



EUROPEAN COMMISSION

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<p>In the published version of this decision, some information has been omitted, pursuant to articles 24 and 25 of Council Regulation (EC) No 659/1999 of 22 March 1999 laying down detailed rules for the application of Article 93 of the EC Treaty, concerning non-disclosure of information covered by professional secrecy. The omissions are shown thus [...].</p>		<p style="text-align: center;">PUBLIC VERSION</p> <p style="text-align: center;">WORKING LANGUAGE</p> <p style="text-align: center;">This document is made available for information purposes only.</p>
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Sir,

Subject: State aid C8/08 – Spain
Ciudad de la Luz film studios

- (1) The Commission wishes to inform the Kingdom of Spain that, having examined the information supplied by your authorities concerning the Valencia Regional Government's financial support for the Ciudad de la Luz film studio complex in Alicante, it has decided to open a formal investigation into the support under Article 88(2) of the EC Treaty.

1. PROCEDURE

- (2) On 22 February 2007, the Commission received a State aid complaint from Complainant A¹ concerning support allegedly given by the Region of Valencia to the Ciudad de la Luz film studios. Complainant A confirmed on 15 March 2007 that its complaint could be forwarded to the Spanish authorities.
- (3) On 10 April 2007, the Commission forwarded the full complaint to the Spanish authorities, requesting information about the alleged aid. The Commission had not previously been notified by the Spanish authorities of any film support measures in Valencia for State aid approval.
- (4) After requesting an extension of deadline on 18 April 2007 (granted on 24 April), the Spanish authorities replied to the Commission's request for information on 15 June 2007.

¹ Complainant A is a major European film studio. It has asked that its identity is not made public.

- (5) On 30 April 2007, Complainant A provided links to articles published in *Variety* allegedly setting out the production subsidies offered for filming in Valencia and confirming that Ciudad de la Luz was attracting large budget film productions².
- (6) The Commission requested additional information from the Spanish authorities on 13 July 2007. After requesting an extension of deadline on 18 July 2007 (granted on 19 July), the Spanish authorities replied to the Commission's request for information on 8 October 2007.
- (7) On 15 July 2007, the Commission received a complaint from Complainant B³. After having obtained the agreement of the complainant, the Commission forwarded its complaint to the Spanish authorities on 2 August 2007.

2. DESCRIPTION OF THE MEASURE

2.1. Ciudad de la Luz

- (8) Ciudad de la Luz is a major film studio complex in Alicante. The Valencia Regional Government took its initial decision to invest in the Ciudad de la Luz project on 24 October 2000. Ciudad de la Luz SA was incorporated on 2 November 2000. Its objective is to carry out the necessary activities for the promotion, organisation, management of the "Ciudad de la Luz" site, including the construction, management and operation of audiovisual and cinematographic facilities, as well as other related leisure and accommodation activities.
- (9) 75% of the original EUR 600,000 share capital of Ciudad de la Luz SA was owned by Sociedad Proyectos Temático de la Comunidad Valenciana (SPTCV), a public entity which carries out investment activities on behalf of the Valencia Regional Government. The remaining 25% belonged to Aguamarga Producciones, a private company.
- (10) In November 2001, the share capital was increased to EUR 9 million, with SPTCV purchasing all the additional shares and taking its holding to 98.4%. SPTCV increased its holding further in February 2003 and May 2004 through similar purchases of new share capital. Aguamarga Producciones sold its share of the Ciudad de la Luz SA⁴ to SPTCV in July 2004 (for EUR 139,059). Since then, the Region of Valencia has held 100% of the share capital of Ciudad de la Luz SAU via SPTCV. However, Aguamarga Producciones continues to be responsible for the remaining construction work, for promoting Ciudad de la Luz and for managing the studios.

² "New Valencia studio offers film rebates"

<http://www.variety.com/article/VR1117958591.html?categoryid=19&cs=1>; "Polanski's Pompeii takes shape" <http://mobile.variety.com/article/VR1117963040.html?categoryid=13&cs=1>

³ Complainant B is a major player in the European film sector. It too has asked that its identity is not made public.

⁴ With the related capital transfer of 7 October 2004, Ciudad de la Luz SA became Ciudad de la Luz SAU, a company with a single shareholder (sociedad anónima unipersonal) with all of its share capital owned by SPTCV.

- (11) The film studio complex opened for filming in late 2005. Construction began in 2002 and has been divided into three phases:
- Phase 1 (completed): 6 air-conditioned soundstages with a combined area of 11,000m², production support buildings, 15,050m² of workshops/storage, and 2 external filming areas (back lots) of a total of 14 hectares.
 - Phase 2 (due to have been completed by the end of 2007) includes a third external filming area (back lot) of 5 hectares, catering facilities, an aquatic filming tank and a large, deep natural-horizon water tank;
 - Phase 3 (to be completed in 2009/10) includes a 5,000 m² sound stage.
- (12) Certain aspects of the "state-of-the-art" facilities at Ciudad de la Luz put it well ahead of the limited number of competing major film studios in Europe in terms of capacity for large budget films. For instance, the 5,000m² sound stage currently under construction at Ciudad de la Luz will apparently be the largest in the world⁵. The Commission notes that large sound stages are only of interest to major film productions.

2.2. 2002 business plan of Ciudad de la Luz: 2002-2014

- (13) In their submission of 13 June 2007, the Spanish authorities provided the profit and loss forecast of Ciudad de la Luz SA prepared in 2002 for the period 2002-2014 - see below.

⁵ Source: *Hollywood Reporter* article "Let there be light" – October 31, 2006:
http://www.hollywoodreporter.com/hr/content_display/international/features/e3i45879d0f686a3095f5df04bc254cf9f3

2002 Profit and loss forecast for Ciudad de la Luz: 2002-2014

	Preparation	Testing	Experimental operation					Consolidation					
	Figures in thousands of euros												
	Years												
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
	A0	A1	A2	A3	A4	A5	A6	A7	A8	A9	A10	A11	A12
DIRECT INCOME FROM PRODUCTIONS													
Total direct income from productions	[...]*	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
INDIRECT INCOME FROM PRODUCTIONS													
Total indirect income from productions	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
OTHER INCOME													
Total other income	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
DIRECT EXPENSES													
Total direct expenses of productions	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
INDIRECT EXPENSES													
Total indirect expenses	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Earnings before interest, tax and depreciation (EBITDA)	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
DEPRECIATION													
Total depreciation	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Earnings before interest and tax (EBIT)	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
FINANCING EXPENSES													
Financing expenses	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Earnings before tax (EBT)	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
TAXES													
Corporation tax 0,35	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Net profit	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]

(14) As shown by the headings in the above forecast, the 13-year period was divided into four phases: preparation (2002-2003), testing (2004-2005), experimental operation (2006-2010) and consolidation (2011-2014). According to the Spanish authorities, this forecast reflects the objective of tendering out the management of the Ciudad de la Luz complex in 2014.

