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PUBLIC VERSION

WORKING LANGUAGE

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<u>**Subject:**</u> **State aid No SA.32019 – Denmark**
Danish radio channel FM4

Madam,

The Commission wishes to inform the Kingdom of Denmark that, having examined the information supplied by its authorities on the measure referred to above, notified on the basis of Article 108(3) of the Treaty on the Functioning of the European Union ("TFEU"), it has decided not to raise objections.

1. PROCEDURE

1. On 1 December 2010 Denmark notified plans of the Danish government to grant aid for the broadcasting channel FM4, operated by a broadcaster to be selected through an open tender procedure. Following a request for information of 20 January 2011, Denmark submitted further information on 7 February 2011.

2. The Danish authorities do not consider that the measure constitutes State aid and they have therefore submitted the notification for reasons of legal certainty.

2. CONTEXT

2.1. The market for radio broadcasting in Denmark

3. Pursuant to an analysis of 7 February 2011 submitted by the Danish government, the Danish radio market consists of four primary actors. The main radio provider is DR which runs 4 national FM channels (P1-P4) as well as several DAB[1] and NET

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channels. The main commercial player is SBS Radio which runs the national FM5 NOVA FM as well as The Voice. In association with SBS, Berlingske Media runs FM6, POP FM and lastly there is the New Radio Aps with Radio 100FM and Radio Soft. Besides these players there are around 300 local radio stations.

4. The market is mainly funded through license fees[2] and advertising revenue. There are no exact figures for 2009, but in 2007 DR used 1.234 million DKK on radio services, while the advertising revenue in the same year was 285 million DKK, which was reduced to 217 million DKK in 2009. The market for radio advertising is around the 2% level of the total advertising turnover in contrast to the average of around 6% in a European context. Currently, there are no real subscription revenue streams available for radio, and as the market for radio advertising has been reduced, the competition between the commercial operators for advertising revenue is significant. The funding for DR has not been influenced in a similar way as the continuity is secured through the license fee. To make capacity available on the FM band, FM4 is to replace the existing FM channel, P2, which is owned and operated by DR. Thus, P2 will terminate transmission. The remaining FM channels and the DAB channels will continue transmitting unchanged.[3]

5. The development of the market and listening share over the last years will be presented below:

Market share development

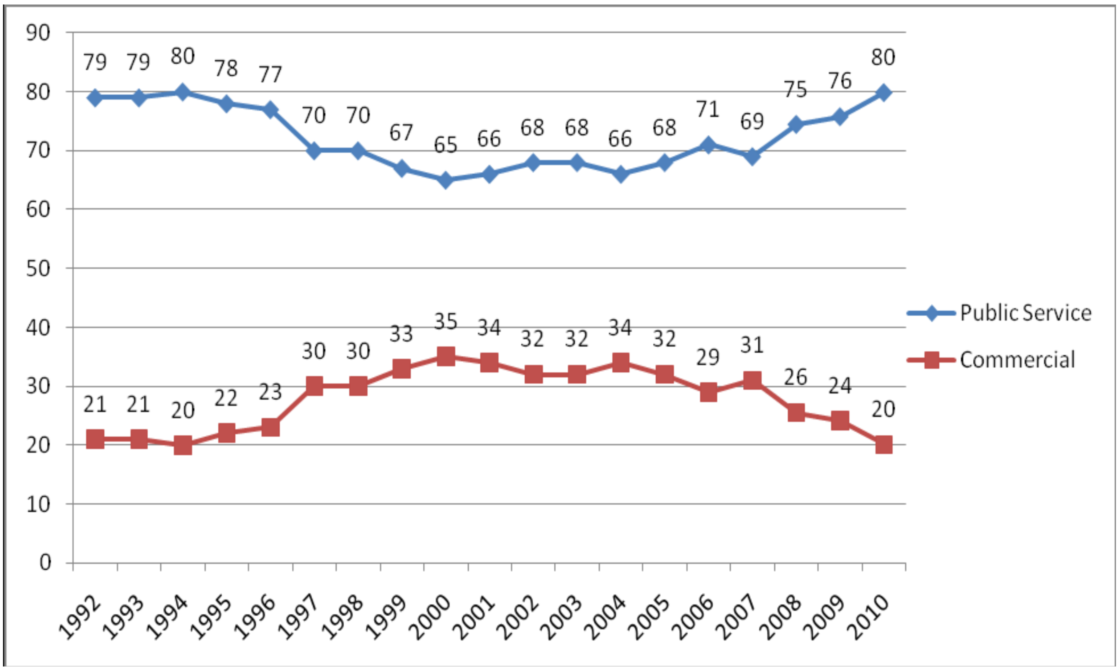
Company	*Channels*	*2010*	*2009*	*2008*
DR	P1	7,1	6,1	4,9
	P2	4,4	3,7	4
	P3	19,8	19,6	20
	P4 Total	43,8	42,6	42,1
	P5	1,3	0,9	1
	DR Boogieradio	0,4	0,3	0,2
	DR Dansktop	0,4	0,5	0,5
	DR Hit	1,1	0,8	0,6
	DR Klassisk	0,4	0,3	0,3
	Remaining DR channels	1,2	1	0,9
	DR Total	**79,9**	**75,8**	**74,5**
SBS Radio	The Voice Total	1,8	1,8	1,7
	NOVA fm	5	4,5	1,3
Berlingske Media	Pop FM	0,5	0	0
New Radio [100 FM]	Radio 100FM	3,2	5,5	5,3
	Radio Soft	0,7	1,2	1,8
	100 FM total	3,9	6,7	7,1
Commercial stations	**Total commercial**	**20,1**	**23**	**25,5**
Sales partnership	SBS Radio Total	8,1	7,4	5
Sales partnership	ddr ex. 100FM	8,1	8,9	10,1
	DDR Total	12	15,6	17,2

Source: TNS Gallup

2 The only radio broadcaster financed by license fees is DR.

3 At the moment DR holds the licence to four of the six national terrestrial radio channels, FM1, FM2, FM3 and FM4. Until now DR has broadcast the radio channel, P2 on the FM4 frequency. As a consequence of the tendering out of the FM4, DR will be left with three FM frequencies, no longer being able to broadcast P2 on FM. The operating costs for P2 in 2011 are 42 million DKK (until November 2011). Since DR will no longer be operating P2 on FM after November 2011, an amount of 50 million DKK will be deducted from the licence fees received by DR in the future.

