

2005, 55% of children were enrolled in municipal kindergartens and 45% in non-municipal kindergartens.

Between 1953 and 1975, kindergartens were regulated as part of the Child Welfare Act with regulations pursuant to this Act.

The first Kindergarten Act (Act No. 30) was adopted on 6 June 1975. According to Section 4 of the 1975 Act, the municipalities had the responsibility for the development, construction and operation of kindergartens.

Since 2001, Norway has moved towards universal access to kindergartens for all children under 6 years.[5] In 2003, the Norwegian Parliament adopted the *"Barnehageforliket"* (hereinafter "the Kindergarten Agreement"), which expresses political intentions concerning the organisation and financing of kindergartens and the future of the sector. For that reason, in 2003, the legal obligation for the municipalities to offer kindergarten places to all children whose parents so wish was strengthened and a legal obligation for the municipalities to support non-municipal kindergartens was introduced.

2.2 The present rules

Today, both municipal and non-municipal kindergartens are regulated by the Act No 64 of 17 June 2005 on Day-Care Institutions (hereinafter "the Kindergarten Act"). With this Act, the municipalities are designated as kindergarten authorities and they have a duty to ensure that there is a sufficient number of places for children below compulsory school age, cf. Section 8, paragraph 1 and 2 of the Kindergarten Act.

According to Section 1 of the Kindergarten Act, a kindergarten shall give children below the age where they are obliged to receive education good possibilities for development and activities. It must also, unless otherwise decided, assist in giving the child an upbringing in accordance with the basic values of Christianity.

Pursuant to Section 2 of the Kindergarten Act, a kindergarten shall be a pedagogic undertaking[6] that should support the homes in their roles of bringing up and taking care of the children, thereby creating a good foundation for the development of the child, lifelong learning and active participation in a democratic society. The kindergarten shall assist the parents with the care and upbringing of children. It shall also promote human dignity. According to paragraphs 5 and 6 of Section 2, the kindergarten has the task of giving the child basic knowledge on central and topical subjects and support its curiosity, creativity and quest for knowledge. Moreover, the kindergarten shall impart values and culture to the child.

In explanatory remarks to the Kindergarten Act[7], it is underlined that:

"*Since the majority of children have kindergarten experience before they start school, it is important to ensure overall continuity in the offer of care and education of children. Kindergarten and school have a joint responsibility for ensuring good continuity and the changeover from kindergarten to school. The provision establishes that life long education, in the broadest possible sense, is ensured*."[8]

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[5] Starting Strong II: Early Childhood Education and Care, OECD 2006, Annex E: Norway, p. 399.
[6] The English translation on the University of Oslo Faculty of Law Library's homepage reads "*Day-care institutions shall be educational undertakings*."
[7] *Rundskriv* F-08/2006.
[8] Translated by the Authority.

According to Section 2, paragraph 9 of the Kindergarten Act, each kindergarten shall establish a yearly plan for its pedagogical activities. In the implementing regulation of 1 March 2006 on a framework plan for the content and tasks of a kindergarten[9], the Norwegian Government has stated the following about the task of the kindergarten:

"*The content of kindergarten shall be all-round and varied, and be formed so that every individual child gets activities and experiences as support for the development of its knowledge, skills and attitudes. At the same time the content shall support linguistic and social competence through joint communication and the gathering of knowledge. …*

The kindergarten shall support the child's curiosity, thirst for knowledge and learning, and contribute to a good grounding for life-long learning. The concept of life-long learning means that learning takes place in different arenas throughout life. Learning happens during the daily interplay with other people and with the environment, and is closely interwoven with play, upbringing and care. Children can learn through all their experiences in all areas. Children's wonder must be met in a challenging and investigative way so that the foundation for an active and developing learning environment is created in the kindergarten. The child's own interests and questions should be the basis for the learning processes and themes within the kindergarten.

The kindergarten shall strengthen the child's learning in formal and informal learning situations. The formal situations are planned and lead by the personnel. Informal learning situations are more closely connected with ordinary daily activities and here-and-now situations, in play, upbringing and interaction. There is no point in drawing a clear line between formal and informal learning situations. Both have pedagogic goals. The seven subject areas must be connected both to formal and informal learning situations.

The kindergarten's personnel must have an active relationship with the child's learning processes. … Support and challenge through varied experiences, knowledge and materials can promote learning. Early activities and experiences influence self awareness. Therefore, the personnel's actions and attitudes in connection with the child's learning experiences are crucial."[10]

Further, the abovementioned regulation of 1 May 2006 states the following concerning the obligation of the kindergarten to give the child basic knowledge on central and topical fields:

"*To make the kindergartens planning of a varied, all-round pedagogic offer easier, the content of the kindergarten is split into seven subject areas which are central to experience, investigation and learning. The subjects are mostly the same as the subjects the child will meet later at school. Good activities, experiences and learning within these subject areas in the kindergarten will be able to give the child a positive relationship to the subjects and motivation to learn more. …*

Each subject covers a wide field of learning. … For each field it is a formulated goal to work for the child's development and learning and a delimitation of the responsibility of the staff."[11]

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[9] *Forskrift om rammeplan for barnehagens innhold og oppgaver.*
[10] Translated by the Authority.
[11] Translated by the Authority.

