Case No: 63768
Event No: 517528
Dec. No: 341/09/COL

EFTA SURVEILLANCE AUTHORITY

EFTA SURVEILLANCE AUTHORITY DECISION
of 23 July 2009
on the notified scheme concerning tax benefits for certain cooperatives

(Norway)

THE EFTA SURVEILLANCE AUTHORITY,[1]

Having regard to the Agreement on the European Economic Area,[2] in particular Articles 61 to 63 thereof and Protocol 26 thereto,

Having regard to the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice,[3] in particular Article 24 thereof,

Having regard to Article 1(2) in Part I and Articles 4(4), 6 and 7(5) in Part II of Protocol 3 to the Surveillance and Court Agreement,[4]

Having regard to the Authority's Guidelines on the application and interpretation of Articles 61 and 62 of the EEA Agreement,[5] and in particular the chapter on business taxation,

Having regard to Decision No 195/04/COL of 14 July 2004 on the implementing provisions referred to under Article 27 in Part II of Protocol 3,[6]

Having regard to Decision No 719/07/COL of 19 December 2007 to initiate the procedure provided for in Article 1(2) in Part I of Protocol 3 to the Surveillance and Court Agreement with regard to the notified scheme concerning tax benefits for cooperatives,

Having called on interested parties to submit their comments[7] and having regard to their comments,

Whereas:

[1] Hereinafter referred to as "the Authority".
[2] Hereinafter referred to as "the EEA Agreement".
[3] Hereinafter referred to as "the Surveillance and Court Agreement".
[4] Hereinafter referred to as "Protocol 3".
[5] Guidelines on the application and interpretation of Articles 61 and 62 of the EEA Agreement and Article 1 of Protocol 3 to the Surveillance and Court Agreement, adopted and issued by the EFTA Surveillance Authority on 19 January 1994, published in OJ 1994 L 231, EEA Supplements No 32 of 03.09.1994. Hereinafter referred to as "the State Aid Guidelines".
[6] Decision 195/04/COL of 14 July 2004 published in OJ C 139 of 25.5.2006 p. 37 and EEA Supplement No 26 of 25.5.2006 p. 1 as amended. The updated version of the State Aid Guidelines is published on the Authority's website: http://www.eftasurv.int/fieldsofwork/fieldstateaid/legaltext/.
[7] Published in OJ C 96 of 17.04.2008 p. 27 and EEA Supplement No 20 of 17.04.2008 p. 44.

I. FACTS

1 Procedure

By letter dated 28 June 2007 from the Norwegian Ministry of Government Administration and Reform, received and registered by the Authority on 29 June 2007 (Event No 427327) and letter from the Ministry of Finance dated 22 June 2007, received and registered by the Authority on 4 July 2007 (Event No 428135), the Norwegian authorities notified the proposed amendments to the rules on taxation of cooperative companies contained in Section 10-50 of the Tax Act, pursuant to Article 1(3) of Part I of Protocol 3 to the Surveillance and Court Agreement.

After various exchanges of correspondence,[8] by letter dated 19 December 2007, the Authority informed the Norwegian authorities that it had decided to initiate the procedure laid down in Article 1(2) in Part I of Protocol 3 in respect of the notified scheme on tax benefits for certain cooperatives. By letter dated 20 February 2008 (Event No 465882), the Norwegian authorities submitted their comments to Decision No 719/07COL to open the formal investigation procedure.

Decision No 719/07COL was published in the Official Journal of the European Union and the EEA Supplement thereto.[9] The Authority called on interested parties to submit their comments thereon.

The Authority received comments from several interested parties.[10] By letter dated 23 May 2008 (Event No 478026), the Authority forwarded these to the Norwegian authorities, which were given the opportunity to react, but decided not to submit further comments.

2 Description of the proposed measure

2.1 Background

In 1992, the Norwegian authorities introduced a scheme concerning special tax deductions for certain cooperatives. According to the scheme, certain cooperatives within the agricultural, forestry and fisheries sectors as well as consumer cooperatives were entitled to tax deductions on the basis of allocations to equity capital. Other forms of cooperatives were not covered by the scheme. The deduction was limited to maximum l5% of the annual net income, and made solely from the part of the income deriving from trade with the members of the cooperative. A deduction corresponding to the maximum allowed would imply a reduction from the normal corporate tax rate of 28% to a rate of 23.8%. The aim of the scheme was to grant a fiscal advantage to the cooperatives on the basis that they were considered to have a more difficult access to equity capital than other undertakings.[11]

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[8] For more detailed information on the correspondence between the Authority and the Norwegian authorities, reference is made to the Authority's Decision to open the formal investigation procedure, Decision No 719/07COL, published in OJ C 96 of 17.04.2008 p. 27 and EEA Supplement No 20 of 17.04.2008 p. 44.

[9] See footnote 8 for the OJ reference.

[10] Section I-5 below.

[11] Section 12.2 of the Proposal by the Norwegian Government of 29 September 2006 (*Ot.prp. nr. 1 (2006-2007) Skatte- og avgiftsopplegget 2007 - lovendringer*).

The scheme was abolished as of the fiscal year 2005. However, in relation to the State Budget for 2007, the Norwegian authorities proposed to reintroduce the scheme in a slightly amended form.[12] Hence, the scheme was notified to the Authority.

2.2 Objective of the scheme

According to the notification, cooperatives must be supported due to the public interest in maintaining undertakings based on principles such as democracy, self-help, responsibility, equality, equity and solidarity as an alternative to limited companies. Thus, in order to ensure the public, intangible interest in maintaining the cooperative societies as an alternative to limited companies, there is a need to compensate the cooperatives for the disadvantage they suffer compared with other companies. The objective of the notified scheme is, according to the notification, to offset some of these disadvantages related to capital supply.

2.3 The proposed measure

The notified measure is laid down in a new Section l0-50 of the Tax Act, according to which cooperatives may be entitled to a tax deduction. The text reads as follows:

"*[…} deduction may be granted for allocations to the collective equity up to 15% of the income. Deduction is only granted with regard to income deriving from trade with members. Trade with members and equivalent trade must appear in the accounts and must be substantiated.*"[13]

According to the Norwegian authorities, the expression "collective equity" does not refer to a balance sheet item of the cooperatives but is a purely fiscal expression. It follows that the collective equity may consist of withheld capital, of bonus funds, which are members' bonus retained in the cooperative in a "subsequent payment reserve"[14] and of individualised funds in the form of a bonus which has been transferred to the members' capital accounts in the cooperative.[15]

"Equivalent trade" is defined in paragraph 3 of Section 10-50 of the Tax Act as fishermen's sales organisations' purchasing from members of another fishermen's sales organisation provided that certain conditions are fulfilled, purchase by an agricultural cooperative from a corresponding cooperative with the aim of regulating the market, and purchases imposed by a State authority.[16]

It follows from the proposed provision that a tax deduction is, in general, only granted with regard to income deriving from trade with members. Hence, no deduction is granted in income from trade with others. As stated in the draft Section 10-50 of the Tax Act, it must be possible to determine the trade with members and equivalent trade on the basis of

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[12] *Ot.prp. nr. 1 (2006-2007) Skatte- og avgiftsopplegget 2007 - lovendringer*.

[13] Unofficial translation by the Authority. The original Norwegian text reads as follows: "*[...] I tillegg kan det gis fradrag for avsetning til felleseid andelskapital med inntil 15 prosent av inntekten. Fradrag gis bare i inntekt av omsetning med medlemmene. Omsetning med medlemmene og likestilt omsetning må fremgå av regnskapet og kunne legitimeres.*"

[14] Section 28 of the Act on cooperatives.

[15] Section 29 of the Act on cooperatives.

[16] The Norwegian authorities have stated that this provision is only relevant for cooperatives whose activities fall outside the scope of the EEA Agreement, cf. letter from the Norwegian authorities of 6 July 2009 (Event No 523765), p. 3. On this basis, the Authority will not go into an analysis of the notion of "equivalent trade".

the accounts of the cooperative. Hence, separate accounting for trade with members and trade with third parties is essential. The cooperative must be able to substantiate trade with members and equivalent trade.

