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FISKERI- OG KYSTDEPARTEMENT

Royal Ministry of Fisheries and Coastal Affairs

EFTA Surveillance Authority
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Your ref.	Our ref.	Date
Event nr 593787 Case nr 68781	201000784- /TA	11 October 2012

Norwegian fish farming – regulation concerning distribution of production capacity

Dear Ms. Sabine Monauni-Tömördy,

Reference is made to previous correspondence in this case, in particular the letter of formal notice from the EFTA Surveillance Authority of 11 July 2012 concerning distribution of production capacity in Norwegian fish farming. The Norwegian Government will in the following provide our observations.

1. SUMMARY

Firstly, we would like to emphasize our principal position that fisheries and aquaculture policies are not part of the EEA Agreement. Although the EEA Agreement does contain certain specific regulations applicable to fisheries and aquaculture, fish products, including farmed salmon and trout, fall outside the scope of the Agreement, cf. Article 8(3) EEA. The relevant provisions of Regulation no. 1800 of 22 December 2004, concerning distribution of production capacity for these products, fall outside the scope of the EEA Agreement, and should be treated accordingly. Hence, it is the Government's opinion that EEA law does not limit Norway's discretion to distribute the production capacity of fish farming, whether assessed under the provisions on the free movement of goods (section 3.1 below) or under the provisions relating to establishment (section 3.2 below).

Should the general provisions of the EEA Agreement nevertheless be applicable, it is submitted that the production capacity regulation is compatible with the EEA Agreement, as it is suitable and necessary in order to fulfill important social objectives

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relating to, inter alia, regional policy and a just allocation of the benefits stemming from the use of common sea areas (section 4 below). As indicated by the Authority, the Government has under any circumstances a certain scope of freedom and discretion within the EEA Agreement, should the Agreement be applicable to this case.

2. INTRODUCTORY REMARKS

The Authority's description of the relevant national aquaculture legislation in section 3 of the letter of 11 July 2012 seems to be adequate. The Government would, however, like to clarify a few points.

The Government would like to point out that the Authority's description does not represent an exhaustive description of relevant measures implemented by the Government to contribute to regional policy objectives and a just allocation of benefits stemming from the use of common sea areas.

> One example of such other measures is the criteria used in the 2009 license allocation round, where small fish farmers, and farmers planning for increased processing with the aim of economic integration in rural coastal districts in Norway, were given priority.[1]
>
> Another example is a provision in the regulation on aquaculture, which offers advantages for farmers who have production in two neighboring administrative regions, provided that they have a certain degree of processing activity in coastal districts above the normal processing levels.[2]

Even though these examples represent regional policy measures, it is important to note that they will not suffice to reach the regional policy objectives of the Norwegian Government. A sound regional policy requires a multiple of supplementary instruments, and the production capacity regulation discussed in the present case plays an important role in the overall policy in this field.

Aquaculture activity plays an important long term role in the economy of fragile coastal regions in Norway. It is therefore recalled that the general purpose and scope of the Aquaculture Act is to promote the profitability and competitiveness of the fish farming industry within the framework of sustainable development, and to contribute to value creation along the Norwegian coast. This purpose and scope has also been an essential part of previous fish farming legislation, such as the Aquaculture Act's predecessor, the Fish Farming Act of 1985. The current provisions concerning distribution of production capacity are in principle based on the Fish Farming Act, as amended in 1991.

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[1] Forskrift om tildeling av løyve til havbruk med matfisk av laks, aure og regnbogeaure i sjøvatn i 2009.
[2] Forskrift om drift av akvakulturanlegg (akvakulturdriftsforskriften) § 48a.

Ownership regulations and production capacity regulations in Norwegian fish farming have in the past been restrictive although the last three decades have seen an easing of the regulations.[3] As further elaborated in our letters of 29 October and 23 December 2010, we would like to remind the Authority that Norwegian ownership regulations have been amended several times during the past 25 years, most importantly in 1985, 1991, 2001 and 2005. The regulations have gradually changed from a very strict system, prohibiting the fish farmers from owning more than one license, to today's balanced regulations. This liberalization has been part of the Government's policy to promote the industry's ability to develop, innovate and compete.

As a further introductory remark, the Government would like to emphasize the aim of the provisions concerning production capacity in Section 3 of the Regulation. These provisions seek to balance the objectives of competitiveness and freedom for the industry with equally important objectives relating to, *inter alia*, regional policy and a just allocation of the benefits stemming from the use of common sea areas. Based on the Authority's letter of formal notice, it is also emphasized that the production capacity regulation is neutral when it comes to the nationality of fish farmers and other participants in the aquaculture sector (section 4 below).