The abovementioned implementing regulation of 1 March 2006 hereafter identifies the seven topics to be 1) communication, language and text, 2) body, movement and health, 3) art, culture and creativity, 4) nature, environment and technique, 5) ethics, religion and philosophy, 6) local milieu and society, and 7) numbers, room and form, including basic mathematics.

In line with the requirement of ensuring a sufficient number of kindergarten places, the municipalities develop and conduct kindergarten services themselves as well as give financial support to non-municipal kindergartens. The intention is to offer kindergarten places to all children whose parents so wish and at reasonable fees for the parents.[12]

Section 12 of the Kindergarten Act provides for a coordinated admission process of children to approved kindergartens in the municipality. Further rules to this effect have been laid down in a regulation of 16 December 2005 on the administrative and procedural rules relating to the admission to a kindergarten. According to the explanatory remarks to that regulation, the overall purpose is to ensure that admission to a kindergarten takes place in a way that secures legal protection and security for the applicants and a correct and efficient administrative procedure. The regulation prescribes, *inter alia*, that a parent can require a written statement of reasoning for a refusal for an application to a particular kindergarten and that the rules in the General Administrative Act (*Forvaltningsloven*) pertaining to access for parties to documents and confidentiality apply, cf. Sections 4-5 and 11 of regulation of 16 December 2005. Moreover, a refusal can be appealed pursuant to the rules laid down in Sections 6-9 of the regulation.

2.3 Financing

2.3.1 Sources of funding

The sources of income of day-care centres are parental payments and public aid in the form of subsidies. The parental fees should not exceed 20% of the cost of services; the rest should be covered from public subsidies. Of the latter, it is the intention that 50% should be borne by the state budget via earmarked grants to the municipalities, and 30% directly from the municipalities.[13]

2.3.1.1 Parental fees

As of 1 January 2006, the applicable rate for parental fees was fixed at NOK 2 250 per month[14] with an intention of a reduction to approximately NOK 1 800.[15] Part-time places are charged in proportion. According to Section 4 of the Kindergarten Act, the maximum limit for parental fees in a particular kindergarten (municipal or non-municipal) may be increased after the consent of parents council.[16]

[12] Full coverage is intended to be met until the end of 2007. Starting Strong II: Early Childhood Education and Care, OECD 2006, Annex E: Norway, p. 400.
[13] See the letter from the complainant dated 23 February 2005, p. 2.
[14] Regulation on maximum price for kindergartens in 2006, FOR-2005-12-16-1480: *Vedtak om fastsettelse av maksimalgrensen for foreldrebetalingen i barnehager for 2006.*
[15] Starting Strong II: Early Childhood Education and Care, OECD 2006, Annex E: Norway, p. 400.
[16] Further provisions regarding parental payments are prescribed in an implementing regulation, FOR 2005-12-16 nr 1478: Forskrift om foreldrebetaling i barnehager.

2.3.1.2 Public payments

Public financing of kindergartens is channelled through the municipalities which cover the costs for their own kindergartens and, according to Section 8, paragraph 6 of the Kindergarten Act, administer grants to non-municipal kindergartens.

Municipal coverage of costs is thus allocated to kindergartens in Norway regardless of their ownership. The municipalities cover costs of ordinary operation of the kindergartens (both municipal and non-municipal) which are not covered by parental contributions and other public subsidies.

The costs of running a *municipal* kindergarten are paid from the municipal treasury and, hence, are based on a cost coverage principle. Being part of the municipality, and not performing any (other) economic activity, the running costs of a municipal kindergarten is subject to the common budgeting and accounting rules for all municipal tasks. In other words, the budget of a municipal kindergarten is an integrated part of the total municipal budget of each municipality, and a municipal kindergarten is financed in the same way as other municipal tasks.[17] It follows from governmental regulations that the total municipal budget should be complete, i.e. all expected costs connected to an activity must be budgeted in full.[18] Thus, the expenditure of the municipal budget is based on the total costs needed for the operation of municipal kindergartens.

Since 1 May 2004, the municipalities have been obliged to cover operational costs of *non-municipal* kindergartens. In order to calculate the level of compensation necessary, the municipalities can choose between the cost coverage principle and the unit cost principle, but the same method must be applied to all non-municipal kindergartens in a particular municipality.[19]

2.3.2 Equivalent treatment

One of the main intentions behind the present Kindergarten Act was to achieve a more equal treatment of municipal and non-municipal kindergartens as regards public subsidies. To that effect, a new Section 7b was added to the Kindergarten Act in 2003 (currently Section 14 of the Kindergarten Act 2005):

"*Approved day-care centres shall be given equivalent treatment as regards public contributions. The King may adopt regulations with further provisions on what is meant by equivalent treatment.*"[20]

