

Case No: 74661  
Event No: 696656  
Dec. No: 445/13/COL

**[non confidential version]\***

**EFTA SURVEILLANCE AUTHORITY DECISION**  
of 13 November 2013  
to open a formal investigation into the additional aid from Innovation Norway to  
Finnfjord AS  
(Norway)

The EFTA Surveillance Authority (“the Authority”),

HAVING REGARD to:

The Agreement on the European Economic Area (“the EEA Agreement”), in particular to Articles 61 to 63 and Protocol 26,

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,

Protocol 3 to the Surveillance and Court Agreement (“Protocol 3”), in particular to Article 1(2) of Part I and Articles 4(4) and 6 of Part II,

Whereas:

## **I. FACTS**

### **1. Procedure**

- (1) Following pre-notification discussions, the Norwegian authorities, by letter of 26 June 2013, notified the additional aid from Innovation Norway (“IN”) to Finnfjord AS (“Finnfjord”), pursuant to Article 1(3) of Part I of Protocol 3.<sup>1</sup>
- (2) By letter dated 5 July 2013,<sup>2</sup> the Authority requested additional information from the Norwegian authorities. By letter dated 19 August 2013,<sup>3</sup> the Norwegian authorities replied to the information request.

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\* In this non confidential version of the decision, information covered by the obligation of professional secrecy has been taken out. Where information has been taken out, this is marked with [...]. Where figures have been excluded, a range within which the figure exists, has, where appropriate, been indicated.

<sup>1</sup> Events No 676810, 676812, 676814-676816, 676819, 676822, 676823, 676825-676827, 676829 and 676832-676834.

<sup>2</sup> Event No 677212.

- (3) By letter dated 28 August 2013,<sup>4</sup> the Authority made a further request for information from the Norwegian authorities. By letter dated 18 September 2013,<sup>5</sup> the Norwegian authorities responded.

## **2. The notified measure – the NOK 16 million grant**

- (4) The notified proposed measure is a direct grant of an additional NOK 16 million from IN to Finn fjord.
- (5) IN informed Finn fjord of its decision to grant the notified measure by letter dated 10 December 2012. The direct grant is intended to cover increased costs related to an energy recovery system that Finn fjord has installed in order to recover heat energy in its ferrosilicon production plant. For the financing of that project, Finn fjord has already received NOK 175 million in state aid from the Energy Fund Scheme (see below). That award of aid was approved by the Authority by Decision No 39/11/COL.<sup>6</sup>
- (6) The proposed direct grant from IN has been notified as an individual aid not awarded on the basis of an aid scheme.

## **3. Loans from IN and SNN**

- (7) The NOK 16 million only partly covered the cost increases. IN has explained that Finn fjord needed an additional NOK [80-95] million.
- (8) Therefore, IN, at the same time as it provided the NOK 16 million direct grant to Finn fjord, also provided Finn fjord with a loan of NOK 18 million. At that time, Finn fjord already owed NOK 100 million to IN. None of those loans have been notified to the Authority. IN holds that they have been granted on market terms and therefore do not involve state aid within the meaning of Article 61(1) of the EEA Agreement.
- (9) In parallel with the loan from IN, Finn fjord secured a NOK [45-60] million from the bank SpareBank 1 Nord-Norge (“SNN”). From before Finn fjord owed NOK [300-325] million to SNN.
- (10) In sum the NOK 16 million direct grant, and the two loans of NOK 18 million and NOK [45-60] million covered the NOK [80-95] million cost increase.

## **4. Innovation Norway (“IN”)**

- (11) IN is a public entity established by the Act on Innovation Norway.<sup>7</sup> It is wholly owned by the Norwegian state through the Ministry of Local Government and Regional Development. It supports innovation by grants financed by public resources.

## **5. Enova SF (“Enova”)**

- (12) Enova SF (“Enova”) is a state enterprise<sup>8</sup> wholly owned by the Norwegian State through the Ministry of Petroleum and Energy. It is responsible for managing the Energy Fund

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<sup>3</sup> Events No 680603-680605 and 680866-680868.

<sup>4</sup> Event No 681073.

<sup>5</sup> Events No 683806, 683807, 683809, 683810, 683813, 683814, 683817 and 683819.