Breakdown in listening share among commercial radio and public service radio



Source: Danish Agency for Libraries and Media. The figures are rounded and the figures from 2008 are non-comparable as a consequence of a new method from 2008 forward (the ppm electronic measurement).

6. DR is the market leader and has managed to increase its market share in the last few years to a level of almost 80%. None of the commercial operators has any potential of challenging this position and of competing efficiently, especially not in the current environment, as a consequence of the competition from the public service radio programming from DR, as well as the level of advertising revenue available. DR invests in its radio programming services and it is well received in the population. DR produces high quality radio programming and effectively competes on all genres and platforms.

2.2. Public service broadcasting in Denmark

7. Public service broadcasting in Denmark is regulated by the Radio and Television Broadcasting Act ("the Act"). According to the Act, the overall public service activities in Denmark through television, radio, internet etc. must provide the Danish population with a wide range of programs and services comprising news coverage, general information, education, art and entertainment. Quality, versatility and diversity must be aimed at in the range of programmes provided. The Act also contains a number of requirements for programming, language and requirements to provide programmes that reflect the diversity of cultural interests in the Danish society.

8. According to the Act, public service providers include DR, the regional TV2 stations and TV2/DANMARK A/S's activities related to the public service remit, the program services on the fourth FM radio channel and the news coverage on the fifth FM radio channel. The detailed program profile for the fourth FM radio channel and the news coverage on the fifth FM radio channel is further defined in the Act.

9. The public service broadcasters - DR, the regional TV2 stations and the fourth FM radio channel - are financed through a pre-defined share of the license fees. The precise distribution of license fees is decided in the media agreement (currently media agreement for 2011-2014). Public service activities on the fifth FM radio channel are financed by its provider, and public service activities on TV2/DENMARK A/S are financed by TV2 DENMARK A/S itself.

10. The precise requirements for public service activities are specified in, respectively, DR's public service contract, the regional TV2 stations' and TV2/DENMARK A/S' public service permit,[4] and in the license for the fifth FM radio channel. According to DR's public service contract, DR must ensure public service on 3 nationwide FM radio channels, an AM radio channel, a number of DAB radio channels and a number of internet radio channels.

11. DR must submit an annual report on its compliance with the public service requirements in a public service review, which the Radio and Television Board ("Radio- og TV-nævnet", hereinafter "the RTB") examines and expresses an opinion on. As regards the fifth FM radio channel the RTB continuously monitors the provider's compliance with the public service requirements.

12. In Denmark, an only commercial radio channel with public service obligations is NOVA FM, which is imposed an obligation to transmit 1000 hours of news programming in accordance with the Act. However, this obligation has been imposed as a part of the acquisition of the licence for FM5 in an auction in which the provider of the public service offered to pay 23 million DKK annually for the permit. Pursuant to the Danish government, NOVA FM's content requirements are substantially less and in no way comparable to the requirements envisaged for FM4.

3. DESCRIPTION OF THE MEASURE

13. The subject of the measure is granting of aid by the Danish government for the operation of the public service radio channel FM4. The objective of the measure is to establish competition on the Danish radio market for public service programming which, presently, is dominated by the public broadcaster DR with almost 80 % audience share. The beneficiary will be a broadcaster to be selected through an open tender procedure. The duration of the measure is from 1 November 2011 to 31 October 2019. The annual budget equals maximum DKK 100 million whereas its total budget is maximum DKK 800 million and. The aid intensity reaches 100%.[5]

3.1. Procurement and public consultation

14. The licence for the radio channel will be awarded through an open tender, which - in addition to a set of detailed minimum requirements for the content on FM4 - includes a beauty contest as well as an element of price competition. The award criteria will be: 1. the quality of the applicant's business plan (35 % weight in the overall evaluation); 2. the price, i.e. annual licence fee funding requested by the bidder, maximum of DKK

[4] TV2/DENMARK A/S and the regional TV2 stations only have public service obligations with regard to TV broadcasting but no obligations to broadcast public service through radio.

[5] For potential revenues other than licence fee, see footnote 8.

100 million a year (25 %); and 3. the programme profile (40 %).[6] The total bid cannot exceed DKK 800 million and the bid for an individual year cannot exceed DKK 100 million.

15. The public service provider must be an independent legal entity with the sole purpose of operating FM4.[7] For this reason, the licence fee made available to the provider is designed to cover the cost of discharging the public service obligations imposed upon the FM4 by the tender specifications. FM4 may not broadcast any advertising and the future public service provider may not sell any broadcasting time.[8] Together with the system of supervision and transparency in accounting as well as the system for avoiding over-compensation, this should according to the Danish authorities prevent cross-subsidisation and any disproportionate distortion of competition. The public service provider may however conduct other business in order to make use especially of its technical equipment, expertise and programme archive.[9]

16. All of the radio channel's content[10] is considered public service by the Danish authorities. The public service content requirements to be imposed on the channel have been developed on the basis of recommendations from an expert committee, which delivered a report on 3 September 2010. In light of these recommendations, the Danish government has opted for a news/talk radio.[11]

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6 The rating is based on an overall assessment where for each of the three award criteria 20 points will be the maximum number of points available.

7 FM4 will have 144 kbit/s DAB capacity available on MUX 2.

8 The provider of the FM4 public service may broadcast sponsored programmes and it is – according to copyright legislation - entitled to receive remuneration from the cable operators, if the channel is retransmitted in cable networks. According to the Danish authorities, an estimate of the possible **revenues from sponsoring fees** is difficult to provide, since it depends entirely on how attractive the channel becomes from a sponsor’s perspective. DR has decided not to accept radio sponsoring fees on its channels, even though this is legally possible, and thus there is no comparable benchmark there. On the TV channels, DR received sponsoring fees of app. 4.0 million DKK in 2009. The radio advertisement market was in 2010 DKK 217 million, and approximately up to 10 % of these constitute sponsoring fees, i.e. in total DKK 21,7 million. In a rough estimate, there might be three possible scenarios for the development of sponsoring fees for FM4, depending on how attractive the channel becomes: 1) The channel becomes of little interest for sponsors, and possible sponsoring fees will be modest, up to 3 million DKK; 2) The channel acquires a medium position and will be able to obtain sponsoring fees in the range of 5-7 million DKK; 3) The channel acquires a highly attractive position vis-a-vis sponsors, and will be able to receive fees of up to 12 million DKK. Any possible **remuneration for cable retransmission** is a secondary (derived) income for the FM4 licensee. FM4 is not a must carry channel, and as such there is no guarantee that a cable operator will retransmit the signal. In case a cable operator chooses to retransmit the signal, the company will receive remuneration. To illustrate, if all 1,7 million Danish cable households had received FM4 throughout 2010, the licencee’s remuneration would have been DKK 2,4 million. It is highly unlikely that FM4 will be retransmitted to all cable households. Thus, the remuneration will be relatively modest. The Danish government does not see any other evident direct sources of revenue, but FM4 is not, as a matter of principle, excluded from applying for grants or donations.

