

Case No: 71056
Event No: 634016 (former 634016)
Dec. No: 137/12/COL

[non confidential version]

EFTA SURVEILLANCE AUTHORITY DECISION
of 19 April 2012
on the state aid to Södra Cell Tofte AS

(Norway)

The EFTA Surveillance Authority (“the Authority”)

HAVING REGARD to the Agreement on the European Economic Area (“the EEA Agreement”), in particular to Article 61(3)(c),

HAVING REGARD to the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice (“the Surveillance and Court Agreement”), in particular to Article 24,

HAVING REGARD to Protocol 3 to the Surveillance and Court Agreement (“Protocol 3”), in particular to Article 1(3) of Part I and Article 4(3) of Part II,

Whereas:

I. FACTS

1. Procedure

- 1) The Norwegian authorities notified the aid to Södra Cell Tofte AS (“SCT”), pursuant to Article 1(3) of Part I of Protocol 3 by letter of 29 December 2011 (Event Numbers 619622, 619623 and 619624). The Authority received updated information by way of email on 23 January 2012 (Event No 622232).
- 2) By letter dated 17 February 2012 (Event No 624039), the Authority requested additional information.
- 3) By letter dated 19 March 2012 (Event No 628573), the Norwegian authorities replied to the information request. The Authority requested and received further information via email in the period between 23 March 2012 and 2 April 2012 (Event Numbers 628971 and 629730).

2. Description of the notified project

2.1 The notified project

- 4) The measure is notified as aid for renewable energy production. The aid is granted to SCT to convert from using conventional energy to only use renewable energy. The objective is to free up self-produced bio energy to replace today’s annual consumption of approximately 16 000 tons of heavy oil corresponding to 183 GWh annually. Moreover,

the measure will also increase the production of electricity from 9 GWh to a total of 26 GWh, an annual increase of 17 GWh. Nevertheless, the aid will not enable SCT to increase the production of chemical pulp.

2.1.1 The future production at SCT with the aid

- 5) The aid measure is directed at replacing the use of 16 000 tonnes of fossil fuels in the lime mud kiln with self-produced bio energy. The phasing out of currently used eucalyptus will increase the amount of black liquor and bark which leads to increased energy production.
- 6) To replace the use of fossil fuels with bio energy, SCT will undertake a portfolio of investments. Pine oil and bark will replace the use of fossil fuel in the lime mud kiln. In order to do so, the following steps have to be taken:
 - 7) First, a pine oil reactor for the production of pine oil will be built. The pine oil will be able to replace 5 800 tonnes of fossil fuel in the lime mud kiln.
 - 8) Secondly, a bark dryer and a lime mud dryer will be installed to allow bark to be used as an energy source for the lime mud kiln. This is necessary because the bark needs to be dried and pulverised before it can be used as bio fuel for the lime mud kiln. A lime mud dryer is also necessary in order to maintain the capacity of the lime mud kiln. This will enable the dried and pulverised bark to replace 4 700 tonnes of fossil fuel in the lime mud kiln.
 - 9) Thirdly, it will be necessary to increase the capacity of the debarking drum. As the eucalyptus chips are phased out and the raw materials are changed to spruce and pine only, it is necessary to increase the capacity of the debarking drum to maintain the annual production of 400 000 tonnes of pulp and to release a sufficient volume of bark to replace all the fossil fuel in the lime mud kiln. This final step will allow the replacement of the final 5 500 tonnes of fossil fuel in the lime mud kiln.
- 10) By converting to the use of bio energy, the electricity production at the plant will increase due to a better energy balance. Under normal operating conditions, the plant will be self-sufficient and an additional 17 GWh of renewable energy (electricity) will be fed into the grid and sold at Nord Pool.
- 11) For an overview of the future production at SCT, see figure 2 below.

