Switching to Action: Commission applies State Aid Action Plan to Digital Switchover

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I. Introduction

On 9 November 2005, the European Commission adopted its decision on the State aid which the Federal Republic of Germany had implemented for the introduction of digital terrestrial television in Berlin-Brandenburg (the ‘Decision’).1 This article discusses the Decision, and in particular the guidance provided by the Commission on the practical application of the analytical framework proposed in the State Aid Action Plan,2 and the types of State aid that may be necessary and proportionate to correct market failures in the context of the switchover from analogue to digital terrestrial broadcasting. The Decision sets out how the Commission will assess State intervention in the digital switchover and what types of assistance it will likely accept. (The latter findings may also be interpreted in more general terms, namely how State assistance should be assessed in the context of an identified Community objective.)

Although the case concerned financial assistance granted to commercial broadcasters in Germany, the Commission probably had Lisbon in mind when it assessed the aid. The case provided the Commission with the perfect opportunity to demonstrate how principles and objectives in the renewed Lisbon Strategy3 should be applied in practice.

In general, public assistance should not replace market mechanisms. Thus, the principal question when it comes to supporting switching to digital broadcasting is whether public authorities need at all intervene to accelerate the switchover. The Commission’s belief is that the switchover should indeed be driven by the market but, if left entirely to the market, it risks slowing down. In the Decision, the Commission demonstrates how three factors influence the assessment of State intervention in the digital switchover process.

First, State aid should be targeted at correcting market failures as set out in the Action Plan. Second, any intervention must respect the fundamental principle of technology neutrality confirmed in the Regulatory Framework. Third, the goal is an efficient digitalisation for the benefit of media plurality and consumer choice.

The first factor applies in general to any assessment of State aid. As a direct consequence of the Lisbon Strategy, this factor entails an economic-based analysis, the details of which still need further clarification by the Commission. The second and third factors are both specific to the digital switchover context. A State measure should not target and favor one technology option (e.g., digital terrestrial broadcasting in this case) over others (e.g., cable or satellite digital broadcasts) and it should create appropriate incentives for an efficient switchover.

For consumers, content and services seem to be the main drivers to switch to digital television. On that basis, the Decision gives some guidance on how the switchover can best be facilitated and encouraged and on the appropriate role of public authorities.

The paper is organised as follows. Section II below summarises the Decision. Section III explains the context to the Decision, in particular the digital switchover and Community policy in that regard and the State Aid Action Plan. Section IV outlines the Commission’s assessment of the (in)compatibility of the aid under Article 87(3)(c) EC. Finally, section V concludes and takes a forward looking approach discussing the significance of the Decision in the light of the ongoing State aid reform and digital switchover process.

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3 The Lisbon Strategy was first launched by the European Council in March 2000 as an agenda for reform to make Europe the most dynamic and competitive knowledge-based economy in the world by year 2010. In view of the Mid-Term Review of the Lisbon Strategy the Commission presented its policy recommendations to advance the implementation of the Lisbon Strategy; Communication to the Spring European Council: Working together for growths and jobs – A new start for the Lisbon Strategy, Communication from President Barroso in agreement with Vice-President Verheugen. Brussels, 2.3.3005, COM(2005) 24 final, (‘Renewed Lisbon Strategy’).
II. Berlin-Brandenburg Decision

1. Factual background

On 14 July 2004, the Commission opened proceedings to investigate the Federal Republic of Germany's financing of digital terrestrial television (‘DTT’) in the region of Berlin-Brandenburg following a complaint by the Association of Private Cable Network Operators. In its decision to initiate the formal investigation procedure, the Commission noted that, apart from doubts over the compatibility of the aid with Article 87(3)(c) of the EC Treaty, the aid appeared to infringe the requirement of technological neutrality. Furthermore, the Commission questioned whether the aid could be regarded as compensation for a service of general economic interest.

The aid measure in question was the financial assistance provided to certain commercial broadcasters by the Media Council of the Media Authority for Berlin-Brandenburg (‘Mabb’). Mabb is charged with promoting, among other things, the development of the technical infrastructure for broadcasting and projects for new broadcasting techniques out of its share of the licence fees paid by German television viewers. For the purpose of promoting the digitisation of broadcasting, Mabb concluded a ‘Switchover Agreement’ with the public service broadcasters ARD, ZDF and RBB and the commercial broadcasters RTL and ProSiebenSat.1. This agreement contained the basic features of the switchover, e.g. a schedule for the individual phases of the switchover and the allocation of program channels to the five operators.

Under the Switchover Agreement, Mabb concluded contracts with the commercial broadcasting groups RTL and ProSiebenSat.1 regarding, for instance, allocation of multiplexes (in the case of commercial broadcasting groups that transmit more than one analogue terrestrial channel, the relevant statutes envisaged the allocation not of individual program channels but of entire multiplexes comprising several channels), the financial assistance to be granted by Mabb, as well as an undertaking by the commercial broadcasting groups to transmit via DTT for five years irrespective of coverage. Similar contracts were concluded with FAB and BBC, which were also present on the analogue terrestrial network before the switchover, as well as with broadcasters that were not broadcast on the analogue network, namely Eurosport, Viva Plus and DSF.

