Subject: State aid No N 540/2008 – Hungary

Cultural aid from Norwegian Funds

Madam,

I. PROCEDURE

1. By e-mail dated 28 October 2008, registered on the same day, the Hungarian authorities notified a new aid scheme concerning aid for cultural purposes to be financed primarily from Norwegian funds. The funding takes place within the framework of the European Economic Area Financial Mechanism and the Norwegian Financial Mechanism set up by the EEA Enlargement Agreement of 2004.

2. The Commission requested additional information on 19 December 2008 and 6 March 2009. The Hungarian authorities replied on 8 January 2009 and 18 March 2009 respectively.

II. DESCRIPTION OF THE MEASURE

3. **Legal basis:** Pursuant to the EEA Enlargement Agreement of 2004 those EEA member states that are not members of the European Union contribute financially to the reduction of social and economic disparities within the EEA. The relevant instruments for the implementation of the financial contribution are the Economic Area Financial Mechanism and the Norwegian Financial Mechanism. Although the two mechanisms concern two different funds, they serve the same purpose and share the same procedural and institutional setup. The relevant legal bases are as follows:

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• Government Decree 201/2005 (IX.27) on the promulgation of the Cooperation Agreement on the implementation of the EEA Financial Mechanism for the period 2004-2009 established on 7 July 2005 between, on the one hand, the governments of the Republic of Iceland, the Grand Duchy of Lichtenstein and the Kingdom of Norway, and on the other hand, the Government of the Republic of Hungary, and of the Cooperation Agreement on the implementation of the Norwegian Financial Mechanism for the period 2004-2009 established on 10 June 2005 between the Government of the Kingdom of Norway and the Government of the Republic of Hungary.

• Government Decree 242/2006 (XII.5) on the implementation of the EEA Financial Mechanism and the Norwegian Financial Mechanism ("Implementing Decree")

• Protocol 38A of the EEA Agreement on the EEA Financial Mechanism

• Agreement between the Kingdom of Norway and the European Community on a Norwegian Financial Mechanism for the period 2004-2009

4. Objective: The objective of the scheme is the promotion of culture and the conservation of cultural heritage.

5. Contents of the aid scheme: The Financial Mechanisms provide support for projects pertaining to one of the priority sectors identified in Articles 6 of the above mentioned cooperation agreements. The very general categories of priority sectors are broken down into focus areas in schedules B of the cooperation agreements. The relevant focus area for the present aid scheme is defined as follows:

• Restoration of historical sites and buildings, based on utilisation plans

• Conservation of world heritage sites in Hungary

• Restoration of museums and establishment of collections for the introduction of certain fields of the European heritage

Accordingly, only projects with one of these objectives are eligible for aid under the notified scheme. In line with these objectives aid will be available for the following purposes: renovation of historical buildings – in particular those that are officially qualified as being part of the UNESCO world heritage –, museums and monuments; conversion of historic buildings to be used as cultural centres; development of cultural sites; collection, renovation and systematisation of items of cultural value and making them accessible to the general public.

6. Only projects with a public purpose are eligible for support, that is to say projects with a predominant profit motive may not receive financing from the scheme. The scheme has a limited budget (in the sense that the expected value of all applications for support exceeds the budget of the measure) and therefore aid will be awarded competitively for the projects that are evaluated as the best ones by a jury. The scheme will finance only investments, operating aid will not be granted. In respect of the purchase of works and material equipment involved in the

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2 Official Journal of the European Union of 29.4.2004 L130/81
investments beneficiaries will be required by law to conduct an open and transparent tender. General horizontal rules concerning the award of aid will apply to the notified scheme. These provide that only costs directly related to the investment can be eligible and that expenditures can only be reimbursed against an authentic invoice. The beneficiaries are required to pre-finance the investments and will only be reimbursed later. A monitoring process following the award of the aid is also set up under which beneficiaries have reporting obligations and upon request must account for the proper use of the aid. These rules are further detailed in the grant contracts concluded after the adoption of the aid, which also include the aid intensities.

7. **Geographical scope** The geographical scope of the scheme is the whole territory of Hungary.

8. **Aid intensity** Concerning aid intensity, investments can be financed up to 100 % of eligible costs.

9. **Accumulation** The relevant rules explicitly provide that the aid cannot be cumulated with aid received from other local, regional, national or Community schemes to cover the same eligible costs.

10. **Duration, budget and form of the aid:** As specified by the cooperation agreements the Financing Mechanisms concern the period 2004-2009. In line with the corresponding sections 1 of Articles 3 of the two cooperation agreements the deadline is 30 April 2009 for concluding the contracts and 30 April 2011 for the submission of reimbursement claims. The total budget of the scheme is EUR 47 million. The aid is in the form of direct grants.

