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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
Case no 68781	201000784- /MAB	16.03.2012

Norwegian fish farming – regulation concerning distribution of production capacity

Dear Mr. Einarsson,

Reference is made to previous correspondence in this case, in particular the letter from the EFTA Surveillance Authority of 14 February 2012 concerning distribution of production capacity in Norwegian fish farming. In the following the Norwegian Government will provide our observations.

1. SUMMARY

The Government reiterates its principal position that fisheries and aquaculture policies are not part of the EEA Agreement. While 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 falling outside the scope of the EEA Agreement, 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 solely under the provisions on the free movement of goods (section 3.1 below) or under the provisions related to establishment and/or capital (section 3.2 below).

Should the general provisions of the EEA Agreement nevertheless be applicable, contrary to the position of the Government, it is submitted that the production capacity

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regulation is compatible with the EEA Agreement as it is suitable and necessary in order to fulfill important social objectives related to, inter alia, regional policy and a just allocation of the benefits stemming from the use of common sea areas (section 4 below).

2. INTRODUCTORY REMARKS

The Authority's description of the relevant national aquaculture legislation in section 3 of the letter of 14 February 2012 seems to be adequate. The Government would, however, like to clarify a few points.

In section 3.2 of the said letter, third paragraph, the Authority holds: "If the amount of biomass on a site is extended – e.g. through the acquisition of one or more concessions belonging to the same geographical defined administrative region – a new clearance must be obtained." The Government clarifies that if the size of the biomass on a site is to be extended a new clearance must be obtained, irrespective of the reason for the extension.

Furthermore, 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 in the 2009 license allocation round where smaller fish farmers, and farmers planning for increased processing with the aim of economical integration in rural coastal districts in Norway, were given priority[1].
>
> Another example is a provision which offer 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 being regional policy measures, none of these measures are, however, sufficient to reach these political intentions.

As the aquaculture activity plays an important long term role in the economy of fragile coastal regions in Norway, it is recalled that the 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

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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

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. 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] Hence, 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 scope of the regulations have gradually changed from prohibition from owning more than one license to today's regulations. This liberalization has been part of the Government's policy to promote the industry's ability to develop, innovate and compete.

As a final 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 related to, *inter alia*, regional policy and a just allocation of the benefits stemming from the use of common sea areas. The provisions represent a regulation related to, and aimed at, the fish products as such. Indeed, the Authority does not seem to question that the maximum production capacity, represented by the Maximum Allowed Biomass (MAB) is to be assessed as a goods issue falling within the particular regulation of aquaculture in the EEA Agreement.[4] The same should apply to the distribution of this production within the capacity ceiling.

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. Thus, the present case deviates from ownership cases previously assessed by the Authority, such as the case related to local ownership in the aquaculture sector[5] as well as the pending case against Norway regarding restrictions on ownership in financial services infrastructure institutions.[6]

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

[4] Letter 14 February 2012, p 10,

[5] ESA ref. no ESA063.400.001

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

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

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

There is no doubt that farmed salmon and trout fall outside the product coverage of the EEA Agreement cf. Article 8(3) EEA. Indeed, this has become quite clear throughout the years, as the European Commission has opened dumping and subsidy investigations – under WTO rules – against Norwegian salmon, and a WTO trade dispute panel gave a ruling in such a case in 2007.[7]

The scope of Article 8(3) EEA is set out in more detail in section 3.2 below. Here it suffices to note that, to the extent that the present case should be assessed under the provisions on *goods* in the EEA Agreement, there are no relevant EEA provisions 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 limitation of the export of salmon and trout.

The relevant question is therefore whether not only the sales, import and export of the said fish products are to be assessed under the goods provisions, but also national provisions on the distribution of this production capacity. The Government submits that also the latter aspects should be assessed under the goods provisions.