The future production line

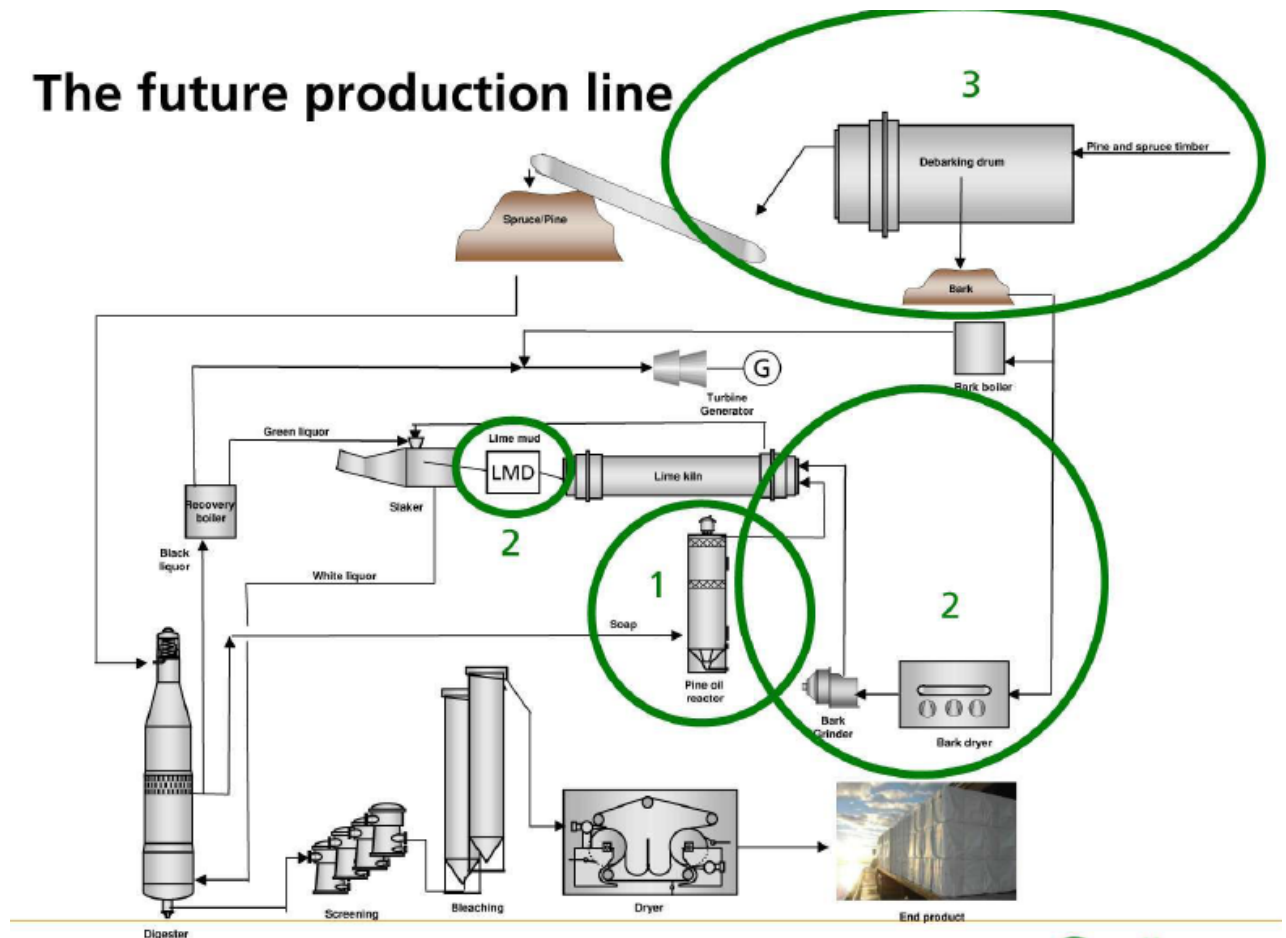


Figure 2: Shows SCT's future production line with the aid, see Event No 619622.

3. The recipient – Södra Cell Tofte AS (“SCT”)

12) The recipient of the aid, SCT, is a limited liability company. SCT is a business unit under Södra Cell AB, which again is a part of Södra AB.

Södra AB is an economic association with a membership of approximately 50 000 forest owners in southern Sweden. The corporation is organised into five business areas:

- Södra Skog AB
- Södra Timber AB
- Södra Cell AB
- Södra Interiör AB
- Södra Wind power AB

13) Södra Cell AB is one of the world's leading manufacturers of paper pulp (both chemical and mechanical pulp) for the open market. Södra Cell AB consists of five plants, three in Sweden (Mönsterås, Mörrum and Värö) and two in Norway (Tofte (SCT) and Follo). Södra Cell AB concentrates its operation and expertise on the production of pulp and do not carry out papermaking.

- 14) Södra Cell Tofte AS (SCT) is located in the municipality of Hurum, in the county of Buskerud, Norway. SCT is the largest Norwegian producer of chemical pulp, with an annual production of 400 000 tonnes¹. 70% of the production is sold to export, while the remaining 30% is sold on the Norwegian market. In a normal year SCT has an annual turnover of NOK 1 600 million². SCT is a large enterprise.

3.1 Products

3.1.1 Pulp

- 15) The raw materials currently used for production of pulp are softwood-species (spruce and pine) mainly from Norway but with some import from Sweden, Denmark, the Baltic countries and Scotland and hardwood (eucalyptus) imported from Uruguay³.
- 16) The pulp made at SCT today is Södra Blue, Södra Green and Södra Gold. The different pulp products can be mixed but the products cannot fully replace each other. With the aid, SCT is planning on phasing out the use of eucalyptus in the production and increase the use of spruce and pine. Thus, in the future, SCT will only produce Södra Blue and Södra Green (only containing spruce and pine)⁴.

3.1.2 Electricity

- 17) Today, SCT produces 269 GWh of electricity, of which 260 GWh is used in internal production. 9 GWh is sold on Nord Pool. The investment will increase the annual production of electricity fed into the grid by 17 GWh to a total of 26 GWh⁵.

4. The Energy Fund Scheme

- 18) The notified aid to SCT is granted on the basis of the Energy Fund scheme which was approved by the Authority's Decision No 125/06/COL of 3 May 2006 on the basis of Article 61(3)(c) of the EEA Agreement⁶. The Energy Fund scheme is a financing mechanism with the objective of encouraging energy saving measures and the production of environmentally sound energy⁷. The fund is managed by Enova SF ("Enova"), a state owned administrative body.