Furthermore, we would like to make the Authority aware of an inaccurate translation on page 9, head 5.2.1 in the Authority's letter of 11 July 2012, which is a point that may seem to have misled the Authority. The Authority holds that the circumstances behind the Regulation were inter alia *"...foreign control over the Norwegian Aquaculture industry, and through that, Norwegian natural resources"* (emphasis added). It is indicated that protection of national industry was the underlying aim of the regulation and that this warrants a more careful assessment. It is true that the need for Governmental control in the sector was highlighted through the sale of Hydro Seafood. That does not mean, however, that the aim was a particular control of foreign industry or the protection of national industry. Importantly, the word "foreign" cited by the Authority simply does not exist in the original text, stating the need for "... *control with the aquaculture industry*".[4] It is therefore in the Government's opinion not appropriate to state that the underlying aim was the protection of national industry. In any event, the Government recalls that the legitimacy of a national measure does not primarily depend on the statement made by the legislator, but on whether the rules in question, viewed objectively, actually promote the objectives.[5]

Finally, the Government recalls that the provisions on production capacity do not represent a regulation of ownership in the involved companies, e.g. in the form of a total

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[3] See our letter 29 of October 2010, section 2 Historical overview.

[4] The original Norwegian text reads: *"De bakenforliggende forhold var salget av Hydro Seafood til nederlandske Nutreco og den debatt dette skapte i forhold til kontroll med norsk havbruksnæring"*. Even the phrase "natural resources", found in the quote in the Authority's letter, is not in the original text.

[5] E.g. Joined Cases C-49/98, C-50/98, C-52/98 to C-54/98 and C-68/98 to C-71/98 *Finalarte and Others*, paras. 40-41.

amount of shares permitted etc. Thus, the present case deviates from ownership cases previously assessed by the Authority, such as the case relating to local ownership in the aquaculture sector[6] as well as the case against Norway regarding restrictions on ownership in financial services infrastructure institutions.[7]

3. THE PRINCIPAL POSITION: THE GENERAL EEA LAW PROVISIONS ARE INAPPLICABLE

3.1 The production capacity regulation should be assessed under the goods chapter

The Authority concludes in the letter of formal notice of 11 July 2012 that the national measures in this case are not to be assessed under the rules of free movement of goods in the EEA agreement.

There is no doubt that farmed salmon and trout fall outside the product coverage of the EEA Agreement cf. Article 8(3) EEA. In practice, this is reflected in the dumping and subsidy investigations the European Commission has opened under WTO rules against Norwegian salmon, one in which a WTO dispute settlement panel gave a ruling in 2007.[8]

The Government maintains the position that the production capacity regulation should be assessed under the provisions on *goods* in the EEA Agreement, and not under the provisions on *establishment*. If this understanding of the scope of the goods provisions is applied, there is no relevant EEA provision making the production capacity regulation incompatible with EEA law. Notably, neither Article 20 EEA nor Protocol 9 to the Agreement hinders the present regulation which – seen in the EEA context – should be viewed as a potential restriction of the export of salmon and trout.

The Authority seems to reject the Government's reasoning by arguing that the product capacity regulation neither has the objective nor the effect of restricting the cross border flow of products, and that Article 12 EEA on export restrictions only relates to direct or indirect discrimination of exported goods and goods sold on the domestic market. The Government submits that these points may be relevant in determining whether a national measure would be compatible or incompatible with Article 12 EEA. They are not, however, decisive in determining under which set of rules the national measure should be assessed. Hence, it seems necessary to reiterate some of the arguments previously presented to the Authority.

It is recalled that aquaculture production licenses for salmon and trout are limited by Maximum Allowed Biomass (MAB), i.e. the maximum biomass permitted to be in the

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[6] ESA ref. no ESA063.400.001

[7] EFTA Court Case E-9/11.

[8] EC — Salmon (Norway) (Panel) 16 November 2007.

water at any point of time. This is a means of regulating and curtailing the production of salmon and trout. Indeed, the Authority does not seem to question that the maximum production capacity, represented by the MAB is to be assessed as a goods issue falling within the particular regulation of aquaculture in the EEA Agreement.[9]

It is also recalled that the MAB that each company may control correlates with the possible production from its fish farms. The Regulation concerns the production capacity and hence how much fish that may be produced, and thus for each company the share of the total MAB in Norway.

By assessing the production capacity regulation under the applicable EEA provisions on *goods*, the Government follows the relevant case law from the EFTA Court and the Court of Justice. This case law clarifies that national provisions relating to the *production* of goods are indeed assessed under the provisions on the free movement of goods. These cases are assessed solely under the free movement of goods provisions, irrespective of whether they relate to a prohibition against certain production,[10] a production monopoly[11] or production quotas.[12] As in the present case, the key appears to be that the national measures were aimed directly or indirectly at the products in question, and not whether the measures would also imply limitations on the establishment of other undertakings. For instance, a monopoly in producing, importing or exporting a product, effectively hinders competing companies from being established. Despite this, none of the cases are assessed under the provision on establishment. The same approach must be correct in the present case, as the Regulation is aimed at the product fish, and the purpose is to regulate the conditions for the production and sale of fish. Consequently, the product element of the measures represents their "centre-of-gravity". As mentioned above, it should be recalled that the provisions do not represent a regulation of ownership in the involved companies, e.g. in the form of a total amount of shares permitted etc.

The arguments presented by the Authority, mentioned above, may indicate that the production capacity regulation would indeed have been *compatible* with the EEA provisions on the free movement of goods, even if salmon and trout were within the product scope of the Agreement. That is, however, a different question than the one relevant here; namely whether the national measure is to be *assessed* under the goods provisions.