It should be recalled that the regulation of production capacity is an inherent part of the Norwegian management of the natural resources that enables fish farming. The Regulation is inseparably linked with the rules governing trade in fish and other marine products and must be assessed accordingly.

Aquaculture production licenses for salmon and trout are limited by Maximum Allowed Biomass (MAB), i.e. the maximum biomass permitted to be in the water at any point of time. This is a mean of regulating the production of salmon and trout. The MAB that each company may control correlates with the possible production from each fish farm. 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. Indeed, the European Commission has, by its trade policy investigations and measures (based on dumping allegations) called for such production ceilings in salmon farming in periods where fluctuations in supply have resulted in lower salmon prices. The MAB regulation aims at limiting the production to a desired level.

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

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 related 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,[8] a production monopoly[9] or production quotas.[10] Like 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 and for investments in the involved markets. 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 these alternative provisions. 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.

It is true, as held by the Authority, that the application of the goods provisions does not as such preclude that other parts of the national measure may be assessed under other parts of the EEA Agreement. However, the Government's opinion is that the Authority does not interpret the case law correctly on this point. Indeed, the national measure in the cases just mentioned, 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. In the same way, 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

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[8] E.g. case 15/79 *Groenveld* (concerning a national prohibition for manufacturer of sausages from having in stock or processing horsemeat).

[9] 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).

[10] E.g. Case 148/85 *Forest* (concerning annual milling quotas for common wheat).

farming must be respected, as this forms the basis for the important provision 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*, contrary to the submissions of the Authority, 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.[11]

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. The conclusion should therefore be that the contested national measures should be assessed solely under the goods chapter and hence be found to be compatible with the EEA Agreement.

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, seems 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.[12] Indeed, a supplementary assessment of other and stricter provisions 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 Articles 31 and 40 of the EEA Agreement are not applicable

Assuming, contrary to the assessment of the Government, that the Regulation must also be assessed as a potential restriction on establishment and/or capital, it nevertheless falls outside the scope of Articles 31 and 40 of the EEA Agreement.

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[11] Case E-4/04 *Pedicel AS vs Sosial- og helsedirektoratet,* paras. 28 and 33.

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

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 is specified. This implies that the fish produced under the Regulation falls outside the scope of Articles 31 and 40 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 same conclusion was drawn by the Authority in the Scottish Salmon case concerning state aid, in which the Authority stated that the application of the EEA Agreement to salmon required a particular legal basis.[13] The Government recalls furthermore, as stated *inter alia* in the Joint Declaration to Protocol 9, that the EFTA States have not adopted the Common Fishery Policy, which is a policy that encompasses the aquaculture sector.

A broader interpretation of Article 8(3) EEA is also 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 Articles 31 and 40 EEA 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 these provisions. It is the derogation from the starting point in

[13] Decision Nos. 195/96/COLand 176/05/COL

Article 8(3) EEA that must be substantiated, not the opposite as argued by the Authority. It cannot be correct, for the same reason, that the derogations from Articles 31 and 40 EEA should be interpreted narrowly. As also noted above, the EFTA Court has confirmed that Article 8(3) EEA should not be interpreted dynamically, see *Pedicel* para. 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 both contains specific regulation regarding fisheries. The question is whether these specific regulations have implications for fish farming.

Point 10 of Annex VIII reads (emphasis added):

> *"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* <u>*establishment*</u> *of non-nationals* <u>*in fishing operations*</u> *or companies owning or operating fishing vessels."*

Point 1(h) of Annex XII reads (emphasis added):

> *"Notwithstanding Article 40 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 ownership by non-nationals of fishing vessels.*
>
> *These restrictions* <u>*shall not prevent investments*</u> *by non-nationals* <u>*in land-based fish processing*</u> *or in companies which are only indirectly engaged in fishing operations. National authorities shall have the right to oblige companies which have been wholly or partly acquired by non-nationals to divest themselves of any investments in fishing vessels."*

The regulations in Annexes VIII and XII must be seen as a 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 only provision that adds to this starting point is the exception regarding investments in land-based fish processing.