* Throughout this public version of this decision, data covered by the obligation of professional secrecy has been replaced by [...].

- (15) The Spanish authorities point out in their submission that the operation of Ciudad de la Luz is (was) expected to generate positive Earnings Before Interest, Tax, Depreciation and Amortisation (EBITDA) by [...], growing to EUR [...] million by [...]. However, after taking into account the depreciation of buildings and technical equipment, Ciudad de la Luz was only expected to generate positive net earnings by [...] (EUR [...]million), growing to EUR [...] million by [...].
- (16) The Spanish authorities have also provided the corresponding projections made in 2002 of the planned investment and cash flows of Ciudad de la Luz SA between 2002 and 2014:

2002 Cash flow forecast for Ciudad de la Luz: 2002-2014

Cash flow – Investment necessary	Preparation		Testing		Experimental operation					Consolidation			
	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
	A0	A1	A2	A3	A4	A5	A6	A7	A8	A9	A10	A11	A12
Opening cash balance	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
+ EBITDA	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
- Investments	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
- Tax	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
+ Capital contribution required	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Closing cash balance	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Accumulated contribution necessary	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Cash flows	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
IRR	[...]												
NPV	[...]												
% debt/capital	[...]												
Accumulated investment	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Accumulated depreciation	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]
Book value of assets	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]	[...]

- (17) According to the Spanish authorities, the above projections were made using the weighted average cost of capital (WACC) of [...] % as discount factor. The WACC was estimated following the common formula which weights the costs and percentage of financial resources used or expected to be used to fund the operation of Ciudad de la Luz from, respectively, debt and equity. The WACC calculations provided by the Spanish authorities show the following:

- The costs of debt were estimated at [...] % but, since no debt funding was envisaged, its contribution to the WACC was 0%.

- The costs of equity, which was expected in 2002 to cover 100% of the funding needs, were estimated at [...]%. This latter rate resulted solely from an estimation of a risk-free rate of [...]% to which no investment-specific risk premium or liquidity premium were added.
- (18) On the basis of the cashflow forecast, the investment was expected to generate an internal rate of return of [...]% and a positive net present value of EUR [...] million. The expected return of [...]% exceeds the cost of capital of [...]% estimated by the Spanish authorities.
- (19) These overall positive results depend chiefly on the cumulative net cash inflow of EUR [...] million which the cashflow forecast shows for 2014. The net cash inflow from the operation of Ciudad de la Luz in 2014 according to the forecast is EUR [...] million⁶. Neither the source of the additional cash inflow of EUR [...] million⁷ in 2014 nor the way in which this figure was estimated have been clearly stated by the Spanish authorities. In this respect, the Commission notes that the Spanish authorities have stated that their 2002 forecasts reflected their objective of tendering out the management of the Ciudad de la Luz complex in 2014.
- (20) The Commission understands that the cash flow and profit and loss forecasts of 2002 submitted by the Spanish authorities and portrayed above constitutes the business plan which was the basis for the decision by the Valencia Regional Government to invest in the construction and operation of the Ciudad de la Luz complex.

2.3. Public support for Ciudad de la Luz

2.3.1. Equity and loan finance

- (21) The forecast made in the initial 2002 cashflow forecast shows that the total investment required was EUR 204 million⁸ at 2002 prices. The bulk of this investment was expected to be in construction and public works in the years 2005-2007. To date, the investment has been financed in two main ways:
- i) equity investments which have now reached EUR 104 million, including land worth EUR 9.8 million contributed in kind to the social capital by the SPTCV;
 - ii) in April 2005, SPTCV granted Ciudad de la Luz SAU a loan of EUR 95 million. The loan was consented for a 10 year period with fixed interest rate set to the 1 year Euribor rate plus 1% and variable interest rate of 1.25% of benefits after tax.

⁶ The net cashflow from operations is calculated as the movement between the opening and closing cash balances expected in 2014: €[...]m - €[...]m = €[...]m.

⁷ This is the difference between the cumulative net cash inflow in 2014 and the net cashflow from operations: €[...]m - €[...]m = €[...]m.

⁸ This figure is the maximum cumulative contribution required (aportación necesaria acumulada) for the project according to the 2002 cashflow forecast.. It occurs at the end of 2007, after which the cumulative contribution required decreases, according to the forecast.

- (22) The 2004 and 2005 reports on SPTCV and Ciudad de la Luz SAU made by the *Sindicatura de Cuentas* refer to a participative loan agreement granted by SPTCV in April 2005. According to the understanding of the Commission, a participative loan is a hybrid of equity and debt that ranks below all other debtors if the company is wound up, though it ranks above shareholders. Participative loans may not be redeemed early unless the equity of the company is increased by an equal amount.
- (23) No interest amounts were included in the 2002 profit and loss forecast. It is therefore possible that the loan had not been envisaged at the time of the original investment decision.
- (24) The Spanish authorities have provided the Commission with a revised forecast, apparently from 2006, showing that the public contributions for the construction costs up to the end of 2007 were expected to be EUR273.5 million. As the third phase of construction is not due to be completed until late 2009, the final public contribution to the construction of the complex alone may be higher than this figure.
- (25) On the basis of the data provided so far by the Spanish authorities, the Commission has not been able to reconcile the figures in the 2002 forecasts with those in the 2006 forecasts.

2.3.2. *Discounts offered by Ciudad de la Luz SAU*

- (26) In practice, SPTCV has been the sole financier of Ciudad de la Luz SAU to date. Most of the operating losses incurred during this period arise from the construction of the Ciudad de la Luz complex and were included in the 2002 forecast. However, according to the Spanish authorities, the discounts which were found to be necessary to attract film productions in the course of the operations of the Ciudad de la Luz complex by 2005/6 were not included in the 2002 forecast.
- (27) In its request for information of 13 July 2007, the Commission had reminded the Spanish authorities that measures which use State resources to support the production of cinematographic or audiovisual works are considered to be State aid and must be notified to the European Commission. All incentives awarded (also by regional and local authorities) need to be notified to the European Commission. However, the Commission had not received any notification of a Valencian film support scheme.
- (28) The Commission had cited a *Screen Finance* article⁹ of February 2007 which appeared to indicate that the Valencia Regional Government had established such a scheme without having notified it to the Commission. In its response, the Spanish authorities explained that the film support in question was not notified

⁹ "Valencia in Spain is offering producers up to €5.4 million (£3.7 million) per film as a grant. Qualifying projects must film for three weeks in Valencia, including two at Alicante's new Ciudad de la Luz studios, spending between 30%-50% of their total shooting time there. In exchange, producers can claim a grant of up to 18% of local spend, with 90% of the grant paid during filming." - *Screen Finance*, February 21, 2007

as they believed that the State resources were provided under the market economy investor principle and therefore did not constitute State aid.

