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[The information in square brackets is covered by the obligation of professional secrecy]

## EFTA SURVEILLANCE AUTHORITY DECISION

of 20 May 2015

on the transmission of electricity to the PCC Silicon Metal Plant at Bakki  
(2015 Transmission Agreement)

(Iceland)

The EFTA Surveillance Authority (“the Authority”),

HAVING REGARD to the Agreement on the European Economic Area (“the EEA Agreement”), in particular to Article 61(1) and Protocol 26,

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(2) of Part II,

Whereas:

### I. FACTS

#### 1 Procedure

- (1) Following pre-notification discussions<sup>1</sup>, by letter dated 25 March 2015 and registered on 31 March 2015, the Icelandic authorities notified for legal certainty an electricity transmission agreement between Landsnet hf. and PCC Bakki-Silicon hf. at Bakki in Húsavík in North-East Iceland pursuant to Article 1(3) of Part I of Protocol 3.<sup>2</sup>
- (2) The notification also refers to previous correspondence sent to the Authority in the framework of previous cases (Decision No 111/14/COL - see paragraph (3) and Decision No 543/14/COL - see paragraph (7) below).

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<sup>1</sup> Doc Nos 748037-39.

<sup>2</sup> Doc Nos 752791-93.

## 2 Background information

- (3) By Decision No 111/14/COL<sup>3</sup>, adopted on 12 March 2014, the Authority approved 23.33 million EUR<sup>4</sup> regional investment aid to PCC Bakki-Silicon hf. for its planned energy-intensive silicon metal plant at Bakki in Húsavík, according to an investment agreement entered into between the company and the Icelandic Government on 27 September 2013 on the basis of Act No 52/2013 (“the PCC Act”). The investment agreement was notified to the Authority on 4 July 2013.
- (4) In order to operate the new silicon metal plant, a power contract and a transmission agreement for that power are required. A first power purchase agreement was signed between Landsvirkjun and PCC on 28 June 2012. The conditions precedent of the contract were not met in time and the contract was terminated.
- (5) On 17 March 2014, Landsvirkjun and PCC signed a second power contract (“the 2014 Power Contract”). A transmission agreement between Landsnet and PCC was also signed on 7 February 2014 (“the 2014 Transmission Agreement”).
- (6) On 17 April 2014, the 2014 Power Contract was notified for legal certainty to the Authority. The 2014 Transmission Agreement was not notified. Neither the 2014 Power Contract nor the 2014 Transmission Agreement fell under the scope of Decision No 111/14/COL.<sup>5</sup>
- (7) By means of Decision No 543/14/COL,<sup>6</sup> the Authority opened a formal state aid investigation, as provided for in Article 1(2) of Part I of Protocol 3 to the Surveillance and Court Agreement, into the 2014 Power Contract and, *ex officio*, into the 2014 Transmission Agreement.
- (8) The 2014 Transmission Agreement was concluded subject to certain conditions that have not been fulfilled, according to information provided by the Icelandic authorities.<sup>7</sup> On 19 March 2015, Landsnet and PCC signed a new Transmission Agreement (hereafter “The Transmission Agreement” or “The Agreement”) replacing the agreement from 2014, which has now been terminated and is without legal binding effects, as foreseen in Article 28 of the new Agreement. The Transmission Agreement has been notified for legal certainty to the Authority and is the object of the present Decision.

## 3 The contracting parties

### 3.1 PCC

- (9) PCC Bakki-Silicon hf. (“PCC”) is a limited liability company incorporated in Iceland in June 2012, majority owned by PCC SE, an international holding company based in Duisburg, Germany. The group employs more than 2 800 employees at 36 sites in 16

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<sup>3</sup> Available at the Authority’s website: [http://www.eftasurv.int/media/state-aid/decision\\_111\\_14\\_COL.pdf](http://www.eftasurv.int/media/state-aid/decision_111_14_COL.pdf).

<sup>4</sup> Net present value (NPV) of the aid was 13.64 million EUR.

<sup>5</sup> See Decision No 111/14/COL paragraphs 10 and 11. OJ C 207, 3.7.2014, p. 42 and in Icelandic and Norwegian in the EEA Supplement to the Official Journal No. 39, 3.7.2014. The full text of the Decision is available at: [http://www.eftasurv.int/media/state-aid/decision\\_111\\_14\\_COL.pdf](http://www.eftasurv.int/media/state-aid/decision_111_14_COL.pdf)

<sup>6</sup> See OJ C 92, 19.3.2015, p.3, and EEA Supplement No 15, 19.3.2015. Available at the Authority’s website: <http://www.eftasurv.int/media/decisions/543-14-COL.pdf>

<sup>7</sup> See letter received 20.10.2014, page 4. Doc No 726154.

countries. Their group sales are generated in three divisions, i.e. chemicals, energy and logistics. In 2013, group sales amounted to EUR 625 million.<sup>8</sup>

### 3.2 *Landsnet*

- (10) Following the liberalization of the electricity sector, the Electricity Act No 65/2003 (“the Electricity Act”) was adopted in 2003 and on 1 January 2005 Landsvirkjun's Transmission Division became Landsnet hf., a limited liability company, owned by the Icelandic Treasury, and later a subsidiary of Landsvirkjun.<sup>9</sup> Landsnet is the Icelandic transmission system operator (“TSO”), i.e. it owns and operates the Icelandic transmission system.
- (11) According to Article 8 of the Electricity Act, a sole company shall be entrusted with the transmission of electricity in Iceland and the balancing of the electricity. According to the Act, the majority stakeholders in the TSO shall be the State and/or entities or companies solely owned by the State. Act No 75/2004 on Landsnet (“the Landsnet Act”) established Landsnet as the sole TSO in Iceland. The operation of Landsnet as a TSO is regulated by Orkustofnun (the National Energy Authority). As a TSO, Landsnet is required to operate in a non-discriminatory manner. Landsnet is under the surveillance of Orkustofnun.
- (12) According to the Landsnet Act, the company’s board of directors was initially appointed directly by the Minister (of Industry and Commerce). The current board of directors is elected by the shareholders of the Company in accordance with the Icelandic Companies Act. According to Article 8(5) of the Electricity Act, the board shall operate independently from other companies operating in the field of generation, sale or distribution of electricity as further outlined in Article 16 of Landsnet’s Articles of Association. At the outset, the Icelandic Treasury was the sole owner of the shares in Landsnet and subsequently the shares were transferred to state owned utilities in Iceland in exchange for their transmission system assets, which became part of Landsnet’s assets.

## 4 The Icelandic Transmission system

- (13) The Icelandic transmission grid includes more than 3.000 km of transmission lines and about 70 substations and transformer stations. As stipulated in Article 3 of Landsnet’s General tariff<sup>10</sup>, the transmission system has 20 points of supply (In-feed) and 65 points of delivery (Out-feed), of which 59 are for distribution systems and 6 for power intensive users. The transmission of electricity to the rural part of Iceland is mainly through a number of connected 132 kV electricity lines. These lines, together with the 220 kV lines in the south-western part of the country, form a circle connecting most of the country to the electricity system. The capacity of the 132 kV transmission system is insufficient and those constraints limit the power transmission between areas (see figure 1).