<sup>6</sup> OJ C 278 22.9.2011 p. 6 and EEA Supplement No 51 22.9.2011 p. 1.

<sup>7</sup> LOV 2003-12-19-130 *Lov om Innovasjon Norge*.

<sup>8</sup> In Norwegian: *Statsforetak*. Enova is organised in accordance with Act No 71 of 30.8.1991 on state enterprises.

Scheme, a state aid scheme for the promotion of environmental protection approved by the Authority by Decision No 248/11/COL.<sup>9</sup> Enova is financed by public resources.

- (13) Under the Energy Fund Scheme Enova arranges competitions for aid where the winning projects are the ones with the best energy result per NOK of aid.<sup>10</sup>
- (14) Enova only grants the last 20% of an individual aid when it has approved a final project report.<sup>11</sup> Where a project turns out to be less costly than budgeted, Enova reduces the aid grant in a pro rata calculation.<sup>12</sup>

## 6. The recipient – Finn fjord AS (“Finn fjord”)

- (15) Finn fjord is a family-owned limited liability company. The plant supported by the proposed aid is located in Finnsnes in the County of Troms, which is the second northernmost county in Norway.

## 7. Cost increases

- (16) In the notification leading to the Authority’s Decision No 39/11/COL of 9 February 2011 approving the NOK 175 million in aid from Enova to Finn fjord, the budget of Finn fjord’s energy recovery project was estimated at NOK 511.66 million. The aid was awarded for the replacement of the existing cooling system with an energy recovery unit. The intention was to annually generate 224 GWh of electrical power and recover 125 GWh of process steam. The expected annual energy production thus amounting to 349 GWh.
- (17) According to the notification in the case at hand, in February 2011, the estimated budget had already increased by almost NOK 190 million from NOK 511.66 million to NOK [680-720] million.<sup>13</sup> Despite this substantial increase, on 7 February 2011 Finn fjord’s board decided to go ahead with the project. Finn fjord did not at that time apply for more aid.
- (18) The cost increase largely stemmed from Finn fjord’s decision to invest in a more powerful steam turbine, which was ordered on 7 January 2011. A legally binding contract for the turbine was concluded on 23 February 2011. By letter dated 16 February 2011, Finn fjord informed Enova that it had ordered the more powerful turbine which would yield an annual production of 344.5 GWh of electrical energy. This higher electrical energy production was thus close to the estimated total production of 349 GWh of electricity and steam. On that basis, Finn fjord requested the exclusion of the steam production from the aided project. By letter dated 17 February 2011, Enova approved the change to the project. It is not clear to the Authority whether all the effects of the change have been taken into account in the new cost estimates for the project.
- (19) Throughout the project phase, Finn fjord has supplied Enova with project-specific progress reports. In its report dated 30 April 2012, Finn fjord referred to further cost increases related to the turbine building, steam and condensation pipes and ditches. The additional costs amounted to approximately NOK 5 million. Finn fjord still aimed at keeping the total project costs below the NOK 700 million estimate.

<sup>9</sup> OJ C 314 27.10.2011 p. 4 and EEA Supplement No 58 27.10.2011 p. 2.

<sup>10</sup> The competition for aid under the Energy Fund Scheme is described in the Authority’s Decision No 248/11/COL (cited above), paragraphs 27-36.

<sup>11</sup> See the Authority’s Decision No 248/11/COL (cited above), paragraph 37.

<sup>12</sup> See the Authority’s Decision No 248/11/COL (cited above), paragraph 38.

<sup>13</sup> The Norwegian authorities have also made reference to a cost estimate of NOK 696 million. In the following, the Authority refers only to the NOK 700 million figure.