It is true, as held by the Authority, that case law on the parallel to Article 12 EEA has focused on the national provisions *"specific object or effect in affecting patterns of exports"*.

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[9] Letter 14 February 2012, page 10.
[10] E.g. case 15/79 *Groenveld* (concerning a national prohibition for manufacturer of sausages on having in stock or processing horsemeat).
[11] E.g. the gas and electricity monopoly cases, Case C-154/94 *Commission v. France*, Case C-157/94 *Commission v. Netherlands*, and Case C-158/94 *Commission v. Italy* (exclusive rights of production, imports or exports).
[12] E.g. Case 148/85 *Forest* (concerning annual milling quotas for common wheat).

The ECJ continues, however, by stating that *if* that is the case, the measure is "thereby" discriminatory and hence incompatible with the export provision.[13] If, on the one hand, the national measure *does* regulate export in a particular way compared with domestic trade (directly or indirectly), it does constitute a discriminatory export restriction.[14] If, on the other hand, the specific object or effect of the national measure is *not* the patterns of exports, this does indeed not in itself imply that the measure should be assessed under a different provision. It simply implies that the national measure is compatible with the EEA Agreement, because it does not constitute a measure contrary to Article 12 EEA.[15]

The same should be the case for the production capacity rules that should be assessed under the goods provisions, even if no specific export related aim or effect is detected. That being said, the Government recalls that the overall production capacity regulation has as its aim and effect to regulate and limit the production and hence also the export of salmon and trout.

The Government notes, furthermore, that the national measure in the cases mentioned above, all of which are assessed only under the goods provisions, may easily be formulated in the same manner as the contested provisions in the present case. For instance, a production quota system, as the one assessed in *Forest,* implies a set total production capacity and a division of this capacity between a number of companies. The Authority has not explained why the national measure in *Forest* should be treated differently from the present case in which the total MAB represents the total production capacity, whereas Section 3 of the Regulation ensures the distribution of this capacity between the fish farmers.

The conclusion that this kind of regulation should be assessed solely under the goods provisions is particularly warranted in cases where the State Parties are provided with additional discretion under the goods provision. A parallel application of the other freedoms would in such circumstances undermine the deliberate choice to provide the State with additional legislative freedom. The particular features of fisheries and fish farming must be respected, as this forms the basis for the scope of the EEA Agreement as reflected in Article 8(3) EEA. Other parts of the EEA Agreement than part II cannot therefore be applicable if this would result directly or indirectly in calling into question the discretion of the states within this field. It is recalled that the EFTA Court in *Pedicel* confirmed that Article 8(3) EEA is not limited to the goods chapter. As stated by the EFTA Court, a broader interpretative approach is necessary, and without applying the general principles of a dynamic and homogeneous interpretation.[16]

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[13] The same "formula" is used in all the cases cited by the Authority on this point, see Case 15/97 *Groenveld*, para. 7; Case 388/95 *Belgium v. Spain*, para. 41; and Case C-205/07 *Gysbrecht*, para. 40.
[14] Case 388/95 *Belgium v. Spain*, para. 42; and Case C-205/07 *Gysbrecht*, paras. 41-44.
[15] Case 15/97 *Groenveld*, paras. 8-9.
[16] Case E-4/04 *Pedicel AS v. Sosial- og helsedirektoratet,* paras. 28 and 33.

In the present case, the production capacity regulation, including the distribution of the capacity, is inseparably linked with the produced goods, goods falling outside the scope of the EEA Agreement. Indeed, the present case is different from *Pedicel* on some points. One of these differences is that *Pedicel* concerned a specific service (advertisement) that in principle is something different than the goods to be sold (wine). It was due to the close link between trade in and advertisement for wine that even advertisement services fell outside the scope of the EEA Agreement. In the present case, the capacity production regulation defines how much of the goods (salmon and trout) that may be produced by the fish farmer. The regulation is therefore an integral part of the regulation of the products, salmon and trout, and how these may be produced.

A parallel may finally be drawn to the Courts' case law on authorization schemes. These are national measures that typically affect the production or distribution of goods, as well as the conditions for establishment and/or the offering of certain services. However, these measures will often fall under the *Keck* doctrine of *certain selling arrangements*, implying that they fall under Article 11 EEA only if directly or indirectly discriminatory. Such authorization schemes, if non-discriminatory, seem to be fully compatible with EU/EEA law without an assessment of the impact on the other freedoms being relevant, even if – or perhaps rather because – these other freedoms may also encompass purely non-discriminatory measures.[17] Indeed, a supplementary assessment of stricter provisions on the other freedoms would in such a case call into question the particular reasons for the case law developed under the goods provisions.

For the reasons set out above, the Government maintains its position that the production capacity regulation should be assessed as an integral element of the regulation of the fish products that fall outside the scope of the general EEA provisions on the free movement of goods. As there are no other provisions applicable to the issues assessed in the present case, EEA law does not call into question the contested Regulation.

3.2 Article 31 of the EEA Agreement is not applicable

In the letter of formal notice, the Authority assumes, contrary to the assessment of the Government, that the Regulation must be assessed as a potential restriction on establishment. The Government submits that even if assessed under the rules on establishment, the Regulation nevertheless falls outside the scope of Article 31 of the EEA Agreement.