<sup>8</sup> Further information is available at: [https://www.pcc.eu/ttw/pcc.nsf/id/EN\\_Home](https://www.pcc.eu/ttw/pcc.nsf/id/EN_Home)

<sup>9</sup> Landsnet is owned by the following state owned utilities: Landsvirkjun 64.73%, RARIK (Iceland State Electricity) 22.51%, Orkuveita Reykjavíkur (Reykjavík Energy) 6.78% and Orkubú Vestfjarða (Westfjord Power Company) 5.98%.

<sup>10</sup> Landsnet’s General tariff is available at: <http://landsnet.is/library/Skrar/Raforkukerfid/Flutningsgjaldskrar/2015/Gjaldskrá%20nr%0Gildir%20frá%201%20februar%202015.pdf>.

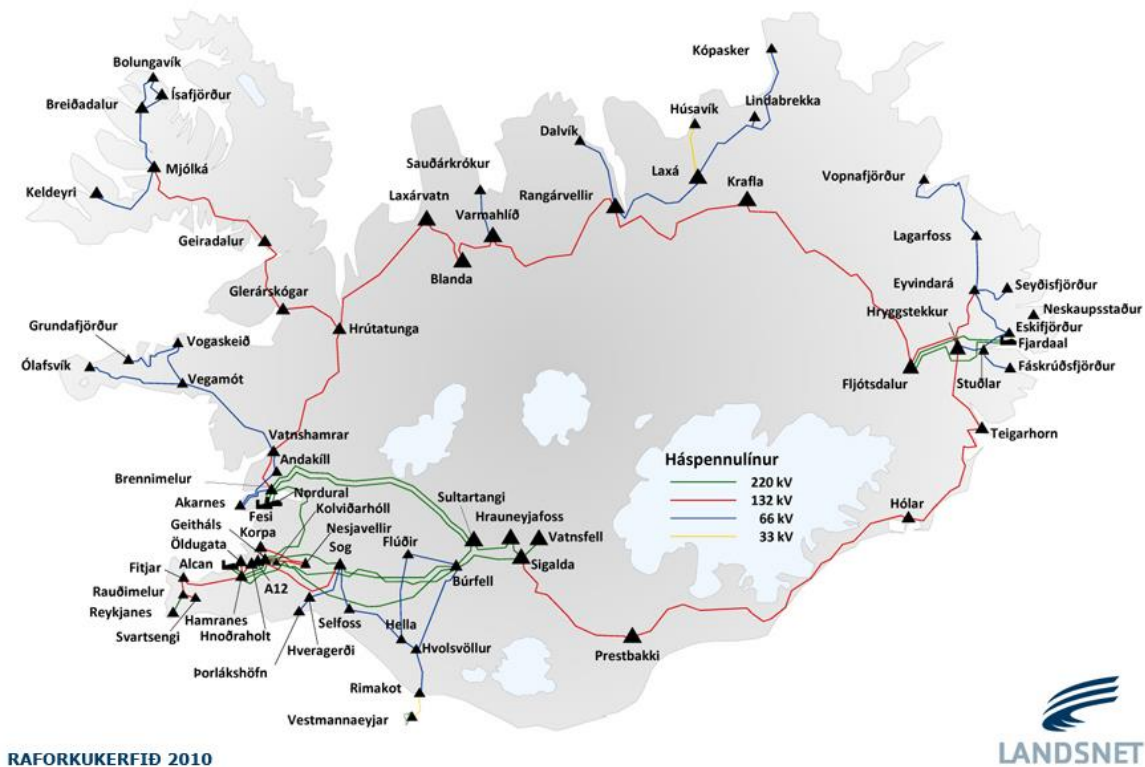


Figure 1. Source: Landsnet

- (14) The transmission lines in the north-eastern part of Iceland consist of connected 132 kV lines from Rangárvellir substation in Akureyri, to the substation at Krafla power station and then onwards to the substation in Fljótsdalur in the eastern part of Iceland. From the substation at Rangárvellir there is a single 66 kV line that stretches to the northeast to the town Kópasker. From that 66 kV line there is also a single 33 kV line, which is one of the oldest transmission lines in the whole transmission system, connecting the town of Húsavík to the transmission system.
- (15) According to the Electricity Act, the TSO is responsible for the connection and access of eligible customers to the transmission system. Eligible customers to the transmission system are mainly distribution system operators (DSOs), power intensive users and power producers. The objective of the transmission system is to deliver electricity from power producers to distribution systems and power-intensive industries. Furthermore, the transmission system operator is obligated by the Electricity Act to ensure the availability of a forecast on the projected demand for electricity and a plan for the development of the transmission system.

## 5 Transmission network charges in Iceland

- (16) In Iceland, transmission network charges are established by Landsnet. However, the charges have to be authorized by the regulator, Orkustofnun.
- (17) Article 12a of the Electricity Act and Article 15 of Regulation No 1040/2005 on the implementation of the Electricity Act, as amended (“the Electricity Regulation”) set out principles governing the establishment of transmission network charges (out-feed):
- Network charges shall be cost-oriented.
  - Tariffs shall be non-discriminatory, objective and transparent and approved by Orkustofnun.

- A revenue cap is established by Orkustofnun, based on historical costs, including depreciation of assets, and a set profit margin. One tariff applies for DSOs, calculated in Icelandic Króna, and another for energy-intensive users, calculated in US Dollars.
- Out-feed tariff for DSOs is based on (i) total electricity transmitted to the DSO's geographical area; plus (ii) direct out-feed from power plants within the area.
- Tariffs for DSOs shall be based on average cost and depend on the network connection level (calculated on the basis of 66 kV) but regardless of the physical distance between the places of supply.
- When power is transmitted directly by the TSO to an energy-intensive user at a voltage 66 kV or below, a surcharge shall be charged to cover the additional cost of stepping down ("the Step-down Surcharge").
- Extra charge shall be levied for the necessary additional costs resulting from connecting new power facilities or new energy-intensive users, which would otherwise increase the fees for the existing users ("the System Contribution"), and reduced tariff if it results in more favourable development or utilisation of the network.

### 5.1 The Transmission Charge

(18) The Icelandic authorities have explained that the Transmission Charge for energy-intensive users is, according to a tariff approved by Orkustofnun on the basis of the Electricity Act,<sup>11</sup> a combination of:

- delivery charge per year;
- capacity charge per MW per year ("the Capacity Charge");
- energy charge per kWh ("the Energy Charge");
- fee for ancillary services per kWh; and
- transmission losses per kWh.

### 5.2 The Step-down Surcharge

(19) The Step-down Surcharge has its legal basis in Article 12a(7) of the Electricity Act, which reads:

"The Transmission System Operator may deliver electricity to energy-intensive users at voltage 66 kV or below, provided a special charge covers the extra costs."<sup>12</sup>

(20) The Step-down Surcharge is an additional fee, added to the Capacity Charge and the Energy Charge and is meant to compensate for the actual cost of stepping down the electricity for an energy-intensive user. The Icelandic authorities have explained that the stepping-down services are not part of the public service obligation imposed on Landsnet, but rather an

<sup>11</sup> Available at <http://landsnet.is/english/transmissionandmarket/transmissiontariff/tariff/>.