- (20) In its progress report dated 29 June 2012, the total cost estimate remained NOK 700 million. However, by that time, it was estimated that the project would incur an additional NOK [5-10] million in increased costs. This cost increase was discussed by Finnfjord's board in a meeting on 19 June 2012. The Norwegian authorities have not explained why the total cost increase of NOK [10-15] million [...] did not lead to an adjustment of the total cost estimate of NOK 700 million in the progress report of 29 June 2012. The Norwegian authorities have explained that Finnfjord, at one point during the spring of 2012 entered into informal discussions with Enova about obtaining additional aid to cover the increased project costs.
- (21) On 5 July 2012, following the informal contacts, Finnfjord formally applied for more aid from Enova. At that time, Finnfjord had revised its total cost estimate to NOK [730-760] million.
- (22) The information provided to the Authority indicates that Finnfjord, on the basis of a budget review finalised on 31 July 2012, realised that the project would incur additional increased costs. The total cost estimate was increased to NOK [740-790] million. 7The cost increases related to: adaptations of existing machinery, adaptations of three existing furnaces, adaptations of smoke ducts, installations in the turbine building and other buildings, longer production shortfalls than expected, and finalisation of the work and the installations. Finnfjord furthermore wanted more aid to ensure that the project would meet its internal requirements of profitability. Finnfjord elaborated on the reasons for the cost increases in its progress report dated 12 September 2012.
- (23) In early August 2012, Finnfjord informally discussed with Enova, the potential postponement of the works on the third furnace and classifying it as a separate project in order to apply for more aid from Enova on the basis of it being a new project.
- (24) When Finnfjord's board met on 25 September 2012 the total cost estimate had been set to NOK [740-790] million.<sup>14</sup> In that meeting Finnfjord's board considered three alternative courses of action:
- i. Completing the project by financing the cost increases by way of the company's general cash flow.
  - ii. Postponing the works on the third furnace, classifying it as a separate project and applying for more aid from Enova.
  - iii. Obtaining NOK [80-95] million of additional financing from Enova (aid), SNN (loan) and IN (loan and aid) in order to complete the project.
- (25) The board decided to proceed according the third alternative.
- (26) IN has provided the Authority with an extract of the board meeting protocol regarding the third alternative. Concerning the applications to Enova and IN for more aid the extract provides the following:

*“Potential grants/loans from Enova and [IN] will be used directly to reduce the liquidity loan applied for [from SNN].”<sup>15</sup>*

<sup>14</sup> The Norwegian authorities indicate that the cost estimates increased further to [approximately NOK 800 million.] It is not clear when these estimates were made, therefore the [NOK 740-790million] from the 25.9.2012 board meeting is referred to in the following.

- (27) According to IN, the board concluded that the first course of action would essentially mean that the project would be financed at the expense of Finnfjord's creditors, which would be legally inadvisable and not a tenable solution in the long term. Also, according to IN, the board did not consider the second alternative a viable course of action as it concluded that the postponement of the works on the third furnace would be prohibitively expensive.

## 8. Overview of the cost increases

Date, event	Estimated budget in NOK million
Initial budget as described in Decision No 39/11/COL of 9 February 2011	511.66
The Norwegian authorities have also made reference to a cost estimate of NOK 696 million. In the following, the Authority refers only to the NOK 700 million figure.	696
7 February 2011, Finnfjord board meeting	[680-720]
5 July 2012, Finnfjord applies to Enova for more aid	[730-760]
31 July 2012, Finnfjord budget review	[740-790]
25 September 2012, Finnfjord board meeting	[740-790]
The Norwegian authorities indicate that the cost estimates increased further to [approximately NOK 800] million. It is not clear when these estimates were made, therefore the NOK [740-790] million from the 25 September 2012 board meeting is referred to in the following.	[approximately 800 ]

## 9. Informal discussions and formal application for more aid from Enova

- (28) The Norwegian authorities have explained that Finnfjord, at some point during the spring of 2012, due to the increased project costs, entered into informal discussions with Enova about the possibility of obtaining more aid. During those informal discussions, Enova signalled that it was reluctant to grant more aid to the project as it doubted whether additional aid would have incentive effect.
- (29) By letter dated 5 July 2012, Finnfjord nevertheless formally applied for additional aid from Enova to cover the increased costs. The estimated total cost was then NOK [730-760] million. The original aid (NOK 175 million) amounted to 34.2% of the initial budget (NOK 511.66 million). Finnfjord applied for NOK [75-85] million in additional aid, as that would bring the total aid amount to [30-40%] of the new total budget estimate.
- (30) By letter dated 20 August 2012, Enova rejected the application for aid. Enova concluded that Finnfjord could not document that the additional aid would provide the company with

<sup>15</sup> Letter from the Norwegian authorities dated 18.9.2013 (Event No 683806). Translation by the Authority: "Eventuelle tilskudd/lån fra Enova og Innovasjon Norge, vil gå til direkte reduksjon av omsøkte likviditetslån."

an incentive to increase the level of environmental protection. In Enova's view the application did therefore not fulfil the requirements of Enova's own rules nor those of the EEA state aid rules. Enova failed to see that aid would have incentive effect as all investments related to the project had been made and most of the equipment had been delivered. In addition, Enova considered that Finn fjord did not document that there was a risk that the project would not have been realised without the additional aid.

