



EUROPEAN COMMISSION

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COMMISSION DECISION
of 29.10.2014
ON THE AID SCHEME
(SA.27317 - C 25/2009 (ex N 673/2008))
which Italy is planning to implement
for digital projection equipment

(Only the Italian text is authentic)

(Text with EEA relevance)

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THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union, and in particular the first subparagraph of Article 108(2) thereof,

Having regard to the Agreement on the European Economic Area, and in particular Article 62(1)(a) thereof,

Having called on interested parties to submit their comments pursuant to the provisions cited above¹ and having regard to their comments,

Whereas:

I. Procedure

- (1) On 30 December 2008 Italy notified the Commission of its intention to introduce tax incentives for film investment, film distribution and digital cinema. The Italian authorities submitted additional information on 2 April 2009 and 23 June 2009.
- (2) By letter dated 22 July 2009, the Commission informed Italy that it had decided to approve Italy's film investment and distribution tax incentives. At the same time, the Commission informed Italy that it had decided to initiate the procedure laid down in Article 108(2) of the Treaty on the Functioning of the European Union in respect of the proposed tax credit for investment in digital projection equipment.
- (3) The Commission's decision to initiate the procedure was published in the *Official Journal of the European Union*²². The Commission called on interested parties to submit their comments.
- (4) A workshop on the subject was held jointly by the Italian Ministry of Culture and Tourism and the European Commission in Rome on 21 October 2009.

¹ OJ C 196, 20.8.2009, p. 9.

² Cf. footnote 1.

- (5) The Commission received comments from interested parties. It forwarded them to Italy, which was given the opportunity to react; the Italian authorities' observations were received on 19 January 2010. Further exchanges of information took place after that, including additional letters from the Italian authorities received on 7 September 2010, 12 April 2011, 1 June 2011, 1 December 2011, 10 May 2012, 14 September 2012, 23 April 2013, 6 December 2013, 18 April 2014, 11 June 2014 and 1 August 2014.

II. Description of the measure

1. The notified measure

- (6) The tax credit for exhibitors installing digital projection equipment was part of a set of tax measures for the film sector introduced by the Italian authorities. Together, these tax measures were intended to stimulate the market dynamics to support Italian cultural films in an environment conducive to competition and to promote such films in Italy and Europe.
- (7) The digital cinema tax credit scheme offers a 30 % tax credit for the costs of introducing digital projection equipment. The maximum annual tax credit is capped at EUR 50 000 per screen.
- (8) The following costs may be eligible:
- a) the purchase of digital projection and reproduction equipment;
 - b) the purchase of equipment and machinery for receiving digital signals via terrestrial and/or satellite transmission;
 - c) the purchase via financial lease or the rental of the equipment, systems and machinery referred to in the above points; the relevant contracts must include an obligation to purchase the assets on expiry of the lease, or a provision for the advance exercise of this option by the user company;
 - d) expenditure on staff training activities;
 - e) associated and ancillary expenditure for renovating and adapting projection booths, equipment and utilities and ancillary premises formerly used for 35 mm film projection.
- The expenditure under the latter two points cannot constitute more than 20 % of the total expenditure incurred for points a), b) and c).
- (9) According to the original notification of the Italian authorities, support would be unconditional for cinemas with between 1 and 4 screens and for multiplex cinemas with between 5 and 10 screens in towns with a population of 50 000 or less. For other multiplexes up to 24 screens, there would be an obligation to show cultural films for 50 % of the screenings and to convert at least 50 % of the screens to digital projection as a condition of the aid.
- (10) The tax credit applies to film companies which are liable for taxation in Italy.
- (11) The legal bases for the scheme are the following:
- a) Law No 244 of 24 December 2007 laying down provisions for drawing up the annual and multiannual state budget (*legge 24.12.2007 n.244*);

- b) Decree-Law No 91 of 8 August 2013, converted, with amendments, into Law No 112 of 7 October 2013 (*decreto legge 8.8.2013, n.91, convertito, con modificazioni, dalla legge 7 ottobre 2013, n.112*);
- c) new provisions implementing the tax credits granted to cinemas for the introduction and acquisition of digital projection equipment and machinery (*Nuove disposizioni applicative dei crediti d'imposta concessi alle imprese di esercizio cinematografico per l'introduzione e acquisizione di impianti e apparecchiature destinate alla proiezione digitale*).