<sup>12</sup> The Authority's informal translations. The Icelandic text reads: "Flutningsfyrirtækinu er heimilt að afhenda raforku til stórnótenda á 66 kV eða lægri spennu enda standi sérstök gjaldtaka undir viðbótarkostnaði."

option the company has in order to provide additional services to its customers.<sup>13</sup> Similarly, customers are not required to contract this service with Landsnet. The step-down service can be provided by the customer itself, by a third party or by Landsnet.

- (21) In order for Landsnet to provide stepping down services to energy intensive users, two conditions have to be met: (i) the delivery of electricity at lower voltage than 132 kV has to be agreed to by the DSO of the area, in order to guarantee the most economic use of existing facilities and distribution capacity, and (ii) extra costs of the stepping down must be covered by a Step-down Surcharge, as this is not a service which is part of the general operation of the transmission system.
- (22) The Step-down Surcharge is calculated on the basis of the actual step-down costs according to a formula in Section B.9 of a grid code issued by Landsnet on 1 March 2015, (“the Grid Code”), on Terms for Delivering Electricity to Power Intensive Users at Voltages below 132 kV.<sup>14</sup>
- (23) The formula currently in force establishes that the share of the step-down costs to be included in the formula shall amount to 80%-100% of the total step-down cost (before 1 March 2015, in all cases this percentage was 80%).
- (24) The formula reads as follows:

$$\text{Surcharge} = \frac{\text{Initial cost} \times \text{Annual percentage} \times \text{Share in stepped-down voltage cost}}{(\text{Energy amount} \times \text{Energy charges} + \text{Power} + \text{Power charges})}$$

Where:

*Initial cost* signifies the starting costs on account of voltage step-down, entered in USD

*Annual Percentage* refers to the percentage of the initial costs to be collected each year, comprising depreciation, financial costs, required rate of return and operating costs.

*The share in stepped-down voltage cost* amounts to **80-100%** of the stepping down expense [*stress added*]

*Energy amount* is the customer’s annual amount of energy, in MWh

*Energy charges* are the charges for energy to power intensive users, according to the Landsnet tariff

*Power* stands for the customer’s agreed peak power

*Power charges* are the charges for power to power intensive users, according to Landsnet tariff.

Figure 2. Source: Section B.9 of the Grid Code, Article 4.2.

- (25) Landsnet has also explained to the Authority that the exact amount of the Step-down Surcharge can only be established once the actual costs of the investments are known. The

<sup>13</sup> According to Landsnet, the Electricity Act was amended in 2011 to include an authorization for Landsnet to provide step-down services. The reason for this authorization was that DSOs were not in all instances in a position to provide the services. Allowing Landsnet to provide these services was considered necessary to guarantee that the stepping-down would not lead to disruption in the operation of the transmission system. Furthermore, it was considered economically feasible as the cost of stepping-down could be lowered with the pooling of such services and the standardisation of the equipment.

<sup>14</sup> The Grid Code is signed on behalf of the Minister of Industry and Commerce. See [http://landsnet.is/library/Skrar/Raforkukerfid/Netmali/B9\\_English%20v2%200\\_published.pdf](http://landsnet.is/library/Skrar/Raforkukerfid/Netmali/B9_English%20v2%200_published.pdf).

Transmission Agreement provides for estimated costs and estimated surcharges, which will be updated if necessary once the actual costs are known.

### 5.3 System Contribution Surcharge

- (26) The System Contribution Surcharge has its legal basis in Article 12a(10), first indent, of the Electricity Act, which reads:

“Additional fee shall be charged in case new power plants or new energy-intensive users cause additional costs for existing users.”<sup>15</sup>

- (27) The Icelandic authorities have provided the following general presumptions for this calculation of the System Contribution<sup>16</sup>:

WACC	Power	Utilization time	Proportion of income for return on investment calculations (ht)	Operating cost rate
5.31%	52 MW	8,000 h/year	27%	1.2%

and the following formula used for cash flow calculations of the investment:

$$\text{Cash flow} = \frac{\text{Investment} \cdot \text{WACC}}{1 - (1 + \text{WACC})^{\text{years}}}$$

$$\begin{aligned} \text{Transmission charges} \\ &= ht \cdot (\text{Delivery charge} + \text{Power} \cdot \text{Capacity charge} + \text{Energy} \cdot \text{Energy charge}) \end{aligned}$$

$$\begin{aligned} \text{System contribution payments} \\ &= \text{Cash flow} - \text{Transmission charges} + \text{Operating cost} \end{aligned}$$

- (28) The income framework of Landsnet is based on the company’s assets, approved by Orkustofnun. Landsnet splits its assets into three categories, as assigned to the in-feed, the main and the out-feed parts of the grid. The following proportional assignment of the asset base for the energy-intensive users is currently applied by the company<sup>17</sup>:

	In-feed	Main	Out-feed
Energy-intensive users	11%	62%	27%

- (29) The connection of an intensive user to the grid belongs to the Out-feed part of the grid. Consequently, when calculating the System Contribution, Landsnet applies 27% of the Transmission Charges which the client would pay, as an income when calculating the return on the investment needed to connect a new production plant to the grid. The proportional assignment of 27% for the out-feed part of the grid is not based on a statutory rule. However, the rationale being that this proportion (27%) is the same as the one assigned to the out-feed part of the grid. Landsnet’s regulated assets are divided between distribution and power intensive users according to a ratio decided on the basis of capacity ratios (power

<sup>15</sup> Informal translation by the Authority. The Icelandic text reads: “Krefjast skal greiðslu ef tenging nýrra virkjana eða stórnótenda við flutningskerfi veldur auknum tilkostnaði annarra notenda kerfisins.”

<sup>16</sup> Doc No 726154, page 6.

<sup>17</sup> *Ibid*, page 7.

consumption) between distribution and power intensive consumers, as approved by Orkustofnun.

- (30) Orkustofnun reviews the profitability calculations provided by Landsnet for the connections of new energy-intensive users in the context of assessing applications from Landsnet for a licence for construction of new transmission facilities with components of 66 kV and above. This is so, since the construction of transmission facilities at the voltage 66 kV and above are subject to a licence issued by Orkustofnun, according to Article 9(2) of the Electricity Act.
- (31) Orkustofnun has confirmed to the Authority that the principles described above in calculating the System Contribution are applied by Landsnet in a systematic and non-discriminatory manner, and that the methodology in calculating the System Contribution is reviewed by Orkustofnun in each investment case for energy-intensive users when the licence for construction of new transmission facilities is requested. Orkustofnun has also explained that the calculations on the System Contribution Surcharges included in the Transmission Agreement provide for estimated figures, the exact amount of such a surcharge can only be known once the actual costs of the foreseen investments are known.<sup>18</sup>
- (32) Moreover, Article 15(11) of the Electricity Regulation provides that the TSO shall inform the new energy-intensive user beforehand of whether a System Contribution Surcharge will be charged and shall provide him with the assumptions on the basis of which it is calculated.