11. **Beneficiaries:** The implementing regulation defines the scope of potential beneficiaries as any legal person or company without legal personality having a permanent establishment in Hungary, as well as State bodies if they fulfil the eligibility criteria in the notice for the applicants for the aid. Thus in principle any entity could submit an application except private individuals if they fulfil the eligibility criteria, which mainly concern proven technical and organisational capacity to manage and execute cultural projects. Further, the condition that the projects must not have a predominant profit motive means that the scope of beneficiaries is restricted to the following not-for-profit entities: a) State bodies, i.e. municipalities, regional authorities, public legal persons that are legally separate from but maintained and financed by the municipality, regional authority or the central government, and b) not-for-profit entities like public purpose societies (both State and privately controlled) and foundations.

### III. ASSESSMENT OF THE MEASURE

**Existence of State aid within the meaning of Article 87 (1) of the EC Treaty**

12. The Commission has first examined whether the notified measure can be characterised as State aid within the meaning of Article 87(1) of the EC Treaty, according to which "save as otherwise provided in the Treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market".
13. The very first condition as regards the presence of aid is whether the beneficiaries qualify as undertakings. If not, aid could only arise by indirectly favouring the production of certain goods or services. It is settled case-law that any entity engaged in an economic activity is to be considered as an undertaking regardless of its legal form or the way it is financed\(^3\). It follows that the fact that an entity operates on a not-for-profit basis or has such legal form, as do all potential beneficiaries of the scheme, does not exclude the possibility that it qualifies as an undertaking.

14. Similarly, even if an entity provides its services totally free of charge to its users or customers and is financed entirely by the State it can still be an undertaking. Accordingly those potential beneficiaries that are public legal persons maintained and financed by the State, e.g. museums or cultural centres in historic buildings that will be renovated, can still be undertakings even if they provide their services to the public free of charge.

15. It is also settled case-law that the concept of economic activity is a functional one\(^4\). This means that even if most of an entity's activities are non-economic and hence it is not undertaking as a whole, it may yet qualify as such in respect of certain functions if they are of economic nature. This is usually the case if the State directly engages in economic activities. By its nature the State as whole is not an undertaking but if it directly (i.e. not via an incorporated company of which it is the owner) engages in an economic activity, for that particular function it is to be regarded as an undertaking. It follows that even if the beneficiary is a municipality or regional authority it qualifies as an undertaking for the purposes of competition law if it directly manages (i.e. without contracting out) the cultural site, monument, museum or cultural centre, provided that the activity it is directly engaged in is an economic one.

16. Ultimately therefore all the beneficiaries can be undertakings depending on whether their activities are of an economic nature regardless of the institutional setup, i.e. whether they are separate legal entities or part of the municipality, regional or central government, whether or not – in case they are not separate legal entities – their operation is contracted out, and regardless of their not-for-profit nature.

17. Accordingly, for the potential beneficiaries it has to be examined whether their activities are of an economic nature. In case-law, the concept of economic activity is defined as offering goods and services on a given market\(^5\). In that respect one important element whether some kind of competition exists, i.e. if there are private entities offering the same or substitutable goods and services. If a market, however limited, exists for the activity concerned then the activity is organised on market principles and it is to be considered economic\(^6\).

18. One of the activities of the beneficiaries for which financing will be available is running and managing a cultural site or a building of cultural value that can be toured by visitors. In some cases this does not involve more than maintaining a historic monument that can be visited free

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\(^3\) Case C-41/90 Klaus Höfner and Fritz Elser v Macrotron GmbH. ECR 1991 I-01979, par. 21
\(^4\) Case 118/85 Commission vs Italy, pt 10;
\(^5\) Case C-35/96 Commission of the European Communities v. Italian Republic ECR 1998 I-0385, par. 36
\(^6\) AG Opinion Case C-205/03 Federación Española de Empresas de Tecnología Sanitaria (FENIN) v Commission of the European Communities, par. 31
of charge, which can hardly be regarded as offering a service on the market. Further, the historic buildings could, for example, house public administration bodies, the activity of which is non-economic. In other cases such activity may involve the management of a major tourist attraction involving guided tours, exhibitions and films. In this context the activity can indeed be characterised as a service that is offered on the market. In that respect the beneficiary (directly the municipality or the public purpose society) is behaving like an economic operator competing for individuals' time and money even if it lacks profit motive. Competition exists in the form of other cultural programmes sometimes offered by private entities. Still within the same category one particular and important project in respect of which an application has already been submitted concerns the activity of cultural centres. The project concerns the renovation of a historic building that is part of the world heritage to be used as a cultural centre, where theatre performances, concerts and other cultural events would take place and would house a gallery as well. It appears that some of the activities taking place in the cultural centre, notably theatre performances, popular music concerts...etc. can attract significant number of customers while they are definitely in competition with other theatres or music clubs (potentially in private ownership), not to mention providers of substitutable services such as cinemas. Furthermore some of the buildings being of historic value, they attract tourism even without offering cultural entertainment. Therefore the Commission takes the view that cultural centres qualify as undertakings for the purposes of competition law.