In general, these contracts provided for: (i) the allocation of program channels (or multiplexes), and (ii) the grant of financial assistance. Channels on six multiplexes were allocated by Mabb without an open tendering procedure. The remaining capacity on these multiplexes was opened up to tender individually, as well as earmarked for providers of other forms of broadcasting (for instance mobile television transmission). As to the financial assistance, the level of the grants was set independently for each broadcaster: for the RTL Group € 265 000 a year (€ 66 250 per program channel), for ProSiebenSat.1 € 330 000 a year (€ 82 500 per program channel), for FAB and BBC World one third of the fees payable to the network operator with the maximum amount of € 68 167 per year, and for Eurosport, Viva Plus and DSF up to € 65 000 each (equivalent to about one quarter of the network fees).

The financial assistance granted directly to the commercial broadcasters also indirectly benefited the network operator, T-Systems (T-Systems had agreed to operate the multiplexes allocated to the other network operator RBB) and T-Systems was the only bidder for the multiplex intended to cover the entire territory of the Federal Republic). This indirect advantage was a consequence of the undertaking by RTL and ProSiebenSat.1 to broadcast via DTT for five years irrespective of coverage, whereby T-Systems was guaranteed participation by and income from the two major German broadcasting groups.

The financial grants were allegedly designed to ensure media diversity, to safeguard infrastructure competition for digital modes of transmission, to use frequencies efficiently and to develop new services and uses. The amounts granted to the broadcasting groups reflected the fact that transmission of a multiplex is 50 % more expensive than transmission of an analogue channel. As a result, the amounts represented around one third of the fees payable by the broadcasting groups to the network operator, calculated in such a way that the broadcasting groups paid the same fee to the network operator for a multiplex as they previously did for an analogue channel. However, each multiplex had four program channels (i.e., four times the transmission capacity of an analogue channel). The public service broadcasters, on the other hand, were to finance the costs of DTT transmission out of the licence fee income accruing to them.

2. State aid criteria

In the decision that initiated the procedure, the Commission examined whether the financial assistance granted by Mabb could be characterised as State aid within the meaning of Article 87(1) EC which provides that:

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4 According to an agreement between T-Systems and RBB, T-Systems takes over the provision, letting and operation of the technical infrastructure for the transmission of DTT on behalf of RBB.
'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'  

The four criteria required for an aid measure to fall within this definition were assessed as follows in relation to the financial assistance granted by Mabb:  

- State Resources. The Commission found that Mabb should be considered a public body established and appointed by the State to perform a public task and that the advantages granted by this body should be considered State resources. The Commission pointed out that the fact that Mabb was an autonomous institution and that its budget consisted of licence fees collected from TV viewers, i.e. private individuals, did not change that finding. Mabb was established by the State Media Treaty of the Länder of Berlin and Brandenburg with its public task laid down in the State Media Treaty and the State Broadcasting Treaty. It was in accordance with the provisions of the State Media Treaty that Mabb concluded the Switchover Agreement, and the subsequent contracts providing for financial assistance to commercial broadcasters.  

- Economic Advantage. The Commission found that the financial assistance seemed to favour the commercial broadcasters as direct beneficiaries, and the network operator T-Systems as indirect beneficiary. As to the former, the Commission's view was that the financial assistance did not compensate broadcasters for giving up their previous analogue licences because: (i) the assistance was also granted to broadcasters that were not present on the analogue terrestrial network, (ii) Mabb could instead have limited the duration of the analogue licences to the switchover date, (iii) the allocation of DTT channels did, at least to some extent, already compensate for the analogue shutdown, and (iv) the assistance was not designed as a temporary support during the simulcast phase. As mentioned above, the network operator T-System benefited indirectly by way of guaranteed revenue following the agreement by the commercial broadcasting groups with Mabb to broadcast via DTT for five years irrespective of coverage. The Commission further noted that the financial assistance to the commercial broadcasters may have resulted in T-Systems being able to charge higher transmission prices while avoiding the need to charge end-users for access to DTT.  

- Distortion of Competition. The Federal Government argued that the financial assistance did not distort competition because an open and transparent tendering procedure had ensured that any broadcaster or network operator could have benefited from the funding; thus the assistance was not selective. The Commission had doubts that the tender procedure provided adequate protection against a distortion of competition. In relation to the broadcasters, the Commission noted that the majority of licences were not subject to any tender procedure and that the two tender procedures that were held were not sufficiently transparent to exclude a degree of selectivity. At the network level, the Commission found that the tender procedures were characterised by a high degree of uncertainty and lack of transparency together with a strong position of the incumbent terrestrial network operator T-Systems. These factors made it difficult for any company other than T-Systems to submit a bid.  