9 The provider of the public service must submit separate financial reports on its public service activities and its commercial activities. The contract notice provides in detail the rules for identifying and accounting separately for costs specific to non-public activities.

10 The provider is not precluded from purchasing programmes on the international broadcasting market. It is left for the provider to decide how and where to purchase programmes.

11 More information is available on: http://kum.dk/nyheder-og-presse/pressemeddelelser/2010/september/nyskabende-radio-pa-fm4/.

17. Once approved by political agreement, a draft contract notice was in public consultation in November and December 2010. Pursuant to the Danish authorities, no entity has filed a formal complaint relating to the tendering out of FM4, including notably possible State aid aspects, and the Danish government is not aware of undertakings intending to submit such a complaint relating to the tender.

18. The tender documents were approved by the RTB in a meeting on 12 January 2011. The tender procedure was launched on 17 January 2011 and it was open for bids until 28 February 2011. It is expected that the winner of the bid will be announced on 8 April 2011, the licence will be awarded to the successful bidder in April 2011, the public service provider will begin broadcasting on 1 November 2011, and the licence will be valid until 31 October 2019 (i.e. for 8 years).

3.2. Risk assessment and reasonable profit

19. In their profitability analysis of 30 November 2010, the Danish authorities aim to demonstrate that the FM4 channel is unique, and that none of the usual benchmarks are appropriate. Thus, the level of reasonable profit for the operator running the FM4 channel could not be established on the basis of comparable profitability rates in the Danish (commercial and public service) radio market, in the international radio market, or in comparable markets, such as TV. According to the Danish authorities, the profitability in the international radio industry measured by different indicators (profit margin, returns on capital employed, EBITDA and EBIT) varies significantly in the markets where the financial accounts have been studied (Denmark, Sweden, Norway, Netherlands). Therefore, reasonable profit for the operator of the FM4 model is established on the basis of a specific assessment of the economic risks undertaken by the prospective provider of the FM4 channel.

20. According to the Danish authorities, pay-radio does not appear a viable business model in the current business environment. This is related to the business model where the success lies in attracting audience measured by rating and share, where the radio station sells time to advertisers by gross rating points, reach, and frequency. But, according to the Danish authorities, it is important to recognize that this is not the model for FM4, where the provisioned services are pre-funded quarterly by the Danish State, which enables the company to leave out a high risk of selling sufficient advertising to cover the costs. This should also secure sufficient continuity to enable risk-taking on the content as well as general programming development and innovation.

21. Reasonable profit for a public service provider without advertising is considered by the Danish authorities a fair rate of return on own capital invested in the enterprise while taking into consideration the relative risks involved in the business operation of providing the specific public services.

22. Pursuant to the Danish authorities, the suggested model for FM4 cannot be compared directly with other types of commercial radio, but mainly with public radio broadcasters without advertising. The FM4 provider will not be subject to the challenges of traditional commercial radio as there is no advertising and the State pays in-advance for the services. There is no cyclical financial performance to observe related to sales and continuity is secured by the state. In this sense, the FM 4 channel is low risk, but will contrary to traditional commercial radio be highly personnel

intensive, either through in-house staff or through purchasing of independent production companies producing radio shows as a consequence of the high quality content requirements. In this respect, the capital requirement is higher than for traditional commercial operators, as the required amount of qualified staff, studios and equipment is higher than for commercial radios that primarily play music by playlists.

The level of own invested capital

23. According to the Danish authorities' analysis, the own invested capital required for the provider of the FM4 channel is estimated to vary between DKK 20 to 25 million for a partnership model (favouring a limited own investment and depending on external partners for the main production) and DKK 40 to 50 million for an in-house production model (favouring own investment and being based on full technical setup with main production remaining inside the company). These two business models represent - in the estimates of the Danish authorities - the maximum and minimum levels of own invested capital necessary for the provider of the public service. The risks for both types of business model are similar and they will be treated equally in terms of returns on own invested capital based on the risk assessment.

The main risk factors for the provider of the public service

24. The Danish authorities have identified the following main risk factors for the public service provider of the FM4 channel:

25. First of all, the FM4 provider should receive a reasonable profit for the risks related to the initial costs before production as well as the distribution between the fixed and variable costs:

- Initial costs required before the start of production: The expenditure required for studio facilities for broadcast, production equipment and the overall organizational cost in the period between where the permit is granted, to the actual beginning of broadcast.

- Variable costs: The FM4 radio will have high variable costs in personnel as own-produced programming is labour-intensive. These costs are related to the production of programming, where especially news, but also factual, culture and drama production can be considered highly personnel expensive. Payments to right holders are also variable costs as these are related to the output specification.

- Fixed costs: Rent, studio facilities, infrastructural transmission costs for FM and DAB,[12] payments to right holders. These costs can be relatively high for FM4.

26. Second, the FM4 provider runs the risk of his miscalculation of the expenses in connection with the bid. Since the FM4 model is unique and since the bidders are able to ask for up to 100 million DKK per year, this risk can be considerable. Thus, the

12 As regards distribution costs, it is necessary to distinguish between costs for DAB and FM band costs: The costs of transmitting on the FM band will need to be negotiated with the owners of the transmitters. Thus, it is for the provider of the public service to ensure that the FM4 will have the necessary signal transmission. FM4's DAB capacity will correspond to 12,5 % of the total DAB capacity on MUX 2, and therefore the FM4 licensee will have to bear 12,5 % of the total cost of DAB distribution on MUX2.

provider of the public service bears the risks in case the costs of complying with the public service obligation throughout the eight year license period turn out to be higher than estimated by the provider at the time of bidding.