3.2.1 Scope of the EEA Agreement

The Authority maintains that it *"follows from the very existence of the sectorial adaptations of Annexes VII (establishment) and XII (capital) [...] that the freedoms of establishment*

[17] See e.g. Case E-5/96 *Ullensaker kommune m.fl. v. Nille AS*, paras. 26-27; and Case C-162/97 *Nilsson et al.*, paras. 28 and 31

and capital movement are, if not covered by the special adaptations, fully applicable, regardless of whether the object of acquisition or investment falls outside the product scope of Article 8(3)".[18] The Government disagrees with this interpretation of the EEA Agreement.

The Authority submits that the Regulation must be assessed under Article 31 EEA. In the following, the Government will consequently focus its response on this provision. The Government would, however, like to underline that the response would be equally valid in an assessment under Article 40 EEA.

When assessing the scope of the EEA Agreement in relation to fisheries and aquaculture, it should be emphasized that the Contracting Parties clearly aimed at limiting the scope of the Agreement with regard to the States` fishery policies. This political intention is held, *inter alia*, in Protocol 46 to the Agreement, stating that *"the Contracting Parties will seek to develop this cooperation on a harmonious, mutually beneficial basis and within the framework of their respective fisheries policies"*. The Government recalls furthermore, as stated *inter alia* in the Joint Declaration to Protocol 9, that the EFTA States have not adapted the Common Fishery Policy, which is a policy that encompasses the aquaculture sector.

Furthermore, and as mentioned above, it follows from Article 8(3) EEA that, unless otherwise specified, the scope of the EEA Agreement is limited to specified products. Article 8(3) explicitly refers to products that are covered not only by the provisions on the free movement of goods (Part II of the EEA Agreement), but the *"Agreement"* as such, unless otherwise specified. This implies that the fish produced under the Regulation fall outside the scope of Article 31 EEA. Article 20 EEA and Protocol 9 contain specific provisions on trade in fish and other marine products, including regulation of competition and state aid, and confirm therefore that Article 8(3) is not limited to the provisions under Part II of the EEA Agreement.

The Government has observed that the same conclusion was drawn by the Authority in the Scottish Salmon case concerning state aid. In the letter of formal notice, the Authority states that it fails to see how the fact that the sector falls outside the scope of the Authority's state aid control has an influence on the interpretation of the Annexes to the EEA Agreement. However, in the view of the Government, it is certainly relevant for the present case that the Authority, in the Scottish Salmon case, stated that the application of the EEA Agreement to salmon required a particular legal basis, as it confirms that attention must be paid to the special regulation of fish in the EEA Agreement.[19]

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[18] Letter of formal notice 11 July 2012, page 6.
[19] Decision Nos. 195/96/COLand 176/05/COL

A broader interpretation of Article 8(3) EEA is confirmed by the EFTA Court in the *Pedicel* case especially paragraphs 33 and 34, in which the Court stated (emphasis added):

> *"33 The inclusion of Article 8 EEA in Part II of the Agreement, which concerns the free movement of goods, and the fact that services are not covered by the Harmonized System, as referred to in Article 8(3) EEA cannot, in the Court's view, be decisive. The issue in question calls for a broader interpretative approach that takes into account all the relevant elements, in particular the purpose of the provision.*
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> *34 That purpose, as stated above, consists, in the context of the present case, in leaving the decision of how to regulate trade in wine to the Contracting Parties who are in principle not bound by the rules on free movement of goods. The Court concludes from this that a service such as the one at issue, which is inseparably linked to the sale of wine, must be deemed to be excluded from the scope of Article 36 of the EEA Agreement."*

Accordingly, the EFTA Court held that Article 8(3) EEA was indeed not confined to part II of the Agreement on the free movement of goods. The Court concluded that also services related to the advertisement of wine fell outside the scope of the EEA Agreement.

The application of Article 31 is therefore conditioned upon an EEA provision making it clear that the regulation of production capacity for salmon and trout is to be assessed under this provision. It is the derogation from the starting point in Article 8(3) EEA that must be substantiated, not the opposite, as argued by the Authority. As noted above, the EFTA Court has confirmed that Article 8(3) EEA should not be interpreted dynamically, as it represents the boundaries of the EEA Agreement without any parallel within the EU legal order, see *Pedicel* paragraph 28. Rather, Article 8(3) represents the main principles as regards the fisheries sector, and any derogation from this main rule must have a sufficient legal basis.

The starting point must therefore be that fish farming in general falls outside the scope of the general provisions of the EEA Agreement, and thus that it is the derogation from Article 8(3) EEA that must be substantiated. Such substantiation is in the Government's view missing.