According to the explanatory remarks in the underlying bill, equivalent treatment with regard to public funding is both an aim in itself and a means to obtain full coverage, lower parental payments and good quality in the offer of kindergartens. In order to meet this requirement, a Regulation relating to equivalent treatment of child care institutions in relation to public subsidies (hereinafter "the Regulation") has been adopted.[21] According to Section 3, paragraph 1, of the Regulation:

[17] Letter of 25 September 2006 from the Norwegian Government to the Authority, p. 4, point 3.2. Since the municipal kindergartens are normally not organised as undertakings (*foretak*), the municipalities do not draw up a separate budget (*særbudsjett*) for them.
[18] Municipal Act no. 107 of 25 September 1992, Chapter 8 and regulations of 15 December 2000 no. 1423 and 1424.
[19] Letter from the Ministry of Children and Family to the Municipalities Central Union of 5 November 2004.
[20] Translated by the Authority.
[21] Regulation No 539 of 19 March 2004.

"It is the municipality that shall see to it that all approved kindergartens in the municipality receive public grants in a way which is equivalent, all taken together."

Moreover, according to Section 3, paragraph 2, 1st sentence of the Regulation, "*[t]he municipality shall cover costs for the ordinary operation of the kindergarten which are not covered by other public grants and fees from parents.*"[22]

In order to avoid excessive funding and to control the increase of expenses in non-municipal kindergartens, paragraphs 2, 2nd sentence, to paragraph 5 of Section 3 of the Regulation establish the following:

"*If the fees from parents in non-municipal kindergartens are set lower than the parents' fees in the municipality's own kindergartens, the municipality has no obligation to cover the difference.*

The municipality has no obligation to extend grants so that the total public financing of a kindergarten exceeds what a corresponding kindergarten owned by the municipality on average receives in the form of public grants.

The municipality has an obligation to give grants so that the total public support consists of at least 85 % of the amount that corresponding kindergartens owned by the municipality in average receive in public support.

The municipality has no obligation to cover increases of costs which exceed the normal increase of prices and costs in the municipal sector."[23]

These limitations have led to the situation in which the benchmark for the calculation of compensation for the non-municipal kindergartens is the average amount of grants to similar municipal kindergartens, and the increase of costs and prices is linked to the municipal sector. If a particular municipality does not itself operate any kindergartens, the relevant data should be obtained by collecting material on the calculation of public funding from five similar municipalities in the county and then get an average. [24]

As can be seen, the regulation applies a cost-coverage principle, as a starting point, but supplements this with a unit-coverage principle linked to the rule that a municipality must pay to a non-municipal kindergarten at least 85 % of the amount spent on municipal kindergartens. The Norwegian authorities have explained that, due to great cost variations between kindergartens caused by e.g. geographical cost differences, personnel education level, children with special needs, granting, for instance, a lump sum to all kindergartens would not fulfil the objective of equal treatment of all kindergartens.[25]

3 THE COMPLAINT

The complaint relates to the difference of treatment stipulated in the above-described rules in Section 3 of the Regulation. According to the complainant, as a result of generally higher costs in municipal institutions compared to the non-municipal kindergartens, public funds are systematically allocated to municipal kindergartens at a higher level than the

[22] Letter of 25.09.2006 from the Norwegian authorities to the Authority, p. 8.
[23] Letter of 25.09.2006 from the Norwegian authorities to the Authority, p. 8.
[24] Explanatory remarks to the Regulation, paragraph 3.
[25] Letter of 25.09.2006 from the Norwegian authorities to the Authority, p. 11.

funds being allocated for the same purpose to non-municipal ones. Therefore, the cost coverage principle, with the limitations as described above, "massively" favours municipal day-care centres. In the opinion of the complainant, the systematically higher public support for municipal kindergartens than for non-municipal kindergartens results in discrimination and, thereby, to an allotting to the municipal kindergartens of State aid that is incompatible with Article 61 of the EEA Agreement. The complainant, furthermore, states that *"The limitations of the Regulation with regard to cost increases will tend to cement this situation"*.[26] While the complaint is not entirely clear, it appears that objections are also raised against the ceiling of cost coverage that a non-municipal kindergarten is subject to.

Furthermore, the complainant argues that, as a consequence of the limitation, according to which the difference between lower parental fees and the maximum price is not covered by municipalities, a price competition between non-municipal day-care centres and the municipal kindergartens can no longer take place.

Finally, in its letter of 12 February 2007, the complainant has argued that also aspects in relation to the return on invested capital and the way transfers to the non-municipal kindergartens are calculated and paid out give rise to difference of treatment.

II. ASSESSMENT

4 ARTICLE 61(1) OF THE EEA AGREEMENT

4.1 Introduction

Article 61(1) of the EEA Agreement reads as follows:
"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, in so far as it affects trade between Contracting Parties, be incompatible with the functioning of this Agreement."

Consequently, the Authority will assess whether the above described funding system of municipal kindergartens constitutes state aid, by asking the following questions:

- Is the support granted by the State or through Stare resources?
- Does it favour certain undertakings or the production of certain goods?
- Is it capable of distorting competition and affecting trade between the Contracting Parties to the EEA Agreement?