27. Third, in case of non-compliance with the public service obligations, the provider must repay an amount corresponding to the costs of non-provided services with an additional 15% penalty compensation to the State. Moreover, in case of grave and repeated non-compliance with the public service obligations, the RTB may withdraw the licence and the funding, thus effectively ending the business as a result.

28. Fourth, the provider will carry all risks related to inflation and price and wage fluctuations. The bidders are required to offer a fixed price for the eight year period with no possibility of subsequent adjustment.

29. Fifth, in order for the whole tender to be successful and attract the most competent bidders, the potential attractiveness of the tender for professional operators also has to be taken into account. Thus, the assessment of what constitutes reasonable profit must take into account that also the best and most well-run commercial radio operators should have an economic incentive to participate in the tender.

30. In Commission's view, the first, second and fourth risks are all closely related, and can be summarised as saying that, since the price is fixed, there is a risk that it may not cover the costs. The third risk - of having to repay sums if the provider fails to comply with the public service obligations - seems to be in the control of the provider. The fifth issue is not actually a risk but a non-risk related consideration in determining the reasonable profit level, namely that whatever level is set should be attractive to potential bidders.

Reasonable profit

31. When taking into account the above "five major risk factors" for the prospective provider, and the estimation that the provider's invested own capital will probably be in the area of either DKK 20 to 25 million or 40 to 50 million, depending on the business model, the Danish authorities consider that a profit based on the rate of return on own capital invested of 5 % is reasonable.

32. The economic incentive for the commercial operators is further enhanced by incentive measures connected with content improvements. These measures will take the form of a set of Key Performance Indicators ("KPI"), which represent an additional combined return of 5%.

33. The maximum return on own invested capital is thus 10%: 5% are related to the risks connected with undertaking the public service obligation, while 5% are designed to ensure incentives to improve the quality of the content. Profits exceeding this amount will be clawed back.

3.3. Mechanism to avoid overcompensation

34. In order to ensure that the provider does not receive overcompensation during the eight year licence period, the Danish authorities will introduce mechanisms (a) to

effectively sanction non-compliance and (b) to require that overcompensation is clawed back. It should be noted that the RTB is responsible for the monitoring, verification and enforcement of the public service contract regarding FM4. The specific procedures are described in the tender documents.

35. The RTB must secure that there is no overcompensation. A respective clause will be implemented in the contract with the provider of the public service to avoid situations of overcompensation. All remaining profit after subtracting a) the 5% reasonably returns on own capital invested; b) the up to 5% extra returns of own capital; and c) the 10% transfer of the annual budgeted expenses, is considered overcompensation.[13]

Reasonable rate of return on own capital invested

36. As described in paragraph 31, the permit-holder is allowed a 5% rate of return on own capital invested.[14]

Programme incentives

37. As indicated in paragraph 32, a set of KPI will be introduced to secure that the provider has an additional incentive for a constant high level of content performance and improvement. This allows increased returns on own capital invested by up to extra 5 %.

38. To ensure that the target is reached, the FM4 channel's performance is measured quantitatively by a questionnaire defined by the RTB. The measurement is to be ordered by the holder of the permit from an external consultancy agency.[15]

39. The KPI target consists of two levels:

- The overall knowledge of FM4 in the population must be at least 60 % in the first year, gradually increasing to 80% in the seventh;

- The quality level is achieved by reaching a target of 85 % of the listeners evaluating the channel 7 to 10 on a scale from 1 to 10. Should one of the parameters reach a target lower than 50%, the KPI cannot be achieved.

40. Failing to achieve either one of these results, in either one of these steps, entails that the KPI is not fulfilled or thus, that the provider of the public service cannot achieve the potential increased rate of return.

Transfer to next year

41. In addition, the company is allowed to transfer 10% of the annual budgeted expenses for projects and to ensure that the company can withstand price fluctuations. At the end of the permit-period reserves will be subject to claw back.

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[13] It should be noted that any derived income, which the provider of the FM4 public service might receive from cable operators, or revenue from sponsoring fees, or any other funds (grants, donations, etc.) will be a part of the income, which provides the basis for calculation of reasonable profit, and thus also subject to the mechanism introduced to avoid overcompensation (including claw back).

[14] “Own capital invested” equals “equity”.

[15] The measurement will be performed once a year.

Model overview

42. The elements included in the mechanism developed to avoid overcompensation can be summarized thus:

1) Return on invested own capital (reasonable profit)	5%
2) Reimbursement for non-compliance	Repayment of amount corresponding to the costs of services not procured with a 15% penalty
3) Incentive: Performance optimization on program quality	Over-performance incentive of 5% extra on own capital invested
4) Transfer to next year (reserve)	10% of the annual budgeted expenses
5) Clawback of overcompensation	100% of the excess result is to be repaid without undue delay (i.e. any profit, which exceeds the amounts in 1) - 4), or which exceeds 10 % of the annual turnover)

3.4. Supervision and transparency

43. The public service provider will be subject to the RTB's supervision with a view to ensure compliance with the public service obligations. Thus, the public service provider must submit an annual report to the RTB regarding the previous year's programme activity, which accounts for its compliance with the requirements in the broadcasting permit. On this basis, the RTB may require the public service provider to adjust the content, including the quality of the programmes and/or the listener satisfaction as documented in public surveys. The listener satisfaction is evaluated on the basis of an analysis conducted by an analysis institute, which must be ordered and paid for by the provider of the public service. A draft contract notice contains an outline of the questionnaire to be used in the analysis.

44. In the opinion of the Danish authorities, the neutrality of the analysis of the listener satisfaction is ensured by a number of requirements: First, the institute conducting the analysis must be a member of ESOMAR[16] and comply with the guidelines of ESOMAR. Second, the sample size must be large enough to establish the level of listener satisfaction with 95% certainty. Third, the form of the analysis is almost completely set out in advance, thus ensuring that neither the institute nor the provider of the public service is generally capable of framing their own questions. Fourth, the result of the analysis must – regardless of the result – be sent to the RTB. Fifth, the RTB may, if substantial reasons require so, choose to disregard uncertainties in the result. Pursuant to the Danish authorities, these factors ensure sufficiently the independence and validity of the analysis and the RTB ex officio must ensure that the institute is independent and approved.