The main part of the Agreement contains no indications in this regard. However, point 10 of Annex VIII on Establishment (and point 1(h) of Annex XII on Capital) contains a specific regulation regarding fisheries. The regulation in Annexes VIII must be seen as confirmation of the general rule laid down in Article 8(3) EEA, emphasizing the exclusion of the fisheries sector from the scope and application of the general provisions of the EEA Agreement. Thus, the regulation in Annex VIII point 10 confirms explicitly that *"Notwithstanding Articles 31 to 35 of the Agreement and the provisions of*

this Annex, Norway may continue to apply restrictions existing on the date of signature of the Agreement on establishment of non-nationals in fishing operations or companies owning or operating fishing vessels." In this respect, the Authority is correct in assuming that this sectorial adaptation is in principle superfluous. However, it is reaffirming an important part of Norwegian fisheries policy that it was vital to make clear in the EEA Agreement.

Thus, the Authority's statement that the very existence of the regulations in Annexes VIII and XII is proof that their interpretation of Article 8(3) EEA must be rejected.

3.2.2 The Authority's interpretation of the Annex on establishment

Given that the Authority's interpretation that the regulation in point 10 of Annex VIII is a deviation from the main rule is applicable, the Annex on establishment would nevertheless entail that the Regulation is in line with the EEA Agreement. Annex VIII point 10 concerns establishment within *"fiske"* (Norwegian text) or *"fishing operations"* (English text). The Government submits that fish farming must be classified as *"fiske"/"fishing operations"*.

The Government disagrees with the Authority' view that the provisions in Annexes VIII point 10 should be construed narrowly. The annex forms an integral part of the fisheries regulation under the EEA Agreement, based on the key provision of Article 8(3) EEA.[20] The EFTA Court has, as noted above, confirmed that this latter provision should not be interpreted dynamically, as it represents the boundaries of the EEA Agreement, without any parallel within the EU legal order. Contrary to the Authority's position, one should be cautious in interpreting annexes to the effect that traditional fishery policy is drawn into the ordinary provision of the EEA Agreement, despite the main principle enshrined in Article 8(3) EEA. There is therefore no legal basis for a "narrow" interpretation of the annexes. For the same reasons, the Government submits that the case law cited by the Authority (n. 4), concerning EU Member States' Accession Agreements, is without relevance.

While a strictly dictionary-based reading of the wording in Annex VIII may have merit as a starting point, this approach is neither under the rules of interpretation in international law nor under EU/EEA law anything more than that. Consequently, one must take into account such other elements as the system and objectives of the legal instrument in question, as well as the context in which the wording occurs.

A comparison with the wording in Annex VIII point 10 and Annex XII 1 (h), is similarly not in and by itself adequate in order to elucidate the meaning of the term *"fisheries"* for our purposes, as the meaning of the terms in this instrument as well must be interpreted before they may be compared. Annex XII specifically allows foreign investments in land-based fish processing. This industrial activity is in several respects

[20] See also Article 119 EEA.

entirely different from the harvesting of fish. Firstly, it is a land-based activity whereas both fishing from a vessel and fish farming is conducted in the water. Secondly, the product as such is the same whether the fish is caught in the sea or farmed. Fish that has been processed through land-based manufacturing is on the other hand transformed into an entirely different product, inter *alia fish* fillets. In the Harmonized Commodity Description and Coding System (HS) of tariff nomenclature these products are different, cf. e.g. Annex II to Protocol 4 of the EEA Agreement.

Norway sought to include investment in the land-based fish processing industry in the EEA Agreement, because investment in the industry from other EEA States was regarded as desirable.[21] The capital intensive process industry was in other words to be strengthened, whereas the reason for exempting fish as a product for both Norway and Iceland was, as the preparatory works put it, to retain control over their resources.[22] The Annex positively allows foreign investments in land-based fish processing, from which fish fillets and other further refined products are produced. Thus, it does not seem logical - certainly without a basis other than a restrictive reading of the words - that the Contracting Parties sought to have divergent rules on establishment for the two different methods of acquiring the product fish, by traditional fishing or aquaculture.

In light of the above, we contend furthermore that the term *"fisheries"* and the term *"fishing operations"*, depending on the context, may include a wide range of activities, not only relating directly to the outright catching of fish using traditional measures, such as a fishing rod or net, or by employing boats or larger vessels. "Fisheries" or "fishing operations" may in this context also include activities of a *similar nature*, particularly those which provide an outcome that is the same. Here we contend that both activities in question enable those who undertake these to bring fish under the control of the person or entity undertaking the activity and subsequently, allow that person or entity to sell, trade, consume or otherwise utilize the fish for personal or commercial purposes.

In this relation, we would like to emphasize that at the time of Norway's entering of the EEA-agreement it was an understanding in Norway that aquaculture was a part of fisheries. One indication of this is the mention of the subject in St. prp. nr. 100 (1991-1992), relating to ratification of the EEA-agreement, where it is stated that *"fisheries include traditional fishing, fish processing and aquaculture"* (office translation).[23]

The Government agrees with the Authority that the modality with which fish is brought under the control of a person or entity by, on the one hand a fishing vessel utilizing a trawl net and on the other a worker at a fish farm, may differ. Nonetheless, the aim of

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[21] St.prp. 100 (1991-92), page 135.
[22] St.prp. 100 (1991-92), page 194.
[23] See St. prp. nr. 100 (1991-1992), page 400 head 10.7.4h, *"fiskerinæringen omfatter tradisjonell fangst, fiskeforedlingsindustrien og oppdrettsnæringen"*.

both activities is to acquire as large quantities of fish as a person or entity may realistically manage for subsequent trading or processing. As we have argued above, it is not first and foremost the wording in isolation but the wording in its context and understood in light of its object and purpose that give meaning to a legal term. The purpose of the regulation in question is in our view to exclude the application of the right of establishment, Article 31 EEA, to the kind of activity in the territory of Norway whereby fish – the key resource the exemption sought to preserve as mentioned in the preparatory works – is harvested. At any rate, it must be acknowledged that the relevant Annexes to EEA Agreement in no way provide the clear regulation of the aquaculture sector that is required in order to deviate from the main rule in EEA Article 8 (3).