In the notification, the Norwegian authorities estimated that the loss in tax revenue resulting from the scheme would amount to between NOK 35 million and NOK 40 million (approximately EUR 4 - 5 million) for the fiscal year 2007.

2.4 Beneficiaries

The scheme will apply to the cooperatives indicated in paragraphs 2 and 4 to 6 of the proposed Section l0-50 of the Tax Act. It follows from these provisions that the notified scheme mainly includes certain consumer cooperatives and cooperatives active within the agriculture, forestry and fisheries sectors.

Concerning consumer cooperatives, it follows from paragraph (2)a of the proposed Section l0-50 of the Tax Act that only consumer cooperatives deriving more than 50% of the regular turnover from trade with members are to benefit from the notified scheme.

Furthermore, cooperative building societies which are covered by the Act on cooperative building societies[17] may also benefit from the tax deduction. This constitutes an extension of the scheme compared to the one in force until 2005, cf. Section I-2.1 above.

Cooperatives other than the ones expressly mentioned in Section 10-50 of the Tax Act are not to be covered by the scheme. According to the Norwegian authorities, the selection of eligible cooperatives is based on the assumption that there is a strong need for compensation for extra costs in the sectors covered by the notified scheme. The cooperatives in sectors which will not be covered by the scheme are, according to the Norwegian authorities, in general smaller companies with limited economic activity or non-economic activity.

2.5 Definition of cooperatives in Norwegian law

A cooperative is defined in Section 1(2) of the Act on cooperatives[18] as an undertaking

"*whose main objective is to promote the economic interests of its members by the members taking part in the society as purchasers, suppliers or in some other similar way, when*

> *1. the return, apart from a normal return on invested capital, is either left in the society or divided among the members on the basis of their share of the trade with the group, and*
>
> *2. none of the members is personally liable for the group's debts, either in whole or for parts which together comprise the total debts.*"[19]

Furthermore, it follows from Section 3(2) of the Act on cooperatives that the members of a cooperative are not obliged to contribute capital to the cooperative unless the individual member has agreed to this in writing when subscribing for membership or in a separate agreement. This requirement is only set aside if the duty to pay a membership contribution

[17] *Lov 6. juni 2003 No 38 Lov om bustadbyggjelag (bustadbyggjelagslova).*
[18] *Lov 29. juni 2007 No 8l Lov om samvirkeforetak (samvirkelova).*
[19] Translation from the website of the Norwegian Co-operative Centre, www.samvirke.org.

is stipulated in the statutes of the cooperative. In addition, it follows from the same provision that any duty to contribute capital must be limited, either to a certain amount or in some other way.

2.6 The cooperative movement in Norway[20]

There are approximately 4 000 cooperatives in Norway with more than 2 million members altogether. The cooperatives operate mainly in agriculture, fisheries, housing and in the consumer sector, but also in other parts of the economy, such as insurance, transport, energy supply, health care, media etc.

The Federation of Norwegian Agricultural Co-operatives (FNAC) includes 14 nationwide organisations involved in activities such as processing, sale and purchasing of agricultural products and goods used for agricultural production (fertilisers, machines etc.), breeding, credit and insurance. The agricultural cooperatives have more than 50 000 individual members (farmers), about 19 000 employees and the annual turnover is over NOK 58 billion (approximately EUR 6 billion). The agricultural cooperatives are owners of some of the most well-known Norwegian brands like TINE (dairy products), Gilde (red meat) and Prior (eggs and poultry). The main objectives of the agricultural cooperatives are to provide channels for processing and marketing of agricultural produce, and to provide good conditions for access to capital and input items to the production on each farm.

According to the Norwegian Raw Fish Act,[21] the Norwegian cooperative sales organisations have an exclusive right to take care of all first-hand marketing of fish and shellfish, except farmed fish. There are six cooperative sales organisations in this sector. The operational area of each organisation is related either to a geographic area and/or to the species. The cooperative sales organisations are owned by the fishermen themselves. In addition to the marketing functions, the sales organisations also have control functions as to the protection of marine resources. The first hand marketing value of fish and shellfish is approximately NOK 6 billion (approximately EUR 620 million). 90% of all fish and shellfish are exported.

Coop NKL BA is the central organisation for the Norwegian consumer cooperatives. Coop is a grocery chain that has approximately 1.1 million individual members organised in 140 cooperatives. It operates more than 1 350 stores with an annual turnover of approximately NOK 34 billion (approximately EUR 3.6 billion) and around 22 000 employees. The market share is 24% of the market for groceries. Coop is also involved in food processing and cooperates with the other Scandinavian cooperative retail organisations with regard to purchasing and processing. The main objectives of the consumer cooperatives are to provide the members with sound and useful goods and services at competitive prices, and at the same time to be an interest organisation for the members in consumer issues.

The Norwegian Federation of Co-operative Housing Associations (NBBL) is a national membership association representing 86 cooperative housing associations, and comprises 772 000 individual members and 378 000 housing units in close to 5 100 affiliated housing cooperatives. Cooperative housing associations vary in size, counting from 100 to 190 000 individual members. Housing cooperatives hold a significant share of the housing market in the cities, in Oslo the market share is close to 40%, the national average being

[20] The information in this Section is largely based on the website of the Norwegian Co-operative Centre, a centre for information, documentation and advice concerning cooperatives and owned by the main cooperative organisations in Norway, www.samvirke.org.

[21] *Lov 14. desember 1951 No 3 om omsetning av råfisk (Råfiskloven)*, cf. in particular Section 3.

15%. The main objectives are to secure good and suitable dwellings for the members and to work for good and stable conditions for cooperative housing.

2.7 Norwegian rules on corporate taxation and the position as regards cooperatives

The general corporate tax in Norway is currently 28%. The tax is applied to the net taxable income of business entities. It also applies when the income is added to the company's equity capital. However, the Norwegian Supreme Court has concluded that share deposits are not taxable income for the receiving company.[22] The reason is that the contributions are deemed to have been previously taxed as the contributor's income. Hence, whereas an undertaking has to pay 28% tax on equity financed through the undertaking's own income, no tax is paid with regard to deposits from the shareholders or the public. It follows that undertakings organised as limited companies etc. may increase their equity capital by receiving non-taxable share deposits from their shareholders or from the public.

Cooperatives, however, do not have this possibility. According to the Norwegian Act on cooperatives, they cannot issue shares to the public or issue other capital certificates or securities. Furthermore, it is considered that the principle of open membership limits the size of capital contributions that the cooperatives can claim from their members.

According to the notification, the obligations and limitations imposed on the cooperatives by law are seen by the Norwegian authorities as essential and inherent in the cooperative principles. Hence, the Norwegian authorities consider that the lifting of these restrictions would violate fundamental cooperative principles. The Norwegian authorities point out that the Norwegian Act on cooperatives may be stricter on this point than the legislation on cooperatives in other European states. As an example, the Norwegian authorities refer to Article 64 of the EC Regulation on the Statute for a European Cooperative Society[23], according to which the cooperative may provide for the issuing of securities other than shares which may be subscribed both by members and non-members. Nevertheless, the Norwegian authorities consider the restrictions imposed on cooperatives in Norway to be necessary.

3 Grounds for initiating the procedure

By Decision No 719/07/COL, the Authority decided to open the formal investigation procedure with regard to the notified scheme. In the opening decision, the Authority's preliminary view was that the scheme constituted state aid within the meaning of Article 61(1) EEA.

Firstly, the Authority considered that the proposed tax benefit for cooperatives confers an advantage on the cooperatives. Secondly, the Authority considered the tax benefit for cooperatives to be selective and had doubts that it would be justified by the nature or general scheme of the Norwegian tax system. On the basis that the scheme would reduce the corporate tax payable by the cooperatives covered, the Authority expressed doubts as to whether the scheme might not distort or threaten to distort competition. Finally, the Authority expressed doubts as to whether the notified measure could be regarded as complying with any of the exemptions set out in Article 61 EEA and therefore be deemed compatible with the state aid rules of the EEA Agreement.