16 ESOMAR promotes the use of a code of practice that governs the conduct of market research. All ESOMAR members agree to abide by the ICC/ESOMAR Code and are subject to ESOMAR's disciplinary procedures.

45. Moreover, to ensure transparency, the public service provider must also submit an annual financial report, which must comply with the substantive obligations as regards separation of accounts in Directive 2006/111/EC on the transparency of financial relations between Member States and public undertakings as well as on financial transparency within certain undertakings ("the Transparency Directive"), regardless of whether the successful bidder falls within the scope of the directive.

46. Finally, the RTB may withdraw the broadcasting permit temporarily or permanently in accordance with the Act.

4. ASSESSMENT

47. This decision only deals with the channel FM4 and does not prejudice the Commission's assessment of other channels in Denmark or other Member States.

4.1. State aid within the meaning of Article 107(1) TFEU

Presence of public resources

48. The broadcasting of the FM4 channel will be financed through public funds[17] by a flat-rate licence fee.[18] The amount of DKK 800 000 is paid out of the budget of the Danish State to a single undertaking and, therefore, the funds thereby obtained are granted by the State within the meaning of Article 107(1) TFEU.

The favouring of certain undertakings

49. Any financial measure granted by the State to an undertaking which, in various forms, would mitigate the charges normally included in the accounts of the undertaking, has to be considered State aid within the meaning of Article 107 TFEU. In this particular case, the public service compensation constitutes a direct cash inflow for the public service provider, similar to commercial revenues, for which the undertaking does not need to compete on the market. In this sense, there is no doubt that the public service compensation, providing an economic and financial advantage to the beneficiary compared with other competitors not receiving the same funds, has to be regarded as favouring an undertaking within the meaning of Article 107 TFEU.

50. Nevertheless, the Danish authorities do not consider the measure to be State aid as according to them, the four criteria in the *Altmark* judgment[19], are complied with.

51. In the *Altmark* judgment, the European Court of Justice ruled that State measures compensating public service costs do not qualify as State aid under Article 107(1) TFEU when the following four conditions are fulfilled:

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17 As for revenues from sponsoring fee and from cable operators, see footnotes 8 and 13.

18 According to the Act, the media license fee is levied on all appliances able to receive and broadcast programs with pictures, and a radio license fee is levied on all appliances able to receive and broadcast radio programs (this includes computers with internet access).

19 Judgment of the Court of Justice of 24 July 2003, C-280/00 Altmark, OJ C 226, 20.09.2003, p. 1.

– The recipient undertaking must actually have public service obligations to discharge and these obligations must be clearly defined;
– The parameters on the basis of which the compensation is calculated must be established in advance in an objective and transparent manner;
– The compensation cannot exceed what is necessary to cover all or part of the costs incurred in the discharge of public service obligations, taking into account the relevant receipts and a reasonable profit for discharging those obligations;
– When the company is not selected following a tender procedure which would allow for the selection of the tenderer capable of providing those services at the least cost to the community, the level of compensation needed must be determined on the basis of an analysis of the costs which a typical well run and adequately equipped undertaking would have incurred in discharging those obligations.

52. As regards the fourth *Altmark* criterion, the Court stated that: *"Fourth, where the undertaking which is to discharge public service obligations, in a specific case, is not chosen pursuant to a public procurement procedure which would allow for the selection of the tenderer capable of providing those services at the least cost to the community, the level of compensation needed must be determined on the basis of an analysis of the costs which a typical undertaking, well run and adequately provided with means of transport so as to be able to meet the necessary public service requirements, would have incurred in discharging those obligations, taking into account the relevant receipts and a reasonable profit for discharging the obligations."*[20]

53. As further explained below, the Commission takes the view that the definition of the public service obligation is sufficient to ensure that the first *Altmark* criterion will be complied with, and the system of supervision and transparency and the model for calculating the level of compensation to be offered to the provider of the public service in return for undertaking the public service obligations ensure that the second and third criteria in the *Altmark* judgment are satisfied.

54. Concerning the fourth *Altmark* criterion, the Commission considers that in the present case, it is not in a position to conclude that this criterion is fulfilled. Firstly, the Danish authorities have not submitted any information on the expected costs of the FM4 channel or any allocation of costs incurred in providing the service of another radio channel similar to the FM4 channel. Furthermore, the tender refers not only to the minimum content obligations, but also to the commitments, which the provider of the public service will assume as part of the beauty contest. For these reasons, it can not be found with certainty whether the measure constitutes State aid. Consequently, the Commission has assessed the compatibility of the measure with the internal market in accordance with Article 106 (2) TFEU as explained below.

55. In order to ascertain whether the funds granted to the public service provider for the financing of FM4 could constitute aid within the meaning of Article 107(1) TFEU, the Commission has also to assess whether it distorts or threatens to distort competition, and whether it affects trade between Member States.

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[20] Judgment of the Court of Justice of 24 July 2003, C-280/00 Altmark, OJ C 226, 20.09.2003, p. 1., para. 93.

Distortion of competition and effect on Union trade

56. The third condition to be met for State measures to fall under the provision of Article 107 TFEU is that they have a real or potential effect on trade between Member States.

57. The provider of FM4 will be competing with other commercial and public radio channels in Denmark not benefiting from support foreseen under the measure. In particular, FM4 will be in direct competition with other channels dedicated to news and talks such as P1 channel run by DR.

58. In principle, it would be possible to argue that FM4 may be in competition also with other channels such as the channels run by SBS Radio, Berlingske Media and New Radio Aps, even though some of them are dedicated predominantly to music, for instance. The presence of a new channel may potentially influence the preferences of viewers to switch from other channels - whether dedicated to news, culture or music - to listen the new FM4 service.

59. It is not necessary, in order to evaluate the impact on trade between Member States, to demonstrate whether the reduction of penetration suffered by other channels after the launching of FM4 will be a direct consequence of the presence of a free-of-charge channel or not. It is sufficient to argue that the possibility for an undertaking to offer a service on conditions which cannot be matched by any other commercial operator (commercial broadcasters need necessarily either to charge a subscription fee or to carry advertising on their channels, or both) may put other undertakings in an unfavourable position.