## 6 The notified measure: The 2015 Transmission Agreement

- (33) As already stated, Landsnet and PCC entered into the Transmission Agreement on 19 March 2015.
- (34) The Transmission Agreement concerns the connection of the new PCC Plant to the transmission system; the transmission of the power purchased by PCC from Landsvirkjun; and the transformation of the purchased power from the transmission voltage to 33 and 11 kV, to enable the in-feed of 52 - 58 MW power.<sup>19</sup>
- (35) The Icelandic authorities have explained that 45 MW thereof will be supplied by Landsvirkjun's planned Power Station at Þeistareykir and the rest from other power plants connected to the transmission system (Table 1 of Annex 1 to the Agreement). The Transmission Agreement has a few conditions precedent, *inter alia*, it is conditioned upon the Authority's approval.<sup>20</sup>
- (36) Taking into account the need to provide transmission services to PCC, Landsnet has decided to profit from this occasion and develop the connections of the north-eastern part of Iceland. The plan is to connect the Þeistareykir Power Station to Krafla substation and from Þeistareykir to the industrial site of Bakki. In order to guarantee the transmission service to PCC, it will be sufficient for Landsnet to connect the industrial site of Bakki to the Power Station at Þeistareykir with a 132 kV line (see figure 3). Furthermore, Landsnet has explained that there is also a need to upgrade the 33 kV connection to Húsavík. The connection of Bakki allows Landsnet to include the new Húsavík connection in the connection of the industrial site at Bakki.

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<sup>18</sup> Doc No 748004.

<sup>19</sup> Article 2.2 of the Agreement.

<sup>20</sup> Article 26.2 of the Agreement.



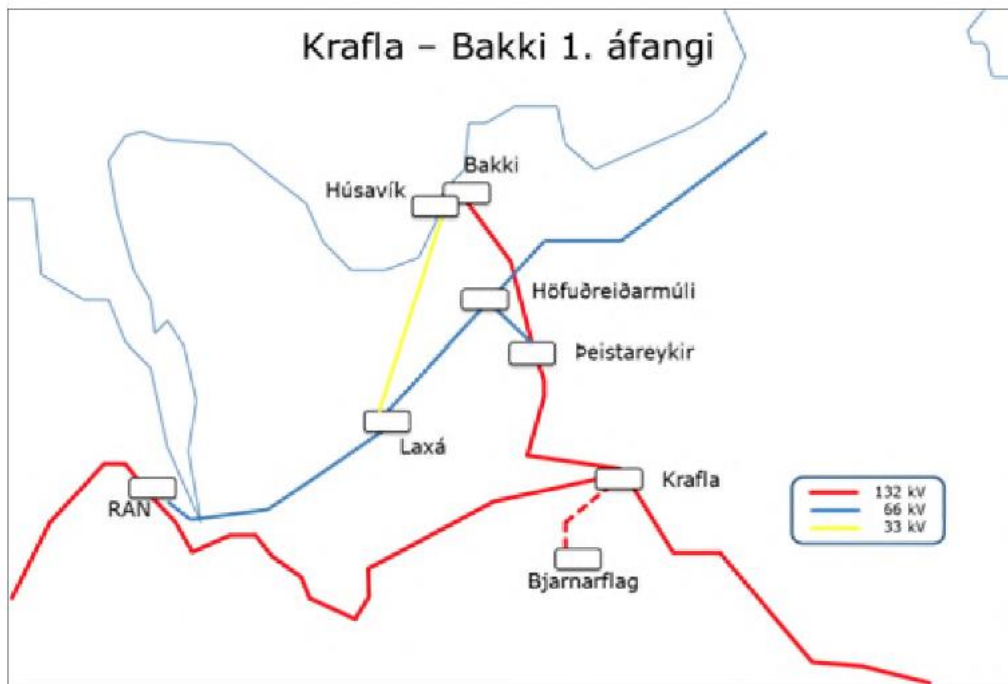


Figure 3. Source: Image 1 of Annex 1 to the Transmission Agreement.

(37) According to Article 10.1 of the Transmission Agreement, the fees are the following:

- the “Transmission Charge”, a fee for transmitting the Contract Power, including a delivery charge, a capacity charge and an energy charge. PCC will also pay for ancillary services, transmission losses and a firm commitment (Take-or-Pay obligation), as defined in the Transmission Agreement; and
- the Step-Down Surcharge, a surcharge for having the Contract Power delivered at 33 and 11 kV voltage instead of the grid voltage level (with reference to Annex 5 to the Transmission Agreement, the Authority understands that the step down here is from 220 kV).

(38) Moreover, the Agreement refers in Annex 1 to the transmission system works to be constructed by Landsnet. Table 4 of Annex 1 to the Agreement provides the estimated costs of the investments needed in order to connect the PCC Plant to the transmission system. However, the Agreement does not foresee a System Contribution Surcharge to be paid by PCC. According to Article 10.1 of the Agreement “[t]here is no basis for payment of system contribution from Bakkisilicon due to Landsnet’s costs associated with the Transmission System Works”.

### 6.1 The Transmission Charge

(39) Article 10.1 of the Transmission Agreement refers to a sample of an invoice attached in Annex 4 to the Agreement. The Transmission Charge to be applied is the one referred to in section 5.1. above.

### 6.2 The Step-down Surcharge

(40) The Transmission Agreement refers to a Step-down Surcharge in Article 10 and Annex 5.

- (41) In order to calculate which amount PCC should pay in order to remunerate the stepping-down services, Landsnet applies a formula which is in line with the one provided for in Article 4.2 of Section B.9 of the Grid Code (see section 5.2. above).
- (42) Annex 5 to the Transmission Agreement establishes nevertheless that the percentage of the stepping-down costs to take into account in the formula is 80 % (as stated in paragraph (23) above the percentage can vary from 80 to 100%). In particular, Annex 5 to the Transmission Agreement includes the exact formula to apply which reads as follows:

$$\text{Surcharge} = \frac{\text{Initial cost} \times \text{Annual percentage} \times \text{Share in stepped-down voltage cost}}{\text{Energy amount} \times \text{Energy charges} + \text{Power} + \text{Power charges}}$$

Where:

*Initial cost* signifies the starting costs on account of voltage step-down, entered in USD

*Annual Percentage* refers to the percentage of the initial costs to be collected each year, comprising depreciation, financial costs, required rate of return and operating costs.