According to the provisions in the Annexes on establishment and capital, establishment and capital movements within "fiske" (Norwegian text) or "fishing operations" (English text) fall outside the scope of Articles 31 and 40 EEA, whereas investments in land-based fish processing activities fall within the said Articles. The question is thus

whether fish farming must be classified as "fiske"/"fishing operations" or as "land based fish processing",

The Government disagrees with the Authority in that the provisions in Annexes VIII point 10 and XII point 1(h) should be construed narrowly. The two annexes form an integral part of the fisheries regulation under the EEA Agreement, based on the key provision of Article 8(3) EEA.[14] 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 Annexes VIII and XII 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 9 and Annex XII 1 (g), 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.

Furthermore, while the Government maintains its principal position that the Regulation falls outside the Agreement, at any rate we disagree that the parts of the preparatory works cited by the Authority may be understood in a manner so as to exclude aquaculture operations from the exemptions to Articles 31 and 40 of the EEA Agreement found in Annex VIII and Annex XII respectively. If anything, the preparatory works suggest the opposite.

Consequently, the Government submits that the wording does not indicate the understanding presented by the Authority. Rather, it must be emphasized that there is a fundamental difference between "land-based fish processing" activities and fish farming.

As becomes clear if the preparatory works are examined in the manner suggested by the Authority, Norway's exemptions specifically do not extend to land-based fish processing. This industrial activity is in several respects entirely different from the harvesting of fish. Firstly, it is a land-based activity whereas both fishing from a vessel

[14] See also Article 119 EEA.

and fish farming is conducted in the water. Secondly, the product as such is the same whether caught in the sea or farmed. Fish that has been processed through land-based manufacturing is 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.

Thus, the exemption extends to the harvesting of the goods fish, but not to the activity of manufacturing such goods into another product. Finally, as the preparatory works indicate (p. 135), Norway sought not to include the land-based fish processing industry in the exemption because investment in the industry from other EEA States was regarded as desirable. 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, as the preparatory works put it, was to retain control over their resources. Since the exemptions positively do not extend to land-based fish processing, from which fish fillets and other further refined products are produced, it does not seem logical—certainly without no basis other than a restrictive reading of the words— that the Contracting Parties sought to exclude the right of establishment and free capital movement with respect to one method of acquiring the product fish but not to another method of acquiring the same product.

In light of the above, we contend furthermore that the term "fisheries” and the term “fishing operations”, depending of the context, may include a wide range of activities, not only related directly to the outright catching of fish with 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 enables those who undertake it to bring fish under the control of the person or entity undertaking the activity and subsequently allows that person or entity to sell, trade, consume or otherwise utilize the for personal or commercial purposes.

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 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 exemption in question is in our view to exclude the application of the right of establishment and free capital movement, Articles 31 and 40 of the EEA Agreement respectively, 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 do in no way provide any clear regulation of the aquaculture sector, which is what Article 8 (3) requires.

4. JUSTIFICATION OF THE LEGISLATION CONCERNING DISTRIBUTION OF PRODUCTION CAPACITY

4.1 Introduction

In the following the Government will present why the production capacity regulation is 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 against Article 31 and/or 40 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 these assessments 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. There has been 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, 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. On the basis of the Authority's letter of 14 February 2012 it is recalled 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.[15]

Three important objectives substantiating the production capacity regulation are set out here.

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[15] 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.

First, the production capacity regulation seeks to contribute to *regional policy objectives*, see also the Authority's letter of 14 February 2012 section 5.4 2. These objectives are, in particular, related to ensuring viable and sustainable local communities. The production capacity regulation shall contribute to, for instance, more attractive work places in rural areas and higher settlement. An important factor in that regard is not only to ensure more working places, but to attract highly skilled workers. It is a considerable challenge that educated persons leave from smaller communities. With management, research and development locally, a key factor for the preservation of viable coastal communities is ensured. These are legitimate objectives in general and they are further substantiated in the present case.