4.1 The Net Present Value method

- 19) In its Decision No 125/06/COL⁸, the Authority set out its interpretation of the relevant provisions in the EAG as well as its considerations underlying the approval of the Energy Fund scheme.
- 20) The Authority's guidelines on state aid for environmental protection ("EAG")⁹ contains separate provisions on renewable energy production for

¹ Event No 619622.

² Event No 619622.

³ Event No 628573.

⁴ Event No 619622.

⁵ Event No 619622.

⁶ As amended by the Authority's Decision No 486/10/COL of 15.12.2010 on the prolongation of the scheme until 31 December 2011. As of 1.1.2012, a new scheme is in place as adopted by the Authority's Decision 248/11/COL of 18.7. 2011. As the measure in this case was notified under the old scheme, an agreement was reached with the Norwegian authorities that the measure would be assessed under the old scheme.

⁷ Decision of Parliament 5.4.2001: Odelstingets vedtak til lov om endringer i lov 29. juni 1990 nr. 50 om produksjon, omforming, overføring, omsetning og fordeling av energi m.m (energilova). (Besl.O.75 (2000-2001), jf. Innst.O.nr 59 (2000-2001) og Ot.prp.nr.35 (2000-2001).

⁸ A copy of the decision can be found at <http://www.eftasurv.int/state-aid/state-aid-register/>.

(i) “investment aid” which covers investments in assets (e.g., machinery, land and equipment) and is based on identifying the investment eligible costs (either directly or on the basis of a counterfactual);¹⁰ and

(ii) “operating aid” which covers operating costs such as salary, taxes, water/energy use etc¹¹.

- 21) Investment aid must be deducted from operating aid¹². On the basis of section 54 of the previous EAG¹³ the Authority approved the grant of state aid covering “*the difference between the production costs (initial investment costs and operating costs) and the market price (operating income)*”. The requirement that operating aid may be granted until the plant has been “*fully depreciated*” was considered to be equivalent to the life time of the plant. Account was also taken of the fact that section 54 states that “*The aid may cover a fair return on capital*”¹⁴.
- 22) The Authority considered that the provision on operating aid does, in fact, indirectly include investment costs due to the fact that operating costs can include depreciation costs for the life time of the plant¹⁵.
- 23) On the basis of those premises, the Authority accepted to calculate the maximum aid amount on the basis of the Net Present Value (“NPV”) calculation based on a discount rate which provides a fair return on capital. Funding would then only be granted for investments in renewable energy production which would otherwise not take place, due to the fact that the energy price obtainable in the market does not cover the costs and therefore renders the NPV of a renewable investment project negative.
- 24) Under the NPV approach, the aid amount is calculated so that the project reaches an NPV of zero, which, for a rational investor, would be the triggering off point for when a project is realised in the market. No aid will be given in excess of the amount necessary to reach the zero present value.
- 25) A project has to comply with the following criteria under the NPV method:
 - Projects generating a negative cash flow under normal operating conditions will not be eligible to receive aid.
 - No aid will be given in excess of the amount necessary to trigger the project (bring the NPV to zero with a fair return on capital).
 - The maximum amount of aid cannot exceed the total investment costs.
 - The aid amount is based on the difference between the production costs and the market price. The production costs include construction costs and operating costs.

⁹ OJ L 144, 10.6.2010, p.1 and EEA Supplement No 29, 10.6.2010, p. 1, also available at: <http://www.eftasurv.int/state-aid/legal-framework/state-aid-guidelines/>.

¹⁰ A counterfactual means a conventional power plant with the same capacity in terms of the effective production of energy. Point 32 of the previous EAG and point 105 of the new EAG.

¹¹ Point 54 of the previous EAG and point 109 of the new EAG.

¹² Point 54 of the previous EAG and point 109 of the new EAG provides that “Where aid is granted in accordance with point (a) any investment aid granted to the undertaking in question in respect of the new plant must be deducted from production costs when determining the amount of operating aid.”

¹³ Point 54 of the previous EAG corresponds to point 109 of the new EAG.

¹⁴ Extracts from points 54 of the previous EAG and 109(1) of the new EAG.

¹⁵ Both point 54 of the previous EAG and point 109 of the new EAG explicitly states that operating costs includes “*depreciation*” costs.

The market price for electricity shall be taken from the relevant Nord Pool prices. Enova determines the price of electricity based on the latest (at the time of the application) six month average of 3-year forward contracts at Nord Pool.

- 26) The NPV approach is coupled to a competition for aid to ensure that the amount of aid is limited to the minimum necessary.