- (29) However, the Spanish authorities provided the Commission with confidential details of the discounts offered to various film productions which have filmed at Ciudad de la Luz. By October 2007, 19 films and 3 commercials had been filmed at Ciudad de la Luz. Almost all of the films (but none of the commercials) received discounts totalling EUR 12 million, excluding VAT. According to the Spanish authorities, the initial plans of Ciudad de la Luz had not contemplated that such incentives would be necessary to attract productions. They note that, for 2006, the difference between of actual operating losses (EUR [...] million) and the initial forecast loss (EUR [...] million forecast in the 2002 projections) results from the fact that the costs of such incentives were not factored in at the time. In their view, the fact that the forecasts would have been equivalent to the actual results but for the incentives shows the accuracy and reliability of the initial business plan.
- (30) In this respect, the Spanish authorities also consider that the objective of Ciudad de la Luz at the outset was to offer competitive studio prices and that, although lower than those of the market leaders, the prices of Ciudad de la Luz are still above those of comparable studios.
- (31) As pointed out by Complainant A, on 16 November 2005, Ciudad de la Luz SAU published an announcement in the Official Gazette of the Valencia Region offering production subsidies (allegedly via sponsorship agreements) to any party interested in using Ciudad de la Luz for filming motion pictures, serials, advertisements, etc.
- (32) The specialist trade paper Screen International published an article entitled "The charge of the Light brigade" in February 2006 about the Ciudad de la Luz complex. It began by noting that the "opening of the City of Light studios gives Spain a facility to compete with the biggest in Europe." It then looked at the package on offer to international film producers.
- (33) According to the article, in order to compete with the "well-established super-studios" Germany's Babelsberg Studios, the UK's Pinewood/Shepperton and Italy's Cinecittà, the region of Valencia has created a temporary system of financial aides to jump start production at the facility¹¹.

¹⁰ €19 million according to the 2006 report of the Valencian Audit Office ([http://www.sindicom.gva.es/web/informes.nsf/0/DDED7B9A9251B641C12573B10045371E/\\$file/06CVIII.pdf](http://www.sindicom.gva.es/web/informes.nsf/0/DDED7B9A9251B641C12573B10045371E/$file/06CVIII.pdf))

¹¹ "To access these funds, a producer needs to team up with a Valencia co-producer. Funds are awarded on a points system, rating everything from the number of weeks the film will shoot in the studio to the number of foreign co-producers and the estimated media impact of the film and talents involved. Productions budgeted at less than \$4.8m (€4m) can obtain up to 10% of the total budget; those costing between \$4.8m-\$48m (€4m - €40m) can receive up to 7.5%; and productions budgeted above \$48m (€40m) up to 5% of the budget. Producers are expected to spend double the funds received in the Valencia region and also to pay back a percentage of the funding from the profits."

- (34) According to Complainant A, the only significant eligibility requirement for the incentive is for the producer / co-producer to be registered in the Valencia Audiovisual Companies Register. Complainant A also alleged that the two main criteria to receive the subsidies were:
- The longer the Ciudad de la Luz complex facilities are used, the higher the possibility to obtain the subsidy (eg, every week the facilities are used shall be accounted in favour of the subsidy applicant); and
 - The higher the budget of the production, the higher the possibility to obtain the subsidy (eg, those productions with budgets lower than €4m shall obtain 10 points, while productions with budgets higher than €40m shall obtain 40 points).
- (35) The Commission notes that the *Sindicatura's* 2005 report censures Ciudad de la Luz SAU for not having awarded its first five sponsorship agreements under the principles of publicity, competition and objectivity which govern both the granting of subsidies and the award of public contracts.
- (36) In view of the above, the Commission cannot be sure that it is fully aware of all the incentives which may be made available to a production filming at Ciudad de la Luz, either by the Valencia Regional Government or by Ciudad de la Luz SAU or by any other Valencian entity. The Commission has also not been informed by the Spanish authorities of how the amounts granted to films were calculated or the conditions attached to the incentives.

2.3.3. *Other incentives for filming at Ciudad de la Luz*

- (37) The Commission also notes that the film productions which were awarded sponsorship agreements by Ciudad de la Luz SA may also have taken advantage of other incentives which are being assessed separately by the Commission.
- (38) For example, in July 2007, the Valencia Regional Government notified a film support scheme to reward films which are commercially successful in Valencian cinemas. It appears to the Commission that the major film productions which are likely to film in Ciudad de la Luz would probably also arrange to meet the criteria for this scheme.
- (39) Similarly, such films may also benefit from the national Spanish film support schemes.

3. COMMENTS FROM THE PARTIES INVOLVED

3.1. Allegations made by the complainants

3.1.1. Different forms of public support

- (40) Both complainants allege that various forms of support provided by the Valencia Regional Government to facilitate the construction and operation of Ciudad de la Luz could significantly distort the European market for large film productions. The forms of alleged support identified by the complainants are:

- Capital injections totalling at least EUR104m¹²;
- Cost-free use of state-owned land valued at EUR9m¹³; and
- Production subsidies which effectively allow Ciudad de la Luz to be used at prices below market rates.

(41) Complainant A notes that large film studios compete on an international scale and that there is intense competition between them to attract and retain large film productions. While welcoming competition on the merits, Complainant A is concerned that it may lose business to Ciudad de la Luz as a result of the advantages conferred on Ciudad de la Luz by allegedly illegal State aid, not as a result of competition on the merits.

(42) Complainant B alleges that the Valencia Regional Government has contributed very substantially to the financing of the project through these three forms of support. It also notes that the initial budget of the project of €100m had already reached €340m, citing an *El Pais* article of 21 May 2006.