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[22] Rt. 1917 p. 627 and Rt. 1927 p. 869.

[23] Council Regulation (EC) No 1435/2003 of 22 July 2003 on the Statute for a European Cooperative Society, OJ L 207, 18.8.2003 p. 1.

4 Comments of the Norwegian authorities

The Norwegian authorities argue that the proposed tax deduction does not confer an advantage on the cooperatives. On the one hand, the Norwegian authorities hold that the tax deduction should be considered "*part of a bargain whereby the tax scheme constitutes payments from the State to cooperative companies for adapting to the current legal framework for cooperatives*".[24] The State thereby safeguards the cooperative form as an alternative to limited companies, which is considered as an intangible benefit in the public interest. On the other hand, the Norwegian authorities argue that the tax deduction should be regarded as compensation for the extra costs incurred by the cooperatives due to the restrictions imposed on them when it comes to access to equity capital, considered as a structural disadvantage for the cooperative. The Norwegian authorities state that it is their assumption that the measure in question merely compensates and counteracts the fundamental disadvantage imposed on the cooperatives when it comes to access to equity capital.

With regard to both arguments, the Norwegian authorities state that the scheme is in accordance with the market investor principle. The argument seems to be based on the view that the aid granted under the scheme will not exceed the extra cost involved in operating as a cooperative nor the public benefit of safeguarding the cooperative form.

Furthermore, the Norwegian authorities maintain that the use of a fiscal measure does not prevent the use of the market investor principle, as the form of aid chosen by the State should be irrelevant.

It follows from the practice of the European Courts and the European Commission that the fact that a measure compensates for a disadvantage suffered by an undertaking, does not imply that the measure cannot be regarded as conferring an advantage on the undertaking. According to the Norwegian authorities, this practice does not apply to the present case. All limited liability companies have the possibility to increase their equity by receiving deposits which are non-taxable income for the company. The scheme merely compensates for the disadvantage and puts the cooperatives on an equal footing with other companies. The Norwegian authorities furthermore argue that the present case can be distinguished from the European Commission's decision in the *OTE* case[25] since the tax benefit and the extra cost due to the obligation in the present case occur simultaneously. The Norwegian authorities read paragraph 101 in the *OTE* case as indicating that this might be of importance for the qualification as state aid.

Concerning the selectivity of the scheme, the Norwegian authorities state that the scheme results in treating cooperatives as if the equity had been financed by shareholders. The tax benefit enables the receiving cooperative to allocate the same amount as equity without having to pay tax, as if it had received a similar amount as share deposits. Consequently, in the opinion of the Norwegian authorities, the general rule concerning equity deposits is made applicable to the cooperatives.

Moreover, the Norwegian authorities claim that the notified scheme is in accordance with the EEA state aid rules and the principles expressed in the Commission Communication

[24] Letter from the Norwegian authorities dated 20 February 2008 (Event No 465882), p. 2.
[25] European Commission's decision in Case C 2/2006 *OTE*.

on cooperatives.[26] The Norwegian authorities in particular refer to Section 3.2.6 of the Commission Communication, according to which specific tax treatment of cooperatives may be welcomed.

Finally, regarding distortion of competition, the Norwegian authorities argue that the scheme merely counteracts an existing distortion at the expense of the cooperatives, and therefore presumably improves the efficiency of the markets affected.

5 Comments from third parties

Following the publication of Decision No 719/07/COL to open the formal investigation procedure with regard to the notified aid to certain cooperatives, the EFTA Surveillance Authority has received comments from a number of third parties.

The comments of the French Government refer, in essence, to the special character of cooperatives, and emphasise that the notified scheme is only intended to compensate the cooperatives for their structural disadvantages.

Cooperatives Europe represents cooperatives across Europe and aims at supporting and developing cooperative enterprises. Initially, the organisation refers to the specific identity of the cooperative, recognised by Community authorities. Cooperatives Europe believes that the specific schemes that cooperatives benefit from should not be compared to the schemes that apply to other forms of enterprises since the schemes are the operational translation of the cooperative principles. Furthermore, Cooperatives Europe argue that specific tax arrangements for cooperatives do not have the objective or the effect of establishing unfair competition, but rather are designed to take into account and to compensate for the limitations that are inherent in the cooperative form in a proportionate way. According to Cooperatives Europe, the scheme is justified by a principle of equality as the cooperatives suffer from certain disadvantages, *inter alia* regarding access to capital. Cooperatives Europe considers that the cooperatives are subject to an autonomous legal scheme which takes their specifics into consideration. It is argued that if a tax scheme specific to cooperatives conforms with the logic of the legal system in the Member State, is a consequence of the modes of operational functioning of the cooperative linked to the cooperative principles and values and is proportional to the limitations imposed by these modes of cooperative functioning, it cannot be considered to be state aid or an advantage but is simply a scheme that stems from a logic of functioning that is different from other forms of enterprise and is justified by an equality of treatment between different forms of enterprises. Finally, Cooperatives Europe argues that the scheme compensates for the disadvantages the cooperatives suffer from and thereby recognises the logic of the cooperative system and its rights to compete on an equal footing.

Kooperativa Förbundet, an organisation for consumer cooperatives in Sweden, supports the arguments submitted by Cooperatives Europe.

Confcooperative - Confederazione Cooperative Italiane is an organisation for Italian cooperatives. It highlights the mutualistic aim of cooperatives and in concluding that the Norwegian legislation is in line with that of other Member States which seek to reduce the disadvantages experienced by cooperatives, especially as regards raising capital,

[26] Communication from the Commission to the Council and the European Parliament, the European economic and Social Committee and the Committee of Regions On the promotion on co-operative societies in Europe COM(2004)18 of 23 February 2004, hereinafter referred to as "the Commission Communication on cooperatives" or "the Commission Communication".

underlines that any excess paid in the coop by members remains the property of the member and thus cannot be taxed in the hands of the cooperative.

Legacoop – Lega Nazionale delle Cooperative e Mutue is an organisation for Italian cooperatives in all sectors. Legacoop refers to the surplus of cooperatives being characterised by the members of the cooperative temporarily renouncing their bonus. The organisation considers that the scheme is in line with the civil and fiscal legislation on European cooperatives, and that the scheme will help reduce the disadvantages of the cooperatives with regard to capital supply.

Coop de France is an organisation for French cooperatives in the agricultural sector. The organisation refers to the European legal framework which has recognised the specific role played by the cooperatives, no matter which sector of the economy they are active in and developed instruments which give them legal safety. Further, the organisation argues that the scheme does not constitute aid but simply compensates the cooperatives for the structural disadvantages inherent in their legal form. Moreover, it is argued that the scheme is within the logic of the system, and hence not selective. This is mainly based on the argument that the capital of the cooperatives is indivisible and consists of non-distributed members' profits. Coop de France also refers to the difficulties for cooperatives when it comes to access to equity capital based on the impossibility to issue shares, the limited number of potential members based on the objective of the cooperative and the impossibility for cooperatives to make use of financial instruments.

Landbrugsrådet is an organisation for cooperatives within the agricultural sector in Denmark. The organisation argues that the scheme creates a level and fair playing field between different types of enterprises by respecting the cooperative nature and the cooperative principles. The scheme does not favour the cooperatives, but adjusts a structural disadvantage.

CECOP-CICOPA-Europe represents the industrial and service cooperatives. The organisation argues that the specific schemes that cooperatives benefit from should not be compared with the schemes that apply to other forms of undertakings, as they are based on the principles that govern the cooperatives. It furthermore argues that when the Authority is comparing the situation for cooperatives with other companies it appears to be establishing a hierarchy between the legal forms, with the cooperative scheme being perceived as an exception. This is not in line with the European Treaty or the Regulation on the Statute for a European company. The organisation, with reference to the Commission Communication on cooperatives, contends that the notified scheme takes into account and compensates for the limitations that are inherent in the cooperative form in a proportionate way.