19. Overall therefore in respect of running and managing a cultural site or a building of cultural value the beneficiaries may or may not be considered as undertakings, depending on the circumstances. One of these circumstances is whether the historic building houses a non-economic actor (government agency or foundation).

20. Another activity that might benefit from the scheme is running and managing a museum. The Commission notes that there is an increased effort by museums to modernise themselves, to popularise their content, to make their content more accessible via multimedia tools...etc. While these projects may be encouraged by the public authorities with the indirect public purpose of educating the public, museums nevertheless in effect offer a service on the broader market of cultural entertainment. The Commission also notes that there are more and more exhibitions, which appeal to the broader public and are therefore viable commercially because the theme is related to popular culture and sales of merchandised items forms an integral part of the project. Moreover, some prestigious museums have actually difficulties in accommodating all visitors who often have to queue to get in. These considerations support the approach that indeed museums often offer a service on the market. Private competition exists as well in the form of e.g. private galleries, but also in the form of alternative entertainment services. On the other hand there exist museums that cannot be regarded as being engaged in an economic activity. For example an exhibition of a museum in a small village on local history might not be characterised as offering goods or services on the market. The Commission takes the view therefore that in respect of running a museum some beneficiaries qualify as undertakings for the purposes of competition law while others not.

21. Finally aid will potentially finance the collection and systematisation of items of cultural value and making them accessible to the general public. This activity may occur outside the context
of museum activities; it may for example involve the collection and systematisation of folk songs, their digitalisation and making them available to the public over the internet and in libraries. In general this activity consists in making cultural content – which can be music, paintings, drawings, sculptures, design objects etc. – available to the public free of charge. Even if the appeal of the content could be (but not necessarily) limited, a market for the consumption of such context exists. Consequently this activity is to be qualified as a service by the beneficiaries concerned, which could plausibly be in competition with other providers of the similar content.

22. Accordingly, depending on the actual circumstances some beneficiaries do not qualify as undertakings whereas the rest do. Regarding beneficiaries that do not qualify as undertakings the financing of the beneficiary is does not qualify as aid within the meaning of article 87 of the EC Treaty. The funding in those cases is either a movement of funds within the State or it finances non-economic activities. Aid does not arise either when these beneficiaries spend the funds, because they are obliged to conduct an open and transparent tender ensuring that market prices are paid to suppliers. As a result there will be no advantage and hence no indirect aid to the latter.

23. However, in respect of the remaining beneficiaries the Commission cannot exclude the presence of State aid within the meaning of Article 87 of the EC Treaty on the grounds that they are not undertakings. Furthermore, within the category of running and managing a cultural site or a building of cultural value, it is also possible that the building houses a tenant that qualifies as an undertaking and which indirectly benefits from the renovation. Consequently in respect of these entities the rest of the conditions of Article 87 of the EC Treaty would have to be examined.

24. Concerning the transfer of State resources the projects are ultimately financed from Norwegian and EFTA funds. However, these funds are first transferred to the Hungarian State, which will then become responsible for disbursing it. Further it is the Hungarian authorities that define the criteria of the award of the aid and thus decide which projects and under what conditions will benefit from the aid. Therefore the Commission finds that the measure involves the transfer of Hungarian state's resources. As to the notion of advantage, benefiting from direct grants definitely confers an advantage upon the beneficiaries. The measure is selective because it benefits certain sectors, namely the sector of cultural entertainment, and certain undertakings only. Since by virtue of the grants in question the competitive position of a selected set of beneficiaries is strengthened vis-à-vis their competitors, competition is distorted.

25. Concerning the affectation of trade between Member States, the Commission acknowledges that the effect on EC trade in some cases could be limited. However, the improved cultural establishments may attract tourists and consumers from other Member States (especially those not involving language barriers, i.e. music, dance, galleries) having thereby an effect on tourism within the EC. Moreover, the provision of aid to the beneficiaries may hinder investments from abroad by undertakings that might consider providing similar services in Hungary. The effects on EC trade are evident in the case of major tourist attractions, which additionally offer programmes such as theatre performances and concerts.
26. Accordingly, the Commission takes the view that in respect of the beneficiaries that qualify as undertakings the notified scheme constitutes aid within the meaning of Article 87 (1) of the EC Treaty.