60. In addition, it must be noted that, according to the Court of Justice, for a State measure to be relevant under Article 107 TFEU, a direct impact on actual trade between Member States is not necessary. It is sufficient that the measure puts the recipient in a more favourable position compared with other undertakings which are competing in intra-Union trade[21]. This is the case with DR but also with SBS Radio, Berlingske Media and New Radio Aps channels.

61. Furthermore, the beneficiary will be in competition with radio broadcasters with a foreign or international company structure (e.g. SBS Radio is a part of ProsiebenSat1 group) and foreign public radio programmes. Also, the beneficiary can participate in the international market of the purchase and sale of programme rights.[22]

62. The distortion of trade may thus be envisaged in consequence of the emergence of a new channel - without advertising - in relation to other channels, such as the channels run by the aforementioned DR, SBS Radio, Berlingske Media and New Radio Aps. In this sense, it can be concluded that the measure under examination may distort competition and have an effect on trade between Member States.

63. Therefore, the measure could constitute State aid in the meaning of Article 107(1) TFEU.

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21 730/79 *Philip Morris v Commission,* 17.9.1980.

22 Cf. point 22 of the Communication from the Commission on the application of State aid rules to public service broadcasting, OJ C 257, 27.10.2009, p. 1.

4.2. Compatibility of the aid with the internal market

64. Having determined that the measure in question could constitute State aid within the meaning of Article 107(1) TFEU, the Commission has to assess whether this aid could be declared compatible with the internal market under the provisions of Article 107(2) and (3) TFEU, or of Article 106(2) TFEU.

65. Denmark is of the view that the operation of FM4 channel, as tendered out by the Danish authorities, constitutes a service of general economic interest, and may thus be funded in compliance with Article 106(2) TFEU and the Communication on the application of State aid rules to public service broadcasting ("the Broadcasting Communication")[23].

66. According to Article 106(2) TFEU as interpreted by the Court and reflected in point 37 of the Broadcasting Communication, in order to qualify for exemption from the competition rules by virtue of the provision of a service of general economic interest, all of the following conditions have to be met:

- the service in question must be a service of general economic interest and be clearly defined as such by the Member State;

- the undertaking in question must be officially entrusted by the Member State with the provision of that service; and

- the application of the competition rules of the TFEU (in this case, the ban on State aid) must obstruct the performance of the particular tasks assigned to the undertaking and the exemption must not affect the development of trade to an extent that would be contrary to the interests of the Union.

67. Article 106 TFEU is a derogatory provision which has to be interpreted restrictively. In this sense, for a measure to benefit from such derogation, it is necessary that all the above-described conditions are fulfilled: it is for the Commission to assess whether these criteria are fulfilled in a particular case.

68. In the case of broadcasting, the Commission, when performing the above task, has also to take into account the "Protocol No. 29 on the system of public broadcasting in the Member States annexed to the TEU and to the TFEU", which was adopted in June 1997 and entered into force on 1 May 1999 ("the Protocol"). The interpretative rules laid down by the Protocol, while stating that the system of public broadcasting is directly related to the democratic, social and cultural needs of each society and the need to preserve media pluralism, underline the competence of the Member States to define the "public service (broadcasting) remit", to assign these services to certain undertakings and to organize the funding of these services.

69. More specifically, Member States have "the competence ... to provide for the funding of public service broadcasting in so far as such funding is granted to broadcasting organisations for the fulfillment of the public service remit as conferred, defined and organised by each Member State, and in so far as such funding does not affect trading

[23] Communication from the Commission on the application of State aid rules to public service broadcasting, OJ C 257, 27.10.2009, p. 1.

conditions and competition in the Community to an extent which would be contrary to the common interest, while the realization of the remit of that public service shall be taken into account".

70. Member States are in principle free to define the public service remit in any economic sector. For broadcasting, the Protocol and the Broadcasting Communication have confirmed this right of the Member States to define and confer public service tasks and to provide for their funding, in so far as such funding does not affect trading conditions and competition to an extent contrary to the common interest.

71. While Member Stales are competent to define the public service remit, to entrust its execution to one or more undertakings and to provide for its funding, the Commission - under the control of the Court - has the duty to check for manifest error and to ensure that such funding does not affect trade to an extent contrary to the common interest.

Definition of the public service remit

72. The licence contains an obligation for the FM4 public service provider to provide, as public services, a set of radio programmes of information, culture and entertainment for general reception. As for its financing, these services are to be financed solely by licence fees.

73. The Commission, as stated in paragraph 71, has only the duty to ensure that no manifest error occurs in the definition of services which fall to be assessed under Article 106(2) TFEU as services of general economic interest. In particular, the Commission has to assess whether the public service mission defined by a Member State does not exceed what can be regarded as services of general economic interest under the rules of the TFEU.

74. In the case under examination, the Commission is of the opinion that a balanced and varied provision of a wide range of news, talks and cultural programming can be considered a public service mission in broadcasting. In particular, a 24-hour news/talks public radio service would help to meet the democratic and social needs of a society, as referred to in the Protocol and the Broadcasting Communication, by allowing the coverage of a wider range of programmes. The public service obligations of the future public service provider of FM4 have been defined in the contract notice and they will be specified in the envisaged entrustment act.

75. In this sense, the provision of a 24-hour news/talks public radio service can be considered as addressing the democratic and social needs of society by ensuring a wider coverage of topics and programmes. The Commission would therefore consider that the task which will be assigned by the Danish government to the FM4 public service provider will fulfill one of the basic goals of public service broadcasting as identified in the Protocol.

76. Moreover, the launching of FM4 will enrich the choice of 24-hour radio services for consumers, thus responding to the mission as identified by the Protocol and the Broadcasting Communication - to preserve media pluralism, in particular in the provision of news, talks and cultural programmes.

77. In view of the above considerations, the Commission cannot detect any manifest error in the Member State's definition of the public service remit.

78. The definition of the public service remit in the licence thus complies with the conditions in points 43 to 49 of the Broadcasting Communication. Therefore, the Commission considers that the first condition of Article 106(2) TFEU, as described in paragraph 66, is met.