#### **10. IN's award of aid and the NOK [80-95] million package**

- (31) On 28 August 2012 Finn fjord initiated an informal dialogue with IN and SNN in order to obtain the NOK [80-95] million necessary to finance the completion of the project.
- (32) By letter dated 1 October 2012, Finn fjord formally applied for additional credit from SNN. Finn fjord formally applied for additional credit and aid from IN on 11 October 2012, without specifying an aid amount.
- (33) It appears that SNN prior to mid-October 2012 had offered Finn fjord a loan of NOK [80-95] million.<sup>16</sup> However, SNN made the offer conditional on collateralisation to the detriment of the collateralisation of a pre-existing loan from IN. This solution was unacceptable for IN. SNN and IN therefore negotiated the following NOK [80-95] million financing package:
  - i. The aid grant from IN of NOK 16 million.
  - ii. A short-term loan of NOK 18 million from IN with a rate of [5-9]% (adjustable in accordance with IN risk loan policy) collateralised *pari passu* with a pre-existing loan of NOK 100 million from IN.
  - iii. A short-term loan of NOK [45-60] million from SNN with an interest rate of [...] NIBOR<sup>17</sup> + [300-600] bps collateralised *pari passu* with a pre-existing loan of NOK [300-325] million from SNN.
- (34) The Norwegian authorities have not explained why IN, instead of granting the NOK 16 million as aid, could not have lent the same amount to Finn fjord.
- (35) The NOK [80-95] million financing package was formalised and accepted by Finn fjord by way of an agreement signed by SNN, IN and Finn fjord on 12 December 2012.
- (36) The NOK 16 million of aid to Finn fjord will only be disbursed with the Authority's approval.

#### **11. Disbursement of the final tranche of aid from the Energy Fund**

- (37) As noted above, Enova only grants the last 20% of an individual aid when it has approved a final project report. On 22 November 2012, the final report from Finn fjord was approved by Enova. On 23 November 2012, Enova disbursed the last NOK 35 million of aid (20% of the total aid amount of NOK 175 million).

<sup>16</sup> According to IN: "When Finn fjord [...] applied for financing of 88 million NOK, [SNN] had already approved a loan of the same amount, but with terms on security that was unacceptable for [IN]" IN letter to the Authority dated 18.9.2013, p. 12.

<sup>17</sup> Norwegian Inter Bank Offered Rate.