General Confederation of Agricultural Co-operatives in the EU (COGECA) represents the overall economic interest of agricultural, agri-food, forestry and fishing cooperatives in Europe. The organisation refers to the fundamental role of cooperatives in these sectors, which has been recognised by many EU Member States, and to the fact that cooperatives have embedded concern for community (sustainable development) in their statutes. The organisation expresses worry that uniform tax treatment of cooperatives and other undertakings may result in cooperatives adopting other legal types of organisation and therefore creating a more difficult access to the market for farmers.

CCAE Confederarción de Cooperativas Agrarias de España, an organisation for agricultural cooperatives, supports the arguments submitted by COGECA, Coop de France and Cooperatives Europe.

Groupement National de la Coopération is an organisation for the cooperative movement in France. It argues that the beneficial fiscal treatment of cooperatives in France and other European countries is intended to ensure fair competition between cooperatives and other undertakings and does not distort competition. The organisation refers to the distinctive characteristics of the cooperatives, and underlines that cooperatives, in order to exist and evolve, need a certain legal and fiscal framework which takes into account their specifics and the conditions under which they perform their activities. It supports the Norwegian view that the scheme does not confer any advantage on the cooperatives and argues that the scheme will not distort competition as it would not be possible to have identical rules for different forms of undertakings with different characteristics. On this basis, the organisation emphasises that the aid would not be disproportionate.

The Norwegian Standing Committee on Co-operative Affairs (hereinafter referred to as "the NSCC") is an organisation for Norwegian cooperatives. The NSCC initially states that there is a fundamental difference between cooperatives and other legal forms of undertakings, namely that the relationship between the cooperative and its members is different from the one between a limited liability company and a shareholder. This will also affect the tax measures imposed on cooperatives.

The NSCC first argues that the measure does not constitute state aid as it is justified by the nature or the general scheme of the tax system. In this regard, the NSCC argues that cooperatives build up their equity capital by not paying out bonuses to its members. Normally, such surplus must be paid out to the members of the cooperative, as it constitutes in fact a deferred price correction which does not belong to the cooperative but to the members. If a reimbursement takes place, it will be tax deductible for the cooperative. If the surplus is not reimbursed, it will in fact constitute an equity contribution from the members of the cooperative. It is then within the logic of the system that the surplus should be tax exempt irrespective of whether it is set aside as equity capital or is paid back as reimbursement to members. Moreover, the underlying rationale of avoiding that an amount is taxed twice, is applicable. Just as private placements are tax exempt in the hand of the limited liability company as they have already been taxed in the hand of the shareholder, the equity contribution by the member of the cooperative should be tax exempt in the hand of the cooperative as it has already been taxed in the hand of the member. On this basis, the NSCC considers that rather than benchmarking the scheme against the rules on income tax, the legal framework should be the rules regarding shareholders contribution to equity capital.

Second, the NSCC argues that the measure does not represent an advantage as it only compensates for structural disadvantages inherent in the legal structure of cooperatives. The NSCC with reference to the opening decision further argues that it is not relevant whether the structural disadvantages are offset by other elements in the regime on cooperatives in Norway, but that the legal test should be whether the particular disadvantage that the measure is aimed at balancing is offset by other measures.

Third, the NSCC claims that the measure is not selective since the different tax treatment of cooperatives and other undertakings reflects the differences pertaining to company law. Therefore, since the tax measure under scrutiny only applies to entities organised as

cooperatives it only concerns a legal form of an undertaking which is open to anyone. Hence, the measure is not selective.

II. ASSESSMENT

1 Scope of the decision

As set out in Section I-2.4 above, the potential beneficiaries under the scheme are mainly cooperatives active within the agriculture, fisheries and forestry sectors, certain consumer cooperatives and cooperative building societies.

Article 8 EEA defines the scope of the Agreement. It follows from paragraph 3 of Article 8 that:

"*Unless otherwise specified, the provisions of this Agreement shall apply only to:*

> *(a) products falling within Chapters 25 to 97 of the Harmonized Commodity Description and Coding System, excluding the products listed in Protocol 2;*
>
> *(b) products specified in Protocol 3, subject to the specific arrangements set out in that Protocol.*"

On this basis, the agriculture and fisheries sectors to a large extent fall outside the scope of the state aid rules of the EEA Agreement.

Hence, this Decision applies to the proposed tax concession for cooperatives, but it does not deal with cooperatives active in the agriculture and fisheries sectors to the extent that the activities of these cooperatives fall outside the scope of the state aid rules of the EEA Agreement.

2 The presence of state aid

2.1 Introduction

Article 61(1) EEA reads as follows:

"Save as otherwise provided in this Agreement, any aid granted by EC Member States, EFTA States 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 Contracting Parties, be incompatible with the functioning of this Agreement."

The Authority recalls that, as a general rule, the tax system of an EFTA State itself is not covered by the EEA Agreement. It is for each EFTA State to design and apply a tax system according to its own choices of policy. However, application of a tax measure, such as the deduction in the corporate tax for certain cooperatives, may have consequences that can bring the tax measure within the scope of Article 61(1) EEA. According to case law,[27] Article 61(1) EEA does not distinguish between measures of State intervention by reference to their causes or aims but defines them in relation to their effects.

[27] Case E-6/98 *Norway v EFTA Surveillance Authority* [1999] EFTA Court Report p. 76, paragraph 34; Joined Cases E-5/04, E-6/04 and E-7/04 *Fesil and Finnfjord, PIL and others and Norway v EFTA Surveillance Authority* [2005] Report of the EFTA Court p. 121, paragraph 76; Case 173/73 *Italy v*

2.2 Presence of state resources

In order to constitute state aid within the meaning of Article 61(1) EEA, the aid must be granted by the State or through state resources.

The Authority recalls that, according to settled case law, the definition of aid is more general than that of subsidy, because it includes not only positive benefits, such as subsidies themselves, but also state measures which, in various forms, mitigate the charges which are normally included in the budget of an undertaking and which thus, without being subsidies in the strict sense of the word, are similar in character and have the same effect.[28]

According to the notified scheme, the cooperatives mentioned in Section 10-50 of the Tax Act will be entitled to a special form of tax deduction. Hence, these cooperatives may deduct allocations to equity capital from their income. The tax deduction implies that the tax payable by the cooperatives covered by the scheme is reduced. The measure entails a loss of tax revenues for the Norwegian State, estimated by the Norwegian authorities to amount to between approximately NOK 35 and 40 million (approximately EUR 4 - 5 million) for the fiscal year 2007. According to settled case law, a measure by which the public authorities grant to certain undertakings a tax exemption which, although not involving a transfer of State resources, places those to whom the tax exemption applies in a more favourable financial situation than other taxpayers constitutes aid granted by the state or through state resources.[29] Consequently, the Authority finds that state resources are involved in the notified scheme.

2.3 Favouring certain undertakings or the production of certain goods

2.3.1 Selectivity

First, the aid measure must be selective in that it favours "*certain undertakings or the production of certain goods*".

The cooperatives eligible under the scheme are undertakings within the meaning of the state aid rules of the EEA Agreement. According to settled case law, the concept of "undertaking" covers any entity engaged in an economic activity, regardless of its legal status and the way in which it is financed.[30]

In order to determine whether a measure is selective, it is appropriate to examine whether, within the context of a particular legal system, that measure constitutes an advantage for certain undertakings in comparison with others which are in a comparable legal and factual situation.[31]

Commission [1974] ECR 709, paragraph 13; and Case C-241/94 *France v Commission* [1996] ECR I-4551, paragraph 20.

[28] See, in particular, Case C-143/99 *Adria-Wien Pipeline and Wietersdorfer & Peggauer Zementwerke* [2001] ECR I-8365, paragraph 38; Case C-501/00 *Spain v Commission* [2004] ECR I-6717, paragraph 90; and Case C-66/02 *Italy v Commission* [2005] ECR I-10901, paragraph 77.

[29] See to that effect Case C-387/92 *Banco Exterior de España* [1994] ECR I-877, paragraph 14; and Case C-222/04 *Cassa di Risparmio di Firenze and Others* [2006] ECR I-289, paragraph 132.

[30] Case C-222/04 *Cassa di Risparmio di Firenze and Others* [2006] ECR I-289, paragraphs 107 et seq. and the case law cited there.