4. JUSTIFICATION OF THE LEGISLATION CONCERNING DISTRIBUTION OF PRODUCTION CAPACITY

4.1 Introduction

The Authority states in its letter of formal notice of 11 July 2012 that the promotion of sustainable settlement and viability in rural areas, and, furthermore, the aim to ensure a just allocation of benefits stemming from the use of common sea areas, could be considered as legitimate objectives. However, the Authority has indicated that the legislation concerning the distribution of production capacity is not suitable and necessary in achieving these legitimate objectives.

In the following, the Government will present why the production capacity regulation is in any event suitable and necessary in achieving important social and political objectives. In conclusion, the Regulation is compatible with EEA law, even if it must be assessed under Article 31 of the EEA Agreement.

The Government recalls, at the outset, that the production capacity regulation is in no way discriminatory – it applies in the same way in law and, in fact, irrespective of nationality or place of establishment. The decisive criteria are therefore whether the regulation fulfills legitimate objectives, and whether it is suitable and necessary in order to reach one or more of these objectives.

Before addressing these three elements, the Government must emphasize that this assessment may imply a delicate and difficult balancing between different objectives, as also noted in section 2 above. These objectives may – or may not, depending on the circumstances – call for different solutions. During the past decade, the Government has witnessed a trend towards larger and more efficient entities in the Norwegian fish farming industry. This trend has been welcomed by the Government, but the objectives of profitability and effectiveness are not the only objectives. The production capacity regulation that applies only to the very largest entities (15 %/25 %), those bigger than

the total salmon production in most other countries,[24] must be balanced against other objectives that *may* pull in another direction.

4.2 Legitimate objectives

There are several objectives substantiating the production capacity regulation, also set out in the previous correspondence.

Firstly, the production capacity regulation seeks to contribute to *regional policy objectives*. These objectives are, in particular, related to ensuring viable and sustainable local communities. The Authority accepts that these are legitimate objectives in the public interest.[25] The production capacity regulation shall contribute to, for instance, more attractive work places in rural areas and higher settlement in these areas. An important factor in that regard is not only to ensure more workplaces, but also to attract highly skilled workers. It is a considerable challenge that educated persons leave smaller communities. With management, research and development locally, a key factor for the preservation of viable coastal communities is ensured. These legitimate objectives are further substantiated in the present case.

Secondly, the regulation shall ensure a *reasonable distribution of the benefits stemming from the use of common sea areas*. Fish farming requires an exclusive use of attractive sea areas. It is a vital principle in Norway that sea areas are public – they belong to the population as a whole. In deviating from this principle, by giving a fish farmer an exclusive right to use the common areas, it is fair and reasonable that the local community offering areas to aquaculture activities gains something in return e.g. that the companies place their headquarters and research departments in small coastal communities. These two elements of the objectives set out above are acknowledged as legitimate by the Court of Justice, and they are also acknowledged by the Authority.[26]

In this respect, we would like to mention that the general sentiment in many local communities is that the development of the aquaculture industry has not led to as many jobs and local spill-over effects as anticipated. Researchers have also observed these trends. They explain these trends with further industrialization, with restructuring in the industry as well as ownership consolidation/concentration, which might have led to the concentration and partial centralization in the distribution of spill-over effects.[27] An easing of the Regulation will further accelerate these trends – also for the largest fish farming companies. Despite the production capacity regulation, the fact remains that

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[24] As pointed out in appendix about Norwegian aquaculture structure and global salmon production in our letter of 16 March this year.

[25] Letter of formal notice 11 July this year, page 10.

[26] E.g. Case C-302/97 *Konle*, para. 40; and Case C-452/01 *Ospelt*, paras. 38-40; and the Authority's letter of 11 July 2012 section 5.2.2 (pages 10-11).

[27] Nofima Report 18/2012, *Kommunenes holdning til økt oppdrettsvirksomhet*, John R. Isaksen, Otto Andreassen and Roy Robertsen.

the aquaculture regulation in general and the production capacity regulation in particular, give substantial freedom for the operators. This freedom is usually positive, contributing to growth and profit. It may, however, imply a risk that the benefits from the aquaculture sector are not sufficiently allocated in line with the objectives set out above, a risk that would clearly increase if the regulation were to be further liberalized.