3.1.2. *Alleged market distortion*

(43) According to Complainant A, most of the existing providers of studio facilities are private sector firms and that the vast majority operate without the level of State support allegedly provided to Ciudad de la Luz. It also alleges that setting up a new film studio complex such as Ciudad de la Luz is a high risk venture against the background of intense competition in the market. In the view of Complainant A, the risks were higher in Valencia as it did not have an established pool of individuals and firms with the necessary expertise to support large film production.

(44) As a result, Complainant A considers that it is highly unlikely that a private investor would support a project such as Ciudad de la Luz, particularly not on the terms allegedly offered by the Valencia Regional Government.

(45) Complainant A has also suggested that the appropriate return on equity figure for investment in an existing film studio would be 15%. In its view, the return which a private investor would seek from a new film studio would be higher, in view of the additional risks and uncertainty of providing venture capital.

(46) Complainant A concludes that the very existence of the Ciudad de la Luz complex distorts competition in the market for film studio facilities, particularly larger film studios. Moreover, Complainant A considers that the alleged State aid effectively allows Ciudad de la Luz to undercut efficient private sector competitors on price.

¹² As noted in paragraph (21), this figure refers only to the capital increases of Ciudad de la Luz SA.

¹³ As noted in paragraph (21), this amount is treated as part of the capital increases of Ciudad de la Luz SA and should therefore be included in the above figure of EUR104m

- (47) In view of this, Complainant A considers that there is a serious risk that the alleged State aid will undermine both its own commercial viability and that of other providers, particularly in the long term.
- (48) In the short term, according to Complainant A, the loss of even a small number of major film productions to Ciudad de la Luz could have a significant impact on its existing competitors, including Complainant A. Complainant A further suggests that the alleged State aid could contribute to some private sector operators leaving the market altogether.
- (49) To support this, Complainant A has provided examples of European studios which have been forced to close in recent years, as well as studios whose planned construction or whose refurbishment has been abandoned.
- (50) The submission from Complainant B, which has been considering entering the market for film studios itself, echoes this view. It refers to the very competitive environment and underlines that the construction and launch of a studio complex is a risky enterprise. In its view, the chance that a private investor would engage in such a project, particularly in proportions similar to those of the Valencian Regional Government, is extremely low, if not non-existent.
- (51) Complainant B alleges that this is confirmed by the refusal of the original minority private investor in the project to take part in the capital increase in 2003. This reduced its share in the project to less than 1%. Complainant B also cites several *El País* articles between May 2003 and December 2006 which it claims repeatedly called into question the viability and profitability of the project.
- (52) Complainant B further alleges that the State aid from which Ciudad de la Luz has benefitted, and from which it continues to benefit, allows the complex to set itself apart from the competitive market, particularly by offering tariffs approximately 25% below those of its competitors, which do not benefit from such State aid. To illustrate this, Complainant B cites an interview with the producer of the €78m film production *Asterix et Obélix aux jeux Olympiques*, the most expensive European film production to date. This production allegedly received a contribution of €4m from Ciudad de la Luz. The producer was quoted as saying that they chose to film at Ciudad de la Luz rather than studios in North Africa because the aid of the Valencia Region brought the Spanish price down to the level of the price of Morocco.¹⁴
- (53) Finally, Complainant B considers that its own plans to launch a film studio complex are directly affected by the alleged distortion of competition created by the alleged State aid to Ciudad de la Luz. As a result, it believes that the conditions under which the Ciudad de la Luz complex has been developed should be closely examined as they appear to suggest that the alleged State aid granted to Ciudad de la Luz (but not notified to the Commission) could distort competition and should be considered as a violation of Article 87 of the EC Treaty.

¹⁴ "L'aide de la région de Valencia a mis le prix espagnol au niveau du prix Maroc." – Jérôme Seydoux, *La Tribune*, 21 May 2007.

3.2. Position of the Spanish authorities as to whether State aid is present

3.2.1. Application of the market economy investor principle

- (54) The Spanish authorities claim that, given the underlying strategy and projections, the expected profitability for SPTCV was comparable to that of a private investor at the time of bringing forward the Ciudad de la Luz project. In their view, the intervention of the SPTCV was guided by economic criteria with a view to obtaining profits which would procure a return on the investment made in the medium term. This assertion is presumably sustained on the calculation of a positive net present value of the cash flow of the project of EUR [...] million and an internal rate of return (IRR) of [...] % between 2002 and 2014, in excess of the alleged cost of capital of [...] %.
- (55) The Spanish authorities stress that, although the projections may show a very long pay-back period, the magnitude of the investment does not lead to considering that duration to be excessive. The alleged reason is that the behaviour which should guide the application of the market economy investor principle under case-law is that of a private holding or group of companies which pursues a structural, global or sectoral policy and is guided by profit-seeking perspectives in the longer term¹⁵. Moreover, the Spanish authorities claim that by October 2007, the initial projections were outnumbered with more profits than initially forecasted, so that the pay-back period envisaged initially should be reduced accordingly.

3.2.2. General infrastructure project

- (56) The Spanish Authorities also claim that the studio complex in Ciudad de la Luz is public infrastructure of general interest. The studios are allegedly available to all audiovisual or cinema production companies at non-discriminatory market conditions independent of nationality. In their submission, this view is sustained by the qualification as public infrastructure contained in the town planning regulations applicable to its establishment, which have been ratified by the competent court of the Tribunal Superior de Justicia de la Comunidad Valenciana in various rulings. The Spanish authorities affirm that no preferential treatment was granted to the enterprise in charge with the building and managing of the complex, Aguamarga Producciones, or to the enterprises producing audiovisual or film works at Ciudad de la Luz.

3.3. Position of the Spanish authorities as to compatibility of State aid

- (57) The Spanish Authorities claim, as a subsidiary argument if the Commission considered that the measures at hand constitute State aid, that such measures would be compatible with Article 87 (3) as regional aid and as aid aimed at promoting culture.

¹⁵ Judgment of the Court of 21 March 1991 in case C-305/89, Italy vs. Commission (Alfa Romeo), ECR p.1603, paragraph 20.

3.3.1. Regional aid

- (58) The Spanish Authorities claim that at least 40% of the public funds injected by the SPTCV into Ciudad de la Luz would be compatible with the Treaty rules, in application of the Guidelines on regional aid applicable between 2000 and 2006, at the time when Ciudad de la Luz was established and started its activities¹⁶. At the time, the province of Alicante was a region to which the benefit of Article 87 (3) a) was applicable. The Spanish authorities claim that, in terms of regional development and cohesion, the contribution to the revenues and employment of the province were sizeable and documented by an economic impact assessment.