2. Doubts raised by the Commission

- (12) The Commission considered in the opening decision that the measure constituted State aid within the meaning of Article 107(1) TFEU. By offering tax incentives, the Italian State was foregoing certain revenues and therefore the scheme involved State resources. The scheme provided an economic advantage to certain undertakings, in this case cinema exhibitors. Given the international trade in films, this selective advantage might affect trade within the Union. The Commission doubted whether the aid could be considered compatible.
- (13) Firstly, the Commission doubted the **necessity** of the proposed digital cinema tax credit. It questioned the maximum tax credit (of EUR 50 000 per screen) proposed: at a tax rate of 30 %, this corresponded to a maximum eligible installation cost of EUR 166 667 per screen (EUR 50 000 x 100/30). This was higher than the estimated costs of digital projection equipment put forward by the Italian authorities, which was EUR 100 000. The Commission doubted whether the maximum tax credit should be so high and whether the conversion costs put forward were a fair estimate. On top of that, the Commission doubted that the installation of 2K³ DCI-compliant⁴ projection equipment was necessary to release Italian or European cultural films.
- (14) Secondly, it doubted the **proportionality** of the proposed aid measure. The Commission noted that larger cinemas were more likely to be able to afford digital projection equipment without public support. Moreover, the Commission noted the availability to exhibitors of commercial transition models, such as the virtual print fee ('VPF') models⁵. It therefore raised the question whether public support on the proposed scale per screen would 'crowd out' commercial alternatives.
- (15) Thirdly, the Commission doubted that the proposed tax credit was an **adequate** aid measure. It noted that the estimated budget of the measure (EUR 16.8 million) corresponded to installation costs of EUR 56 million, which was significantly lower than the estimated costs of conversion (EUR 395.7 million on the basis of EUR 100 000 per screen). Next to the adequacy of the available funding, the

³ 2K refers to a screen resolution of 2048 x 1080 pixels.

⁴ DCI refers to the DCI specifications, originally defined for the US market in 2005 by a joint venture of the US film majors (Disney, Fox, Paramount, Sony Pictures Entertainment, Universal and Warner Bros. Studios), called Digital Cinema Initiatives.

⁵ These commercial transition models are based on the payment of a virtual print fee by distributors for the digital projection of their films in cinemas. The VPF system is based on the notion of using some of the savings realised by the distributor that distributes films digitally in order to contribute to the payment of digital equipment costs borne by cinema exhibitors. Typically such VPF deals involve an intermediary third party (an 'integrator') that collects VPFs from distributors, and installs and possibly finances the equipment in cinemas. Cf. also paragraph (50) for an overview of the available VPF models in Italy.

Commission also questioned whether the proposed measure was sufficiently targeted to achieve the aim of increasing the circulation of cultural Italian and European films. It doubted that the Italian authorities would be able to ensure that digitally equipped exhibitors would introduce alternative commercial models that would offer Italian cinema audiences a wider choice of cultural films. As the use of a tax credit required that a beneficiary must have sufficient tax liabilities and as the measure implied a 70 % investment by the exhibitor, the Commission doubted whether the cinemas most in need of the aid would be able to take advantage of it. The Commission moreover had doubts that the one-off support envisaged (the notification announced a pilot measure of two years) would provide a sustainable solution to the expected shorter lifespan and increased running costs associated with the installation of digital equipment.

- (16) Fourthly, the Commission raised questions on the **economic, social and cultural impact** of the aid. While it recognised that it could be in the common interest for a Member State to use State aid to invest in the transition to digital technology in cinemas, it asked to be assured that the measure would be technologically neutral. In particular, it asked for confirmation that exhibitors would not be induced to invest in one digital standard in preference to another. In addition, it asked the Italian authorities to ensure that films released digitally in an open standards format lower than the digital standard of the support equipment could also be screened. Moreover, it noted that aid for installing digital projection equipment could indirectly benefit the US film majors (in the case of DCI-compliant equipment). The increased demand from the proposed aid might raise the price of the limited supply of projection equipment. As a result of the aid, the critical mass of digital cinemas could be reached more quickly in Italy, which in turn might accelerate the switch to digital distribution and thereby the closure of those cinemas that were not able to install digital equipment by that time. Taken together, the Commission doubted that the potential distortions of competition would be balanced by the social and cultural advantages of the aid.

3. Modifications to the proposed measure since the opening of the procedure

- (17) Following the opening of the investigation procedure by the Commission, the Italian digital cinema tax credit measure has been implemented within the *de minimis* thresholds⁶. Subject to approval by the Commission, the Italian authorities seek to fully implement the measure beyond the *de minimis* thresholds.
- (18) The Italian authorities estimate that the budget of the measure will amount to approximately EUR 7.5 million for the period 2014–2015.

⁶ Until the end of 2010 guided by the Commission Communication ‘Temporary Community framework for State aid measures to support access to finance in the current financial and economic crisis’ (OJ C 83, 7.4.2009, p.1). After the end of 2010, the measure was implemented on the basis of Commission Regulation (EC) No 1998/2006 of 15 December 2006 on the application of Articles 87 and 88 of the Treaty to *de minimis* aid (OJ L 379, 28.12.2006, p. 5). In 2013, the Commission adopted a new *de minimis* Regulation, Commission Regulation (EU) No 1407/2013 of 18 December 2013 on the application of Articles 107 and 108 of the Treaty on the Functioning of the European Union to *de minimis* aid (OJ L 352, 24.12.2013, p. 1).