In addition to the fact that the differences in Mabb’s financial assistance to the respective commercial broadcasters distorted competition between the broadcasters, the Commission considered that the measure had the potential to distort competition in a number of other media sectors. The assistance to the commercial broadcasters in their use of DTT helps them reach a wider audience thereby increasing their appeal to advertisers as against other media. Also, selective support to the DTT platform would mean the artificial development of a transmission technology, which would affect viewers’ decision between the different broadcasting platforms (e.g. DTT, cable, and direct-to-home satellite).  

- Effect on Trade. The Commission noted that both the commercial broadcasting groups, RTL and ProSiebenSat.1, and the network operator, T-Systems, are internationally active and compete with other international companies. Consequently, the financial assistance granted by Mabb affects trade between Member States.

3. Compatibility assessment

Having concluded that the criteria under Article 87(1) EC for a measure to be characterised as a State aid were fulfilled in respect of the grants to the commercial broadcasters, the Commission went on to assess the compatibility of the financial assistance with the common market under Articles 87(3)(c), 87(3)(d) and 86(2) EC.  

At the level of the network operator, the Commission found that although there appeared to have been an indirect advantage granted, it was unable to establish whether there had been an actual transfer of State resources within the meaning of Article 87(1) EC.
a. Necessary and proportionate aid
After having identified potential market failures linked to the digital switchover, the Commission found that the aid granted by Mabb to the commercial broadcasters was not compatible with the common market because it was not necessary and proportionate to address such market failures. The Commission’s reasoning is discussed in more detail below, but the main points can be summarised as follows:
- State aid to reduce the burden of transmission costs is not the appropriate instrument to address the problem of coordination between market players. Limiting the duration of the simulcast phase and achieving a simultaneous switchover may instead be attained by, for example, setting a common expiry date for all analogue licences.
- State aid for broadcasters’ transmission costs is not an appropriate instrument to encourage a prompt switchover and release of frequencies. In the absence of evidence that the aid represents the minimum necessary for broadcasters to switch to DTT, regulatory intervention in respect of the transmission licences would be a less distortive means and would not interfere with the allocation of spectrum and the efficient, economic-oriented use of frequencies.

Since it was the responsibility of the broadcasters to verify whether or not the aid had been notified and approved, the Commission considered it of ‘prime importance’ to recover the aid from the commercial broadcasters.

b. Promotion of culture
Article 87(3)(d) EC allows State aid to promote culture ‘where such aid does not affect trading conditions and competition in the Community to an extent that is contrary to the common interest’. However, as emphasised by the Commission, this provision must be applied narrowly and only in cases where there is a clearly identified or identifiable culture product. The aid granted by Mabb concerned the transmission of broadcasting signals. In dismissing this justification, the Commission noted that the aid was neither related to any particular cultural content that would otherwise not be broadcast nor was it targeted at certain types of broadcasters which would not otherwise be present on the terrestrial platform.

c. Public service compensation
The Federal Government furthermore argued that the transmission of broadcasting channels via DTT qualified as a service of general economic interest (‘SGEI’), and that aid to the commercial broadcasters was justified since they had been entrusted with this SGEI. The Commission dismissed this argument and questioned whether or not it had been made ‘on an ad hoc basis’.

SGEI must be clearly defined by national authorities and must be entrusted explicitly to a particular undertaking. The Commission pointed out that in this case the alleged public service compensation was paid to the commercial broadcasters, which were not charged with any public service tasks.

III. State aid reform and switchover policy
As noted above, the Decision gives interesting guidance as to how the Commission intends to structure its reformed State aid control and how it believes the digital switchover can and should be promoted by Member States.

The Commission’s reasoning in the Decision must be viewed in its proper context, which is why the relevant developments relating to State aid control and the digitisation of broadcasting are outlined below, before coming back to the reasoning in the Decision.

1. State aid control
In view of the developments of the last two decades, State aid policy has gradually established itself as a necessary and important pillar of competition policy. This is reflective of the need to ensure a level playing field for all undertakings active within the European Community. As European markets become more integrated, the distortive effects of State aid are more visible and directly felt. The scope of State aid control is also expanded by the opening up of markets to competition through liberalisation.

Under the EC State aid rules, the Commission assesses whether aid is compatible or not with the common market. As part of this exercise, the Commission will consider whether the aid falls within one of the exemptions contained in Article 87(3)(a)-(e) of the EC Treaty. However, the Commission has a considerable discretion to decide whether the aid is compatible with the common market. Under the theory of compensatory justification, the Commission stated the

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7 European Community Law on State Aid, M.D’Sa, pages 133-136. See also ‘Reforming state aid policy to best contribute to the Lisbon Strategy for growth and jobs’, Knorr, Competition Policy Newsletter Number 2, Summer 2005, noting the Commission’s possibility to elaborate on the interpretation of the common interest.
general basis on which it would exercise its discretionary power under Article 87(3) (then Article 92(3)) EC:

‘if the Commission has to use its discretionary power not to raise objection to an aid proposal, it must contain a compensatory justification which takes the form of a contribution by the beneficiary of aid over and above the effects of normal play of market forces to the achievement of Community objectives as contained in derogations of Article 92(3).’