[31] Case C-487/06 P, *British Aggregates Association v Commission*, paragraphs 82 et seq.; Case C-409/00 *Spain v Commission* [2003] ECR I-1487, paragraph 47; Joined cases C-428/06 to C-434/06 *UGT-Rioja and others*, not yet reported, paragraph 46.

The Authority will hereinafter examine these elements with regard to the tax deduction in favour of certain cooperatives laid down in Section 10-50 of the Tax Act.

Reference framework

In order to classify a tax measure as selective, the Authority must begin by identifying and examining the common or "normal" regime under the tax system applicable which constitutes the relevant reference framework.[32]

In Norway, cooperatives are subject to the generally applicable corporate tax. The objective of the corporate tax is to tax profits (net income) made by companies. However, according to the proposed Section 10-50 of the Tax Act, certain consumer cooperatives, cooperatives active within the agriculture, fisheries and forestry sectors and cooperative building societies are entitled to a deduction of up to 15% of their income deriving from trade with their members. Thus, the tax base of these undertakings is reduced, and thereby also their corporate tax. This tax rule deviates from the normal rules on corporate tax payable by undertakings in Norway.

In the notification, the Norwegian authorities argue that the relevant reference system in the present case is the general framework for capital supply. The Authority is of a different opinion. As the tax exemption for certain cooperatives constitutes a derogation from the generally applicable corporate tax, the Authority finds that the relevant reference against which the notified measure has to be judged is the corporate tax system. Hence, the corporate tax constitutes the relevant reference framework against which the derogation must be measured.

Factual and legal situation

Next, the Authority must assess whether, under a particular statutory scheme (in this case the corporate tax), a state measure is such as to favour certain undertakings or the production of certain goods within the meaning of Article 61(1) EEA in comparison with other undertakings which are in a legal and factual situation that is comparable in the light of the objective pursued by the measure in question.[33]

Accordingly, the Authority must assess and determine whether any advantage granted by the tax measure at issue may be selective by demonstrating that the measure derogates from that common regime inasmuch as the measure differentiates between economic operators who, in light of the objective assigned to the tax system of the State concerned, are in a comparable factual and legal situation.[34]

Following the case law mentioned above, the Authority must therefore assess whether under the corporate tax, the 15 % deduction of the cooperatives' income derived from trade with their members favours certain cooperatives within the meaning of Article 61(1) EEA in comparison with other undertakings which are in a legal and factual situation comparable in the light of the objective pursued by the corporate tax.

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[32] Cases T-211/04 and T-215/04 *Government of Gibraltar v Commission*, not yet reported, paragraph 143.

[33] Case C-75/97 *Belgium v Commission* [1999] ECR I-3671, paragraphs 28-31.

[34] Cases T-211/04 and T-215/04 *Government of Gibraltar v Commission*, not yet reported, paragraph 143 with further references.

As mentioned above, the objective pursued by the corporate tax is to tax profits made by companies.

In this context, the Authority is aware of the specifics of cooperatives. In particular, the Authority notes that according to the Commission Communication on cooperatives, "*[c]ooperatives operate in the interest of their members, who are at the same time users, and they are not managed in the interests of outside investors. Profits are received by members in proportion to their businesses with the cooperative, and resources and assets are commonly held, non-distributable and dedicated to the common interests of members. Because personal links among members are in principle strong and important, new membership is subject to approval while voting rights are not necessarily proportional to shareholdings (one man one vote). Resignation entitles the member to repayment of his part and implies reduction of the capital.*"[35]

Consequently, a pure mutual cooperative is defined, firstly, by a specific relationship with the members of the cooperative, meaning that the members are actively involved in the running of the business of the cooperative, and that there is a large extent of interaction between the members and the cooperative reaching beyond a merely commercial relationship. Secondly, the assets of the cooperative are commonly held by the members and the profits are distributed exclusively among the members of the cooperative based on the members' business with the cooperative.

On the basis of the principles set out above, the Authority does not exclude that pure mutual cooperatives and other companies can be considered not to be in a comparable legal and factual situation where the objective of tax on corporate profits is concerned.

However, in the present case, it appears that the pure mutual character of some of the cooperatives covered by the notified scheme is questionable. A large part of the business of certain cooperatives covered by the scheme is not related to trade with the members, but to trade with other clients. In this regard, the Authority refers to the limitation set out in Section 10-50 of the Tax Act whereby only consumer cooperatives with more than 50% of the regular turnover related to trade with members are to benefit from the notified scheme. In the opinion of the Authority, such prevalently mutual cooperatives are quite different from the pure cooperative model described in the Commission Communication on cooperatives.

In addition, the scheme covers only those cooperatives specified in draft Section 10-50 of the Tax Act, namely certain consumer cooperatives, cooperatives active within the agriculture, fisheries and forestry sectors and cooperative building societies. Only these cooperatives are entitled to a deduction of up to 15% in the part of their income deriving from trade with their members. Consequently, the tax advantage concerned is accorded on account of the undertaking's legal form as cooperative and of the sectors in which that undertaking carries on its activities. It is therefore clear that the measure is selective in relation to other comparable economic operators.

By applying a different taxation on certain cooperatives' profits from trade with their members depending on their sector of activity, the Authority considers that Section 10-50 of the Norwegian Tax Act differentiates between economic operators who, in the light of

[35] Section 1.1 of the Commission Communication on cooperatives.

the objective assigned to the corporate tax system which is taxation of profits, are in a comparable factual and legal situation.

Justification by the nature and logic of the system

According to well-established case law, the concept of state aid does not refer to state measures which differentiate between undertakings and which are, therefore, *prima facie* selective where that differentiation arises from the nature or the overall structure of the system of which they form part.[36] The case law of the EFTA Court and of the Community Courts has established that a specific tax measure intended partially or wholly to exempt undertakings in a particular sector from the charges arising from the normal application of the general system can be justified by the internal logic of the tax system if it is consistent with it.[37]

Therefore, the Authority must determine whether the differentiation between certain cooperatives and other undertakings is none the less not selective because it arises as a result of the nature or general scheme of the system of charges of which it forms part. Hence, whether the differentiations derive directly from the basic or guiding principles of that system.[38]

It follows from case law that it is for the EEA State which has introduced such a differentiation to show that it is justified by the nature or general scheme of the system in question.[39] The Norwegian authorities argue that the tax deduction applicable to certain cooperatives is justified by the nature or general scheme as it implies that the Norwegian system of equity financing for corporations by receiving non-taxable deposits is made applicable also to the cooperatives. In other words, the scheme would be aimed at balancing a disadvantage for the cooperatives which is inherent in their legal form.

In the opinion of the Authority, in the case at hand, the justification provided by the Norwegian authorities that the deduction in the corporate tax rate should be regarded as a compensation for the extra costs incurred by the cooperatives due to their difficult access to capital cannot be considered to fall within the logic of the corporate tax system. Corporate tax is a tax levied on a company's income from normal trade whereas share deposits and other equity deposits are not qualified as income according to Norwegian tax law.[40] Thus, even if the objective pursued by the Norwegian authorities is laudable, it does not seem to derive directly from the basic or guiding principles of the system in which the measure is embedded, namely the tax system. The Authority recalls that according to

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[36] Case 173/73 *Italy v Commission* [1974] ECR 709, paragraph 33; Case C-143/99 *Adria-Wien Pipeline and Wietersdorfer & Peggauer Zementwerke* [2001] ECR I-8365, paragraph 42.

[37] Case E-6/98 *Norway v EFTA Surveillance Authority*, cited above, paragraph 38; Joined Cases E-5/04, E-6/04 and E-7/04 *Fesil and Finnfjord, PIL and others and Norway v EFTA Surveillance Authority*, cited above, paragraphs 84-85; Joined cases T-127/99, T-129/99 and T-148/99 *Territorio Histórico de Alava et a v Commission* [2002] ECR II-1275, paragraph 163; Case C-143/*99 Adria-Wien Pipeline* [2001] ECR I-8365, paragraph 42; Case T-308/00 *Salzgitter v Commission* [2004] ECR II-1933, paragraph 42; Case C-172/03 *Wolfgang Heiser* [2005] ECR I-1627, paragraph 43.