- (19) The period covered by this decision runs until 31 December 2022. The Italian authorities expect that the tax credit will be used most intensively in the years 2014 and 2015.
- (20) The draft implementing regulations that the Italian authorities seek to implement in full (beyond the *de minimis* thresholds) differ on a number of important points from the original notification.
- (21) First, the requirement for medium and large cinemas to screen a certain amount of Italian and European cultural films as a condition for obtaining the aid has been removed from the modified implementing regulations. In recent years, the Italian authorities have found it difficult to monitor compliance with this requirement in the case of medium to large cinemas. Moreover, they state that removing this requirement is necessary to restore a level playing field between the larger cinemas that need aid and the maxi-circuits that dominate the Italian cinema market (cf. paragraph (37)).
- (22) Second, and linked to this, a threshold of 60 screens is introduced in the modified implementing regulations. Cinema exhibitors that own or manage a higher number of screens are excluded from the tax credit. The Italian authorities consider this a sound alternative to the programming requirements initially imposed as a way of ensuring that the measure reaches its objectives and excluding those market players that, because of their market strength, should be able to make the transition without aid.
- (23) Third, the modified implementing regulations require a declaration from the beneficiary in order to ensure that overcompensation or redirection of aid is avoided if the tax credit is combined with commercial (VPF) models.
- (24) Fourth, the modified regulations allow for the combination of aid up to a maximum aid intensity of 75 % of the total costs. For cinemas of one or two screens, the maximum cumulative aid intensity is 90 %.
- (25) On top of these changes, since 2012 it has been possible for beneficiaries to transfer the digital tax credit benefits to suppliers of digital equipment, banks, financial intermediaries and insurance agencies (cf. paragraph (56)).

III. Comments from interested parties

- (26) The Commission received around 20 submissions from interested third parties in response to the public consultation on the aid measure that was held in 2009. The responses were submitted by:
- European and Italian trade organisations representing distributors and cinemas, the French Commission Supérieure Technique de l'Image et du Son (CST), and the European Digital Cinema Forum (EDCF);
 - the French authorities, German and UK film funds, and the network of European regional film funds (Cineregio); several contributions also referred to the EFAD publications on the subject⁷;

⁷ European Film Agency Directors (EFAD), *San Sebastian Statement: Urgent and comprehensive public support needed for the digitisation of cinemas* (San Sebastian, 21 September 2009), and

- a number of businesses, film sector professionals and individuals from Italy, France, Switzerland and the UK.

Moreover, a workshop on the subject was held in Rome in October 2009.

- (27) Regarding the **necessity** of the aid, all contributions underlined the need for State aid in the transition to digital cinema, which was seen as an inevitable development. Both the French authorities and the UK Film Council explained that the general benefits of digital cinema were accompanied by an asymmetrical distribution of the costs associated with the transition (carried by the exhibitor) and the direct financial benefits (for the distributor). This asymmetrical situation made it difficult to complete a timely transition without external assistance. In this context, the contributors identified a clear risk that many of Europe's smaller, independent and/or remote cinemas would leave the market if digital projection systems were not made more accessible and affordable. In its Statement of September 2009 the EFAD said that 30 % of European screens were at risk of disappearing. Both the French authorities and the German Federal Film Board emphasised that, in the absence of aid, not only the exhibition of films but also their distribution would suffer. A long transition, with the parallel circulation of analogue and digital film copies, would prove too costly, especially for the smaller film distributors. Ultimately, the absence of aid would have a significant negative impact on European film circulation, cultural diversity and the access of European citizens to culture.
- (28) All contributions also stressed that the so-called DCI standards were widely accepted as the common standard for digital cinema. The promotion of one global standard was seen as a positive element rather than a disadvantage for cinemas because it created a level playing field.
- (29) With regard to the costs of installing digital projection equipment, EUR 100 000 per screen was generally not seen as an exaggerated estimate. Instead, several contributors contended that costs could be much higher, for instance when substantial work on the projection booth was required, which could be the case especially for small cinemas. Some contributions nevertheless identified a downward trend in the pricing of digital cinema equipment.
- (30) Several contributions argued that, even if the costs of conversion were much higher than the State support available (as seemed to be the case for the Italian tax credit), the State aid should be seen as complementary to other sources of revenue, for example virtual print fees and exhibitors' own funds.
- (31) Regarding the **proportionality** of the aid, some of the interested parties criticised the tax credit as they expected larger cinemas to be most likely to benefit from the aid. Others argued that aid for larger cinemas could be appropriate, possibly on the basis of programming obligations. Some contributions however echoed the EFAD Statement and stressed that it was important not to introduce differences in treatment, for instance (in the specific Italian tax credit case) arising from the different level of tax liabilities of the cinemas involved, but also (more generally) arising from a restriction of access on the basis of the programming, size and location of cinemas. The International Federation of Film Distributors'

Associations (FIAD) argued that even major exhibitors might not be considered profitable in the current cinema market and general economic context.