4.2 State resources, selectivity and economic advantage

The municipal kindergartens are financed directly from the municipal budgets. State resources are thus evidently involved. The funding system is selective in nature as it benefits only the kindergarten sector by providing the beneficiaries with an economic advantage which they would not enjoy under normal market conditions.

[26] Letter of 23.02.2005 from the complainant to the Authority, p. 4.

4.3 Municipal kindergartens are not undertakings

For a measure to be covered by Article 61(1) of the EEA Agreement, it has to be granted to undertakings. The term undertaking has been developed mainly in relation to Articles 81 and 82 of the EC Treaty to which Articles 53 and 54 of the EEA Agreement correspond, but must be construed the same way as regards Article 87 (1) of the EC Treaty to which Article 61(1) of the EEA Agreement corresponds. The concept of an undertaking encompasses every entity engaged in an economic activity.[27] Any activity consisting in offering goods and services on a given market is an economic activity.[28] It must therefore be assessed whether the municipalities, when providing kindergarten places for their constituency, are engaged in an economic activity by offering goods or services on a market or whether their activities are non-economic in nature.

Many activities conducted by organisations performing largely social functions, which are not profit-oriented and which are not meant to engage in industrial or commercial activity, will normally not be covered by the European Community's competition and internal market rules. This concerns several non-economic activities of organisations such as trade unions, political parties, churches and religious societies, consumer associations, learned societies, charities as well as relief and aid organisations.[29] The European Court of Justice has regarded that courses given by educational institutions under the national education system do not constitute services within the meaning of the EC Treaty.[30] Only services provided for remuneration are to be considered as services within the meaning of the EEA Agreement. An essential characteristic of remuneration lies in the fact that it constitutes consideration for the service in question, and is normally agreed upon between the provider and the recipient of the service. The Court of Justice considered that that characteristic is absent in the case of courses provided under the national education system. The State, in establishing and maintaining such a system, is not seeking to engage in gainful activity but is fulfilling its duties towards its own population in the social, cultural and educational fields. Secondly, the educational system was, as a general rule, funded from the public purse and not by pupils or their parents. That parents sometimes must make a certain contribution to the operating expenses of the system did not alter that conclusion.

In the practice of the European Commission, this case law was also applied, for instance in the assessment of measures granted to the French professional football clubs[31] or the measures in favour of the *Přerov* logistics College in the Czech Republic[32].

With regard to the definition of what constitutes an economic activity, further guidance is given in *Poucet and Pistre*, *Cisal* and *AOK Bundesverband.*[33] The sickness funds in question were based on the principle of national solidarity and were entirely non-profit making. The benefits paid were not proportional to the amount of the compulsory contributions. The institutions fulfilled an exclusively social function and did not exercise an economic activity. In all three cases, the Court of Justice concluded that the activities

[27] Case C-41/90 *Höfner and Elser* [1991] ECR I-1979, paragraph 21.
[28] Case 218/00 *Cisal* [2002] ECR I-691, paragraph 23.
[29] Communication from the Commission Services of general economic interest in Europe, OJ C 17 of 19.01.2001, p. 4.
[30] Case 263/86 *Humbel* [1988] ECR 5365, paragraphs 15-20, and Case C-109/92 *Wirth* [1993] ECR I-6447, paragraphs 14-19.
[31] State aid N 118/00 – France, *Subventions publiques aux clubs sportifs professionnels*, decision of 25.04.2001, SG (2001) D/288165.
[32] State aid NN 54/2006 – Czech Republic, *Přerov* logistics College, decision of 8.11.2006, C (2006) 5228.
[33] Joined Cases C-159/91 and C-160/91 *Poucet and Pistre* [1993] ECR I-637, Case 218/00 *Cisal*, cited above, Joined Cases C-264/01, C-306/01, C-354/01 and C-355/01 *AOK Bundesverband* [2004] ECR I-2493.

were non-economic in nature. The bodies concerned could, therefore, not be considered as undertakings within the meaning of Articles 81 and 82 of the EC Treaty.

The Kindergarten Act of 2005 itself illustrates the social character of the services provided. According to the Act, the purpose of kindergartens is to provide children under compulsory school age with good opportunities for development and activity in close understanding and collaboration with the children's homes.[34]

The similarities to the school system are striking. The kindergartens are educational institutions,[35] assisting homes with the care and upbringing of children, laying a sound foundation for the children's development, life-long learning and active participation in a democratic society.[36] The municipality is obligated to ensure that there are a sufficient number of day-care places for children under compulsory school age in line with the needs of the inhabitants in the municipality. The aim is to achieve full coverage in 2007.[37]

The fact that the parents are not obliged to send their children to kindergartens does not alter the character of the social and educational service offered by the municipalities towards their inhabitants. Moreover, the sector falls within the responsibility of the Ministry of Education. The Ministry has underlined that the more appropriate translation of the Norwegian term "*barnehage"* would rather be "*pre-school education"* than "kindergarten".[38] The manager of a kindergarten should be a qualified pre-school teacher or otherwise have completed three years of studies at educational college.[39] The municipalities may decide to establish a joint coordinating committee for municipal day-care institutions and primary schools[40], which highlights the direct link between the two types of institutions.