Compatibility of the aid

27. For the parts of the scheme that qualify as State aid its compatibility would have to be assessed.

28. Article 151 of the EC Treaty provides that "the Community shall contribute to the flowering of the cultures of the Member States, while respecting their national and regional diversity and at the same time bringing the common cultural heritage to the fore." "The Community shall take cultural aspects into account in its action under other provisions of this Treaty, in particular in order to respect and to promote the diversity of its cultures."

29. According to Article 87(3) (d) of the EC Treaty, "aid to promote culture and heritage conservation where such aid does not affect trading conditions and competition in the Community to an extent that is contrary to the common interest" may be considered to be compatible with the common market.

30. Therefore aid may be compatible if it has as its purpose cultural conservation, it is necessary for the Community objective as referred to in Article 151 of the EC Treaty and finally it represents a proportional way of achieving this objective ("does not affect trading conditions and competition in the Community to an extent that is contrary to the common interest"). These conditions have to be examined individually.

31. The Commission considers that all the projects eligible for aid in the present scheme as listed in pars 5–6 serve cultural purposes. There are investments – such as a café and restaurant in the cultural centres, and cultural sites – that are not directly related to culture but the Commission considers these to be an integral part of a modern cultural institution or well managed cultural site. Furthermore the Hungarian authorities explicitly limited the scope of eligible costs concerning these ancillary investments to the creation of the interior structure (walls, sewerage…etc), i.e. the costs of installations and equipment necessary for the operation of a café or a restaurant are not eligible. It appears therefore that the scheme genuinely serves the purpose of conservation of cultural heritage.

32. Concerning the issue of indirect aid to the tenants (paragraph 23) the Hungarian authorities confirmed that should a projects concern the renovation of a building where the tenant of the building is an undertaking that is not engaged in a cultural activity will not be eligible for support.

33. The Commission considers that the scheme is necessary for achieving the objective of promoting culture. The Commission recalls that the beneficiaries in question are not-for-profit entities, which lack capital; their own resources are insufficient even for their maintenance. Although in some instances they are in competition with operators that rely completely on the market, the market supply is insufficient to guarantee the quantity and quality of cultural offer deemed desirable by the Hungarian authorities. Accordingly State aid seems to be the only means to realise the projects.
34. The Commission considers that the measure is proportional. The objectives are very narrowly and precisely defined in the form of a quasi-exhaustive list of eligible projects. As a consequence the aid is well targeted and spill-over effects are kept to the minimum. Appropriate arrangements (acceptance of expenses only against proper documentation of costs, detailed description of eligible expenses in individual aid contracts, monitoring and repayment obligation in case of misuse) are put in place to guarantee that aid is actually used for the pursued objectives. The objective of supporting culture is achieved with as little extra distortion as possible as all beneficiaries have to purchase the goods and services necessary for the investments via an open and transparent tender. Furthermore, with regard to cafés and restaurants, their operation will also be tendered out and the winner of the tender has to invest in the equipment thereof. The Commission also notes that in view of the often local character and limited market share of the assisted undertakings, the aid granted is unlikely to produce a disproportionate negative effect on intra-Community trade. Another aspect of proportionality is the incentive effect of the aid. This means that projects in respect of which works have already started without State aid should not in principle benefit from financing, which was not obvious in this case given that the Financing Mechanisms run from 2004 until 2009. However, the Hungarian authorities confirmed that the deadline of 30 April 2009 is for concluding the aid contracts only and that according to the rules of the scheme such contracting must precede the financing and the starting of the projects. It is to be recalled also that most beneficiaries do not have the necessary capital or financial position to be able to borrow, making them unable to start the projects without the financing from the scheme. Thus the Commission finds that the aid measure has an incentive effect and does not replace works that would have happened anyway without state intervention.

IV. CONCLUSION

35. On the basis of the above assessment, the Commission has come to the conclusion that certain parts of the aid scheme do not qualify as aid within the meaning of Article 87 of the EC Treaty, while the parts that do qualify as aid in the same sense are compatible with the common market under Article 87 3) d) of the EC Treaty.

V. DECISION

36. The Commission has accordingly decided not to raise any objections to the above-mentioned measure on the ground that part of the scheme does not qualify as aid within the meaning of Article 87 of the EC Treaty and that the parts that do qualify as aid in the same sense are compatible with the common market under Article 87 3) d) of the EC Treaty.

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Yours faithfully,  
For the Commission

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