- (32) On the availability of commercial business models for the transition and their applicability to smaller cinemas, opinions diverged somewhat. Some argued that there was no standard business model for the digital cinema transition. Others argued that a large number of cinemas could not access the VPF deals offered by third-party integrators (cf. also footnote 5) because of the nature and volume of their programming (the volume of virtual print fees generated depended on the number of films programmed in their first week of release and/or the number of screens the cinema had). Europa Distribution argued that the commercial business models worked only for the more profitable cinemas and big, commercial distributors. According to the EFAD background paper, only approximately 10 000 European screens out of a total of 30 000 could be equipped through the VPF model. One contribution claimed that the commercial VPF models were equally suited for smaller cinemas. In any case, the French authorities argued that the available commercial transition models did not cover all the costs of digital cinema conversion (such as the upgrade of projection booths) and moreover always required a contribution by the cinema exhibitor as well. Public support could play a crucial complementary role in these cases too.
- (33) Regarding the **adequacy** of the aid, interested parties said that, in general, State aid would help smaller cinemas to face the strong competition of large multiplex cinemas and would create a level playing field. The installation of digital cinema equipment was expected to result in a wider choice for audiences. Contributors also emphasised other advantages associated with digital cinema, such as the quality of the projection, the programming flexibility and the lower distribution costs. The French authorities argued that the adequacy of digital cinema support should be looked at not in terms of an increase in programming diversity, but rather in terms of preventing the closure of cinemas. It was in their view through the digitisation of the diverse types of cinema that a diverse range of films would be offered. The European Digital Cinema Forum argued that, if the tax credits could be offset against VAT, even the less profitable cinemas would be able to benefit from the Italian measure.
- (34) Some contributions did mention the short-term nature of the tax credit and contrasted this with the longer-term challenges posed by the digital cinema transition. However, it was also argued that the standards were sufficiently established to guarantee that they would last for at least a decade, or that the lifespan of digital cinema equipment could not yet be determined. The German Federal Film Board said that support for the digital cinema transition would be less costly than the costs associated with rebuilding cinemas and cultural diversity that would be needed after the disappearance of those players that were unable to finance the transition themselves. Germany also emphasised that the specific national and regional context of each Member State would require a specifically designed aid measure and a tailored form of aid. The EFAD Statement echoed this sentiment and emphasised that there was no one-size-fits-all solution. The Italian association of cinema exhibitors (ANEC) expected that the context would have changed sufficiently by the end of the lifespan of the digital equipment to make replacement less of a challenge. The European Digital Cinema Forum moreover stated that any additional running costs might be offset by new revenue streams for the cinemas concerned.

(35) Regarding the **economic, social and cultural impact** of the aid, the contributions generally emphasised the need for one digital cinema standard and the wide recognition of DCI standards. The EFAD Statement argued that support for digital cinema should not impose a technological solution but should at the same time take stock of the technological situation in the sector. Europa Distribution's contribution warned that failure to follow the industry standard would lead to the closure of many cinemas. In any case, ANEC confirmed that cinemas were free under the measure to invest in the standard of their choice. Several contributions argued that DCI-compliant equipment could also be used to screen alternative programmes of different (lower) digital standards, whereas the reverse (screening DCI-compliant film copies on e.g. 1.3K equipment) was not possible. The contributors did not identify a risk of price increases. Instead, prices were expected to fall over time. Both the contribution of the French authorities and the EFAD background paper emphasised in this respect that any aid measure should be designed with a view to avoiding the distortion of competition in the digital equipment market. Any aid measure should therefore be based on an evaluation of digital equipment costs and the aid should be capped in line with those cost estimates. The Commission's concern that State aid might accelerate the switch-over and with it the closure of cinemas (cf. paragraph (16)) were not reflected in the contributions. Instead, State aid was put forward as a sustainable solution to the digital cinema challenge. The Italian federation of arthouse cinemas drew attention to the limited geographic reach of cinemas, which it said meant that the distortive effects on competition would be small.

IV. Comments from Italy

1. Necessity of aid

(36) The Italian authorities have provided the Commission with information on the characteristics of the Italian cinema market (last updated in October 2013). The total number of Italian screens is estimated at 3 936, located in 872 cinema sites. Four categories can be distinguished:

- a) Big cinema networks⁸ of more than 60 screens. There are only two such networks, UCI and The Space. They represent 787 screens in 76 sites.
- b) Small cinema networks. There are 15 such networks, each comprising in total 60 screens or less. In total, the cinemas in this category represent 513 screens in 104 sites.
- c) Small commercial cinemas. These account for 1 287 screens, located in 351 cinema sites.
- d) Smaller sites, comprising almost only single-screen cinemas (90 % of the sites), alongside seasonal cinemas and/or church cinemas. There are 1 340 such sites, corresponding to an estimated 1 500 screens.

(37) While the largest cinema networks (category a)) represent 40 % of the national market share, the cinemas in category d) account for only 5 to 10 % of the market share.

⁸ The Italian authorities have defined a cinema network as a company owning at least 15 screens in a minimum of three cinema sites.