A second trend clearly seen by the Government, and emphasized by researchers, is that the municipalities' willingness to prepare common sea areas for aquaculture is dependent on the degree of the industry's value creation locally. This is quite logic, as the municipality gives the fish farmer an exclusive right to use common sea areas, it is legitimate to expect to receive positive effects (spill-over effects) in return. Thus, there seems to be coherence between the spill-over effects from the industry into the local communities and the willingness of the municipalities to prepare common sea areas for aquaculture.[28]

Value creation and spill-over effects could be measured in different ways. When assessing spill-over effects in the present case, the Government considers it necessary to take into account a wide range of considerations. For instance, the spill-over effects, such as the aquaculture industries purchase of local services, e.g. accounting and legal counseling, might in some cases fall outside the scope of measuring a business value creation.[29]

A third, albeit interconnected objective, is to ensure not only a reasonable distribution of *benefits* from fish farming, but also a reasonable distribution of the *production capacity rights as such*. As fish farming is an activity that must be limited in scope and that by definition uses common sea areas as a production site, it is reasonable that this exclusive right is shared by several fish farmers. It is therefore a separate objective to ensure that production capacity is indeed shared between more parties and not only between very few, extremely large companies. Even this objective, the Government submits, is acknowledged by the European Court of Justice in relation to agriculture, as the Court has held that *maintaining the distribution of land ownership* and *a reasonable use of available land* are legitimate objectives.[30] This assessment is equally valid with regard to aquaculture that indeed forms part of the agricultural and fishery policy areas within the European Union.

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[28] *Kampen om plassen på kysten*, Bjørn Hersoug and Jahn Petter Johnsen (red.), Universitetsforlaget, 2012. Chapter 9: *"Økonomer i kystsonen: Kan kunnskap om verdiskaping gi bedre arealforvaltning?"* J.R. Isaksen and E. Mikkelsen, page 159 – 178.

[29] A report, *"Eierskapsstruktur i norsk havbruksnæring"*, Pöyry for Marine Harvest, page 13 takes a narrow approach of what value creation is when comparing value creation and company size.

[30] Case C-452/01 *Konle*, para. 39; and Case C-370/05 *Festersen*, paras. 27-28.

The Government therefore disagrees with the Authority's opinion that this third objective is *"a purely economic objective"*.[31] It is rather an integral part of the regional policy objective.

4.3 Suitability

The next question is whether the production capacity regulation is suitable in contributing to the realization of one or more of these objectives.

The Authority argues that it must be likely that the measure contributes to the achievement of the objectives, and that this must be demonstrated with specific evidence. The Authority finds that these conditions for establishing the suitability of the national measure are not complied with.

The Government maintains that the production capacity regulation is indeed appropriate in achieving the set objectives. It is the Government's opinion that the Authority relies on too strict suitability requirements. In a case like the present, it is very difficult to measure the individual effects of several measures that work together in achieving the objectives.

In cases like the present, where the states enjoy a margin of discretion, and where it is difficult to measure the individual effects of several national measures, the state must have *"a margin of discretion in determining ... the measures which are likely to achieve concrete results"*.[32] Hence, it seems that the state has a margin of discretion in establishing whether the measure will be suitable. Moreover, it is sufficient that there is a partial effect. [33] The ECJ seems to reject the suitability of a measure only if the effect is purely theoretical.[34]

Furthermore, it must suffice that there is *a reasonable relationship between the measure and the aim pursued.* This is indeed the test held by the ECJ in the Hauer case concerning the fulfillment of the aim of *agricultural structural policy.*[35] This test of *reasonableness*, and whether it is *reasonable to assume* that the measure would contribute to the achievement of the objective[36], is therefore of general application in cases with the features set out in the preceding paragraph. It is not, as seemingly argued by the Authority, limited only to cases concerning public health.

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[31] Letter of formal notice 11 July this year, section 5.2.2, page 10.

[32] Case C-394/97 *Heinonen*, para. 43; and Case C-434/04 *Ahokainen*, para. 32.
[33] *Ahokainen*, para. 39; and the Opinion in *Ahokainen*, para. 24.
[34] Case C-366/04 *Schwarz*, paras. 35-36.
[35] Case 44/79 *Hauer*, para. 23.
[36] See e.g. the EFTA Court in Case E-16/10 *Philip Morris*, para. 82.

Indeed, the *reason d'être* of the requirements for suitability to be established in each case does not seem to relate so much to which objective is pursued (whether public health or other legitimate objectives), but rather to the complexity of the matter and to the actual possibility of providing relevant evidence in the concrete case. In some cases, "hard" evidence may be available, whereas in other cases one is confined to drawing conclusions from "softer" evidence, such as social science and from actual experience.[37]

In this case, concerning distribution of production capacity, such a reasonable relationship does exist between the measure and the objectives, as required by *Hauer*. It is indeed reasonable to assume that the production capacity regulation will contribute to the fulfillment of regional policy aims, to a reasonable allocation of benefits from fish farming, and to a reasonable distribution of production capacity rights as such.

Indeed, the regulation clearly ensures a distribution of production capacity. That is the direct consequence of the regulation. However, it also contributes to the two former objectives relating to regional policy and a just allocation of the benefits stemming from the use of common sea territory.

It is the Government's experience that the Regulation leads to a more sustainable development of small coastal communities. This effect is, admittedly, difficult to measure. There are, however, two trends within fish farming that sufficiently substantiate these effects.