The ‘grey area’ a discretionary power inevitably creates coupled with an arguably not always consistent application of the State aid rules led to some criticism of the Commission’s practice. Some of that criticism may have influenced the Commission’s proposal to reform the State aid rules, such as:

- No Systematic Economic Analysis. The Commission has been criticised for not applying sufficient economic analysis to State aid control. State aid should be economically necessary to bring about the desired development. The Commission has at times failed to carry out an explicit cost-benefit analysis of the impact of State aid, and examine whether State aid represents the optimal, least restrictive and proportional measure to achieve the stated aim.

- Not Clearly Identifying Market Failures. The Commission has been criticised for failing to establish why the normal play of market forces would not achieve the desired goal.

- Unclear Objectives. The objectives of the Commission’s State aid policy have at times been unclear.

2. Lisbon Strategy and competitiveness

The renewed Lisbon Strategy acknowledges the overall and urgent need for economic growth and competitiveness in Europe. To this aim the Commission has recognised the necessity to get to work with ‘every one of the tools’ at its disposal, including the State aid rules. As a result, State aid has been given an important role in the Commission’s Lisbon Action Programme, which sets out the priorities for the EU and for Member States. The Lisbon Strategy further stresses that modern information and communication technology infrastructures throughout the territory of the EU are a prerequisite for reaping the benefits of a revived Lisbon Strategy.

3. State aid reform

The reform of the State aid rules follows a wider process of economic change. In fact, the Commission believes that the unique tool of State aid control is one of the most important ways in which competition policy can contribute to European competitiveness. The way in which the Commission intends to use State aid control to address the challenges ahead may be summed up in the ‘slogan’ of the Action Plan: ‘less and better targeted State aid’.

There are two limbs to this motto. The first part – ‘less aid’ – refers to the goal of minimising aid, given that while most businesses compete to survive and succeed, others are granted artificial advantage through public support. Such aid prevents market forces from rewarding the most competitive firms, hence overall competitiveness suffers. The second part – ‘better targeted aid’ – refers to the objective to target support so that it fills the gaps left by genuine market failures, hence empowering more undertakings to become active competitors.

The Action Plan rests on long-standing State aid principles, which are clarified and updated. A modernised aspect is the increased emphasis on a refined economic approach, which is a product of the Lisbon Strategy: the promotion of the economic objectives of the Lisbon Strategy requires that State aid is directed, through economic analysis, towards the correction of identified market failures. The Action Plan focuses on the need to identify market failures in order to find the most appropriate State aid measures to address
the specific need while at the same time keeping market distortion at a minimum.\textsuperscript{19}

This economic-focused State aid policy is based on the twin principles of efficiency and equity: (i) ‘efficiency’ meaning that State aid should be used to promote overall growth by targeting the gaps that markets alone will not fill, and (ii) ‘equity’ meaning that State aid should be fairly distributed in view of non-economic objectives. In common for both principles is that they should ensure Member States the best value for money and that measures effectively address identified priorities. In addition, and in response to criticism that the State aid rules are unnecessarily complicated, two further fundamental elements of the reform are transparency and proportionality.\textsuperscript{20}

4. Digital broadcasting

The shift to a digital, knowledge-based economy is a key factor to drive growth, competitiveness and job creation.\textsuperscript{21} To this end, digital television is an important technological development promoting the growing potential of the information society. Consequently, it is not surprising that the Commission strongly supports the development of digital television.\textsuperscript{22} In this respect, the Commission’s intention is to provide orientation to assist Member States in determining which national measures facilitate the digital switch-over process in conformity with EU law.\textsuperscript{23}

There is no set common analogue switch-off date for all Member States. Instead, the Member States have adopted more or less different strategies towards digital switchover. For instance, the United Kingdom started using DTT multiplexes as early as 1998 to develop a pay-TV platform competing with cable and satellite and financed by subscription revenues. Since May 2002, the United Kingdom has offered a variety of free-to-air channels, financed either by public funds or advertising revenues, and it now has the largest DTT-subscriber base in the EU. Recently, late-comers, such as Germany and Italy, have also seen rapid development of digital television. A report for the Commission published in August 2005 remarks that the Berlin-Brandenburg area has achieved a complete migration from analogue to digital terrestrial television. However, the report also comments upon the (then on-going) Commission proceedings against Mabb’s intervention in the Berlin-Brandenburg area as a warning to government agencies that they need to consider the impact that their actions may have on competition between different multi-channel platforms.\textsuperscript{24}