- (38) The tax credit scheme targets the cinemas in categories b) to d). In particular in view of the strong market presence of the two big cinema networks, the Italian authorities consider that State aid is necessary to complete the digital transition of these cinema exhibitors, which are all small or medium-sized.
- (39) According to data provided by the Ministry of Culture and Tourism a total of 1 603 screens applied for digital cinema tax credits during the period 2010–2013 (April 2014 data). The measure, implemented within the *de minimis* rules, proved particularly popular immediately after its launch in 2010, when 671 screens benefited.
- (40) Yet the implementation of the aid measure under the *de minimis* rules has proved insufficient to turn the situation round. In particular medium-sized multi-screen cinemas have, as a result, been able to digitise only some of their screens.
- (41) The Italian authorities say that the digitisation of Italian cinemas is still lagging behind. In October 2013, the digitisation rate stood at about 62 %⁹. According to estimates provided by the Italian authorities in June 2014, at least 700 cinema screens remain to be digitalised.
- (42) As a result, a considerable number of cinemas, mostly small to medium-sized, are at risk. Their disappearance would not only signify job losses at the level of exhibitors, but would in turn impact the distribution of films and restrict choice for the audience.
- (43) The Italian authorities have in particular highlighted the role of single-screen cinemas and medium-sized cinemas in Italy. The continuing presence of the first group is crucial to ensure equal access for all citizens to cinemas, including those located in small rural and mountain towns. The second group of medium-sized cinemas forms the backbone of the distribution and exhibition of quality films in Italy. Their continuing presence is important as they offer an alternative to the two large cinema networks that dominate the market.
- (44) The Italian authorities expect that traditional film will completely disappear from the market within a period of only a couple of weeks or months. As the cut-off point draws nearer, the Italian authorities stress the need to implement the measure beyond the *de minimis* thresholds.
- (45) With regard to the maximum tax credit proposed (EUR 50 000 per screen) and the estimated costs of digital projection equipment, the Italian authorities have adjusted their estimates of the average cost of digital conversion per screen to EUR 50 000–60 000 (figures provided in April and June 2014). The maximum tax credit in other words corresponds to conversion costs that are significantly higher than the estimated average conversion costs. However, the Italian authorities argue that the tax incentives are calculated on the basis of a percentage of the expenses that are actually incurred. Based on an average investment of EUR 50 000, the tax incentive provided (at 30 %) would equal EUR 15 000. In practice, therefore, the maximum tax credits have not as a rule been applied. Nevertheless, the maximum cap guarantees that, in case of atypically high conversion costs, the aid amounts remain limited in absolute terms.

⁹ Data of the national association of cinema exhibitors (ANEC), provided by the Ministry of Culture and Tourism.

(46) With regard to the necessity of aid, it is furthermore important to note that the latest indications by the Italian authorities still point to a cost of digital conversion amounting to several tens of thousands of euros per screen. For many cinemas, especially the smaller ones, it is not possible to raise these funds from private sources, especially in the current Italian and European economic climate.

2. Proportionality of aid

(47) In general terms, the Italian authorities stress that the tax credit is complementary to the commercial transition models and is not in a competitive relationship with VPF models.

(48) The modified implementing regulations contain a number of provisions that ensure that the aid measure remains proportional. These take into account the market mechanisms available for digital cinema conversion (i.e. the VPF models).

(49) First of all, only cinema exhibitors of 60 screens or less may apply for tax benefits. This means that the two Italian maxi-circuits (UCI and The Space) are excluded from the aid. The Italian authorities say that the classic VPF model has been applied successfully to the conversion of these dominant market players. Moreover, taking into account their market strength (cf. paragraph (37)), they should not be dependent on State aid for digital conversion.

(50) According to the information provided by the Italian authorities, the two large cinema networks are the only ones that have made use of the classic VPF model. However, smaller cinema operators have also accessed commercial mechanisms to facilitate their digital transition. An alternative VPF model, tailored for medium to small cinemas, has been developed in Italy on the basis of an agreement between the distributors' and exhibitors' associations. Table 1 below outlines the main differences and similarities between the classic and alternative VPF models as implemented in Italy.

The classic VPF model in Italy	The alternative VPF model in Italy
A third party 'integrator' (which in turn has VPF contracts with distributors) signs an agreement with a cinema exhibitor.	Based on an agreement between the distributors' association and the exhibitors' association. There are no third parties involved.
The exhibitor does not own the digital equipment and does not pay for it up-front.	The exhibitor owns the digital equipment from the start and covers the entire purchase cost up-front.
Both the distributors and the exhibitor contribute to the gradual amortisation of costs through respectively VPF fees and monthly payments. The division of costs is typically 75 % for distributors and 25 % for exhibitors.	Film distributors pay virtual print fees for digital screenings of films. These fees may cover up to 75 % of the digital conversion costs. The exhibitor is in any case expected to cover EUR 5 500 of the costs.

Table 1: Comparison between the classic and alternative VPF models in Italy

- (51) Secondly, taking this into account, the Italian authorities have modified the implementation regulations to ensure there is no overcompensation or redirection of aid if the tax credit is combined with any of the commercial (VPF) models. A declaration is required from the beneficiary that the tax benefit is requested to cover only its own effective costs (cf. paragraph (23)). The Italian authorities have stated that checking by the Ministry of Culture and Tourism, on a case-by-case basis, will guarantee that the aid covers only the part of the investment that effectively has to be carried by the cinema exhibitor.
- (52) Thirdly, maximum cumulative aid intensities have been introduced to keep the aid measure proportionate. These distinguish between the smallest cinema sites (with one or two screens) and other cinemas (cf. paragraph (24)).