3.3.2. Aid to promote culture

- (59) The Spanish authorities consider that an analysis of the compatibility of the measures under scrutiny must include the application of the cultural exception provided for in Article 87 (3) d). The support contained in the measures under scrutiny to audiovisual production in general and to the film industry in particular justifies, in their view, that such measures meet the conditions of that exception.
- (60) More specifically, the Spanish Authorities stress that the cultural exception laid down in the Treaty does not distinguish between State measures that support cultural production and State measures that support cultural infrastructure. In the case at hand, measures concerning both film production and audiovisual infrastructure are present. Allegedly, the incentives to film in Ciudad de la Luz meet all the compatibility criteria laid down in the Commission's Cinema Communication, though they have not been notified by the Spanish authorities to the Commission. However, in the view of the Spanish Authorities, the fact that the compatibility criteria laid down in the Commission's Cinema Communication are confined to the support of audiovisual production does not imply that the above exception does not apply also to investment in cultural infrastructure.

4. ASSESSMENT OF THE MEASURE

- (61) Article 87(1) of the EC Treaty declares:

Save as otherwise provided in this Treaty, any aid granted by a Member State 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 Member States, be incompatible with the common market.

- (62) In order for Article 87(1) to be applicable, there needs to be i) an aid measure imputable to the State which ii) is granted by State resources, iii) affects trade between Member States, iv) distorts or threatens to competition in the common market and v) confers a selective advantage to undertakings.

¹⁶ OJ N°C 74 of 10.3.1998, p.9.

4.1. Existence of aid

- (63) The resources indicated in the description of the measure, consisting of equity investment, a loan and incentives for filming contributed by the Regional Government of Valencia via the SPTCV to Ciudad de la Luz SAU are State resources.
- (64) It is however necessary in the case at hand to ascertain whether these State resources have been contributed at the conditions to which a market economy investor would have consented. In that respect, the figures of forecasts of profit and loss and cash flow accounts submitted by the Spanish authorities can be deemed to portray the projections made at the time when the most significant investment decision in the construction of the Ciudad de la Luz complex was taken. They allow, therefore, for the assessment of the application of the market economy investor principle to the investment of State resources into Ciudad de la Luz.
- (65) Subsequent deviations from those projections, whether positive or negative, should only be taken into account insofar as they were a possible risk that could be factored in at that time. Since the Spanish authorities do not claim that the prospects of further revenues than initially expected were factored in when deciding on the investment, the contention that higher actual profits than expected from the operation of Ciudad de la Luz by October 2007 comes to reduce the real pay-back period of the investment must be dismissed for the purposes of the application of the market economy investor principle. In any event, it has to be borne in mind that any higher actual profits than initially forecast may be at least in part dependent on the financial incentives, not foreseen in the initial plan, provided to customers of Ciudad de la Luz. Furthermore, the Spanish authorities omit to consider that the pay-back period envisaged in 2002 should be increased to take into account the higher than expected losses incurred by Ciudad de la Luz in 2006 (see paragraph (29)).

4.1.1. Market economy investor principle

- (66) As further indicated below, there are serious doubts that the basis for calculation of the expected profitability of the project are appropriate, independent from whether the expected revenues and costs of operation forecasted up to 2014 were plausible in 2002. The questions to be assessed are whether the basis for calculation are those which would govern the involvement of a private investor into the Ciudad de la Luz project and, if not, based on figures corrected if appropriate, whether a private investor would have invested nearly EUR 200 million in the project by 2002-2007 as the SPTCV did.

Profitability of the project

- (67) The figures submitted by the Spanish authorities indicate that, by 2002, the operation of the Ciudad de la Luz project was expected to be loss-making until 2009 inclusive. There are few indications, if at all, of market investors knowingly accepting to pour funds into a loss-making venture for eight years, that is, until 2010 *in casu*. For the subsequent period 2010-2014, the indicators of profitability of the operation portrayed below show also very poor results

both in absolute terms and compared with those of competing studios in the recent period.

Profitability indicators of the operation of Ciudad de la Luz 2010-2014¹⁷

	2010	2011	2012	2013	2014	Full period
Return on sales (ROS)	[...]%	[...]%	[...]%	[...]%	[...]%	[...]%
Return on capital (ROCE)	[...]%	[...]%	[...]%	[...]%	[...]%	[...]%
Return on equity (ROE)	[...]%	[...]%	[...]%	[...]%	[...]%	[...]%

Source: Submission of information of 13 June and 10 October 2007, Commission calculations

- (68) In absolute terms, the operation of Ciudad de la Luz shows a low return on sales of 5% even for the period 2010-2014, when the first accounting profits of operation were expected after an initial unusually long take-up phase of eight years during which the return on sales is negative.
- (69) Insofar as the profitability of the operation of competing studios may provide an adequate benchmark for assessing the expected operation of the Ciudad de la Luz project, the information available indicates that the latter was not expected to outperform their competitors even in the long term. On virtually all indicators, the projections for Ciudad de la Luz are appreciably below those of other competing studios in place.

Profitability indicators of the operation of competing studios

	2006	2005	2004	2003	Full period
Pinewood Shepperton plc					
ROS	15,0%	1,2%	11,8%	4,9%	8,6%
ROCE	6,2%	0,3%	4,6%	1,9%	3,2%
ROE	10,5%	0,8%	8,8%	68,6%	7,8%
Studio Babelsberg AG					
ROS	21,7%	27,8%	-21,0%	n.a.	16,4%
ROCE	6,7%	10,0%	-3,9%	n.a.	4,8%
ROE	4,3%	6,5%	-2,5%	n.a.	3,1%

Source : Annual Company Reports, Commission calculations

- (70) In particular, as concerns the indicator on which a possible private investor would place more emphasis, the projections of a 1.0% return on equity for Ciudad de la Luz for the period of full commercial exploitation 2010-2014 are respectively three-fold and nearly eight-fold lower than the return offered by competing studios, namely Studio Babelsberg AG (3.1%) and Pinewood Shepperton plc (7.8%). It could therefore appear doubtful that a private investor wishing to enter or to expand into the film studio business would have supported the operation of the project even by 2010, when the first net income were expected to be generated.
- (71) It could nonetheless be claimed that, even with a lower profitability than competing operations, a private investor would have supported Ciudad de la

¹⁷ The indicators are defined as follows:

Return on sales = net income / direct and indirect revenues

Return on capital = net income / book value of assets

Return on equity = net income / equity (aportación de capital 2002-2007)

Luz with a sufficient prospect of return for its investment. In that respect, the figures submitted by the Spanish authorities indicate that the project was expected to be profitable overall. The IRR of [...] % up to 2014 is in excess of the [...] % WACC by [...] %. This implies that an investor whose funding cost would be equal to the [...] % WACC would have obtained a remuneration of [...] % for the funds invested.