Regarding the role of national authorities in the switchover to digital broadcasting, it is important to note that television broadcasting, except for content, falls under the so-called Regulatory Framework which covers the whole range of electronic communications.\textsuperscript{25} The Regulatory Framework is designed to take account of the convergence of digital technologies that allow everything from phone calls to entertainment to be delivered over many different networks to different devices; PCs, televisions, mobile phones, etc. To this end, the underlying principle is that any regulatory measure should be technology neutral, i.e. applying the same regulatory principles regardless of the specific transmission technology involved.\textsuperscript{26}

The principle of technological neutrality entails that regulation should neither impose nor discriminate in favour of the use of a particular type of network transmission technology. However, the principle does not preclude a Member State from taking proportionate steps to promote specific technologies for transmission of digital television as a means to increase spectrum efficiency.\textsuperscript{27} The Commission urges Member States to assess the need for and the implications of their policy interventions. It is important to keep in mind that digital switchover implies more than a mere technical migration; considering the role of TV in modern societies, the impact is not only economic but also social and political.\textsuperscript{28}

The Commission believes that national switchover plans should adopt a platform-neutral approach to digital television, taking into account competing delivery mechanisms (primarily satellite, cable and terrestrial).\textsuperscript{29} Indeed, digital broadcasting can be supported by various transmission networks; the Commission stresses the principle of technological neutrality in that the digital switchover should be an inclusive process encompassing various networks, business models and services.\textsuperscript{30}

\begin{thebibliography}{9}
\bibitem{19} Speech by Neelie Kroes, (SPEECH/05/440).
\bibitem{20} The Action Plan aims to modernise the State aid control regime into transparent rules and procedures that are as simple, user-friendly, clear and predictable as possible. Speech by Neelie Kroes, (SPEECH/05/440).
\bibitem{23} COM(2003) 541 final, ‘Communication from the Commission on the transition from analogue to digital broadcasting’ (from digital ‘switchover’ to analogue ‘switch-off’), and the related Commission Staff Working Paper.
\bibitem{26} Framework Directive, recital 18.
\bibitem{27} COM(2005) 204 final, ‘Communication from the Commission on accelerating the transition from analogue to digital broadcasting’.
\end{thebibliography}
IV. Assessment of the aid

The Commission provided some guidance on the allowed scope for Government intervention in the digitisation of television broadcasting in an earlier decision relating to Austrian aid measures supporting the digital switchover. However, the Berlin-Brandenburg Decision elaborates on this previous guidance and sets some important limits to Government intervention under the reformed State aid rules. In the Austrian Decision, the Commission focused mainly on describing the objectives and the 'positive elements' of the notified measures, and how the measures coincided with the Commission's policy and Communications on the digital switchover. In the Berlin-Brandenburg Decision, the Commission rather emphasised the types of problems or 'market failures' the digital switchover may imply and which of these may merit State intervention. The Commission in a sense took one step back to clarify its standpoint and set some limits to government support.

As explained above, the Commission assessed the assistance provided by the Federal Government under Article 87(3)(c) EC, i.e. aid to facilitate the development of certain economic activities or certain economic areas. The points that stand out in this assessment are:

- the Commission’s emphasis on its support for the digital switchover and the acknowledgment that the process may be delayed if left entirely to market forces,
- the key role of properly identifying genuine market failures specific to the relevant situation, and
- that the existence of a common Community interest is not a ‘universal justification’ for State assistance.

Two Step Approach. The objective of ensuring fair competition and promoting competitiveness and technological development requires well targeted aid. For this purpose, the Commission followed the two-step approach in the Action Plan when assessing the State intervention.

The assessment must first clearly identify a genuine market failure in the economic activity in question, i.e. the problem to be addressed. In its analysis of market failures specific to the digital switchover, the Commission carefully followed the structured method of the Action Plan. Accordingly, the Commission considered five possible market failures, namely:

i. coordination problems (frequency spectrum is insufficient to transmit analogue and digital TV signals in parallel – the so-called simulcast phase – and all market players must therefore agree on a switchover timetable),

ii. positive externalities (i.e., the general social benefit of more channels and services may exceed the private individual benefit of the incumbent broadcasters in switching),

iii. strengthening of competition between transmission platforms,

iv. risk for network operator, and
v. promotion of innovation and specific advantages of the terrestrial platform.

The conclusion was that only (i) ‘coordination problems’ between the different market players in achieving a smooth switchover process, and (ii) ‘positive externalities’ associated with the freeing-up of frequency spectrum constituted genuine market failures specific to the digital switchover process that could justify State assistance.

The finding of genuine market failures linked to the digital switchover is necessary but in no way sufficient in itself. Although the identified market failures may in principle justify State assistance, and hence a departure from the principle of technological neutrality; the State assistance must ultimately be the appropriate, necessary and proportionate instrument to remedy these market inefficiencies.

It was this latter consideration in particular that led the Commission to the conclusion that the financial assistance by the Federal Government was not justified under the State aid rules. The Commission stated that it was ‘not convinced that the aid is an appropriate, necessary and proportionate instrument to remedy a market failure and to promote the roll-out of [DTT].’