3. Adequacy of aid

- (53) In the opening decision, the Commission doubted that the estimated budget of the measure was sufficient to cover the estimated costs of conversion. The updated budget and cost estimates provided by the Italian authorities (cf. paragraphs (18) and (45)) give an updated assessment of the situation addressed by the aid measure. On the basis of an average tax credit of EUR 15 000 and taking into account the estimated budget of the scheme (cf. paragraph (18)), the measure could benefit 500 screens over the period 2014–2015, when the aid measure is expected to be used most intensively. This corresponds to a substantial part of the screens that remain to be digitalised (cf. paragraph (40)).
- (54) While the cultural programming requirement has been removed from the aid scheme, the Italian authorities have argued that the scheme still has a strong cultural objective. The achievement of the complete digitisation of the Italian cinema market will result in a better circulation of different types of film and increase circulation potential for ‘niche’ works. If the various types of cinema in Italy could not all make the digital transition, culture would suffer.
- (55) The Italian authorities maintain that the tax credit measure implies an offset against not just direct taxes owed to the Italian Revenue Agency (corporate tax) but also indirect taxes (such as VAT) and withholding tax and social security obligations (paid by employers on behalf of their employees). All these taxes are taken into account when calculating the tax credit benefits. This increases the accessibility of the scheme, as its use does not depend on the level of profits realised by the undertaking concerned.
- (56) Moreover, Article 51 of Decree-Law 83 of 2012 introduced the possibility of transferring tax credits to suppliers of digital equipment, banks, financial intermediaries and insurance agencies (cf. paragraph (25)). This increases the accessibility of the aid measure for the smaller cinemas, especially if they are family-run and have no employees.
- (57) Already during the implementation of the measure under *de minimis* rules, the tax credits have been of benefit to all types of cinema, including the smallest cinemas in the market. The pie chart below (figure 1) gives an overview of the beneficiaries of the scheme (2010–2013) demonstrating this.

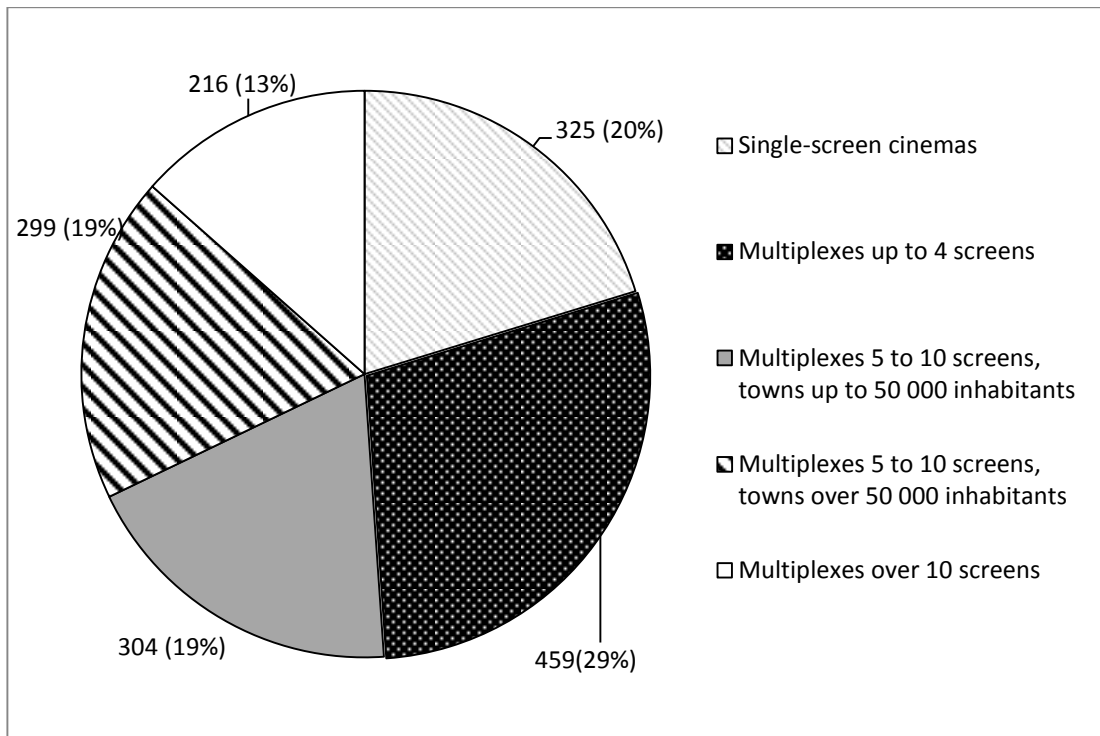


Figure 1: Beneficiaries per type of cinema (2010–2013, based on the number of screens) (data last updated in April 2014 and provided by the Ministry of Culture and Tourism)

(58) The data provided moreover show a marked increase in the number and share of small cinemas benefiting from the tax credit in 2012 and especially 2013. All in all, according to data received from the Italian authorities, 325 cinemas or 24.3 % of the 1 340 smallest cinema sites in Italy were able to use the tax credit to make the digital transition between 2010 and the end of 2013.