Second, the regulation shall ensure a *reasonable distribution of the benefits* from fish farming. Fish farming requires an exclusive use of attractive sea areas. It is a vital principle in Norway that sea areas are there for everyone – 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 these areas will also gain something in return such as e.g. headquarters and research departments in small local communities. This objective is acknowledged as legitimate by the Court of Justice.[16]

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 is, the Government submits, 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.[17] The same should apply with regard to aquaculture.

4.3 Suitability

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

In cases as the present one, where the states enjoy a wide margin of discretion, and where it is very difficult to measure the individual effects of several measures that work together in achieving fairly similar objectives, the state must also have "a margin of

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[16] Case C-302/97 *Konle*, para. 40; and Case C-452/01 *Ospelt*, para. 39.

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

discretion in determining … the measures which are likely to achieve concrete results."[18] Hence, it seems that the state has a margin of discretion in establishing whether the measure will be suitable. Moreover, as held in *Ahokainen*, it is sufficient that there is a partial effect. As held by AG Maduro in that case, the question was whether "the measure has any benefits at all for the legitimate interests on which the Member State relies"[19]. The ECJ seems to reject the suitability of a measure only if the effect is purely theoretical.[20]

On this background, the Government disagrees with the Authority when indicating with reference to *Festersen*, that a measure must more or less *guarantee* an effect. This is, the Government submits, not the correct test, The Government is unaware of other cases using this seemingly very strict suitability test. The Court of Justice has rather used a more realistic test in other cases, also concerning the agriculture sphere to which aquaculture also belongs, asking whether there is *a reasonable relationship between the measure and the aim pursued.*[21] A similar test is applied by the EFTA Court in the Philip Morris case, referring to whether "it was reasonable to assume that the measure would be able to contribute to the protection of human health".[22]

In this case concerning distribution of production capacity such a reasonable relationship does exist between the measure and the objectives. 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 related 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 district communities. This effect is, admittedly, difficult to measure. There are, however, two trends within fish farming that sufficiently substantiates these effects. See also the enclosed overview of the fish farming activity in Norway.

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[18] Case C-394/97 *Heinonen*, para. 43; and Case C-434/04 *Ahokainen*, para. 32.

[19] *Ahokainen*, para. 39; and the Opinion in *Ahokainen*, para. 24.

[20] Case C-366/04 *Schwarz*, paras. 35-36.

[21]Cse 44/79 *Hauer*, para. 23.

[22] Case E-16/10 *Philip Morris*, para. 82.

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 main office etc. in typical rural parts of small, district municipalities. This is important as these departments attract a high share of highly skilled and educated persons. It is a huge challenge that educated persons leave from smaller 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.

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 that the medium sized companies. The production capacity regulation therefore benefits more to district communities when divided between several parties. The activities of the largest companies generally lead to fewer work places in rural areas, to reduced settlement in areas 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. Also smaller companies may make similar adaptions. However, the experience is 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.

4.4 Necessity

Finally, the Government maintains that the regulation is necessary. The Government has hence, so far, 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. This issue is, however, under further evaluation.

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

It should be recalled that the production capacity regulation seeks to strike a fair balance: It offers fish farmers huge discretion in organizing their activities, enabling them to grow into the world`s largest fish farmers. 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 reasonable and balanced approach within the discretion for the states in organizing their fisheries policy.

5. CONCLUDING REMARKS

The Government hopes that these observations, and earlier correspondence and meetings in this case, form a good basis for the Authority's assessment of the Case. We are, however, open for further dialogue with the Authority, *inter alia* to discuss our policy and relevant measures in light of what is draw up by the Authority in section 5.4 and 5.5 of its most recent letter.

Yours sincerely,

Magnor Nerheim
Director General

Martin Bryde
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