[38] Cases T-211/04 and T-215/04 *Government of Gibraltar v Commission*, not yet reported, paragraph 144 with further references.

[39] Case C-159/01 *Netherlands v Commission* [2004] ECR I-4461, paragraphs 43-47.

[40] Cf. Section I-2.3 above.

consistent case law the objective pursued by state measures is not sufficient to exclude those measures outright from classification as aid for the purposes of Article 61(1) EEA.[41]

Moreover, in the present case, the Authority notes that the notified scheme is not intended to apply to all cooperatives, which in principle should suffer from the same structural disadvantage as pointed out by the Norwegian authorities. On the contrary, the scheme only covers cooperatives in those sectors which are expressly mentioned in the draft Section 10-50 of the Tax Act. The Norwegian authorities have not submitted any arguments showing that the delimitation of the scheme to these cooperatives is in line with the nature and general scheme of the tax system. The preparatory documents to Section 10-50 of the Tax Act simply refers to the cooperatives covered by the scheme as representing the traditional cooperative sectors,[42] a consideration which is not relevant in the framework of corporate taxation. Furthermore, according to the Norwegian authorities, the delimitation is based on an assumption that the cooperatives to be covered by the scheme are in more need of the aid than cooperatives in other sectors. However, the Norwegian authorities have neither submitted any objective information supporting their assumption nor any other objective, substantiated justification for this differentiation.

In line with case law,[43] the Authority considers that the need to take account of certain requirements (in this case the particularities of the cooperatives as organisations), however legitimate, cannot justify the exclusion of selective measures, even specific ones, from the scope of Article 61(1) EEA as account may in any event usefully be taken of the given objectives when the compatibility of the state aid measure is being assessed pursuant to Article 61(3) EEA.

As an additional point, the Authority refers to the comments of the Norwegian Standing Committee on Co-operative Affairs and the observation that a tax exemption for cooperatives could be justified on the basis of double taxation arguments and accordingly fall within the nature and logic of the corporate tax system. However, based on the information available to it, the Authority cannot exclude that there would be situations where the capital would neither be taxed in the hands of the cooperative nor in the hands of the members.

Moreover, with regard to the present case and in the absence of any convincing arguments to the contrary, the Authority is of the opinion that making a favourable tax treatment applicable only for some cooperatives without providing any objective justification for this differentiation cannot be considered to be in line with the logic of the tax system.[44] Even if the tax measure in question determines its scope on the basis of objective criteria, the fact remains that it is selective in nature.[45]

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[41] Case C-241/94 *France v Commission* [1996] ECR I-4551, paragraph 21, Case C-342/96 *Spain v Commission* [1999] ECR I-2459, paragraph 23.

[42] *Ot.prp. nr. 1 (2006-2007) Skatte- og avgiftsopplegget 2007 - lovendringer*.

[43] Case C-487/06 P, *British Aggregates Association v Commission*, paragraph 92.

[44] In this regard, the Authority refers to the European Commission decision in the case concerning a Danish scheme on compensation for CO^2 duty, cf. Case C 41/2006 (ex N 318/2004), not yet published. In paragraph 44 of the decision, the Commission states that the scheme in question only covers some of the undertakings that are in the factual situation that the scheme, according to the Danish authorities, seeks to rectify. The Commission sees this as a derogation from the general logic that the Danish authorities argue should apply and concludes that, therefore, the scheme is not in line with this logic.

[45] Joined Cases T-92/00 and T-103/00, *Territorio Histórico de Álava - Diputación Foral de Álava and others v Commission* [2002] ECR II-1385, paragraph 58

Against this background, the Authority considers that the tax deduction applicable to certain cooperatives derogates from the ordinary corporate tax regime, does not seem to be justified by the nature or general scheme of the system, and must therefore be considered selective.[46]

2.3.2 Advantage

Second, in order to determine whether an economic advantage has been granted to the cooperatives covered by the scheme, the Authority must assess whether the measure relieves the beneficiaries of charges that they normally bear in the course of their business. The Authority is of the opinion that the question of whether the scheme confers an advantage to the cooperatives covered must be considered in the light of the corporate tax system which applies both to lucrative undertakings and to cooperatives, including those not covered by the scheme.

According to the notified scheme, certain cooperatives are entitled to a deduction of up to 15% in the part of their income deriving from trade with their members. Thus, the tax base of these undertakings is reduced, and thereby also their corporate tax. As a result, the measure relieves them of charges that are normally borne from their budgets. This tax rule deviates from the normal rules on corporate tax payable by undertakings in Norway.

The Norwegian authorities and several of the third parties who have submitted comments to the opening decision argue that the proposed tax deduction does not confer an advantage on the cooperatives. Firstly, according to the Norwegian authorities, the scheme is in line with the market investor principle and should be considered as payment to the cooperatives for upholding their legal form, which is of public interest. Secondly, the tax deduction is a compensation for the extra costs incurred by the cooperatives due to the restrictions imposed, in particular with regard to access to equity capital, and it does not involve any overcompensation.

First, concerning the market investor principle, the argumentation seems to be based on the view that the aid granted under the scheme will not exceed the extra costs involved for an undertaking in operating as a cooperative (overcompensation) nor the public benefit of safeguarding the cooperatives. The Norwegian authorities argue that the market investor principle applies where the State purchases intangible benefits for the public interest at market price, at least where the intangible benefit for the State is completely external to the interests of the undertaking concerned.[47]

The Authority considers that there are several reasons why the market investor principle is not applicable in the present case. Initially, the Authority does not agree with the position of the Norwegian authorities that operating as a cooperative does not involve any advantages for an undertaking. In this regard the Authority refers to the Commission Communication on cooperatives, where the European Commission sates, *inter alia*, that

[46] Case C-222/04, *Cassa di Risparmio di Firenze* [2006] ECR I-289, paragraphs 134-138; Case C-148/04 *Unicredito Italiano* [2005] ECR I-11137, paragraphs 48-49.

[47] The Norwegian authorities refer to the Opinion of Advocate General Fennelly in Case 251/97 *French Republic v Commission* to justify their argumentation. According to the argumentation put forward by the French authorities in this case it is possible to argue, in essence, that when the State purchases goods or services or more intangible benefits in the general public interest at market price, there is no aid element at all, or that there is aid which is, at least potentially, compatible, cf. paragraph 20 of the Opinion. The Advocate General, however, did not follow the argumentation of the French authorities in this case.

the cooperative model may be "*a means for building or increasing the economic power of Small and Medium-sized Enterprises (SMEs)*".[48]

Further, the Authority considers that the intangible benefit that the State intends to "purchase" in the present case is the upholding of the cooperative sector in Norway on the present conditions when it comes to restrictions on access to equity capital. The Authority is of the opinion that it is impossible to apply the market investor principle to this case for the simple reason that no private market investor could ever make a similar transaction to the one that the Norwegian authorities are proposing. In this case the State is not acting as a market investor or undertaking. On the contrary, the State is performing its sovereign and administrative functions, the imposition of taxes being one of the key components of these functions. Hence, the Authority cannot see that the market investor principle is applicable.

The Norwegian authorities have also argued that the scheme does not involve overcompensation and that the aid granted does not exceed the public benefit of safeguarding the cooperatives. The Authority notes that the Norwegian authorities have not submitted any figures or other information in this regard, but merely stated that they assume this to be the case. Therefore, the Authority cannot accept this argument.

Second, the Authority will examine whether it can be concluded that the scheme does not involve an advantage for the cooperatives covered by it on the basis that the aid is granted in order to compensate the cooperatives for structural disadvantages. It has been recognised that structural disadvantages may, in certain specific situations, be offset by aid measures.[49] The compensation of a disadvantage has been considered not to constitute an advantage in some situations, in particular where former state-owned monopolists are restructured and turned into market players when opening the market for competition. These precedents refer to a factual situation which is different from the one in the present case. Furthermore, neither the case law of the European Courts nor the practice of the European Commission appear to support that a measure such as the one notified does not confer an advantage on the undertaking in question merely because it compensates a "disadvantage" suffered by the undertaking.[50]

Against this background, the conclusion of the Authority is that the proposed tax concession confers an advantage on the cooperatives covered by the scheme.