## 12. Comments by the Norwegian authorities

- (38) When IN decided to conditionally grant the NOK 16 million of aid, it was aware of Enova's rejection of Finn fjord's application for supplementary aid and the reason for the rejection. IN stresses that the aid awarded provides incentive effect and is fully compatible with the general objectives of the Environmental Aid Guidelines ("EAG")<sup>18</sup> and the Authority's Decision No 248/11/COL on the Energy Fund.
- (39) IN has explained that Finn fjord was facing a temporary capital shortage that threatened the completion of its energy recovery project. The capital shortage could have led to the turbine not being installed. Furthermore it could have halted the rebuilding of furnace 3 and one of the boilers which could have resulted in a reduction of the annual electricity production capacity in the order of 100-120 GWh.
- (40) IN warns that a strict interpretation of the requirement for incentive effect may prevent an aid recipient from choosing better technologies and methods which become visible during the progress of a project. According to IN, the grant constituted a decisive element for releasing the financial package that was required for the completion of the project and therefore had a clear incentive effect. Moreover IN refers to the general policy orientation of the EAG in section 1.2.5 *i.e.* to take into the assessment that state aid may be conducive to the objective of environmental protection which can provide opportunities for innovation, create new markets and increase competitiveness through resources efficiency and new investment opportunities.
- (41) IN is of the view that without the additional aid, the internal rate of return (IRR) would have been too low to make the investment sustainable. With the increased costs, IN, updating Enova's estimates, has calculated the IRR of the project without the additional NOK 16 million to [approximately 11%].<sup>19</sup> According to IN, with the aid of NOK 16 million, the IRR would increase to [11.5-12%]. The IRR, accepted by the Authority in its Decision No 39/11/COL was 12.35%. IN stresses that the level of the rate of return does not serve as an indication of expected profitability, but rather as a measure of the financial buffer needed to offset the risk involved in the realisation of the project.
- (42) IN furthermore stresses that Finn fjord had already been found eligible for aid in accordance with the EAG. During its processing of the application for aid IN complied, as far as possible, with the methods used by Enova to ascertain that the relevant requirements of the EAG were being met to the same extent as in the case of the original aid from Enova. According to IN the aid intensities set by out by the EAG have not been exhausted. On this basis, IN considers the aid to be necessary and proportionate.
- (43) IN stresses that the award of the NOK 16 million does not represent a form of rescue aid. Finn fjord was able to pay its suppliers. However, had Finn fjord not secured the aid and the additional financing in the form of the loans from IN and SNN, the further work on the project would have been halted or its scope would be significantly reduced.
- (44) Enova on the other hand has restated that it did indeed reject Finn fjord's application for aid due to the lack of incentive effect. As a justification for that conclusion, Enova has pointed to the following circumstances: at the point in time where Finn fjord requested further aid from Enova all the investments relating to the project had been carried out and most of the equipment had been delivered, Finn fjord did not report on particular challenges as late as in its progress report provided on 23 July 2012, and Finn fjord, when

<sup>18</sup> OJ L 144 10.6.2010 p. 1 and EEA Supplement No 29 10.6.2010 p. 1.

<sup>19</sup> See annex 6 to the letter of the Norwegian authorities of 18.9.2013 (Event No 683819).

applying for additional aid, could not document that there might be a risk that the project would not be realised without the additional aid. Thus Enova holds that Finnfjord cannot document that the additional aid would provide it with an incentive to increase the level of environmental protection. Enova has clarified that it did not consider the additional aid applied for to fulfil the requirements under the rules of the Energy Fund nor the EAG.



## II. ASSESSMENT

### 1. The presence of state aid

(45) 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.”*

(46) This implies that 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 a selective economic advantage to the beneficiary; (iii) has an impact on trade between Contracting Parties and is liable to distort competition.

### 2. The notified aid – the NOK 16 million direct grant

(47) The aid measure must be granted by the state or through state resources. In that context, it is recalled that IN is a public entity the grants of which are funded by the Norwegian State. The notified measure is therefore financed from resources from the state and transferrable to Finnfjord under the control of a public entity controlled by the state. Thus, the Authority considers that state resources are involved.

(48) The notified measure must confer on Finnfjord advantages that relieves it of charges that are normally borne from its budget. The measure must furthermore be selective in that it favours *“certain undertakings or the production of certain goods”*. The NOK 16 million direct grant is a transfer of cash that Finnfjord would not have received in its normal course of business. Therefore, the Authority concludes that this direct grant provides a selective economic advantage to Finnfjord.

(49) The measure must be liable to distort competition and affect trade between the Contracting Parties to the EEA Agreement to be considered state aid within the meaning of its Article 61(1). According to settled case-law, the mere fact that a measure strengthens the position of an undertaking compared with other undertakings competing in intra-EEA trade, is considered to be sufficient in order to conclude that the measure is likely to affect trade between Contracting Parties and distort competition between undertakings established in other EEA States.<sup>20</sup> Finnfjord produces ferrosilicon and microsilica, which it sells on the European market.<sup>21</sup> Thus, the Authority concludes that the aid affects trade between the Contracting Parties to the EEA Agreement and distorts competition in the EEA as the beneficiary is active in a sector where trade between Contracting Parties takes place.

(50) Based on the above findings, the Authority concludes that the notified measure in the form of a direct grant of NOK 16 million from IN to Finnfjord constitutes state aid within the meaning of Article 61(1) of the EEA Agreement.

<sup>20</sup> Case E-6/98 *Norway v EFTA Surveillance Authority* [1999] Ct. Rep. 76, paragraph 59; Case 730/79 *Philip Morris v Commission* [1980] ECR 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”*.

<sup>21</sup> As described in the Authority’s Decision No 39/11/COL (cited above).