First, the problem that broadcasters need to agree on common dates for switching off analogue transmission and for switching on digital transmission was
not appropriately addressed by the financial support in question. The switchover may indeed be delayed if there is no coordination but, since the broadcasters operate on the basis of licences, such problems could have been resolved by common expiry dates for all analogue licences set by, e.g., Mabb.

Second, the financial assistance was not needed to free up the spectrum by compensating the commercial broadcasters for giving up their analogue licences. Instead of granting financial assistance, Mabb could have limited the analogue licences to the switchover date. Moreover, the commercial broadcasters present on the analogue terrestrial network had already been compensated through the allocation of DTT licences and the Commission did not see that the grant was designed as a temporary support to facilitate the transition. If the financial assistance was viewed as an incentive, the Commission noted that the Federal Government had provided no reasoning or calculations showing that the assistance constituted the minimum necessary for broadcasters to switch to DTT. In fact, the financial assistance (reducing the transmission costs of the broadcasters) influenced the decisions by market operators, thereby potentially distorting the process of spectrum allocation and the efficient use of frequencies.

After having concluded that the financial assistance granted by Mabb was incompatible with the common market, the Commission in the Decision went on to describe what would in general constitute appropriate market assistance during digitisation best serve consumers and viewers to achieve effective competition and a smooth digital switchover?

V. Importance of decision

The Decision is significant mainly for two reasons:
1. In applying the Commission’s general methodology for assessing State measures in support of a common Community policy in line with the Action Plan. Has the Commission, with the Berlin-Brandenburg Decision, provided Member States and market operators with greater legal certainty and clarity as to how State aid control will work?
2. With reference to the Austrian Decision, in providing further guidance on how public assistance during the process of digital switchover should be construed in line with the Commission’s policy on digitalisation and technology neutrality. Will the Commission’s guidance on appropriate State assistance during digitisation best serve consumers and viewers to achieve effective competition and a smooth digital switchover?

1. Analytical framework and legal certainty

The goal is a modernised State aid control regime that efficiently maintains a level playing field for competition in the single market and where rules and procedures are transparent, clear and predictable.

a. Economic approach

Following the modernisation of EC competition rules, the emphasis has been on the compatibility of competition policy with economic learning.

A desire to align State aid control with economic thinking is therefore not surprising, and the Commission’s refined economic-based approach under the Action Plan seems to have received broad approval.

Economic analysis should ensure that State aid is directed towards the correction of identified market failures. In other words, the correct use of an economic-based approach would be as a means to better target

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42 Points 132-133 of the Decision.
43 Speech by Neelie Kroes, SPEECH/05/440.
44 For instance, the newly-created office of the Chief Competition Economist, Lars-Hendrik Röller, in place since 1 September 2003.
State subsidies.\textsuperscript{46} The Commission repeats that market failure is a key element of the economic approach; there is, however, not much guidance in the Decision on what constitutes the other elements.\textsuperscript{57}

Commissioner Neelie Kroes has said that the Commission will put the Action Plan’s principles into practice through a process of issuing further guidance on individual measures. This could for instance take the form of a Commission Communication or further Commission Decisions.\textsuperscript{58} The refined economic analysis guiding State aid control may require further clarification in order to ensure that the other element of the Action Plan is achieved; namely, transparency.\textsuperscript{49}

It has been suggested that the Commission, in State aid cases, should undertake a basic analysis of the degree of market competition and that it should use similar market definition rules and assessments as those applied to other areas of competition law.\textsuperscript{48} This would require a more structured and sophisticated analysis of the definition of the relevant product and geographic market, entry barriers, and so on.\textsuperscript{50}

b. Identification of genuine market failures

The re-orientation of State aid control towards correcting market failures requires in the first place that market failures are properly identified. In this exercise, the refined economic approach constitutes a significant element.\textsuperscript{51} The Commission has noted that much of the challenge in State aid control in fact lies in properly assessing market failures. Indeed, the effectiveness of State aid control depends on how the assessment and balancing of market failures, on the one hand, and competition distortion, on the other, is carried out.

The Decision illustrates how the Commission assesses the existence of market failures specific to the digital switchover. The Commission considered the five potential market failures identified in the Action Plan and applied them to the particular context of the digital switchover in the region of Berlin-Brandenburg. In other words, it is important to determine which market failures are specific to the economic activity in question, i.e. genuine market failures. The Commission in the Decision disregarded three market failures which may have been present, but which were not considered specific to the digital switchover and, thus, could not justify the public assistance in question.

While this economics-based approach is welcome, the Commission’s ‘reformed’ State aid control requires a detailed and clear analysis of the facts and the functioning of the relevant market(s) if it is to deliver transparency and legal certainty for all market participants.