The social, cultural, educational and pedagogical nature of kindergartens is further illustrated by the fact that care, upbringing and learning in kindergartens promote human dignity, equality, intellectual freedom, tolerance, health and an appreciation of sustainable development. Kindergartens provide children with opportunities for play, self-expression and meaningful experiences and activities in safe, yet challenging surroundings.[41] Kindergartens shall give children basic knowledge of central and topical fields and shall nurture children's curiosity, creativity and desire to learn and offer challenges based on the children's interests, knowledge and skills. They must also impart values and culture, provide room for children's own cultural creativity and help to ensure that all children experience happiness and the ability to cope in a social and cultural community.[42] The learning process shall cover a wide field of activities stemming from language developments to social and local interaction, and to first perceptions of numbers and mathematics.[43]

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[34] Kindergarten Act, Section 1.
[35] See above point 2.2.
[36] Kindergarten Act, Section 2, second paragraph.
[37] Full coverage is intended to be met until the end of 2007. Starting Strong II: Early Childhood Education and Care, OECD 2006, Annex E: Norway, p. 400.
[38] Letter of 25.09.2006 from the Norwegian authorities to the Authority, p. 1.
[39] Kindergarten Act, Section 18.
[40] Kindergarten Act, Section 5, first sentence.
[41] Kindergarten Act, Section 2, third paragraph.
[42] Kindergarten Act, Section 2, fifth and sixth paragraph.
[43] Regulation on framework for the tasks and content of the day-care institutions FOR 2006-03-01 nr 266: *Forskrift om rammeplan for barnehagens innhold og oppgaver*, Section 3.

Therefore, it is nothing that indicates that the municipalities by providing these services have any intention whatever to engage in a gainful activity. On the contrary, the municipalities are fulfilling their duties towards their own populations in the social, cultural and educational fields.

The parents are obliged to pay a fee of NOK 2250[44] to cover a part of the operating expenses (around 20% of the costs)[45]. The fact that the fee is fixed and does not depend on the actual cost of the service for the individual child. This demonstrates the principle of solidarity. The fee does not increase for children with special needs, for example due to disability. That the fee is not linked to the costs is further illustrated by the fact that parents with more than one child benefit from a reduction of the fee of minimum 30% for the second child and minimum 50% from the third of more children.[46] In addition, all municipalities shall ensure that families with low income can be offered reductions or exemptions from the parental fees.[47] Yet, in the Authority's view, it cannot alter the nature of the service that parents sometimes must make a certain contribution to the operating expenses of the system.[48]

In addition to cultural, educational and social aspects of the activities of municipal kindergartens, the provision of kindergarten services is a task of the municipality acting as a public authority. Under Norwegian law, the decision to admit children to the municipal kindergartens is regarded as an administrative act and not a private law decision. The municipality is the local authority for kindergarten institutions and provides guidance and ensures that they are operated in accordance with current rules.[49] The municipality is obligated to ensure that there are a sufficient number of kindergarten places for children under compulsory school age. The pattern of development and modes of operation shall be adapted to local conditions and needs. The municipality co-ordinates the admission process with equal treatment of children and giving priority to children with disabilities.[50] The municipality is responsible for ensuring that kindergarten facilities for Sami children in Sami districts are based on the Sami language and culture. In other municipalities steps shall be taken to enable Sami children to secure and develop their language and their culture.[51] According to case law of the Court of Justice, exercising powers which are typically those of a public authority is not of economic nature.[52]

On the basis of the factors taken together, it is the opinion of the Authority that the tasks performed by the municipal kindergartens are of general interest, and not market-based. The municipal kindergartens are not undertakings in the meaning of Article 61 (1) of the EEA Agreement. Grants to those institutions are consequently not state aid in the meaning of this provision.

[44] See above under 2.3.1.1.
[45] In the Kindergarten Agreement it is estimated that around 80% of the cost would be covered by the public sector. In the OECD report referred to above, it is stated that the parental fee is capped at no more than 20% of the costs.
[46] Regulation on parental payments, Section 3, first paragraph.
[47] Regulation on parental payment, Section 3, third paragraph.
[48] Case 263/86 *Humbel*, cited above.
[49] Kindergarten Act, Section 8.
[50] Kindergarten Act, Sections 12 and 13.
[51] Kindergarten Act, Section 8, third paragraph.
[52] Case C-364/92 *Eurocontrol* [1994] ECR I-43 and Case C-343/95 *Calí* [1997] ECR I-1547.

4.4 No effect on cross-border trade

That being said, the Authority has found it useful to assess in the following whether there are other reasons that lead to the conclusion that the contested legislation falls outside the scope of Article 61 (1) of the EEA Agreement.

In order for a measure to fall within the scope of Article 61(1) of the EEA Agreement, there must be an effect on cross-border trade.