4.2 Competition for aid under the Energy Consumption - Industry programme

- 27) Grants under the Energy Fund scheme are disbursed under programmes. The funding in the present case is granted on the basis of the Energy Consumption -Industry programme. The Energy Consumption – Industry programme is aimed at measures to reduce energy consumption and/or conversion to renewable energy carriers in the Norwegian mainland industry.
- 28) Enova supports various forms of environmental measures under the Energy Consumption – Industry programme, such as energy recovery, conversion to renewable energy and energy efficiency. Projects are required to have an energy result of minimum 0.1 GWh in order to be eligible for the Energy Consumption -Industry programme¹⁶.
- 29) In order to attract aid applications, Enova makes calls for project proposals at least biannually. Calls for project proposals are announced in major national and regional newspapers in Norway. Interested parties are welcomed to apply for aid throughout the year.
- 30) Interested parties are encouraged to discuss their projects with Enova prior to formally submitting the application for aid. According to the Norwegian authorities, this practice enhances the quality of the applications and ensures that applicants fulfil the minimum requirements and fall under the scope of the Energy Consumption – Industry programme. According to the information provided by the Norwegian authorities, Enova receives approximately 30-40 applications under the Energy Consumption – Industry programme every year.
- 31) All submitted applications are subjected to detailed scrutiny by the case handler team in Enova. To prevent overcompensation of eligible projects, all projects are subject to the following procedure:
- i) When receiving applications for aid, Enova assesses the technical potential for energy production/saving and the relevant costs and benefits described in the application.
 - ii) After the incentive effect is documented by the applicant, Enova undertakes a financial analysis of the projects (the NPV approach) to determine the aid needed to ensure a normal return on capital. Projects with an estimated return on capital which exceeds what is considered normal for the relevant industry will not be eligible for aid.
 - iii) The projects are ranked on the efficiency ratio of KWh energy produced/saved per NOK of aid granted. Eligible projects are awarded aid until the annual budget of the Energy Fund is allocated. Thus, eligible projects might not be awarded aid due to competition from other projects with a better production to aid ratio and limited budgets.
- 32) The selection process for eligible projects, as described above, is conducted in a non-discriminatory, transparent and open manner.

¹⁶ A further description of the programme can be found at www.enova.no.

4.2.1 Södra Cell Tofte AS' project

- 33) SCT applied for aid from Enova on 7 November 2010. On the basis of SCT's application, using the NPV method, Enova found the following investment costs eligible:

Eligible investment costs:

Component	Amount (NOK)
Pine oil reactor for the production of pine oil	[...]
Drying and processing units for bark and lime mud.	[...]
Increase the capacity of the debarking drum.	[...]
Total	[...]

- 34) The lifetime of the project is set at 15 years, excluding the construction period. This is in line with the national depreciation rules¹⁷. The project is expected to be operational from 2014 and set to generate a positive cash flow in 2014.
- 35) In order to ensure that aid is only granted to the most efficient projects, the NPV is coupled to a competition for aid where the applicants compete on producing/saving the most energy for the least amount of aid. Eligible projects are granted aid until the annual budget of the Energy Fund is allocated.
- 36) The discount rate and price of electricity are important inputs in the NPV. For projects awarded aid under the Energy Consumption – Industry programme, the internal rate of return have to provide a fair return on capital to ensure that the projects are sufficiently profitable. Enova determines the price of electricity based on the latest (at the time of the application) six month average of 3-year forward contracts at Nord Pool. At the time of SCT's application, this was NOK 0.345/KWh.
- 37) In applying the NPV methodology, Enova ensures that the aid to the project is strictly confined to the extra costs necessary to meet the environmental objectives.
- 38) The payment and monitoring of the funding is the responsibility of Enova on the basis of the rules laid down in the General Conditions for grants from the Energy Fund¹⁸. Payments are made in instalments based on the actual costs of the investments. 20% of the total award is withheld until Enova has received and approved a final report on the project, which must be submitted two or three months following production start¹⁹. The aid amount may be reduced if, on the basis of the report, it appears that actual investment costs are lower than first assumed. However, if the investment turns out to be more costly than assumed the risk is on the bidder as no additional grants are awarded by Enova.

¹⁷ Event No 628573.

¹⁸ The present General Conditions for the Energy Fund grants are in line with the Norwegian Government's Economic Regulations and stipulate the rights and obligations of Enova and the recipient of funding. In addition a letter of award to each recipient of funding specifies further conditions.

¹⁹ The time limit for submission of the report is stated in the letter of award.

4.2.2 Efficiency ratio

- 39) SCT competes for aid on the basis of the project's efficiency ratio. The applicants under the Energy Consumption- Industry programme compete on producing/saving the most energy for the least amount of aid. Eligible projects are granted aid until the annual budget of the Energy Fund is allocated .
- 40) In the SCT project, the level of aid needed to ensure that the project would be undertaken has been negotiated to a level giving Enova 2 KWh per NOK granted aid, which is similar to other large scale projects granted aid in 2010²⁰.

5. Financing of the project

- 41) The SCT project will receive a grant of NOK 100 million from the Energy Fund. The Norwegian authorities have informed the Authority that the remaining project costs (NOK [...] million) will be financed by SCT through equity capital²¹.

II. ASSESSEMENT

1. The presence of state aid

- 42) State aid within the meaning of Article 61(1) of the EEA Agreement.

Article 61(1) of the EEA Agreement 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.”

- 43) In its Decision No 125/06/COL, the Authority concluded that disbursements to undertakings under the Energy Fund scheme constitute state aid within the meaning of Article 61(1) of the EEA Agreement. There is nothing in the current notification to alter that conclusion.
- 44) It is recalled that SCT has been granted aid under the Energy Consumption – Industry programme of the Energy Fund. First, the funding under the Energy Consumption – Industry programme is coming from various sources controlled by the State and therefore constitutes state resources. Secondly, financial grants are awarded to undertakings which therefore receive an economic advantage they would not have received in their normal course of business. Thirdly, SCT receives a grant under the Energy Consumption – Industry programme in which a limited number of undertakings are awarded aid, and thus are selective. Finally, SCT produces pulp which it sells on the European market. SCT also sells electricity at Nord Pool which implies that some of the electricity is exported to other EEA countries²². Thus, the aid affects trade between the Contracting parties to the EEA Agreement and has the potential of distorting competition because the beneficiary is active in sectors where trade between the Contracting parties takes place.