*The share in stepped-down voltage cost* amounts to **80%** of the stepping down expense [*stress added*]

*Energy amount* is the customer's annual amount of energy, in MWh

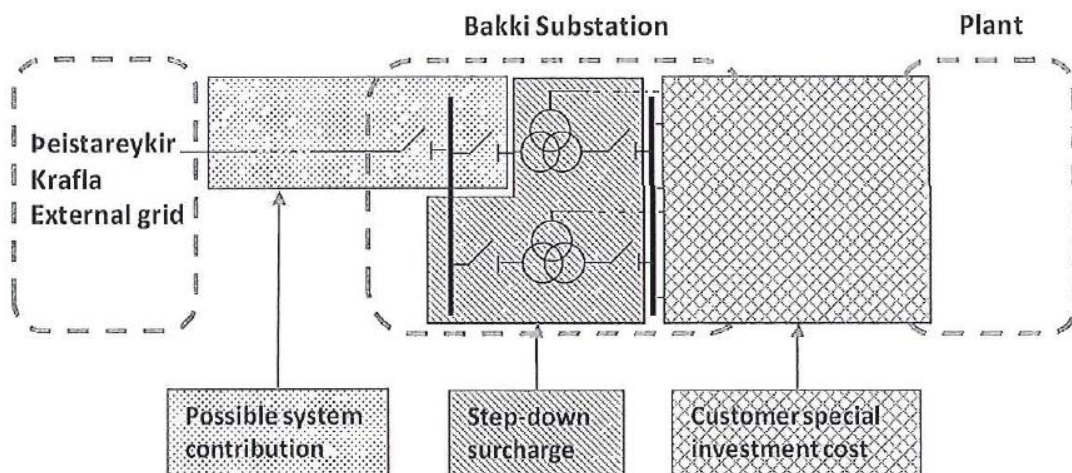
*Energy charges* are the charges for energy to power intensive users, according to the Landsnet tariff

*Power* stands for the customer's agreed peak power

*Power charges* are the charges for power to power intensive users, according to Landsnet tariff.

Figure 4. Source: Annex 5 to the Transmission Agreement.

- (43) Annex 5 to the Transmission Agreement, referred to at Article 10.1 of the Agreement, also contains the following diagram:



Customer-specific investment cost (B.9 art. 4.3)

Figure 5. Source: Transmission Agreement (Annex 5).

### 6.3 *System Contribution Surcharge*

- (44) The Icelandic authorities have provided information as to the transmission constructions foreseen by Landsnet which are necessary for supplying the power from Þeistareykir Power Station to the planned industrial site at Bakki<sup>21</sup> (see Figure 3):
- Addition of one circuit breaker at Þeistareykir.
  - New 220 kV transmission line, 29 km, from Þeistareykir to Bakki.
  - Installation of two 220 kV circuit breakers at Bakki.
  - Building of housing for a substation at Bakki.
- (45) Without the PCC project, Landsnet will not be under an obligation to connect the industrial site of Bakki to Þeistareykir Power Station, since PCC will be the first company to be established in Bakki. However, irrespectively of the PCC project, Landsnet will have to ensure the connectivity of the Power Station at Þeistareykir to the transmission system at Krafla (see figure 3).<sup>22</sup> Also irrespectively of the project, the transmission line to Húsavík has to be upgraded (see paragraph (14) above).
- (46) The Icelandic authorities have explained that the cost of connecting Þeistareykir Power Station and the industrial site at Bakki are estimated at ISK [...]. However, PCC would only need a 132 kV power line (as opposed to a 220 kV line) and therefore the Icelandic authorities have submitted that approximately ISK [...] would be needed for the purposes of connecting the industrial site at Bakki to Þeistareykir Power Station if only PCC's requirements were taken into account, and not those of potential future customers at the planned industrial site at Bakki.<sup>23</sup>
- (47) Futhermore, the Icelandic authorities have explained that by deploying a 220 kV Bakki connection, the cost for upgrading the Húsavík connection can be lowered by [...]ISK.
- (48) Against this background, the Transmission Agreement foresees in Table 4 of Annex 1 that no System Contribution Surcharge has to be paid by PCC.

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<sup>21</sup> Annex 1 to the Transmission Agreement and Doc No 726154, page 3.

<sup>22</sup> PCC has also signed a power contract with Landsvirkjun, which has also been notified to the Authority (see Decision 207/15/COL of 20 May 2015 on the sale of electricity to the PCC Silicon Metal Plant at Bakki under the 2015 Power Contract). The majority of the contracted power in that power contract is not existing capacity in Landsvirkjun's current generation system and investment in generation capacity is therefore needed to provide the power. For the purposes of providing the power, Landsvirkjun plans to build a geothermal power station at Þeistareykir. The new Power Station to be built at Þeistareykir will have the capacity of 45 - 50 MW of power from seven wells that have already been drilled. Surplus capacity available in Landsvirkjun's generation system will be provided for the remaining 8 - 13 MW needed for PCC's Plant. However, Landsvirkjun has confirmed to the Authority that the Power Station at Þeistareykir will be launched regardless of whether or not PCC's project at Bakki materialises. Moreover, on 13 April 2015, Landsvirkjun signed an agreement with a contractor for the initial building phase of the power station (see <http://www.landsvirkjun.is/fyrirtaekid/fjolmidlatorg/frettir/frett/framkvaemdir-hefjast-vid-theistareykjavirkjun/>). Landsnet as a TSO has an obligation to connect the power plants to the transmission system and this obligation will stay irrespectively of whether PCC's project is materialised.

<sup>23</sup> Doc No 726154.

## 7 The scope of this Decision

- (49) In this Decision, the Authority will assess the terms of the 2015 Transmission Agreement concerning the Step-down Surcharge and the System Contribution. It therefore falls outside the scope of this Decision to assess whether there is potential state aid involved in any other elements of the Transmission Agreement and to what extent the transmission tariff might entail state aid, apart from the Step-down Surcharge and the System Contribution.

## 8 Comments by the Icelandic authorities and Landsnet

- (50) The Icelandic authorities and Landsnet consider that the Transmission Agreement does not entail state aid in favour of PCC in the meaning of Article 61(1) EEA, and the Agreement has been notified for legal certainty.
- (51) First, it is argued that the Agreement does not provide any advantage granted through state resources. According to Landsnet, if any of its customers would not pay all the costs associated to their connection to the transmission system, that could possibly affect other customers but under no circumstances would it affect the State or state resources, which is one of the cumulative criteria of the state aid notion. Second, Landsnet argues that even if the Agreement is signed by a public company, nothing in this case suggests that the State specifically incited or commanded the company to subscribe the Agreement and therefore it is not imputable to the State, as required by the state aid notion.<sup>24</sup>
- (52) The Icelandic authorities also argue that the Step-down and System Contribution Surcharges are calculated according to statutory rules, and therefore PCC is not exempted from the payment of any charge that should be borne by the company.
- (53) Finally, the Icelandic authorities state that the Agreement has no impact on the internal market.<sup>25</sup>

## II. ASSESSMENT

### 1. The presence of state aid

- (54) 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.”*

- (55) Accordingly, a measure constitutes state aid within the meaning of Article 61(1) of the EEA Agreement if the following conditions are cumulatively fulfilled: the measure (i) is granted by the State or through state resources; (ii) confers an economic advantage on the

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<sup>24</sup> Doc No 752793, pages 4 and 9-10.