The first element is that the biggest companies have their management and headquarters in larger cities. The two largest companies – Marine Harvest and Lerøy Seafood – having in total 35 % of the production capacity – perform these tasks in Bergen, the second biggest city in Norway. Of the eight next companies based on total size – in sum representing 29 % of the capacity – four have their headquarters etc. in typical rural parts of small, district municipalities. This is important as they attract a high share of highly skilled and educated persons. It is a huge challenge in Norway that educated persons leave small communities. With management, research and development locally, a key factor for the preservation of viable coastal communities, and a just allocation of benefits from fish farming, is ensured. A report states that a further consolidation within the salmon and trout farming industry probably will reduce the number of headquarters.[38] In our view, it is likely to assume that a further consolidation will increase the centralization of management and headquarters, such as in the case of the two biggest companies which have their management and headquarters in Norway's second largest city, Bergen.

The second trend element concerns concentration to fewer cites for slaughter and other processing activities. The biggest companies have – relative to their size – clearly fewer processing cites than the medium-sized companies. The production capacity therefore

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[37] See e.g. the Opinion in Joined Cases C-376/98 and Case C-74/99 (Tobacco Directive I), paras. 157-160.
[38] *"Eierskapsstruktur i norsk havbruksnæring"*, Pöyry for Marine Harvest, page 23.

benefits district communities to a larger degree, when it is divided between several fish farmers. The activities of the largest companies generally lead to fewer work places in rural areas, and reduced settlement in areas that are already scarcely populated – presumably in order to enhance profitability for the owners.

There is, of course, no clear division between fish farmers under and above the ceiling of 15 % production capacity. Some smaller companies make adaptions similar to those of the bigger companies. However, the Government has experienced that many small and medium-sized fish farmers do indeed keep a larger part of their activities locally – offering more attractive employment for many groups, also high-skilled and educated workers. Local activities also lead to spin-off effects, such as the need for service related businesses.

The Authority argues that the effects described above do not suffice, because there is no direct link between the production capacity regulation and for instance "the use of locally recruited employees, local slaughtering facilities, local head offices, local suppliers or an industry structure with a certain amount of smaller players". It is true that the link is somewhat indirect. However, in the Government's opinion, the link is sufficiently clear to conclude that there is indeed a reasonable relationship between the national provisions and these aims. In principle, an alternative way of regulating the industry could be to set up very specific requirements relating to the criteria mentioned by the Authority (and/or other criteria). This would, however, imply the application of a different type of much more detailed regulation than has hence far not been regarded as the most appropriate form of regulation for this industry.

As also stated by the Authority in the letter of 11 July this year, cod farming is a rather new and less established industry than farming of salmon and trout. In the Government's view, this fact has so far not made it necessary to adapt similar legislation concerning the distribution of the cod farmers' production capacity.

4.4 Necessity

Finally, the Government maintains that the regulation is necessary. The Government has not been able to find other measures that are less restrictive to trade, but at the same time *equally effective* for the fulfillment of the relevant objectives. The promotion of sustainable settlement and viability in rural areas is an objective, which might be approached in different ways e.g. with direct financial support to these areas. In our view this is not an appropriate measure, as it might raise subsidy investigations or similar trade disputes.

The Authority indicates that the production capacity ceiling could be replaced by an authorization scheme. It is difficult to see that this would sufficiently ensure the objective of a reasonable distribution of capacity rights to a scarce resource. Moreover, an authorization scheme must presumably be strict and detailed in order to be equally effective for the fulfillment of the objective relating to regional policies and a just

allocation of benefits from fish farming. That, in turn, questions whether it will be less restrictive to trade than today's regulation.

The Government acknowledges that the criteria for authorization for fish farmers controlling between 15 % and 25 % of the total MAB are fairly general. They do nevertheless, the Government submits, offer the parties involved a reasonable degree of information and clarity.

The Authority also criticizes the fact that some of the criteria mentioned in the relevant provisions are based on other objectives than those found by the Authority to be legitimate in substantiating a restriction on establishment. However, whether to grant authorization, and on what conditions, implies a balancing of different objectives. Some of these would indicate that authorization should be given, whereas others would indicate a negative answer to the application for authorization. It must be fully legitimate to mention objectives that may draw in both directions. This does not at all indicate that the restrictive effect (e.g. when declining an application) is based on objectives that are not legitimate.

It should finally be recalled, in this connection, that the production capacity regulation seeks to strike a fair balance: On the one hand, it offers fish farmers wide discretion in organizing their activities, enabling them to grow into – by far – the world's largest farmers of salmon or trout. On the other hand, it sets *some* limits to this discretion in order to avoid effects of undesired over-concentration and centralization. The Government finds this to be a reasonable and balanced approach within the discretion for the states in organizing their fisheries policy.

5. CONCLUDING REMARKS

The Government has observed that the present case is a subject for discussion in the upcoming package meeting at the end of October this year. Do not hesitate to contact the Ministry if you have further observations or questions regarding this case.

Yours sincerely,

Magnar Nerheim
Director General

Martin Bryde
Deputy Director General