²⁰ Event Numbers 619622 and 628573.

²¹ Event No 619622.

²² See in this respect Case 730/79 *Philip Morris v Commission* [1989] ECR p. 2671, paragraph 11, where it is stated that “When State financial aid strengthens the position of an undertaking compared with other undertakings competing in intra-Community trade the latter must be regarded as affected by that aid.”

- 45) For these reasons, the grant of NOK 100 million to SCT constitutes state aid within the meaning of Article 61(1) of the EEA Agreement.

2. Procedural requirements

- 46) Pursuant to Article 1(3) of 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”.
- 47) The aid to SCT is granted under the Energy Fund scheme, which was approved on the basis of the previous Environmental Aid Guidelines. On 16 July 2008, the Authority adopted the new Environmental Aid Guidelines (“EAG”). According to the new EAG, investment grants which exceed the threshold set out in paragraph 160(b)(i) of EUR 7.5 million, must be individually notified²³. The aid of NOK 100 million (approximately EUR 12.8 million²⁴) to SCT was therefore notified on the basis of paragraph 160(b)(i) of the EAG.
- 48) On 29 December 2011, the Norwegian authorities notified the aid to SCT. The Norwegian authorities have not paid out any of the aid before the Authority has adopted a final decision. The Authority can therefore conclude that the obligations pursuant to Article 1(3) of Part I of Protocol 3 have been respected.

3. Compatibility of the aid

- 49) As the aid to SCT exceeds the threshold set out in paragraph 160(b)(i) of the EAG, the project must be individually notified. Paragraph 160(b)(i) of the EAG provides that the Authority has to carry out a detailed assessment under Chapter 5 of the EAG in order to verifying the compatibility of the aid with the EEA Agreement. The detailed assessment is a “proportionate assessment” that is, it should be proportionate to the extent to which competition is distorted in individual cases²⁵. The detailed assessment requires a balancing of the positive and negative elements of the aid measure. Thus, the Authority must assess whether the aid addresses a market failure, it is the appropriate instrument, has an incentive effect, is proportional and the impact of the aid on trade and competition. In the end, the Authority must verify that the overall balance is positive so that the positive effects of the aid outweigh the negative effects.
- 50) The Authority has examined the aid to SCT under the EAG and the Energy Fund scheme. As set out above, the Authority approved in its Decision No 125/06/COL the NPV method which limits the maximum amount of aid to what is necessary to bring an, otherwise negative, NPV up to zero. The NPV method is coupled to a competition for aid where aid applicants compete on efficiency ratio of KWh energy produced/saved per NOK of aid granted to ensure that aid is only granted to the most efficient projects.

3.1 Positive effects of the aid

- 51) The main positive element to take into consideration when assessing the compatibility of the aid is that it induces undertakings to pursue environmental protection which they would not otherwise have pursued²⁶.

²³ Paragraph 200(ii) of the EAG provides that the thresholds set out in paragraph 160 apply as of the first day following the adoption of the EAG.

²⁴ Based on the Authority’s exchange rate for 2012 (EUR 1 = NOK 7.7540), available on the Authority’s website: <http://www.eftasurv.int/state-aid/rates>.

²⁵ Paragraph 164 of the EAG.

²⁶ Paragraph 166 of the EAG.

3.1.1 Existence of a market failure

- 52) The environmental objective of the aid is to replace the use of conventional energy with renewable energy. In addition, the aid will also contribute to a slight increase in the production of renewable energy.
- 53) The Norwegian authorities have indicated that the hydropower produced in Norway can meet 98.5% of the current Norwegian electricity demand. In practice, a part of the demand is covered by conventional energy and other renewable energies than hydropower. Moreover, Norway exports energy to other Nordic countries. The other Nordic countries rely on conventional power to a greater extent than Norway.
- 54) The Authority notes that there is a commonly acknowledged market failure consisting of undertakings acting in their own interest without incentives to take into account the costs of negative externalities (pollution) arising from their production. An essential step on the way to achieve the aim of reducing CO₂ emission is to encourage the replacement of conventional energy with renewable energy and production of renewable energy. The investments SCT needs to replace conventional energy with renewable energy are, however, expensive compared to business as usual where SCT will continue to use conventional energy. The sales price for pulp remains the same regardless of whether it has been produced with conventional or renewable energy. The Norwegian authorities have stated that the project would not have been undertaken without aid and that the objective of the Energy Fund is aimed at this market failure by contributing to the costs of producing greener energy in order to encourage the establishment of green energy producers.
- 55) Although replacing conventional energy with renewable energy will somewhat increase SCT's production of electricity, this is by no means sufficient to recoup the extra costs for investing in a more environmental friendly production process.
- 56) The EAG requires that state aid is targeted at the market failure by having a substantial impact on environmental protection in quantifiable terms. The environmental effect of the planned project will be the replacement of 16 000 tonnes of fossil fuels with bio energy. In addition, 17 GWh of electricity will be produced from renewable energy. This will prevent the emission of 16 000 tonnes of fossil fuels into the atmosphere annually, in addition to an increased production of green electricity. Seeing that the aid will help to replace conventional energy with bio energy, the Authority considers that the state aid to SCT contributes to environmental protection in quantifiable terms.