<sup>25</sup> Doc No 752793, page 5.

beneficiary; (iii) is selective; (iv) it is liable to affect trade between Contracting Parties and distort competition.<sup>26</sup>

## 2. The Step-down and the System Contribution Surcharges

- (56) As a preliminary point, the Authority observes that transmission tariffs are one of the key elements of the EEA internal electricity market.
- (57) Directive 2003/54/EC *concerning common rules for the internal market in electricity*<sup>27</sup> provides that national regulators shall ensure non-discriminatory and cost-reflective transmission tariffs by fixing or approving the tariffs or the methodology underlying the calculation of the tariffs.<sup>28</sup> The Authority is of the view that a tariff within the meaning of Directive 2003/54/EC covers not only the Transmission Charge, but also the System Contribution, since the latter is established in order to cover costs of accessing the transmission network. The system of allocating costs to transmission users is not regulated by internal market legislation, and different tariff schemes coexist in the EEA. An overview of the transmission tariffs in Europe can be found in a recent ENTSO-E synthesis, according to which infrastructure is the main component of the Icelandic transmission tariff and energy-intensive grid users pay for the infrastructure connecting their installation to the transmission grid based on actual costs (not fully socialized via the tariff).<sup>29</sup>
- (58) This is in line with the information provided by the Icelandic authorities in the case at hand, according to which Article 12a of the Electricity Act provides that for connecting new energy-intensive users in Iceland: (i) *Step-down Surcharge* shall be charged in case the electricity is delivered at voltage below 66 kV, for covering the extra costs of the stepping-down (see Article 12a(7) of the Electricity Act); and (ii) *System Contribution* (connection fee) shall be charged for necessary additional costs resulting from the connection (see Article 12a(10) of the Electricity Act, and also Article 15(11) of the Electricity Regulation).<sup>30</sup>
- (59) To be qualified as state aid an advantage must be granted by the State or through state resources. The advantage can also be granted through a public undertaking provided there is imputability to the State.<sup>31</sup> However, the question of whether there is imputability to the State is only relevant if the Transmission Agreement is not concluded on market conditions in line with the market economy operator (MEO) test.<sup>32</sup> In other words, the Authority does not need to assess the question of imputability –or the other criteria of the state aid notion-

<sup>26</sup> According to settled case-law, classification as aid requires that all the conditions set out in the provision are fulfilled, see judgment in *Belgium v. Commission* (“*Tubemeuse*”), C-142/87, EU:C:1990:125, paragraph 25.

<sup>27</sup> Incorporated into Annex IV (point 22) to the EEA Agreement by Joint Committee Decision No 146/2005 of 2 December 2005.

<sup>28</sup> See Recital 18 and Articles 20 and 23.2 of the Directive.

<sup>29</sup> See ENTSO-E: Overview of transmission tariffs in Europe: Synthesis 2014. June 2014. The main features of charging mechanism in force for first connection to transmission grid are described in Appendix 6: First connection charges.

<sup>30</sup> Doc No 722917.

<sup>31</sup> Judgment in *France v Commission* (*Stardust Marine*), C-482/99, EU:C:2002:294, paragraphs 50-59.

<sup>32</sup> This principle is explained in the Authority’s state aid guidelines Part VI: Rules on public service compensation, State ownership of enterprises and aid to public enterprises, Application of state aid provisions to public enterprises in the manufacturing sector (OJ No L 274, 26.10.2000, page 29 and EEA Supplement No 48, 26.10.2000).

inssofar Landsnet entered into an agreement that any private operator on the market would have accepted.

- (60) The Authority observes that the main issue of this case is to examine whether PCC will receive an economic advantage in the case of the Step-down Surcharge and the System Contribution, in the form of preferential charges via the Transmission Agreement through exemptions from costs that normally would be borne by the company in its normal course of business.<sup>33</sup> Inssofar as the Step-down Surcharge and the System Contribution paid by PCC deviate from the statutory rules and the general principles and established administrative practice in Iceland, this may entail an advantage, and if the other criteria of Article 61(1) of the EEA Agreement were also to be met, this would entail state aid. This issue will be addressed below.
- (61) The Authority observes that the information made available indicates, at the outset, that the connection of the PCC Plant at Bakki would be a part of an overall plan to connect the envisaged power station at Þeistareykir to the planned industrial site at Bakki and to establish a new connection line to Húsavík (upgrading the current 33 kV connection).

### 2.1. The Step-down Surcharge

- (62) As described above, the Step-down Surcharge is established by statutory rules and is intended to compensate for the actual extra costs related to the stepping-down of the electricity from 220 kV or 132 kV (the voltage of the grid) to the lower delivery voltage requested by the DSOs or energy-intensive user.<sup>34</sup>
- (63) The Transmission Agreement prescribes at Article 10.1 that a Step-down Surcharge will be charged for having the contract power delivered at a 33 kV and 11 kV voltage, as further laid down in the Grid Code B.9 and in Annex 5 to the Transmission Agreement.
- (64) In Annex 5 to the Transmission Agreement the estimated actual equipment cost is ISK [...] and the breakdown of the equipment cost as a basis for the Step-down Surcharge is as follows:

<b>Equipment</b>	<b>Voltage</b>	<b>Estimated cost</b>
One circuit breaker bay at Bakki substation	220 kV	[...] ISK
Two step-down transformers at Bakki (80 MVA), including cells and shelter	220/33/11 kV	[...] ISK
Two circuit breaker bays at Bakki substation	33 kV	[...] ISK
Protection and metering	220 kV	[...] ISK

Figure 6. Source: Transmission Agreement

<sup>33</sup> It is established case law that a state intervention favours an undertaking if it provides the undertaking with an economic advantage, which it would not have obtained under normal market conditions. See judgments in *France v Commission*, C-301/87, EU:C:1990:67, paragraph 41; *De Gezamenlijke Steenkolenmijnen v High Authority of the European Coal and Steel Community*, 30/59, EU:C:1961:2, paragraph 19; *France v Commission (Kimberly Clark)*, C-241/94, EU:C:1996:353, paragraph 34; and *Fleuren Compost*, T-109/01, EU:T:2004:4, paragraph 53.

<sup>34</sup> According to Article 12a(7) of the Electricity Act, as amended by Act No 19/2011.

- (65) The Icelandic authorities have referred to Article 13 of the Electricity Act as regards the permission for Landsnet to deliver electricity to energy-intensive users at 132 kV voltage or below. The Authority notes that the relevant provision of Article 13 was added to the Electricity Act in 2011 by Act No 19/2011, providing for an exemption for Landsnet to deliver electricity to energy-intensive users at a voltage below 132 kV.
- (66) The Transmission Agreement refers to the Step-down Surcharge as established in Landsnet's Grid Code B.9. The Authority observes that the legal basis for the Step-down Surcharge is in Article 12a(7) of the Electricity Act, and recalls its wording:
- “The transmission system operator may deliver electricity to energy-intensive users at a voltage of 66 kV or below, provided the extra costs are covered by a special surcharge.”<sup>35</sup>
- (67) It is the Authority's understanding that the Step-down Surcharge is intended to cover the extra costs of the stepping-down to the voltage level requested by the energy-intensive customer. The Icelandic authorities have submitted the formula (see paragraph (42) above) applied in the case of PCC, for calculating a surcharge on the Capacity Charge (per year) and Energy Charge (per kWh) as part of the Transmission Charge for energy-intensive users. The Authority observes that the formula only takes into account an 80% share of the total actual expenses related to the stepping-down.<sup>36</sup> The Grid Code B9 allows Landsnet to take into account from 80 to 100% of the related costs.
- (68) However, the Icelandic authorities have explained to the Authority that the reason to take into account only 80% of the total costs related to the stepping-down is due to the existence of synergies such as joint utilization of facilities, equipment and reserve components. The existence of those synergies have been confirmed to the Authority by Orkustofnun. According to Orkustofnun, the synergies that Landsnet obtains might entail a disadvantage for the customers that has to be assessed (see Doc. No 747838). The Authority has also been informed that at the new substation at Bakki, not only PCC but also RARIK – the DSO for Húsavík, will benefit from the Step-down services. Consequently, it would be incorrect to charge PCC 100% of the costs when taking account of the synergies and given that PCC will not be the only beneficiary of those services.<sup>37</sup>
- (69) Landsnet has informed the Authority that the estimated Step-down Surcharge has been calculated to be [...] % on top of the tariff for power intensive users.<sup>38</sup> The current transmission tariffs for the power intensive users are in USD and published on Landnet's webpage<sup>39</sup>:

Power intensive users transmission tariffs

Delivery charge:	55.395 USD per year
Capacity charge:	32.268 USD MW per year
Energy charge:	1.632 USD per MWh

<sup>35</sup> The Authority's informal translation. The original text reads as follows: “*Flutningsfyrirtækinu er heimilt að afhenda raforku til stórnotenda á 66 kV eða lægri spennu enda standi sérstök gjaldtaka undir viðbótarkostnaði.*”

<sup>36</sup> See formula in Figure 2 of this Decision.

<sup>37</sup> Doc No 752793, page 5.

<sup>38</sup> Doc No 752793, page 6.

<sup>39</sup> See: <http://www.landsnet.is/english/transmissionandmarket/transmissiontariff/tariff/>.

- (70) As a consequence, the Step-down Surcharge included on top of the capacity and energy charge would be [...] USD per year and [...] USD per MW respectively.
- (71) The Authority concludes that no advantage is conferred upon PCC as regards the Step-down Surcharge, since the Surcharge is calculated according to the methodology established in the Grid Code, which is applied on a non-discriminatory basis to all the power intensive users, and Orkustofnun agrees that this methodology is correct. Assessing the particular facts of the case, in particular taking into account the existence of certain synergies for Landsnet and the fact that PCC will not be the only entity benefitting from the stepping-down services, the Authority accepts that PCC is not obtaining any exemptions from costs that should normally be borne by the company.
- (72) Since the criteria in Article 61(1) of the EEA Agreement are cumulative, there is no need to establish whether state resources were involved in the case at hand. The same applies to other criteria in Article 61(1).

## 2.2. *The System Contribution Surcharge*

- (73) The Icelandic authorities have explained that the general Transmission Charge for energy-intensive users does not include a fee for connecting new customers to the transmission grid. They have explained that according to statutory rules the connection of new customers shall not result in increased cost for the existing customers.<sup>40</sup> It is the Authority's understanding that the payment (the System Contribution Surcharge) shall be established on the basis of the necessary costs of connection.
- (74) The Authority understands that Article 12a(10) of the Electricity Act provides that the TSO shall charge for the additional costs that connecting a new energy-intensive user would otherwise entail for the existing grid users. However, if no extra cost exists for the other users, no system contribution is requested under the Electricity Act. As a consequence, the Authority needs to verify whether the connection of PCC to Landsnet's grid will entail an extra cost for other users of the system which would be reflected in higher tariffs.
- (75) The Icelandic authorities have explained that the "income framework" of Landsnet is based on its asset base, which are assigned to the in-feed, the main, or the out-feed part of the grid. They have provided the following proportional assignment of Landsnet's assets, as regards the energy-intensive part, stating that this is the current proportional assignment of the assets as calculated by Landsnet:<sup>41</sup>

	In-feed	Main	Out-feed
Energy-intensive users	11%	62%	27%

- (76) Landsnet applies this proportion when calculating the System Contribution; it currently allocates 27% of the future revenues from new energy-intensive users (stemming from the general Transmission Charge) to the investment costs of connecting them to the grid. Landsnet has explained that this is an administrative practice applied on a non-discriminatory basis to all energy-intensive users. The Authority observes that this practice is not published, neither by Landsnet nor by Orkustofnun. However, the practice has been confirmed by Orkustofnun. In fact, Orkustofnun has explained that, in general, it approves

<sup>40</sup> Doc No 722917.

<sup>41</sup> Doc No 725496. The Icelandic authorities have not provided information as to the breakdown of the asset base between the energy-intensive part and the DSO's part.



the methodology, which is described by Orkustofnun as general principles.<sup>42</sup> The methodology is applied by Landsnet when calculating the System Contribution in the context of assessing the profitability calculations attached to Landsnet's applications to Orkustofnun for new transmission facilities with components of voltage 66 kV and above, for which a licence is required from Orkustofnun, according to Article 9(2) of the Electricity Act.

- (77) Landsnet has not yet applied for a licence to Orkustofnun for the PCC project. Therefore, in the present case, Orkustofnun has not yet reviewed the calculation. However, Landsnet's calculations are based on the principles set out above and they are in line with its previous practice, as approved by Orkustofnun.<sup>43</sup> Taking these facts into account, the Authority considers that the general methodology to calculate the System Contribution Surcharge does not entail a selective economic advantage for PCC. Furthermore, the Authority notes that the Transmission Agreement provides for an estimate of the possible system contribution (see table 4 of Annex 1 to the Agreement). Consequently, once all the investment costs are known, should the figures be different, the System Contribution Surcharge could be recalculated.
- (78) The Authority also notes that for this project, Landsnet will design and construct certain transmission facilities required to accommodate the provision of electric transmission services to the PCC Plant. In particular, this entails the construction of a new power line from Þeistareykir Power Station to the planned industrial site at Bakki and from Þeistareykir Power Station to the national grid at Krafla power station (see Figure 3). According to information provided by Landsnet, the transmission line will be designed and constructed with adequate transmission capacity to supply electricity to PCC and to other future users at Bakki, at 220 kV.<sup>44</sup> Landsnet has explained that under Article 9(1) of the Electricity Act, it is under the obligation to develop the transmission system in an economic manner. According to the data provided to the Authority, the most economical way to develop the system in the area is to build a 220 kV system to serve PCC and other future users at Bakki.
- (79) Furthermore, Landsnet has explained that there is also a need to upgrade the 33 kV connection to Húsavík and that the connection is a part of the Implementation Plan of the Network Development Plan for 2016.<sup>45</sup> The connection of Bakki allows Landsnet to include the new Húsavík connection in the connection of the industrial site at Bakki. Landsnet has foreseen three options to upgrade the Húsavík connection. By using the 220 kV Bakki connection, the cost for upgrading the connection can be lowered by [...]ISK. Orkustofnun has confirmed to the Authority that the Húsavík line is one of the oldest transmission lines in Iceland and that it needs to be upgraded.
- (80) The Authority acknowledges that Landsnet, in its capacity as TSO, has the obligation to develop and design the transmission system in the most economically efficient manner. In this case, taking into account the different options and the costs of those options, Landsnet is acting in line with the Electricity Act while opting for deploying the line at 220 kV, since

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<sup>42</sup> Doc No 748004.