Entrustment and supervision

79. The Broadcasting Communication requires in its points 50 and 51 that the undertaking in question should be entrusted with the service of economic interest by an official act. The official act of entrustment of the public service will take the form of a licence permit awarded by the RTB. This permit will refer to the precise minimum content obligations, applicable legislation, the relevant parts of the tender documents, and the extra commitments, which the provider of the public service will have to assume as part of the beauty contest.

80. Apart from the Act, the draft contract notice contains very specific requirements regarding the public service obligations of the future provider of the FM4 public service. The public service obligations, the conditions for providing the compensation, as well as the arrangements for avoiding and repaying any overcompensation will also be specified in the envisaged license.

81. The public service provider of the FM4 radio channel must account for compliance with the public service requirements in an annual public service review which must be submitted to the RTB and approved by it. The RTB will monitor the application of the formal agreement between Denmark and the entrusted undertaking in a transparent and effective manner.

82. The public service remit will thus be entrusted to an undertaking in accordance with points 50 to 52 of the Broadcasting Communication and the supervision of the supply of the public service by the independent RTB will be in accordance with points 53 to 55 of the Broadcasting Communication. Therefore, the Commission considers that the second condition of Article 106(2) TFEU, as described in paragraph 66, is met.

Funding

83. The exact amount of the licence fee will be decided through the tender as described above, the maximum annual fee being DKK 100 million. With the funds thereby collected, the FM4 has to discharge all the public service obligations set out in the tender specifications. The public service provider is not entitled to collect advertising revenues.

84. The means of funding thus complies with points 56 to 59 of the Broadcasting Communication.

Transparency

85. The public service provider must be an independent legal entity with the main purpose of operating FM4. It will be required to separate accounts between the public service activity and non-public service activities as well as to comply with the requirements in Articles 1(2) and 4 of the Transparency Directive.

86. However, the public service provider may conduct other activities than the FM4 operation with the purpose of making use of its technical equipment, programme archive, etc. According to the contract notice, any such activities must be considered non public service activities. Any such other activity must be linked to/derived from the public service activity, e.g. the production of a CD, or publishing of a book on the basis of program material from the public service activities, and it will be made on market terms. As part of the yearly financial report, the provider of the public service must submit a separate report for the public service activity and a separate report for other activities. The provider of the public service must at all times be able to account for which specific activities are considered public service and which are not.

87. According to the contract notice, cost allocation between the public service and the non-public service activities must be based on market price, and this price is to be fixed according to a recognised method, which ensures allocation of all income and the <u>full costs</u> on each activity (activity area) as foreseen in point 66 of the Broadcasting Communication.

88. As all of the radio channel's content is considered public service by the Danish authorities, it can be concluded that the public financing will actually be limited to the net costs of the public service remit.

89. The obligation of the public service provider to separate accounts between the public service activity and non-public service activities thus complies with the transparency requirements in points 60 to 69 of the Broadcasting Communication.

Overcompensation

90. The FM4 channel - consisting of mainly news, current affairs and cultural and debate programming - is not in itself economically viable for commercial broadcasting, especially not in a small market like the Danish, without a significant compensation for the public service obligations imposed. Given the specificity of the services provided and the ban on advertising, it can be assumed that the provision of such service of general interest would not be possible to the same extent without the aid granted.

91. A model calculating the amount of compensation for the provider of the public service is an integral part of the tender in order to ensure that it will not be overcompensated. The model consists of 4 elements: 1/ The provider of the public service is entitled to compensation for the performance of the public service tasks and a reasonable profit; 2/ It will be offered incentive measures with a view to improve the quality of the channel; 3/ The provider of the public service will be allowed to transfer up to 10 % of the annual budgeted expenses to the following financial year to withstand cost fluc-

tuations; 4/ Profit that exceeds the limits set above will be clawed back by the Danish government.

92. As described in paragraphs 31 to 33, a 5 % return and the additional profit of 5 % on own capital invested is considered by the Danish authorities to be a reasonable profit. The 5% return on own capital invested is not a flat rate, but the maximum rate of return possible. Meeting the KPI allows an increased profit of up to 5% which is not a flat rate either. The Commission believes that the KPI model ensures that the KPI will be genuinely challenging for the public service provider to achieve in order to create an efficient and well-run public service radio channel throughout the eight year license period.

93. The total percentage of possible profit is thus between 0% and 10%. This level of profit seems reasonable in light of the two main risk factors of inflation and fixed prices. It reflects that, while FM4 should not be perceived as a high risk endeavour, the risks of inflation and fixed prices are there and will limit the number of bidders due to the detailed requirements. The detailed requirements will limit the attractiveness of the tender, but these requirements are a prerequisite in order for FM4 to be capable of competing with DR's radio channels, rather than with (other) commercial operators. The level of profit seems to be set at a level where interested economic operators either individually or by cooperating are thought to show an interest in bidding.

94. In addition, as indicated in paragraphs 35 and 41, in order to maintain full control of the level of profitability, it has been decided that profits which exceed 10 % of the annual turnover will - in any event - be clawed back.

95. Thus, the model for calculating the amount of compensation - together with the element of price competition in the tender and the supervision and transparency requirements - ensures that the provider of the public service does not receive overcompensation. As mentioned, the implementation of the model is supervised and approved by the RTB, on the basis of the annual financial reports and reports on program activity submitted by the public service provider.

96. The compensation for providing the public service obligations thus complies with points 70 to 76 of the Communication

Financial control mechanisms

97. The implementation of the model for avoiding overcompensation is supervised and approved by the RTB, on the basis of the financial reports and reports on program activity submitted by the public service provider. The RTB approves its statements, including statements regarding its profit. An in depth review is carried out every year by the RTB, as explained in paragraphs 98 and 99.

98. The contract notice indicates that the public service provider must once a year submit a statement to the RTB, describing and documenting the previous year's program activity and the fulfillment of the requirements in the licence. The provider of the public service is also required to submit financial reports to the RTB. A certified public accountant must sign an auditor's statement, certifying that the required

auditing principles are met and that the required business methods and internal controls have been followed throughout the previous year. The RTB may carry out an audit by its own accountant. In case of non-compliance with the licence permit, the RTB may withdraw the licence, in which case the provider of the public service must refund any excess licence fee.

99. The RTB will as soon as any overcompensation is observed carry out a claw-back of the excess profit (i.e. based on an ex post assessment). The RTB may either require the provider of the public service to refund the amount or it may be deducted in the following payment of licence fees to the public service provider, which is paid out quarterly in advance.