For the reasons set out above, the Authority considers the aid to be targeted at the market failure consisting of the lack of investments in renewable energy²⁷.

3.1.2 Appropriate instrument

- 57) In accordance with paragraphs 169 and 170 of the EAG, the Authority has assessed whether state aid is an appropriate instrument to obtain the objective of environmental protection.
- 58) At the present, there are no national or EEA standards applicable to alleviate the negative elements in this market. The pulp sector and other heavy industry sectors have traditionally relied heavily upon conventional energy. Consequently, the Norwegian authorities have initiated positive individual incentives in order to reduce pollution and other negative impacts on the environment. This has been done by establishing the Energy

²⁷ Paragraph 167 of the EAG.

Fund as administered by Enova. According to the information submitted by the Norwegian authorities, the SCT project will not be eligible for green electricity certificates, as only electricity produced in new boilers and turbines is included in the certificate system²⁸.

- 59) The Norwegian authorities are therefore of the opinion that state aid is the most appropriate instrument to address and correct the market failures, and so, lead to higher environmental protection. The Authority therefore considers that positive encouraging incentives, such as state aid, are appropriate to achieve the objective of increased environmental protection by way of decreasing the use of conventional energy and converting to renewable energy.

3.1.3 Incentive effect and necessity of the aid

- 60) According to paragraph 143 of the EAG, “(t)he Authority considers that aid does not present an incentive effect for the beneficiary in all cases in which the project has already started prior to the aid application by the beneficiary to the national authorities.” SCT submitted its application for aid to Enova on 7 November 2010, i.e. before the start-up of the project. Therefore, the incentive effect referred to in paragraph 143 of the EAG is met. Under the detailed assessment, the Authority must further assess the incentive effect and necessity of aid in accordance with paragraphs 171-173 of the EAG.
- 61) According to paragraph 171 of the EAG, the aid “*must result in the recipient changing its behaviour to increase the level of environmental protection*”. Normally, this can be demonstrated by showing that the project realised with aid has an increased environmental benefit compared to the credible counterfactual²⁹. However, the Authority notes that the reference to a counterfactual situation is linked to the method in the EAG for determining eligible investment costs. As a consequence of accepting the NPV method as the basis for determining the maximum aid amount, the appropriate manner to examine the incentive effect is not a comparison with an alternative behaviour, but rather whether the use of the NPV method is evidence that SCT would not, without the aid, have engaged in the same activity because of its intrinsic benefits³⁰. Such an approach will equally show whether the aid has changed the behaviour of the recipient. This approach is indirectly expressed in point 172(g) of the EAG which states that, where the project is not profitable (without the aid), aid will normally have an incentive effect³¹.
- 62) The Authority notes that the NPV method consists of determining the amount required to bring an otherwise negative NPV up to zero. As stated in Decision No 125/06/COL, no rational investor can be expected to launch a project with a negative NPV and for this reason the NPV calculation can serve as a demonstration of the indispensability of the aid granted.
- 63) Enova applies the NPV method in order to determine how much aid is needed in order to trigger the investment. A project is triggered when it reaches an NPV of zero with a reasonable rate of return. Experience has shown Enova that companies usually require a rate of return between 12% - 16% for energy investments outside their core activity under

²⁸ According to the Norwegian authorities, if SCT should qualify for green certificates for the electricity production of 17 GWh, they will have to renounce the total grant from Enova – see Event No 628573.

²⁹ Paragraph 172(a) of the EAG.

³⁰ Paragraph 27 of the EAG in the chapter on “*Incentive effect and necessity of the aid*” states that “*investments which increase the level of environmental protection may at the same time increase revenues and/or decrease costs and thus be economically attractive in their own right.*”

³¹ Paragraph 172(g) of the EAG states that where the profitability level is negative over the life time of the project (*i.e.* full depreciation) aid will normally have an incentive effect.

normal market conditions as there might be specific risks related to such investments³². Without the aid, the rate of return in the SCT project would be 3.50%³³. SCT is not prepared to carry out the project with a rate of return of 3.50%. After negotiations with Enova, SCT accepted a rate of return of 8.98%³⁴. The Norwegian authorities have explained that Södra AB usually requires a significantly higher rate of return for energy projects³⁵. However, SCT accepted a lower rate of return in this project as SCT regards it as being of strategic importance in terms of their overall aim to terminate the use of fossil fuels and convert to bio energy³⁶.

- 64) Further, the Authority considers that the expected environmental effect is linked to the change in behaviour as required by point 172(b) of the EAG: SCT would not, without the aid, have converted to the use of renewable energy which will eliminate the use of 16 000 tonnes of fossil fuels.
- 65) There are no ongoing negotiations at national or Community level to introduce new mandatory standards for the use of renewable energy in the pulp industry.
- 66) In light of the above, the Authority considers the aid to have incentive effect.