The criterion is normally easily met. Whenever state financial support strengthens the position of an undertaking (given that undertakings are in fact involved) compared with other undertakings competing in intra-EEA trade, the latter must be regarded as affected by that measure. Therefore, the Authority will assess whether there are any intra-EEA trade in the provision of kindergarten services which would be affected by the support of municipal kindergartens. In the assessment whether trade affectation is present, the Authority must identify the factual circumstances of the case.[53]

In the case at hand, there are several ways trade could potentially be affected. One is that the users of services from other EEA states would be more inclined to use the Norwegian service than the one in other EEA states. A second possible effect is that the support the municipal kindergartens receive would enable them to expand the scope of their services abroad. The third possible effect is that foreign service providers would be affected in their actual or potential operation in Norway.

Since the municipalities are only obliged to offer services to their own inhabitants, it is almost excluded that parents living in other EEA States would choose a Norwegian kindergarten instead of their local day-care facility.

Bearing in mind that the municipal kindergartens are covered solely for the costs of their operation of day-care services in that particular municipality, the support will not enable them to expand their services to other EEA states.

On the provider side, the Authority has not been able to identify a single instance of establishment of foreign kindergartens in Norway.

In 2003, the Authority examined a scheme concerning real estate leaseholds for private kindergarten facilities in Oslo.[54] In this decision, the Authority concluded that the state support in this case did not affect trade. The background for that conclusion was, amongst others, information submitted by the municipality of Oslo. The municipality had contacted the Ministry of Children, Private Barnehagers Landsforbund and PEDLEX Norsk Skoleinformasjon. None of these institutions had any knowledge of any private foreign ownership interests in Norwegian kindergartens.[55]

Also the Norwegian national court Tinn og Heddal Tingrett concluded in its judgement of 27 April 2006 that currently there is no foreign day-care service provider in the

[53] T-316/04 *Wam SpA*, judgement of 6 September 2006, not published yet.
[54] Decision of the Authority 291/03/COL of 18.12.2003 regarding the establishment of private day-care facilities on public sites with subsidised real estate leasehold in Oslo.
[55] Annex 8 to the notification of establishments of private day-care facilities on public sites with subsidised real estate leasehold fee. Letter from the Norwegian authorities to the Authority dated 22 October 2003 (Event No 03-7289-A).

municipality of Notodden which is the authority granting support to 7 local day-care institutions being subject to the court judgement.[56]

According to the complainant, the situation has changed since 2003. The complainant has provided a list of 10 allegedly foreign kindergarten providers.[57] The Authority has carefully examined the list to establish whether the providers are foreign.

The list submitted by the complainant shows that all 10 undertakings have been registered as so-called NUFs. NUF is an abbreviation for *Norsk Utenlandsk Foretak* and is a simplified method of registering branches of foreign companies in Norway without them having to comply with the general company legislation in Norway. Originally meant to ease the requirements for foreign companies to establish themselves in Norway, it has become increasingly popular for small Norwegian companies to register themselves as NUFs for many reasons (so-called Norwegian NUFs). Compared to Norwegian Limited Companies, the advantages are that almost no stock capital is needed, and that there is no audit obligation. Compared to personal companies (*enkeltmannsforetak*) there are numerous advantages with regard to social security benefits. Several companies specialise in helping Norwegian companies establish a NUF. The most common way is to establish a limited company in England with a share capital that might be limited to 1 pound and after that register it as a NUF in Norway.

The list of 10 allegedly foreign companies all appear to be so-called Norwegian NUFs registered in the UK and the Seychelles, with, to the Authority's knowledge, no business activities in the country of registration. They all have Norwegian names and are, as far as it can be judged from the names, run by Norwegians. The Authority has examined the companies in the UK Company register[58] with the same Norwegian names without, however, being able to verify that these companies have any business activities in the UK apart from being registered there. The only undertaking which is clearly operational in the UK, Occupational Psychology Services Ltd., is offering services such as organisational behaviour, psychometrics, career development and counselling.[59] This company has a branch registered in Norway under NACE Code 85.327 Barnehager. The Authority has contacted both the mother company in the UK and the contact person in Norway and it appears that neither Occupational Psychology Services Ltd. nor its Norwegian branch actually provide day-care facilities for children. Therefore, it can be concluded that the documents submitted by the complainant do not provide any evidence that there are foreign companies running kindergarten activities in Norway.

The Authority is not in possession of any other information that there presently exist cross-border elements with regard to the provision of kindergarten services in Norway. Given the present state of regulation of the Norwegian day-care facilities, with the regulation on maximum parental payments and the principle that only costs are covered, it is very unlikely that foreign providers would consider establishing themselves in Norway.

Given that the presence of foreign kindergartens is non-existent or marginal and that this situation is not likely to change in the near future, the Authority concludes that the trade

[56] Case number 05-031989TVI-TINN.
[57] Letter from the complainant dated 23.02.2005, p. 7 and Annex 8 to this letter.
[58] www.companieshouse.gov.uk
[59] www.opsltd.com

between Contracting Parties is not affected and that also for this reason the contested Norwegian rules fall outside the scope of the State aid rules.[60]

4.5 Conclusion

Based on the abovementioned considerations, the Authority concludes that neither are the municipal kindergartens undertakings in the sense of Article 61 of the EEA Agreement, nor is trade affected as required by that provision. Therefore, the current system of public financing of municipal day-care institutions does not qualify as state aid within the meaning of Article 61(1) of the EEA Agreement.