100. The measure thus provides sufficient financial control mechanisms to comply with points 77 to 79 of the Broadcasting Communication.

Proportionality

101. As far as the third and last condition indicated in paragraph 66 is concerned, it has to be examined whether the State aid is actually necessary for the purpose of having the service of general economic interest carried out and whether the amounts do not exceed the necessary level. Moreover, in accordance with Article 106(2) TFEU as interpreted by the Protocol and the Broadcasting Communication, the Commission has to assess whether the development of trade is not affected by the decision of a Member State to provide a certain service of general economic interest on certain conditions to an extent that would be contrary to the Union's interest. This formulation of Article 106(2) TFEU indicates that a certain effect on trade and its development can be tolerated because of the general-interest nature of the service provided.

102. In the case at hand, FM4 will not be able to raise funds on the market like a commercial broadcaster. This particular arrangement makes the service provided by FM4 a unique service in the market place, as no other operator is capable of providing the same service on the same financial terms.

103. In other words, in the absence of any possible commercial income[24], the production of FM4 programmes in the form requested by the State authorities would not have been financially possible without the transfer of public funds. Being unable to carry advertising, the only funding source available - for the explicit requirement set by the public authorities in the entrusting act - is public funding derived from the licence fee. Therefore, prohibiting these funds would make the performance of the particular task *de facto* impossible.

104. The main risk for the FM4 public service provider is the acceptance of a fixed price for an eight year period, which is not adjusted according to inflation, combined with a highly detailed set of obligations. In effect, there seems to be a limited scope for budgetary cuts since it is not possible during financial hardship to lower the quality standards.

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[24] For exceptions, see footnote 8.

105. On the other hand, the risks related to the FM4 channel are mitigated significantly by the fact that there is a constant and predefined funding stream up to DKK 100 million per year. Moreover, the public service provider does not have to establish a sales division to ensure revenue streams through advertising. Overall, the very specific public service requirements and the fixed price probably entail an overall risk, which is somewhere between small and moderate for radio broadcasters.

106. For the purposes of the assessment, the Commission has to ensure that the funding granted to the undertaking does not exceed the costs (in this case the full cost, as the service does not collect commercial revenues[25]) incurred for the provision of that service. This is, in consequence of the funding system adopted - i.e. quarterly advance payments with ex-post funding review on the basis of the actual expenses incurred - in the opinion of the Commission, ensured.

107. It can be concluded that the amount of licence fee used to finance FM4 seems proportional to the actual costs which will incur for the provision of the service. In fact, no market revenues will be collected by the public service[26] : and at the same time, the provider of the FM4 will have to cover the costs of the necessary resources from the amount received from public funds to fulfill all its public service obligations.

108. In the case at hand, the competitors of FM4 can suffer a reduction in their market shares. This effect is to be expected from the outset as a result of the Member State's decision to provide the said service of general economic interest. Nevertheless, it must be noted that DR - i.e. the largest competitor – should be able to maintain a large part of its customer base despite losing market share.

109. It is not necessary for the purposes of this decision to perform a complete market analysis. It is sufficient to demonstrate that although a certain impact on competition and trade can be detected, this effect is not excessive to the extent that it is precludes the development of competition and trade in the sector concerned.

110. Overall, it can be estimated that the launching of FM4 will enrich the choice of Danish consumers, as there will be in future one more channel available. Consumers will adopt the new FM4 and retain the existing channels by DR (apart from P2 channel, see paragraph 4) and other broadcasters.

111. Moreover, even if the State financing of FM4 would lead to more serious economic difficulties for its competitors, such effects could be accepted under Article 106(2) TFEU in order to allow services of general economic interest to be delivered. Article 106(2) TFEU, as stated above, accepts a certain effect on competition and trade as a consequence of ensuring the provision of a public service remit.

112. The tendering out of the FM4 channel is meant to create competition between public service programming, while limiting the effects on the commercial radio market. This is done, mainly, by prohibiting advertising on FM4, and by imposing obligations as regards content, which ensure that FM4 will be different from the existing commercial radio channels.

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25 For exceptions, see footnote 8.

26 For exceptions, see footnote 8.

113. In the present case, it can be concluded that the decision of the Danish authorities to provide a channel with no advertising, although having an effect on trade, does not affect the development of that trade to an extent contrary to the Union interest. In this sense, while the competitive environment for private services might be affected by FM4, the freedom to provide services and the functioning of the internal market as such for radio are not affected to an extent contrary to the Union interest.

114. The measure ensures overall, that the public service provider will not engage in activities which result in disproportionate distortions of competition contrary to points 92 to 97 of the Broadcasting Communication. To sum up, the Commission concludes that the financing of FM4 by licence lee fulfils also the third condition described in paragraph 66 which must be satisfied in order to benefit from the application of Article 106(2) TFEU.

5. Conclusion

115. The funding of FM4 using financial resources from the licence fee could constitute State aid, taking into account the *Altmark* judgment. However, on the basis of the foregoing assessment, the conditions laid down in Article 106(2) TFEU are fulfilled and the Commission could therefore consider the aid for 2011 to 2019 compatible with the internal market.

116. The Commission therefore concludes that the provider of FM4 will perform a service which is clearly in the public interest and it will receive compensation for this service which will cover its actual costs and a reasonable profit. The public service compensation arrangement is fully complying with all relevant conditions of the Broadcasting Communication. The compensation is not affecting the development of trade to an extent as would be contrary to the interests of the Union.

117. The public funding of FM4 can thus be accepted because it allows the provision of services of general economic interest without being disproportionate and without affecting the development of trade to an extent contrary to the common interest.

118. The Commission takes note of Denmark's intention to clearly define in an official act the methods for determining the amount of the compensation and avoiding overcompensation for any future aid, in conformity with the Broadcasting Communication.

6. Decision

119. The Commission has accordingly decided to consider the compensation of the public service of the FM4 channel compatible with the internal market. Consequently, the Commission has decided not to raise any objection to the measure at issue.

120. If this letter contains confidential information which should not be disclosed to third parties, 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 the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site: http://ec.europa.eu/EU_law/state_aids/state_aids_texts_en.htm.
Your request should be sent by registered letter or fax to:

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Yours faithfully,

For the Commission

Joaquín Almunia
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