- (72) Furthermore, the discounts which have been given by Ciudad de la Luz SAU were not foreseen in these figures according to the Spanish authorities. At this stage, the Commission is not in a position to ascertain whether further resources were granted to SPTCV in addition to those committed on the basis of the 2002 forecast. If this is the case, the Commission would request that the Spanish authorities to provide all the information necessary, including the related business plan, to allow the Commission to assess the additional resources, for instance the funds needed to finance the unforeseen discounts.
- (73) However, the Commission has serious doubts about whether these figures are realistic. In particular, the Commission doubts that the WACC and the terminal value of the project have been calculated correctly.

The cost of financing for the project (WACC)

- (74) In their calculation, the Spanish authorities assume that the WACC is determined solely by the cost of equity, which is fixed a [...] %. The justification of this value is however lacking.
- (75) Firstly, looking at the cost of equity in isolation, the Commission considers that the [...] % WACC used for the financial forecast of Ciudad de la Luz is extremely low and well below the costs of funding, not only of a private investor, but also a public investor and, most likely, the SPTCV itself.
- (76) The Commission considers that the cost of equity should be equal to the sum of the risk-free rate (e.g. that of 10-year public bonds) and a risk premium which depends on the market situation, on sector specific factors and on the company specific factors.
- (77) The cost of equity submitted by the Spanish authorities is lower even than the risk-free rate. For instance, by 2002, the average yields of Spanish 10-year bonds were 4.96%. This implies that if the SPTCV had had the same credit rating as the Kingdom of Spain and would have funded its investment in Ciudad de la Luz through bond issuances, its funding costs would have been [...] % higher than the WACC used in the business plan. In other words, the lower WACC accepted by the SPTCV implies that the investment in Ciudad de la Luz was deemed to be safer than investment in bonds of the Kingdom of Spain. However, that 10-year public bond benchmark is considered as a nearly risk-free investment, unlike investment in the construction and operation of film studios.
- (78) The cost of funding would be significantly higher than 4.96% for any market economy investor, and therefore the funding costs significantly higher than the alleged WACC.

- (79) Furthermore it is apparent from the information they have submitted that the Spanish authorities have not requested any risk, liquidity and volatility premium over the risk free investment benchmark for their equity investment, as any sensible market economy investor would have requested. The Spanish authorities have not provided any elements in support of this choice. Additionally, the Spanish authorities did not provide any element which would enable the Commission to ascertain how sector (e.g., the dynamics in the film studio business) and company specific factors (e.g., the fact that Ciudad de la Luz was a start up company) would influence the risk premium and therefore the cost of equity of the project.
- (80) In conclusion, the Commission doubts at this stage that the [...] % WACC calculated by the Spanish authorities reflects the fair cost of capital of the project. Consequently, the business plan established on the basis of this WACC value may not have reflected the realistic prospects of profitability offered by Ciudad de la Luz.
- (81) Secondly, the Commission does not understand why the WACC is based on the cost of equity only, while cost of debt is not accounted for in the calculation. In this respect, the Commission notes that Ciudad de la Luz has to repay the interest on the EUR 95 million loan obtained from SPTCV¹⁸.

Loan repayment terms

- (82) Additionally, the conditions applied to that loan appear questionable. The interest on the loan is calculated in a fixed and a variable part. The fixed part is, set at the one-year EURIBOR reference rate plus 1%, which appears a very low spread for an unsecured 10-year loan¹⁹.
- (83) The unusually low fixed part of the loan could be in principle compensated by the prospect of an adequate remuneration of the participative loan thanks to the variable part linked to the profitability of the project. However, this could not be the case for the project under scrutiny, because the project is not likely to produce significant profits over the lifetime of the loan. Indeed, the variable part set at [...] % of profits before tax, which, according to the figures in the business plan, would amount to less than EUR [...] for the whole 2005-2014 period.
- (84) Finally, the Commission considers that it is unusual that the loan was foreseen to be paid back in April 2015, that is after the date of the termination of the project (and possibly its disposal), planned for 2014.

¹⁸ By the same token, the Commission does not understand why no financial costs were included in the forecast profit and loss statement for the period 2002-2014.

¹⁹ Regarding the fixed part, the Commission has not been able to understand from the information provided by the Spanish authorities exactly which interest rate will be used. Indeed, the Spanish authorities mention 'a fixed interest rate of one-year EURIBOR plus a 1% spread' ("*un tipo de interés fijo EURIBOR a un año más un diferencial de un punto porcentual*"), without specifying if the one-year EURIBOR rate is updated yearly or simply kept fixed at its April 2005 level. In the latter case, the relevant rate would be 3.3%. If such a rate were to be fixed for 10 years, in addition to presenting a very low spread, would also benefits the borrower at the expense of the lender, because normally long term maturities (and exposure for the lender) are normally remunerated with a higher interest rate than short term maturities. Indeed, any lender accepting a fixed interest rate based on one-year EURIBOR in April 2005 (a time of historically low interest rates) would have foregone revenue from subsequent increases in the EURIBOR reference.

- (85) On the basis of these elements, the Commission doubts that the conditions applied to EUR 95 million loan by the SPTCV are those which a market investor would have asked.