4. Economic, social and cultural impact

(59) The Italian authorities stress the cultural importance of ensuring a comprehensive digital cinema transition. The installation of digital equipment brings with it a number of important advantages (such as increased flexibility) for the whole cinema sector (and ultimately cinema audiences). Yet the costs of conversion are high and unequally spread, with cinemas carrying most of the burden. In particular the smaller market players are not able to make the transition without State aid. The market transition (VPF) models developed do not suffice to offset this imbalance and not all cinemas can access them to the same extent.

(60) The Italian authorities confirm that, in their view, the scheme’s mechanisms do not call into question the principle of technological neutrality.

V. Assessment of the aid measure

1. Existence of aid

(61) Article 107(1) TFEU states that ‘Save as otherwise provided in the Treaties, 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 internal market.’

- (62) As explained in the opening decision and more briefly in paragraph (12), the measure constitutes State aid within the meaning of Article 107(1) TFEU. The source of funding is tax incentives, so the Italian State is foregoing certain tax revenues. Under the scheme, certain film companies will benefit from this financial advantage, and the measure therefore provides a selective advantage to certain undertakings. The beneficiaries compete with other undertakings that do not necessarily benefit from the scheme. Consequently the scheme distorts or threatens to distort competition. In view of the international trade in films, the measure may affect intra-Union trade.

2. Compatibility of the aid

- (63) The Italian authorities justify the measure as aid to promote culture. They have continually stressed the cultural importance of completing the digital cinema roll-out in Italy as soon as possible. The aid measure aims to ensure that all types of cinema are able to make the digital transition, despite the high costs of conversion.
- (64) When the opening decision on the measure was adopted, the Commission had not defined its policy on digital projection support. Since then, the Commission has adopted a new Communication on State aid for films and other audiovisual works¹⁰, which updated the rules used for assessing the compatibility of State aid for films and other audiovisual works under Article 107(3)(d) TFEU.
- (65) The new Cinema Communication explicitly acknowledges that aid to cinemas may be assessed as aid to promote culture within the meaning of Article 107(3)(d) TFEU. Therefore the compatibility of the aid at issue here may be assessed under this provision. The Cinema Communication stipulates that aid for the modernisation of cinemas, including their digitisation, can be justified on that basis if such aid is necessary, proportionate and adequate.

a) Necessity of the measure

- (66) As demonstrated by the Italian authorities and confirmed by the comments from interested parties, the digital cinema transition poses a challenge for the film sector that affects European cinema as a whole, and smaller cinemas in particular. The disappearance of cinemas, in particular independent small and medium-sized venues in smaller towns, would reduce the diversity and regional reach of the films offered. In other words, a long and uneven transition has a negative impact on film exhibition, distribution and, ultimately, European audiences.
- (67) Despite the implementation of the tax measure under the *de minimis* rules, Italy continues to lag behind in the digital cinema transition.
- (68) At the same time, as the market has passed the ‘tipping point’ of conversion, with more than 60 % of the screens in Italy digitalised at the end of 2013, the situation has worsened for those cinemas that are dependent on State aid to make the

¹⁰ Communication from the Commission on State aid for films and other audiovisual works (OJ C 332, 15.11.2013, p. 1).

transition. Indeed, the availability of 35 mm films is not guaranteed in the short term.

- (69) The measure targets not only the smallest cinemas, but also larger commercial cinemas and networks. However, the largest cinema networks (of more than 60 screens) are excluded from aid. The Italian authorities have argued that the tax benefits granted to all cinemas of a lesser size reinstates a level playing field in the sector, which is dominated by two very large cinema networks.
- (70) The tax credit aims to help those cinemas that are unable, especially in the current economic climate, to raise sufficient private funds for a costly cinema conversion.
- (71) Taking into account the above, the Commission considers that the aid measure can be considered necessary to retain and restore a diverse cinema landscape in Italy in a digital context. The continued presence of different types of cinema, from single-screen arthouses to multi-screen venues with commercial programming, is crucial to help ensure that a diverse range of cinema continues to be offered to the Italian public. As recognised by the submissions received from interested parties, the digital cinema transition challenges the film sector as a whole, with only the largest cinema networks easily accessing commercial transition models. The market data supplied by the Italian authorities have demonstrated that the *de minimis* implementation of the measure has not sufficed to complete this transition, especially for those cinemas that have more than one screen. Even if it is true that certain cinemas were able to access VPF deals, it is also true that commercial transition models do not cover all the costs of the digital cinema conversion (cf. paragraph (32)). Public support can be considered necessary in these cases too, as long as it is designed in a complementary fashion, ensuring that the measure remains proportional regardless of the type of cinema concerned.