<sup>43</sup> The methodology to calculate the System Contribution Surcharge regarding the PCC project are the same as those used by Landsnet in the framework of another similar project. This methodology, based on principles, was approved by Orkustofnun. See the Authority's decision No 67/15/COL, on the sale and transmission of electricity to United Silicon in Helgúvík.

<sup>44</sup> Doc No 705962.

<sup>45</sup> See Framkvæmdaáætlun 2014-2016. Available in Icelandic at: [http://www.landsnet.is/library/Skrar/Landsnet/Upplýsingatorg/Skyrslur/Kerfisaetlanir/2014/Umhverfissk%C3%BDrsla%20kerfis%C3%A1%C3%A6tlunar%202014-2023%20vi%C3%B0aukar%20\(2,95%20MB\)](http://www.landsnet.is/library/Skrar/Landsnet/Upplýsingatorg/Skyrslur/Kerfisaetlanir/2014/Umhverfissk%C3%BDrsla%20kerfis%C3%A1%C3%A6tlunar%202014-2023%20vi%C3%B0aukar%20(2,95%20MB)).

this is the most economically efficient option. This is due to the fact that further power plants are foreseen in the Master Plan (535 MW in total),<sup>46</sup> and more industrial plants can be accommodated at Bakki.

- (81) The Authority further understands that the Electricity Act states that intensive users should pay a System Contribution Surcharge if the connection of the new plant causes additional costs for the existing users. However, the payment of the System Contribution Surcharge is not required in all cases and it has to be calculated according to the extra costs linked to the PCC project (customer-specific costs) and not to the investments that Landsnet, as a TSO, has the obligation to undertake.
- (82) The investments described above have three objectives: (i) connecting the Bakki industrial site to the transmission system, (ii) connecting the PCC plant and (iii) upgrading the connection for the distribution system in Húsavík. The Authority agrees that in the calculations on the possible System Contribution Surcharge, only the customer specific investments have to be taken into account. In particular, this implies that the calculations have to be based on the costs of a connection of 132 kV, which is the voltage that the PCC project requires, and not of 220 kV.
- (83) The Authority observes that the whole project entails different costs, not all of them PCC customer-specific. The whole project entails (i) a connection between the substation at Krafla and the Þeistareykir Power Station (ii) a connection between Þeistareykir and the industrial site at Bakki, and (iii) the connection of Húsavík.
- (84) The cost of the connection between Krafla and Þeistareykir is estimated at [...]ISK. However, this cost cannot be considered customer specific for PCC, since the objective is to connect the substation of Krafla power station to Þeistareykir Power Station, which is not strictly necessary for the PCC Project but rather in line with Landsnet's business plan to reinforce the connections in the North-East of Iceland, including upgrading the connection to Húsavík. As described in paragraph (45) and footnote 22 above, Landsvirkjun has confirmed the development of the Þeistareykir Power Station, irrespectively of whether or not PCC's project materialises.<sup>47</sup> Consequently, Landsnet as the Icelandic TSO has the obligation to connect the power plants to the transmission system, irrespectively of the PCC project.
- (85) The Authority observes that the Icelandic authorities have submitted calculations pertaining to the investment costs for the transmission construction necessary for supplying the power from Þeistareykir to the industrial site at Bakki, at ISK [...] (approximately EUR [...]). The Authority agrees that the connection between the Power Station and Bakki should be considered a customer-specific cost that PCC should pay but only the estimated cost of a 132 kV line. In fact, Article 15(11) of the Electricity Regulation establishes that the system contribution has to be decided on necessary costs of connection for the intensive user. Consequently, the cost to take into account in the PCC's System Contribution Surcharge is ISK [...] (approximately EUR [...]), which is the necessary investment cost if Landsnet would only construct a line to fulfil the requirements of PCC (132 kV).

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<sup>46</sup> See Kerfisaætlun 2014-2023. Available in Icelandic at: [http://www.landsnet.is/library/Skrar/Landsnet/Upplýsingatorg/Skyrslur/Kerfisaatlanir/2014-2023/Nýtt\\_LANDSNET\\_kerfisaetlun\\_opnur\\_LowRez.pdf](http://www.landsnet.is/library/Skrar/Landsnet/Upplýsingatorg/Skyrslur/Kerfisaatlanir/2014-2023/Nýtt_LANDSNET_kerfisaetlun_opnur_LowRez.pdf), pages 16-17.

<sup>47</sup> According to information from Landsvirkjun, an agreement has been signed with a contractor for the initial building phase of the Power Station. See also footnote 22 above.

- (86) Based on these premises, PCC's customer-specific costs are around ISK [...], applying the calculation methodology referred above (See section I.5.3 and paragraphs (73) to (76) above), the possible system contribution surcharge to be paid by PCC would be around [...] ISK. However, when taking into account that the cost for upgrading the connection to the distribution system in Húsavík will be lowered by at least [...] ISK, the result is that PCC is not required to pay a System Contribution Surcharge. Consequently, the PCC connection will not increase the tariff for other users of the transmission system and therefore, in accordance with Article 12a(10) of the Electricity Act, no System Contribution Surcharge should be imposed.
- (87) The Authority recalls nevertheless that Annex 1 to the Transmission Agreement provides for an approximate calculation of the System Contribution Surcharge. The exact figure can only be established once the actual value of the investments and savings are known. However, those calculations must be carried out in line with the principles described in this decision.
- (88) The Authority also points out that Article 15(11) of the Electricity Regulation sets out that the TSO shall inform the new energy-intensive user beforehand of whether a System Contribution will be charged and shall provide him with the assumptions on the basis of which it is calculated. According to the information provided in the case at hand the estimated System Contribution set out in Table 4 in Annex 1 to the Transmission Agreement is in line with the statutory rules in Iceland.
- (89) On the basis of the above, the Authority concludes that there is no advantage involved in the Transmission Agreement as the calculation of the System Contribution is in line with the statutory rules. Therefore, no advantage is conferred upon PCC in the context of the System Contribution.
- (90) Since the criteria in Article 61(1) of the EEA Agreement are cumulative, there is no need to establish whether state resources were involved in the case at hand. The same applies to the other criteria in Article 61(1) EEA.

### **3. Conclusion**

- (91) The Authority finds that neither the the Step-down Surcharge nor the System Contribution calculation, as agreed in the 2015 Transmission Agreement, entail the granting of state aid within the meaning of Article 61(1) of the EEA Agreement.

HAS ADOPTED THIS DECISION:

#### *Article 1*

The Step-down Surcharge and the System Contribution calculation provided in the Transmission Agreement signed between Landsnet and PCC on 19 March 2015 do not constitute state aid within the meaning of Article 61(1) of the EEA Agreement.

#### *Article 2*

This Decision is addressed to Iceland.

*Article 3*

Only the English language version of this decision is authentic.

Done in Brussels, on 20 May 2015

*For the EFTA Surveillance Authority*

Oda Helen Sletnes  
*President*

Frank Büchel  
*College Member*