Final disposal value in 2014

- (86) As mentioned in paragraph (14), the cash flow forecast shows a net cash inflow of EUR [...] million in 2014, EUR [...] million of which derives from the operation of the complex. The basis for the cash inflow of the remaining EUR [...] million in 2014 has not been clearly explained by the Spanish authorities. As the Spanish authorities have stated the objective of tendering out the management of the Ciudad de la Luz complex in 2014, the Commission can only infer that the figure of EUR [...] million may represent the expected disposal value of the business in 2014 (at 2002 prices) or the price expected to be paid by the successful tenderer for the management of Ciudad de la Luz.
- (87) In financial terms, that distinction does not change the estimation of possible returns. However, the Commission notes that in 2002, the assets value forecast for 2014 was estimated by the Spanish authorities to be EUR [...]million. Consequently, the cash inflow of almost double this amount forecast for 2014 appears to imply to the Commission that the prospective new manager of the Ciudad de la Luz complex will also own it.
- (88) In other words, the positive IRR of [...] % which underpins the assertion that the SPTCV operated in accordance with the market economy investor principle is premised on the assumption that the Ciudad de la Luz business would be worth EUR [...] million in 2014. In the Commission's understanding, the Spanish authorities consider that they should be able to sell the business in an open tender by 2014 to a buyer offering that amount.
- (89) The Commission finds this claim questionable. The Spanish authorities have not provided any information on the methodology and on the specific assumptions they have employed to calculate the final disposal value of the project. It is therefore impossible for the Commission to assess the specific elements that have contributed to obtaining such a value. This notwithstanding, the Commission considers that the EUR [...] million figure is likely to be an overestimate, on the basis of the financial prospects of the project contained in the 2002 forecasts and communicated to the Commission.
- (90) Indeed, looking at the profitability forecasts, the EUR [...] million disposal value implies an unusually high price/earnings ratio (or pay-back period) of 117 (years) and represents nearly twice the book value of the assets of Ciudad de la Luz by 2014 as estimated by the Spanish authorities (EUR [...] million). Although the projection of the future value of a business to be sold twelve years later is admittedly fraught with uncertainties, the Spanish authorities have provided no elements to justify these figures. Indeed, they have provided neither plausible reasons why a prospective buyer in 2014 could have been expected to offer 117 times the amount of the annual net income generated by Ciudad de la Luz that very year (its best in terms of profitability), nor any explanation for the

huge gap between the book value of the assets and the estimated cash inflow in 2014.²⁰

- (91) In support of these doubts, the Commission notes that, according to press reports, in July 2004, the sale by Vivendi Universal Group of the Babelsberg Studios GmbH, a business comparable in many respects to and competing with Ciudad de la Luz, was effected for a symbolic amount of one euro. The basis on which two years earlier, in 2002, the Spanish authorities planned a disposal value of EUR [...] million in 2014 for Ciudad de la Luz business is, therefore, unclear. Indeed, it was common knowledge within the industry that the Babelsberg Studios had been loss-making for Vivendi Universal Group since they acquired them in 1992.
- (92) In conclusion, the Commission doubts that a market economy investor acting in lieu of the SPTCV in 2002 and thereafter would have accepted the final disposal value of the project in the business plan and injected the funds necessary to run the business up to 2014.

Conclusion on the market economy investor principle

- (93) On the basis of the elements exposed in this section, the Commission has strong doubts that the public intervention in this project is in line with the market economy investor principle and does not confer to Ciudad de la Luz an advantage in the sense of Art. 87 (1).

Other incentives to film productions

- (94) As noted in section 2.3.3, there may have been other incentives offered to film productions. If this is the case, in addition to the above consideration of the financing of Ciudad de la Luz SAU, the Commission would need to consider whether or not these incentives came from State resources.

4.1.2. Economic advantage to undertakings and selectivity of the measure

- (95) Ciudad de la Luz SAU is the only beneficiary of the State funds contributed to the construction and operation of the studio complex Ciudad de la Luz.
- (96) The central question is whether or not the studio complex carries out an economic activity. As there are several privately-owned, commercial film studios across Europe, the Ciudad de la Luz complex joins an existing market in which other players already compete. Furthermore, according to the Spanish authorities, Ciudad de la Luz does not provide its services for free. Consequently, the Commission considers that the Ciudad de la Luz complex carries out an economic activity.
- (97) As indicated above, the Spanish authorities contend simultaneously that a market investor would have supported the project based on its profitability prospects and that the project amount to general infrastructure. This raises the question of whether the public support of a studio complex is not selective but

²⁰ If, in first approximation, the book value of the assets were taken as the prospective selling price in 2014, the entire operation of Ciudad de la Luz between 2002 and 2014 would have been forecasted to generate losses for an investor, with a negative IRR of -0.77%.

benefits society at large. The funding, construction and operation of a film studio complex is intended solely for the benefit of companies active in the audiovisual sector. Consequently, this public support selectively favour a very specific and identifiable category of undertakings.

- (98) In the case of any incentives to film productions from State resources, the Commission would consider these to be selective in nature as the only beneficiaries are likely to be film production companies. This would imply that the State would be favouring certain undertakings and the production of certain goods and therefore the Commission would consider that such incentives threaten to distort competition in the EU. The Commission notes that film producers may have combined such incentives with film production support measures such as the Spanish national film support measures and the reward scheme for films successfully released in Valencian cinemas which the Spanish authorities have recently notified to the Commission.

4.1.3. Distortion of competition and effect on trade between Member States

- (99) From the scale of the Ciudad de la Luz complex, it appears to have been conceived with large film productions in mind. Its California-based designer, Gary Bastien, is a noted Hollywood studio architect. The four smallest soundstages are each 1,620m², with a clear height of 12.5m and elephant doors which are 10m wide and 8m high. The two larger soundstages are each 2,340m², with a clear height of 15m and elephant doors which are 24m wide and 8m high. A 5,000m² 'super-soundstage' is apparently under construction as the final phase of the complex. According to the trade press, this would make it the largest soundstage in the world.
- (100) The facilities at Ciudad de la Luz would therefore appear to put it first in terms of capacity of the premises to attract large film productions in Europe. The main clients for large film studio facilities are major international film production companies, mainly based in the United States (e.g., Fox, Universal, Time Warner, Columbia, Paramount & Disney). The production budgets involved in such films are often around USD 100 million. As these companies are present on the global market, they are able to choose between large film studios all over the world.
- (101) The existing large film studios in Europe which would compete with Ciudad de la Luz probably include the recently constructed Korda Studios in Hungary, Babelsberg in Germany, Barrandov in the Czech Republic, Cinecittà in Italy and Pinewood in the UK.
- (102) In this competitive context, the alleged State aid in favour of Ciudad de la Luz SAU has allowed it to propose low tariffs and substantial incentives. As detailed above, the Commission doubts that Ciudad de la Luz would have been able to compete in this market without its ongoing financing from State resources. Consequently, Ciudad de la Luz appears to distort price competition on the market for the provision of studio services in the EU.

(103) Moreover, since large film productions are mobile and that there are competing large film studios in other Member States, the aid to Ciudad de la Luz SAU is liable to distort competition and affect trade between the EU Member States.

(104) In the case of any incentives to film productions from State resources, since film productions are traded at an international level, the financial advantage granted to the beneficiaries by such incentives affects trade between Member States.

4.1.4. Lawfulness of the aid

(105) The State funds in favour of Ciudad de la Luz SAU are likely to constitute State aid within the meaning of article 87(1) of the EC Treaty. If the presence of State aid is confirmed, since it has not been notified, the aid would be unlawful.