5. ASSESMENT OF THE COMPATIBILITY OF THE MEASURE HAD IT CONSTITUTED AID UNDER ARTICLE 61 (1) EEA.

As already stated, it is the conclusion of the Authority that the allegedly discriminatory aid measures do not constitute aid within the meaning of Article 61 (1) of the EEA Agreement. In order to respond to the complaint, the Authority has, however, found it useful to asses whether the different rules pertaining to the public financing of municipal and non-municipal kindergartens would have been incompatible with the EEA Agreement if the financing had qualified as an aid measure under that provision.

According to Article 59(2) of the EEA Agreement:

"Undertakings entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly shall be subject to the rules contained in this Agreement, in particular to the rules on competition, in so far as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them. The development of trade must not be affected to such an extent as would be contrary to the interests of the Contracting Parties."

The provision in Article 59 (2) of the EEA Agreement entails any potential aid to municipal kindergartens can be regarded as compatible state aid in the form of compensation for the provision of services of general economic interest provided that certain criteria are fulfilled. First of all, the public service must be clearly defined and properly entrusted to the undertakings in question. Furthermore, the amount of public funding granted cannot go beyond what is necessary to finance the costs of the public service.

In the opinion of the Authority, the considerations presented above under point 4.3 also support the conclusion that, if one were to view the operation of a municipal kindergarten as an economic activity, then this operation would also have the character of a service of general economic interest covered by Article 59 (2) of the EEA Agreement. For the same reasons, the Authority finds that the provisions in the Kindergarten Act and the Ministry's different implementing regulations ensure a sufficient a clear definition of the public service tasks of the municipal kindergartens.

[60] See also Commissions decisions in State aid N 465/2005 – The Netherlands, School Support Services, decision of 23.11.2005 C (2005) 4439; State aid NN 54/2006 – Czech Republic, *Přerov* logistics College, decision of 8.11.2006, C (2006) 5228; State aid N 258/00 – Germany, Leisure pool Dorsten, decision of 12.01.2001, SG (2001) D/285046; State aid No 543/2001 – Ireland, Capital Allowances for Hospitals, decision of 27.02.2002 C (2002) 608; State aid NN 55/2005 (ex N 595/2004) – Poland, Heritage conservation, decision of 20.07.2005, K (2005) 2714.

As already stated, the allocation of public support to municipal kindergarten is based on cost coverage principle. The complainant has not argued that municipal kindergartens are overcompensated in the sense that they receive a higher amount from their municipalities than their actual costs. Nor has the Authority uncovered elements in the Norwegian legislation that indicates that this is so. Hence, the only compatibility question, had state aid been involved, relates to the claim that it would be incompatible with Article 61 of the EEA Agreement that the Section 3 of the Norwegian Regulation did not ensure identical treatment of municipal and non-municipal kindergartens.

The question of discrimination regarding aid between the public and private sectors under the EC Treaty was examined in the judgment in *Falck*. After emphasizing that the responsibility for granting aid falls primarily upon the government concerned, the Court of Justice clarified the role of the Commission in the following terms: "*[i]t is true ... that although any aid measure is likely to favour one undertaking in relation to another, the Commission cannot approve aid the grant of which may result in manifest discrimination between public and private sectors. In such a case the grant of aid would involve distortion of competition to an extent contrary to the common interes*t".[61]

The mere fact that aid is only granted to some undertakings is, in this respect, not sufficient to establish manifest discrimination according to case law. Within the limits set by Articles 61 (2 and 3) and 59 (2) of the EEA Agreement and the rules in this Agreement on free movement, it is up to each State to delimit the types of activities and undertakings they wish to support without the supervisory authorities having the competence to verify that no other undertakings find themselves in a comparable situation. Moreover, for the purposes of a supervisory control under Article 59 (2) of the EEA Agreement, the Authority's role is limited to arresting manifest errors by the EFTA States.[62]

On that basis, the Authority infers from case law that there is no requirement of completely identical treatment of all aid beneficiaries to the extent that the difference in aid does not amount to an infringement of the provisions on free movement, which is not the case with regard to the contested aid measure. Only where the purpose and effect of the difference of treatment is to create a *manifest* discrimination between public and non-public undertakings, has the Authority competence to set aside an aid measure on the basis of considerations pertaining to equality.[63]

In the opinion of the Authority, the very purpose behind the contested Norwegian rules indicate that they clearly did not have as their purpose to systematically discriminate against non-municipal kindergartens with intention of placing municipal kindergartens in a favourable competitive position. On the contrary, the intention of the Norwegian legislator with the provision in Section 7b (now Section 14) of the Norwegian Kindergarten Act was to introduce a system whereby equality in substance was obtained.[64] Moreover, the law does not distinguish between public and private and there are publicly owned day-care institutions among the non-municipal centres.