3.1.4 Proportionality of the aid

- 67) Paragraph 174 of the EAG requires that the amount of state aid must be limited to the minimum to bring about the investment. In making this assessment account shall be taken (i) of an accurate cost calculation (limiting the costs to the necessary); (ii) of the presence of a non-discriminatory selection process; and (iii) that the aid should not exceed the lack of profitability (including a normal return over the life time).
- 68) The second criterion is dealt with first. SCT applied for aid under Enova's Energy Consumption - Industry programme in 2010. The programme is announced in all major national and regional newspapers in Norway and described in full on Enova's website. All applicants are welcome to discuss their projects with Enova prior to submitting an application. All applications are subject to the same criteria: (i) projects which are sufficiently profitable without the aid are not eligible for support, (ii) the rate of return cannot exceed the level of what can be considered as a normal return, (iii) all projects must have a total energy goal of at least 0.1 GWh, and (iv) a project lifetime of minimum 10 years (after construction). These criteria are applied to all applicants in an objective and non discriminatory manner.
- 69) The Norwegian authorities have provided a description of the costs and their calculation³⁷. The calculation of eligible cost seems accurate. This, however, does not ensure that the costs are limited to the minimum necessary. The criterion that costs are kept to the minimum can be verified by examining the NPV method coupled to the competition for aid under the Energy Consumption- Industry programme. In the same context, the question of whether the aid exceeds the lack of profitability can be answered.
- 70) As regards the requirement that the aid does not exceed the lack of profitability, this is the objective of determining the amount of aid needed by calculating its NPV. By calculating

³² Event No 628573.

³³ With an NPV of zero.

³⁴ With an NPV of zero.

³⁵ Enova has provided the Authority with examples of different rates of return required by Södra AB in other energy projects - Event Numbers 619622 and 628573.

³⁶ The term strategic does not refer to SCT's financial strategy in this case – see Event No 619622.

³⁷ Event Numbers 61622 and 628573.

the NPV of a project, Enova determines the amount of aid necessary to trigger it. Aid is only granted to bring the NPV to zero (with a reasonable return on capital).

- 71) Furthermore, as regards the limitation of the costs to the minimum necessary, the Authority notes that only the most efficient projects are selected. The applicants compete on producing/saving the most energy for the least amount of aid. The SCT project had an efficiency ratio of 2 KWh per NOK granted aid, which is similar to other large scale projects receiving aid in 2010³⁸. Enova's efficiency requirements therefore ensure that the aid to SCT is limited to the least amount necessary to trigger the project.
- 72) In conclusion, the Authority considers that the open, transparent and non-discriminatory selection procedure in addition to the application of the NPV method coupled with the competition for aid, ensure that the overall aid amount is limited to what is necessary to carry out the project. In light of this, the aid to SCT is proportionate.

3.2 Analysis of the distortion of competition and trade

- 73) The Authority has examined the distortion of competition in light of the impact of the aid on competition and trade between undertakings in the relevant markets.
- 74) Based on the information provided by the Norwegian authorities, the Authority has concluded that the relevant product market should be the market for production of chemical pulp³⁹.
- 75) By taking into account the information provided by the Norwegian authorities, the Authority has concluded that the geographical market for pulp is global⁴⁰. Pulp is traded between suppliers and buyers located on different continents. Big suppliers of pulp are the Nordic countries, North America, Latin America and Russia, while buyers of pulp are Europe (without the Nordic countries), Japan, China, India and Mexico⁴¹. The market is characterised by many suppliers. Södra Cell AB has a market share of 4%, whilst SCT has a market share of 0.75% on the relevant market.
- 76) With regard to point 177 of the EAG, on the basis of the information provided by the Norwegian authorities, the Authority finds it unlikely that SCT will be able to increase the production of pulp as a result of the aid. The aid measure will not increase SCT's production capacity of pulp⁴², nor will it enable SCT to produce a new or higher quality product⁴³. Pulp is sold on the market without any form of labelling with regard to environmental product image. The Norwegian authorities have submitted that it is unlikely that a more environmentally friendly production process will influence customers to purchase more pulp from SCT⁴⁴. In light of this, the more environmentally friendly production process is unlikely to have an impact on customer demand and general market conditions for SCT's product⁴⁵.
- 77) In addition, SCT also produces electricity which is being sold on Nord Pool. The aided measure will increase the amount on electricity SCT will sell on Nord Pool from 9 GWh to 26 GWh annually. The Norwegian authorities submit that the relevant product market

³⁸ This is somewhat lower than the average efficiency ratio in 2010. This is because most of the projects granted aid under the Energy Consumption – Industry programme in 2010 were small companies receiving smaller amounts of aid.

³⁹ Event No 619622.

⁴⁰ Event Numbers 619622 and 628573.

⁴¹ Event No 628573.

⁴² Paragraph 177(a) of the EAG.

⁴³ Paragraph 177 (c) of the EAG.

⁴⁴ Event No 628573.

⁴⁵ Paragraph 177(b) of the EAG, and see Event No 628573.

shall be defined as the market for wholesale supply of electricity. The Norwegian authorities base their view on the Concluding Report for the inquiry into the Norwegian energy market published 10 January 2007. The Norwegian authorities are of the opinion that the structure and functioning of the Norwegian electricity market has not significantly changed since then and thus, can still apply. The excess energy produced by SCT, approximately 26 GWh annually, will be fed into the grid and sold at Nord Pool. Once delivery has been made, it is no longer possible to separate supplies from different generators. The electricity price is primarily determined by supply and demand in the Nordic power market.