2.4 Distortion of competition and effect on trade between the Contracting Parties

As regards the criteria in Article 61(1) EEA on aid which distorts or threatens to distort competition in so far as it affects trade between Contracting Parties, it follows from case law that it is not necessary to establish that the aid has a real effect on trade between the Contracting Parties and that competition is actually being distorted, but only to examine whether the aid is liable to affect trade and distort competition.[51]

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[48] Section 2.1.1 of the Commission Communication on Cooperatives.

[49] Case T-157/01 *Danske Busvognmænd v Commission* [2004] ECR II-917.

[50] Case 30/59 *Gezamenlijke Steenkolenmijnen* [1961] ECR p. 3, 29-30; Case C-173/73 *Italy v Commission* [1974] ECR 709, paragraphs 12-13; Case C-241/94 *France v Commission* [1996] ECR I-4551, paragraphs 25 and 35; Case C-251/97 *France v Commission* [1999] ECR I-6639, paragraphs 41, 46-47 and the Commission's Decisions in Case C 2/2006 *OTE*, paragraph 92.

[51] Case C-372/97 *Italy v Commission* [2004] ECR I-3679, paragraph 44; Case C-66/02 *Italy v Commission*, paragraph 111 and Case C-148/04 *Unicredito Italiano* [2005] ECR I-11137, paragraph 54.

The Norwegian authorities argue that the aim of the scheme is to counter the existing competitive disadvantage for cooperatives when it comes to access to equity capital. On this basis they maintain that the scheme does not distort or threaten to distort competition. The Authority notes that the effect of the scheme is to reduce the corporate tax of the cooperatives covered by the scheme compared to other companies. Thereby, the competitive position of these cooperatives is strengthened. The fact that the cooperatives are subject to certain limitations according to Norwegian law, which are not imposed on *inter alia* limited companies, cannot be decisive in this regard.

Moreover, where aid granted by the State strengthens the position of an undertaking compared with other undertakings competing in intra-EEA trade, the latter must be regarded as affected by that aid. Conversely, it is not necessary that the recipient undertaking itself be involved in the said trade.[52] The proposed tax deduction strengthens the position of the cooperatives in relation to their competitors which are organised differently. The tax deduction applies to all main forms of cooperatives, and at least some of them are also active on markets within the EEA. In this regard, the Authority notes that the consumer cooperative Coop NKL BA has a market share in the market for groceries in Norway of 24%. Furthermore, Coop NKL BA cooperates with the other Scandinavian cooperative retail organisations with regard to purchasing and processing.

On this basis, the Authority concludes that the notified scheme is liable to distort competition and to affect trade between the Contracting Parties to the EEA Agreement.

2.5 The Commission Communication on cooperatives

The Norwegian authorities seem to argue that the notified scheme does not constitute state aid as it is in accordance with the principles expressed in the Commission Communication on cooperatives. The Norwegian authorities refer in particular to Section 3.2.6 of the Commission Communication, where the European Commission *inter alia* states that specific tax treatment of cooperatives may be welcomed. This section reads as follows:

"*Some Member States (such as Belgium, Italy and Portugal) consider that the restrictions inherent in the specific nature of co-operative capital merit specific tax treatment: for example, the fact that co-operatives' shares are not listed, and therefore not widely available for purchase, results almost in the impossibility to realise a capital gain; the fact that shares are repaid at their par value (they have no speculative value) and any yield (dividend) is normally limited may dissuade new memberships. In addition it is to be mentioned that co-operatives are often subject to strict requirements in respect of allocations to reserves. Specific tax treatment may be welcomed, but in all aspects of the regulation of co-operatives, the principle should be observed that any protection or benefits afforded to a particular type of entity should be proportionate to any legal constraints, social added value or limitations inherent in that form and should not lead to unfair competition. In addition any other granted "advantages" should not permit the undesirable use of the co-operative form by non bona fide co-operatives as a means of escaping appropriate disclosure and corporate governance requirements. The Commission invites Member States when considering appropriate and proportionate tax treatment for equity capital and reserves of co-operatives, to take good care that such provisions do not create anticompetitive situations (...)*".

[52] Case C-66/02 *Italy v Commission*, cited above, paragraphs 115 and 117, and Case C-148/04 *Unicredito Italiano*, cited above, paragraphs 56 and 58.

However, the Authority notes that in Section 3.2.7 the Commission Communication goes on to state that "*[c]ooperatives that carry out economic activities are considered as "undertakings" in the sense of Articles 81, 82 and 86 to 88 of the European Community Treaty (EC). They are therefore subject in full to European competition and state aid rules, and also to the various exemptions, thresholds and de minimis rules.*"

On this basis, the Authority is of the opinion that while the specifics of the cooperatives must be taken into account when examining this case, the Commission Communication, read as a whole, cannot be invoked to argue that state aid granted to cooperatives escapes the scope of the state aid rules in the EEA Agreement.

Therefore, the Authority finds that the Commission Communication on cooperatives, read as a whole, does not necessitate any changes to the conclusion that the proposed tax concession confers an advantage on the cooperatives covered by the scheme.

2.6 Conclusion with regard to the presence of state aid

On the basis on the considerations set out above, the Authority has reached the conclusion that the notified scheme concerning tax concessions for certain cooperatives constitutes state aid within the meaning of Article 61(1) EEA.

3 Procedural requirements

Pursuant to Article 1(3) in Part I of Protocol 3, "*the EFTA Surveillance Authority shall be informed, in sufficient time to enable it to submit its comments, of any plans to grant or alter aid (…). The State concerned shall not put its proposed measures into effect until the procedure has resulted in a final decision*".

The Norwegian authorities notified the proposed scheme concerning tax benefits for certain cooperatives by letters dated 28 June 2007 and 16 October 2007 and have not implemented the scheme pending a final decision by the Authority.

The Authority can therefore conclude that the Norwegian authorities have respected their obligations pursuant to Article 1(3) in Part I of Protocol 3.

4 Compatibility of the aid

The Authority notes that the Norwegian authorities have, neither in the notification of the scheme nor in their comments to the Authority's opening decision, submitted any arguments concerning the compatibility of the aid. The Authority has nevertheless assessed the compatibility of the notified measure with Article 61 EEA on the basis of the information before it.

The Authority considers that none of the derogations mentioned in Article 61(2) EEA can be applied to the case at hand.

As far as the application of Article 61(3) EEA is concerned, the tax benefit for cooperatives cannot be considered to fall within the scope of Article 61(3)(a) EEA since none of the Norwegian regions qualify for this provision, which requires an abnormally low standard of living or serious underemployment. Nor does the scheme seem to promote the execution of an important project of common European interest or remedy a serious disturbance in the economy of the Norwegian state, as would be necessary for compatibility on the basis of Article 61(3)(b) EEA.

Concerning Article 61(3)(c) EEA, aid could be deemed compatible with the EEA Agreement if it facilitates the development of certain economic activities or of certain economic areas without adversely affecting trading conditions to an extent contrary to the common interest. The Authority notes that the measure is neither limited to the regions covered by the Norwegian regional aid map nor falls under any of the existing state aid guidelines concerning compatibility with the EEA Agreement on the basis of its Article 61(3)(c).

As no guidelines are directly applicable to the notified scheme, the Authority will assess the compatibility of the scheme directly under Article 61(3)(c) EEA.[53] Derogations within the meaning of Article 61(3)(c) EEA must be interpreted narrowly[54] and may be granted only when it can be established that the aid will contribute to the attainment of an objective of common interest, which could not be secured under normal market conditions alone. The so-called "compensatory justification principle" was endorsed by the Court of Justice of the European Communities in the *Philip Morris* case.[55]

Appreciating the compatibility of state aid is fundamentally about balancing the negative effects of aid on competition with its positive effects in terms of common interest.[56] In order to be declared compatible under Article 61(3)(c) EEA, a state aid scheme must:

- be aimed at a well-defined objective of common interest,
- be well-designed to deliver the objective of common interest, and in that regard, be an appropriate instrument, have an incentive effect, and be proportionate,
- not distort competition and trade in the EEA to an extent contrary to common interest[57].