b) Proportionality of the measure

- (72) The Italian authorities have excluded cinema exhibitors of more than 60 screens from the tax credit. The Italian cinema market structure shows a clear gap between operators of up to 60 screens and those of a larger size (cf. paragraphs (36) and (37)). The threshold introduced therefore seems proportional in view of the objective of the scheme.
- (73) Moreover, the tax credit covers only part (30 %) of the transition costs and is capped at EUR 50 000 per year. By making the amount of aid a percentage of actual digitisation costs, the Italian authorities have guaranteed that the aid remains proportionate, even when the costs may vary on a case-by-case basis. As several contributors pointed out (paragraph (29)), the costs for digitisation can rise significantly above average in some cases, for instance when substantial work on the projection booth is required. In such atypical cases, the cap of EUR 50 000 nevertheless ensures that the absolute aid amounts remain proportionate.
- (74) Whereas the opening decision raised questions on the ‘crowding out’ of commercial digital cinema conversion models, paragraph (50) demonstrates that two different commercial conversion models have been developed in Italy. They can be combined with the proposed digital cinema tax credit. The Italian authorities have

included specific provisions in the modified implementing regulations to ensure that the combination of private and public digital cinema conversion financing does not result in overcompensation or redirection of aid (e.g. to distributors or VPF integrators). In this way, the Italian authorities promote an optimal synergy between the available market models and State aid, in order to foster a complete digital roll-out.

(75) The tax credit can also be combined with other aid measures. In order to ensure the proportionality of the aid, the Italian authorities have introduced maximum cumulative aid intensities of 90 % for small cinema sites (single- and two-screen cinemas) and 75 % for other types of cinema.

(76) More generally, the application has to be accompanied by a certified document specifying the actual expenditure incurred for each screen and checks are to be carried out by the Ministry of Culture and Tourism on a case-by-case basis. The implementing regulations moreover indicate that the tax credit will be recovered (plus interest and penalties) if the requirements are not met.

c) Adequacy of the measure

(77) The clarifications provided by the Italian authorities, and the introduction of the transferability of the tax credits, ensure that the measure will have an impact on the intended beneficiaries of the scheme. Even the least profitable cinemas should be able to access the scheme.

(78) The measure is no longer proposed as a pilot measure, but would be in force until the end of 2022.

(79) The data provided by the Italian authorities (paragraphs (57) and (58)) demonstrate the accessibility of the measure to all types of cinema targeted, in particular the smaller ones. While other factors may play a role, it should be noted that the marked increase in the number of cinemas of 1 to 4 screens benefiting from the tax credits (under the *de minimis* rules) in 2012 and 2013 coincides with the introduction of the transferability of the tax credits in 2012 (paragraph (25)).

(80) More generally, the measure seems adequate for the purpose of safeguarding the diversity of cinemas present on the Italian market, ranging from single-screen outfits to small commercial cinemas and various types of multiplex cinema. This diversity of screens is a prerequisite for achieving a diverse range of films offered on those screens.

d) Distortion of competition and effect on trade

(81) The distortions of competition and the effect on trade are limited. The cross-border effect of cinemas is limited to the presence of international cinema operators and the international dimension of the film trade in general. However, individual cinema locations have an inherently limited geographic reach, as audiences will not travel far to visit a cinema.

(82) The measure relates to investment aid and provides a one-off benefit to cinemas that are facing a one-off transition. The tax credit ensures that all cinemas

can complete the digital switch-over, but does not unduly distort competition in terms of their daily operation.

- (83) The completion of the digital cinema transition across Europe is moreover expected to benefit the European film industry as a whole. In this regard, the doubts on digital cinema standards raised in the opening decision are no longer relevant. The contributions from third parties have shown that there is a consensus in the trade in favour of the prevalent digital cinema standards.

VI. Conclusion

- (84) In the light of the foregoing, the Commission takes the view that the aid pursues a well-defined cultural objective. The doubts with regard to necessity, proportionality, adequacy and impact raised in the opening decision have been addressed. The distortions of competition and the effects on trade that the measure will have are limited in such a way that they are not contrary to the common interest. Accordingly, the tax credit for digital projection equipment can be considered compatible with the internal market on the basis of Article 107(3)(d) of the Treaty on the Functioning of the European Union.

HAS ADOPTED THIS DECISION:

Article 1

The State aid measure which Italy is planning to implement for digital projection equipment on the basis of Law No 244 of 24 December 2007, Decree-Law No 91 of 8 August 2013 and the draft provisions implementing the tax credit granted to cinemas for the introduction and acquisition of digital projection equipment and machinery is compatible with the internal market within the meaning of Article 107(3)(d) of the Treaty on the Functioning of the European Union.

Implementation of the aid measure is accordingly authorised.

Article 2

This decision is addressed to the Italian Republic.

Done at Brussels, 29.10.2014

For the Commission

Joaquín Almunia
Vice-President

Notice

If the decision contains confidential information which should not be published, please inform the Commission within fifteen working days of the date of receipt. 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 the decision. Your request, specifying the relevant information, should be sent by registered letter or fax to:

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