The Commission’s reasoning in the Decision for disregarding certain alleged market failures is fairly brief, but some principles can be discerned:
- The Federal Government had not provided convincing evidence that broadcasting transmission in Berlin-Brandenburg was characterised by a structural problem between competing platforms. Moreover, if there were a competition problem at network level, aid to the network operator would have been a more transparent way of assisting the development of the DTT platform.\textsuperscript{53}
- As regards the potential risk to the network operator, the Commission acknowledged that the Berlin-Brandenburg switchover was the first in Europe and therefore uncertain. However, it then went on to find that ‘there is no particular reason to believe that the market cannot cope with this type of risk’ in view of the launch of other transmission platforms.\textsuperscript{54}
- As regards the promotion of innovation and specific advantages of the DTT platform, the Commission noted that in Berlin-Brandenburg neither the capacity allocation nor the public support measures were focused on any innovative media or telecom services in particular. DTT did not represent a clearly superior technological solution in comparison to other transmission platforms.\textsuperscript{55}

In other words, the State must clearly evidence the market failure in question and chose the most direct means of remedying it.

2. On the way to a smooth switchover?

The digital switchover process is still in a transitional phase, which will significantly impact how the market

\textsuperscript{46} During a conference on 14 June 2005 organised by Wilmer Cutler Pickering Hale and Dorr LLP and the University of Leiden, Professor Claus-Dieter Ehlermann questioned ‘What economists could do to provide a clear method to assess the right amount of aid needed in a given economic context’. Chief Competition Economist Röller pointed out that state aid policy is partly political and economics should not be over-used. (Röller, ‘EC state aid control: the case for reform’, G.C.R, Volume 8, Issue 6, July 2005, pages 37-38.)

\textsuperscript{47} Similar questions were raised by respondents to the Action Plan, Results of the Consultation on the State Aid Action Plan – Detailed Summary (9.2.2006), page 10.

\textsuperscript{48} SPEECH/05/440 Neelie Kroes.

\textsuperscript{49} State Aid Action Plan Consultation document, points 17 and 22.

\textsuperscript{50} For instance, Leonard Waverman argues for a similar approach under state aid rules as under Articles 81 and 82 with an analysis of the degree of market competition, Waverman, ‘State aids: bring back economic analysis’, G.C.R No. 11, Dec. 2003, pages 37-40.

\textsuperscript{51} G.C.R notes that there is not clear how rigorous the new economic-based analysis will be. G.C.R refers to economics consultants stating that, at present, the state aid reform entails minimal market definition and little research into actual effects of aid on competition. (G.C.R, 21 June 2005, ‘Kroes defines her agenda’, www.globalcompetitionreview.com.)

\textsuperscript{52} State Aid Action Plan Consultation document, point 23.

\textsuperscript{53} Points 108 to 112 of the Decision.

\textsuperscript{54} Points 113 and 114 of the Decision.

\textsuperscript{55} Points 115-119 of the Decision.
place will develop. The Commission has called for an acceleration of the switchover process at Member State level, and it has recognised that market forces alone may not be sufficient to drive this process. While it is true that developing services and building infrastructure are mainly tasks for the private sector; it is necessary to create a favourable environment for private investment. This may involve not only developing an investment friendly legal framework, but also stimulating demand, e.g., through State support measures.

State intervention can take various forms, and the choice must be made with care. In general, State aid is only the ‘second best’ option; the preference should always be with alternative less market distortive measures. The chosen measure should create the right incentive and improve the functioning of the market. In this respect, the Commission encourages states clearly to make better use of alternative measures, and the Commission may even want to know whether other policy instruments than State aid have been explored. Having said that, in certain circumstances State aid may be the most appropriate measure in correcting market failures and, thereby, improving the functioning of markets. This is subject to State aid being carefully targeted. State intervention should go to the heart of the distortion. Normally, this means that corrective measures should be as specific as possible in order to prevent unwanted side-effects and that it should seek to address the particular causes of market failure in the industries or sectors they apply. Aid to individual companies is unlikely to be the best method of correcting market failure.

The measures proposed by the Commission in the Decision as appropriate to support the digital switchover have in common that they are designed for and directed at what the intervention specifically seeks to achieve; namely, an efficient roll-out and wider consumer choice. The measures try to address the problems causing delay in the switchover process. To the contrary, the measures adopted by Germany at issue in the Decision were not designed towards specific market failures but targeted at the economic activity of specific broadcasting companies. According to the Commission, the risk associated with these measures was that competition would be distorted in favor not only of the companies in question but also the network operator and the terrestrial platform itself (as compared to, e.g., cable and satellite). Distortion could also occur vis-à-vis other media, for instance, affecting new markets besides free-to-air broadcasting.