The Authority must assess whether the objective pursued by the measure is necessary, in line with objectives of common interest and, if so, whether this is the least distortive method of pursuing that objective.

Well-defined objective of common interest

The Norwegian authorities have argued that the ultimate objective of the notified scheme is to ensure that the cooperative form is upheld. The Norwegian authorities argue that facilitating the cooperatives' access to equity capital is essential in order to attain this objective.

The Authority recognises that cooperatives have certain specific features, as set out in the Commission Communication on cooperatives. The Commission Communication states that the promotion of the cooperative model can in principle lead to a more efficient functioning of the economy and have positive social effects. The Commission Communication seems to indicate that in view of the broad equity, social and coordination gains that the cooperative model is considered to provide, and which would not otherwise

[53] Case T-288/97, *Regione Autonoma Friuli Venezia Giulia v Commission* [2001] ECR II-1169, paragraph 72.
[54] Case C-301/96 *Germany v Commission* [2003] ECR I-9919, paragraphs 66 and 105.
[55] Case 730/79 *Philip Morris v Commission* [1980] ECR I-2671.
[56] See the Commission's State Aid Action Plan of 7 June 2005, COM (2005) 107, paragraph 11.
[57] See Commission decision of 24 January 2007 C (2006) 6630, in case N 270/2006, paragraph 67.

be available on the market, maintenance of the cooperative model may be viewed as a common interest objective. Furthermore, the possible role of the cooperative model as a means for building or increasing the economic power of SMEs, providing services that lucrative companies would not provide and contributing to the building of a knowledge-based society is underlined.[58] It should be kept in mind, however, that the definition of a cooperative in the Commission Communication seems to be relatively strict, as the Commission Communication in general seems to concern pure mutual cooperatives.[59]

On this basis, the Authority is of the opinion that the scheme is aimed at a well-defined objective of common interest, to the extent that it is aimed at pure mutual cooperatives.

Well-designed scheme

The second step is to assess whether the aid is properly designed to reach the objective of common interest pursued, in this case to ensure that the cooperative form is upheld by facilitating the cooperatives' access to equity capital.

A distinction could be made between pure mutual and non-pure mutual cooperatives, mutuality being the key hallmark of cooperatives. The stronger the cooperative is characterised by mutuality the more the cooperative could be regarded as different from lucrative undertakings. Therefore, the objective of common interest of upholding cooperatives as defined in the Commission Communication on cooperatives can best be reached by granting aid to cooperatives which are truly mutual.

Concerning the concept of mutual cooperatives, the Authority has doubts as to whether it would be sufficient in order for a cooperative to qualify as a mutual cooperative in the sense of the Commission communication on cooperatives that the cooperative trades mainly with its members. The Authority is of the opinion that the qualification of a cooperative as truly mutual would also depend on a number of other factors, such as the frequency of contacts between the cooperative and the members; the active involvement of the members in the running of the cooperative; the active involvement of the members in the management and decision making of the cooperative; the non-automacy of membership in the cooperative, but active application and approval from existing members; large part of the bonuses paid to members in proportion to the profits; large parts of benefits reserved for members in comparison to benefits for clients that are not members; etc. In the view of the Authority, an assessment of whether a cooperative is genuinely mutual would have to take into account these and similar criteria.

The Authority notes that some of the cooperatives to be covered by the present scheme are pure mutual cooperatives whereas others are prevalently mutual cooperatives. With regard to consumer cooperatives it is stated in the draft Section 10-50 of the Tax Act that only prevalently mutual consumer cooperatives are covered by the scheme.[60] Thus, in the present case it appears that the pure mutual character of some of the cooperatives covered by the notified scheme is questionable. For instance, a large part of the business of certain cooperatives covered by the scheme, in particular the consumer cooperatives, is not related to trade with the members, but to trade with other clients. Furthermore, due to the size of some of the cooperatives covered, the active involvement of the members in the running

[58] Section 2.1.1 of the Commission Communication on cooperatives.

[59] Section II-2.3.1 above.

[60] This condition is not applicable to other cooperatives, and the Authority has no information as to whether any non-prevalently mutual cooperatives in other sectors are to be covered by the scheme.

of and management of the cooperative will be limited. In addition, membership seems to a large extent to be automatic, at least with regard to consumer and housing cooperatives. Hence, in the Authority's view, the scheme is not designed only to cover cooperatives with a particularly strong mutual identity.

Furthermore, in relation to the assessment of whether the scheme is well designed to reach the objective of common interest, it must be considered whether the targeted activity entails any additional costs which are compensated by the aid. The Authority notes that the Norwegian authorities have not provided any data allowing the Authority to quantify, in a direct or indirect manner, the costs involved for an undertaking in assuming the cooperative form. Hence, it is also not possible for the Authority to assess whether the aid is necessary and proportionate to the objective pursued.

On the other hand, the Authority notes positively that the proposed tax deduction will, according to the notification, only be granted with regard to income deriving from trade with members and equivalent trade. Moreover, the notified scheme requires separate accounting for trade with members and trade with other parties in order for cooperatives to receive aid under the scheme.

Nevertheless, for the above mentioned reasons, the Authority has doubts as to whether the notified scheme is well-designed to reach the objective of common interest which is to uphold the cooperative form, and in particular pure mutual cooperatives, by facilitating the access to equity capital.

No distortion of competition and trade in the EEA to an extent contrary to common interest

Finally, it must be assessed whether the potential to distort competition and trade in the European Economic Area is of a nature contrary to the common interest.

Concerning the potential distortion of competition and trade, the Authority notes that the scheme must be classified as operating aid as it relieves the beneficiaries of charges normally borne by undertakings in the ordinary exercise of their commercial activities, in this case, the corporate tax.

Operating aid may only exceptionally be considered compatible with the EEA agreement if it allows fostering a common interest objective that otherwise could not be reached. The Authority questions whether the objective pursued by the Norwegian authorities of upholding the corporate form of cooperatives by facilitating their access to equity capital could not have been reached with other, more proportionate, measures. In particular, the Authority stresses the fact that some of the cooperatives covered by the scheme are large undertakings operating in highly competitive markets within the EEA.

Conclusion

As stated above, the Authority considers that the scheme would be aimed at a well-defined objective of common interest, at least to the extent that it is aimed at pure mutual cooperatives. However, it appears that the pure mutual character of some of the cooperatives covered is not given. Hence, the Authority is of the opinion that the aid cannot be considered to be well targeted. In addition, the Authority is not in a position to assess whether the aid is necessary and proportionate to the objective pursued.

On the basis of the above, the Authority finds that, even though the objective of the scheme can be considered a well-defined objective of common interest, the Norwegian authorities have not demonstrated that the positive effects of the aid will outweigh its negative effects. Therefore, the scheme cannot be considered to be compatible with Article 61(3)(c) EEA.

5 Conclusion

On the basis of the foregoing assessment, the Authority considers the notified tax exemption for certain cooperatives to be state aid incompatible with the state aid rules of the EEA Agreement.

The Authority would like to stress that the present decision, as set out in Section II-1 above, does not apply to cooperatives active in the agriculture and fisheries sectors to the extent that the activities of these cooperatives fall outside the scope of the state aid rules of the EEA Agreement.

HAS ADOPTED THIS DECISION:

Article 1

The planned scheme concerning tax exemptions for certain cooperatives constitutes state aid which is incompatible with the functioning of the EEA Agreement within the meaning of Article 61 EEA.

Article 2

The notified scheme may not be implemented.

Article 3

This Decision is addressed to the Kingdom of Norway.

Article 4

Only the English language version is authentic.

Done at Brussels, 23 July 2009

For the EFTA Surveillance Authority,

Per Sanderud
President

Kristján Andri Stefánsson
College Member