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[61] Case 304/85 *Falck v Commission* [1987] ECR 871, paragraph 27. See similarly Case T-244/94 *Wirtschaftsvereinigung Stahl* [1997] ECR II-1963, and Case T-239/94 *EISA* [1997] ECR II-1839, paragraph 100.

[62] Case E-9/04 *The Bankers'and Securities Dealers Association of Iceland* [2006] EFTA Court Report, page 42, paragraph 65, and T-106/95 *FFSA* [1997] ECR II-229, paragraphs 108 and 192. See also "Community framework for State aid in for form of public service compensation" (2005/C 297/04), point 9.

[63]Case T-89/96 *British Steel* [1999] ECR II-2089, paragraph 129, and Case T-243/94 *British Steel plc* [1997] ECR II-1887, paragraph 145.

[64] In this context, it should be noted that the introduction of an obligation on municipalities to finance non-municipal kindergartens has *de facto* led to an increase in public financing of these institutions.

According to the complainant, the first allegedly discriminatory element of the Norwegian system is related to the cost coverage principle. In the opinion of the complainant, this system favours municipal kindergartens as these centres traditionally have had higher average costs and therefore will receive more than their private counterparts, thereby infringing the EEA rules. The Authority does not share this view. Regardless of whether or not the use of a cost coverage principle in practice will lead to a higher average payment to municipal kindergartens, such a result cannot be classified as manifest discrimination in the sense of the case law cited above.

The second element of alleged discrimination relates to the ceiling for cost coverage to non-municipal kindergartens contained in Section 3, paragraph 3, of the Regulation according to which a municipality has no obligation to extend grants so that the total public financing of a kindergarten exceeds what a corresponding kindergarten owned by the municipality on average receives in the form of public grants.

The Authority cannot see that this provision is liable to distort the conditions of competition to an extent contrary to the common interest thereby giving rise to manifest discrimination against, in particular, non-municipal kindergartens. The purpose of the rule seems to be to prevent a municipality having to pay for a service level higher than that the municipality in general has decided to have in its own kindergartens. This purpose cannot be seen as an element protecting municipal kindergartens from equal competition from non-municipal centres, nor can the Authority see that it has a manifestly discriminatory effect. This is so even if it might entail that a non-municipal kindergarten, having a higher actual cost level than the average of municipal centres, would not receive full compensation, while a similar municipal kindergarten centre would receive full compensation. In the review of the compatibility of aid as a compensation for the fulfilment of a public service obligation, it is not the task or competence of the Authority to examine whether the aid measure entails complete equality of treatment between all operators, but merely whether the measures, taking its purpose and overall effect into consideration, results in manifest discrimination.

The third element which, according to the complainant, results in discrimination, concerns paragraph 4 of the Section 3 of the Regulation, *i.e.* the rule according to which a municipality has no obligation to cover *increases* of costs which exceed the normal increase of prices and costs in the municipal sector. This rule will not affect new establishments of non-municipal kindergartens. It will, however, have the *de facto* effect of making it more difficult for an existing non-municipal kindergarten to *change* its service level by opting for a different and more expensive high quality concept than the one run hitherto.

Even so, in the opinion of the Authority, Articles 59 (2) and 61 of the EEA Agreement do not require an EEA State to design a system of compensation for public service obligations according to which an undertaking has a right to be able to change its business concept and still receive full compensation. With the provision in paragraph 4 of Section 3 of the Regulation, a municipality may decide to increase the support if it finds the rise justified, but is only obliged to compensate for the general rise in prices and costs in the municipal sector. While a municipality controls the expenditure level of its own kindergartens by way of its ownership, it has no similar control over the potential rise of costs connected to a non-municipal kindergarten.

A State has no obligation to offer the performance of public service tasks to all interested undertakings. It can no more have an obligation to ensure that the operators chosen for the

fulfilment of the public service task are put in a situation whereby they can thereupon compete between each other on having completely identical financial support with regard to the fulfilment of the public service task. Moreover, in combination with the so-called 85% rule a non-municipal kindergarten might actually end up being overcompensated compared to its actual costs.

Finally, the Authority cannot see that any other elements of the financing system as raised by the complainant, including the lack of compensation for the difference between the maximum parental payments and a lower fee set by non-municipal kindergartens, are of such a character that the support, to the extent that it should constitute aid under Article 61 (1) of the EEA Agreement, would be incompatible with Article 59 (2) of the EEA Agreement.

In conclusion, it is the opinion of the Authority that even if the contested Norwegian rules had constituted aid within the meaning of Article 61 (1) of the EEA Agreement, the measures would not fall foul of the EEA Agreement by virtue of the reasons advanced in the complaint.

HAS ADOPTED THIS DECISION:

1. The EFTA Surveillance Authority concludes that the system of financing municipal day-care institutions in Norway does not constitute State aid within the meaning of Article 61 (1) of the EEA Agreement.

2. This Decision is addressed to Norway.

Done at Brussels, 27 February 2007

For the EFTA Surveillance Authority

Bjørn T. Grydeland
President

Kurt Jaeger
College Member