(106) In the case of any incentives to film productions from State resources, such incentives would most probably constitute State aid within the meaning of Article 87(1) EC. The compatibility of the aid would therefore need to be assessed. Again, since it has not been notified, the aid would be unlawful.

4.2. Compatibility of the aid

4.2.1. Regional aid

(107) Ciudad de la Luz has been constructed in the assisted area of Alicante with a maximum possible aid intensity of 40% for eligible investments in 2000-2006. Regional aid would in any case only be allowed for eligible investments, provided the conditions laid down in the guidelines are fulfilled. On the basis of the information available, it appears that the aid would come under the multi-sectoral framework of 1998, which could have the effect of reducing the aid intensity below 40%. At this stage, and pending further information to be supplied by the Spanish authorities, it is therefore not possible to say whether and to which precise extent a part of the aid could ultimately be found compatible with the spirit, if not with the letter, of the aid rules applicable at the time the investment decision was made.

4.2.2. Aid to promote culture

(108) The Commission is of the opinion that the cultural derogation provided for in Article 87(3)(d) of the EC Treaty, as any exception of the general rules of the Treaty, has to be interpreted restrictively.

(109) In the present case, the Commission considers that there is no element indicating that such exception can be applied to State aid providing the construction and operation costs of a new, large film studio complex.

(110) Firstly, the project is clearly built *ex nihilo* and is not promoting heritage conservation.

(111) Secondly, the Ciudad de la Luz complex is an environment in which virtually all types of audiovisual works can be developed, regardless of their content. As a result, it seems difficult to sustain that the film productions made at Ciudad de

la Luz promote any aspect of European culture. Consequently, the Commission considers that it would be difficult to demonstrate that constructing and operating Ciudad de la Luz on a commercial basis, a major new film studio complex far away from any existing audiovisual companies in Spain was necessary for the promotion of culture.

- (112) Thirdly, the scale of the Ciudad de la Luz complex targets large, international film productions. The Commission notes there are already a number of competing large film studios in Europe, as well as other film studios in Spain. Indeed, the best-known Spanish films, including 2004 Oscar-winner *The sea within*, have all been made at smaller facilities. Consequently, the construction of the Ciudad de la Luz complex does not appear to be proportionate to the objective of promoting Valencian, Spanish or even European culture.
- (113) Fourthly, Ciudad de la Luz does not limit its services to cinematographic productions: indeed, commercials have also been filmed at the complex. Nor do the Spanish authorities contend that the selection of films shot at Ciudad de la Luz has been, is or will be based on any verifiable cultural criteria established ex ante. Moreover, the information available so far does not indicate that Ciudad de la Luz competes for attracting films based on cultural considerations but rather on a purely commercial rationale.
- (114) Therefore, the Commission considers that the cultural derogation provided for in Article 87(3)(d) of the EC Treaty could in principle only be applied to the funding offered to film productions for filming at Ciudad de la Luz (EUR 12 million as of October 2007 provided directly by Ciudad de la Luz SAU according to the information provided by the Spanish authorities; possibly more according to available trade publications²¹).
- (115) The 2001 Cinema Communication²² provides the basis on which the Commission applies the cultural derogation of Article 87.3(d) to aid schemes supporting the production of audiovisual works. .
- (116) However, since the Spanish authorities have not provided details of the funding entity and of the conditions under which the funding was provided, the Commission is not in a position to assess their compatibility with the EC Treaty. The Commission only notes at this stage that a film support scheme which has an eligibility requirement that the film is shot in a specific film studio for a specified period of time would be deemed to be aid for a specific film-making

²¹ See *Screen Finance*, February 21, 2007 and *Variety*, February 2, 2007. The articles mention grants of up to €5.4 million for filming for at least three weeks in Valencia, including at least two weeks in Ciudad de la Luz. Allegedly, all films automatically receive 12% of their expenditure in the region and an additional 6% is available depending on a production's 'media, economic and industrial impact': <http://www.variety.com/article/VR1117958591.html?categoryid=19&cs=1>.

²² Communication from the Commission to the Council, the European Parliament, the Economic and Social Committee and the Committee of the Regions on certain legal aspects relating to cinematographic and other audiovisual works (COM(2001)534 final of 26/9/01, OJ C 43 pp6-17 of 16/2/02); prolonged in 2004 (OJ C 123 pp1-7 of 30/4/04) and 2007 (OJ C 134 p5, 16/6/07).

activity and would not therefore be considered compatible under the Cinema Communication²³.

5. CONCLUSION

- (117) In the light of the foregoing considerations, the Commission, acting under the procedure laid down in Article 88(2) of the EC Treaty, requests the Kingdom of Spain to submit its comments and to provide all such information as may help to assess the measures under consideration. The Commission would also request the Spanish authorities to provide their latest actual and forecast data for the Ciudad de la Luz complex up to the completion of construction.
- (118) The Commission requests your authorities to forward a copy of this letter to the potential recipients of the aid immediately.
- (119) The Commission wishes to remind the Kingdom of Spain that Article 88(3) of the EC Treaty has suspensory effect, and would draw your attention to Article 14 of Council Regulation (EC) No 659/1999, which provides that all unlawful aid may be recovered from the recipient.
- (120) The Commission warns the Kingdom of Spain that it will inform interested parties by publishing this letter and a meaningful summary of it in the Official Journal of the European Union. It will also inform interested parties in the EFTA countries which are signatories to the EEA Agreement, by publication of a notice in the EEA Supplement to the Official Journal of the European Union and will inform the EFTA Surveillance Authority by sending a copy of this letter. All such interested parties will be invited to submit their comments within one month of the date of such publication.

If this letter contains confidential information which should not be published, please inform the Commission within fifteen working days of the date of receipt. In that respect, where figures or information portrayed in this decision are deemed to be confidential, the Spanish authorities are requested to provide a range indicating the order of magnitude concerned (e.g. between X and Y EUR million, between X and Y %) and/or to limit deletions to sentences or phrases which are confidential. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to publication of the full text of this letter. Your request specifying the relevant information should be sent by registered letter or fax to:

European Commission
Directorate-General for Competition
State Aid Greffe
SPA 3 6/5
B-1049 Brussels

Fax No: +32 2 296.12.42

²³ See the fourth compatibility criterion in section 2.3(b)(4) of the Cinema Communication.

Yours faithfully,

For the Commission

Neelie KROES

Member of the Commission