- 78) The Authority notes that the detailed assessment is a “proportionate assessment”, that is, it should be proportionate to the extent to which competition is distorted in individual cases⁴⁶. In the present case, the market shares of SCT on both relevant markets are very limited. Even when taking into account the market shares of the parent company, Södra Cell AB, it is evident that the aid will not appreciably affect competition and trade. The Authority therefore concludes that the effects on competition and trade are very limited.

3.2.1 Dynamic incentives/crowding out

- 79) In accordance with paragraphs 178 and 179 of the EAG, the Authority has assessed whether the aid may distort dynamic incentives or crowd out investments in the specific technology in other EEA states.
- 80) The Authority considers that the aid will not crowd out investments in other EEA States or distort dynamic incentives for investing in the technology. On the basis of the information provided by the Norwegian authorities, the Authority finds it unlikely that the investment aid will provide SCT with a first mover advantage in the relevant market as the production process is based on commercially available technology nor will any new products or production technologies result from the investment.

3.2.2 Maintaining inefficient firms afloat

- 81) In accordance with paragraph 180 of the EAG, the Authority has assessed whether the aid will contribute to keep an inefficient firm afloat.
- 82) On the basis of the information provided by the Norwegian authorities, the Authority concludes that SCT is not an inefficient company which would need to be held afloat with the aid. Enova has examined the financial statements of SCT for the last five years to ensure that the undertaking is not experiencing financial difficulties. The electricity produced will be sold on the Nord Pool exchange. The Norwegian market is not characterised by overcapacity and inefficient market structure.

- 83) In light of the above, there is no evidence that SCT is in financial difficulties.

3.2.3 Market power/exclusionary behaviour

- 84) In accordance with paragraphs 181-182 of the EAG, the Authority has assessed whether the aid will affect SCT’s market power in the relevant markets.
- 85) According to the information provided by the Norwegian authorities, the world-wide annual production of pulp amounts to approximately 52.5 million tonnes. Södra Cell AB’s total production amounts to 2 million tonnes of which SCT’s annual production of 400 000 tonnes is included. This gives Södra Cell AB an overall market share of 4% and SCT a market share of 0.75% of the global market. Neither SCT nor Södra Cell AB are

⁴⁶ EAG paragraph 164.

dominant on the pulp market nor will the aid enable SCT to increase production. It is therefore unlikely that SCT will be able to increase its market position in the pulp market.

The buyers of pulp have a number of suppliers to choose amongst. If SCT changes its behaviour in the market (for example by increasing prices), potential buyers can choose among a number of alternative suppliers, thus, the behaviour would be counterbalanced by the market forces as the buyer would simply change its source of supply. As a result, the Authority is of the opinion that the aid will not allow SCT to increase its market position on the relevant market as a consequence of the aid.

- 86) On the Norwegian electricity market, relatively small players will not realistically be able to dictate or substantially influence prices. The national market power of SCT is 0.007%. With the aid, it is expected that SCT's market power will increase to 0.02%, hence, the structure of the market for electricity production is not likely to be altered by the grant of aid to SCT. By comparison, the largest electricity producer in Norway, Statskraft Energi AS, has a market share of 30% owning facilities with a total capacity of 8 667 MW producing an annual 35 900 GWh⁴⁷. Thus, the Authority considers it unlikely that the aid will significantly strengthen or maintain market power of SCT on the electricity market.

3.2.4 Effects on trade and location

- 87) In accordance with paragraphs 183-185 of the EAG, the Authority has assessed whether the state aid will have effects on trade and location.
- 88) The pulp produced by SCT is sold on a global market. Based on the available information, there is nothing that indicates that certain territories will benefit from more favourable production as a consequence of the aid.
- 89) The electricity produced by SCT will be sold on Nord Pool. The Authority considers it unlikely that the aid will attract more investments to the region where SCT is located.
- 90) In light of the above, the Authority considers that the aid will not have a significant effect on trade and location.

3.3 Balancing

- 91) On the basis of the above, the Authority considers that the positive effects of the aid to SCT, namely the fact that the aid is aimed at converting from the use of conventional energy to the use of self produced bio energy, outweigh the negative potential which the aid might have on competition and trade.

4. Conclusion

- 92) On the basis of the foregoing assessment, the Authority considers that the aid to Södra Cell Tofte AS which the Norwegian authorities are planning to implement, is compatible with the functioning of the EEA Agreement within the meaning of Article 61 of the EEA Agreement.

HAS ADOPTED THIS DECISION:

Article 1

⁴⁷ See Event No 619622.

The EFTA Surveillance Authority raises no objections to the aid to Södra Cell Tofte AS amounting to NOK 100 million.

Article 2

The implementation of the measure is authorised accordingly.

Article 3

This Decision is addressed to the Kingdom of Norway.

Article 4

Only the English language version of this decision is authentic.

Decision made in Brussels, on 19 April 2012.

For the EFTA Surveillance Authority

Oda Helen Sletnes
President

Sabine Monauni-Tömördy
College Member