Various market studies have found that there seems to be a weak consumer demand for DTT services coupled with ignorance and confusion. Responses to a simple general questionnaire have shown that one of the main obstacles to a speedy switchover is viewers’ unawareness and indifference. Even among young people, who could not imagine a world without the Internet and mobile telephony, the immediate advantages of digital broadcasting are not clear. They are satisfied with what they receive by analogue broadcast, and/or through cable, and do not see the need for digital TV. The US Consumer Electronics Association (CEA) has noted that many people currently purchase sets without digital capabilities because their favourite programming is not transmitted digitally so they do not see the need to spend more for a digital-ready set. Consumers seem to be waiting for the complete and final shutdown of analogue broadcasting. (So the call for a final date for turning off analogue television is perhaps motivated.) However, those who have switched to digital TV are usually well informed, e.g. on the differences in quality between analogue and digital broadcasts.

Having regard to the principle of technological neutrality, an appropriate incentive for an intervening measure in the switchover process would consequently be to encourage and facilitate for consumers to actively make choices. Consumers and viewers should be at the centre of any switchover strategy. The Commission has pointed out that the challenge of the switchover process lies in stimulating demand so that it is in fact such a service-led process. Italy is an example of a country that has successfully used demand-side intervention by subsidising set-top boxes. As one of the last to launch digital terrestrial television, Italy has seen rapid developments and now has one of the highest number of households with DTT.

Furthermore, exploring measures to inform and educate consumers for the purpose of stimulating demand would be in line with the Commission’s call for better use of alternative, general, measures. The
Commission is probably right in stating that ‘the question is not the technological possibilities for service improvement but the market demand to support it’.68

Similarly, the United States has developed a program to subsidise the purchase of digital-to-analogue converter boxes for the purpose of preparing consumers for the end of analogue broadcasts. Through the digital-to-analogue box subsidy program, coupons will be issued to eligible households for the purchase of certain kinds of set-top boxes.69

It is primarily for market players to offer packages of services and equipment that are attractive to viewers. Program-related enhancements, better picture and audio quality, and data and interactive services need to find their way to the consumers.

The European Parliament has also noted that the challenge lies in stimulating demand to ensure that the digital switchover process is led by the range of services on offer. The Parliament stressed that the ‘changing digital environment must be approached from the standpoint of policy objectives, with the aim being constantly to seek to ensure added value for consumers’.70 Ways of addressing the issue of market demand could be, as the Parliament notes, to ensure that consumers are provided with more information about the possibilities offered by digital platforms and the requisite equipment.71 The US Digital Television task force for the Federal Communications Commission similarly believes that consumers have not been sufficiently educated about digital TV and what the coming change means to them.72

The Commission has noted that there are significant costs and difficulties associated with the need, for instance, to develop attractive services to drive demand.73 In the Decision, measures to target this problem, e.g., grants for the development of innovative digital services, are proposed. The Commission also proposes measures intended to facilitate consumer choice, e.g. subsidising the equipment needed to receive digital transmission in the first place. It is recognised that low-cost and widely available set-top boxes is a requirement for a successful switchover.74 Lowering the switching costs for consumers could also take the form of tax incentives with a discounted rate on audiovisual licence-fee for households who have switched to digital, general VAT reduction on all DTV equipment and services (i.e. converters, IDTVs, digital pay TV subscriptions).75

It may be questioned whether the Commission’s detailed guidance in the Decision leaves sufficient room for considerations of the differences that exist between national markets. (The Commission noted, however, that there are ‘numerous possibilities for Member States to actively promote the digitisation of broadcasting’76.) The Commission has acknowledged that each country follows its own switchover path. In respect of costs and difficulties associated with the switchover, the case scenarios vary significantly from one EU Member State to another.77 What may be considered ‘attractive’ content depends on market conditions and varies between countries.78

In conclusion, the Commission wants to accelerate the digital switchover process and acknowledges that to this end market forces may not be enough. Keeping in mind that State aid is no more than the ‘second-best’ option, the central question is why the market does not deliver the desired outcome. The guidance provided in the Decision on appropriate and well targeted public support for the switchover process seems in line with the problems identified on both sides of the Atlantic relating to a lack of consumer demand for DTT services and unawareness of the benefits of digitalisation. In general, government support to stimulate technology neutral demand and ensure full consumer access to digital networks and public services over such networks will be compatible with the EU State aid rules.

69 Congressional Budget Office Cost Estimate, S. 1932 Deficit Reduction Act of 2005, 27 January 2006. Other US measures to support digital switchover include reimbursement of the Metropolitan Television Alliance (an organisation formed by New York City television broadcast station licensees) for costs incurred in the design and deployment of a temporary digital television broadcast system to ensure that New York city area broadcasters can provide the area with digital TV. A program will also be implemented through which eligible low-power television stations may receive compensation toward the cost of the purchase of a digital-to-analogue conversion devices that enable them to convert incoming digital TV signals of their corresponding full-power television stations to analogue format for transmission on the low power television stations’ analogue channels. Low-power television stations will furthermore be reimbursed for upgrading to digital TV technology.
74 Report for the Commission by Analysis.
75 Digital Switchover in Broadcasting – A BIPE study for the European Commission, DG Info Society, Executive Summary, 12 April 2002.
76 Point 130 of the Decision.
78 Report for the Commission by Analysys.
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