### 3. Procedural requirements

- (51) 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”*.
- (52) By letter dated 26 June 2013, the Norwegian authorities notified the aid measure of NOK 16 million. The aid has been granted conditionally subject to the Authority’s approval and has consequently not been disbursed.
- (53) The Authority notes that the Norwegian authorities have not provided detailed information on the legal basis for IN’s grant of individual aid to Finnfjord. On the basis of the information provided, it appears that the aid has been granted on the basis of an aid scheme that has not been notified to the Authority as the Norwegian authorities consider it to be covered by the General Block Exemption Regulation (the “GBER”).<sup>22</sup> The Norwegian authorities have concluded that the aid to Finnfjord had to be individually notified as it, in cumulation with the aid from Enova, exceeds the threshold for which individual awards of aid are subject to the notification obligation.<sup>23</sup> The grants from Enova and IN represent investment aid to the same undertaking for the same investment project.
- (54) Given that the proposed aid constitutes new aid that is not exempted from the notification obligation, the Authority concludes that the Norwegian authorities have complied with their obligations stemming from Article 1(3) of Part I of Protocol 3.

### 4. The legal basis for assessing the compatibility of the aid

- (55) Support measures caught by Article 61(1) of the EEA Agreement are generally incompatible with the functioning of the EEA Agreement, unless they qualify for a derogation under Article 61(2) or (3) or Article 59(2) of the EEA Agreement.
- (56) IN argues that the aid to Finnfjord is compatible with Article 61(3)(c) of the EEA Agreement and the EAG. IN stresses that the aid at hand does not represent a form of rescue aid.
- (57) On the basis of Article 61(3)(c) of the EEA Agreement *“aid to facilitate the development of certain economic activities or of certain economic areas”* may be considered compatible with the functioning of the EEA Agreement, where such aid does not affect trading conditions and competition in the EEA to the extent that is considered to be contrary to the common interest.

<sup>22</sup> Commission Regulation (EC) No 800/2008 of 6.8.2008 declaring certain categories of aid compatible with the common market in application of Articles 87 and 88 of the Treaty (OJ L 214 9.8.2008 p. 3), incorporated into point 1j of Annex XV to the EEA Agreement.

<sup>23</sup> See Article 6(1)(b) in conjunction with Article 7(1) of the GBER.

Article 6(1)(b) reads as follows “This Regulation shall not apply to any individual aid, whether granted ad hoc or on the basis of a scheme, the gross grant equivalent of which exceeds the following thresholds (...) (b) investment aid for environmental protection: EUR 7,5 million per undertaking per investment project;”.

Article 7(1) reads as follows: “In determining whether the individual notification thresholds laid down in Article 6 and the maximum aid intensities laid down in Chapter II are respected, the total amount of public support measures for the aided activity or project shall be taken into account, regardless of whether that support is financed from local, regional, national or Community sources.”

- (58) By Decision No 39/11/COL the Authority approved the initial aid from the Energy Fund Scheme to Finnfjord's energy recovery project after having carried out a detailed assessment of that aid in accordance with chapter 5 of the EAG. The Authority concluded that the notified aid from Enova contributed to the protection of the environment by incentivising Finnfjord to carry out an energy saving measure it would not have carried out without the aid. The Authority now has to assess the compatibility of the aid from IN in light of these circumstances.
- (59) Given the fact that it has already assessed the compatibility of the aid from Enova to the Finnfjord energy recovery project, the Authority does not doubt that the additional aid, due to its relatively small amount compared to the initial aid, is aimed at a market failure.<sup>24</sup> Furthermore, given that the aid is necessary and has incentive effect, the Authority has no doubts that the distortions of competition and effect on trade would be limited<sup>25</sup> so that the overall balance would be positive.<sup>26</sup>
- (60) However, the Authority has doubts related to the appropriateness,<sup>27</sup> necessity and incentive effect<sup>28</sup> of the aid. These doubts are elaborated on in the following.

## 5. Necessity and incentive effect of aid

- (61) According to the EAG,<sup>29</sup> in order to be compatible with the functioning of the EEA Agreement, aid needs to provide an incentive effect. Whether the notified aid is necessary to produce a real incentive to undertake investment which would not otherwise be made is a crucial element in the compatibility assessment. It has to be verified whether the aid is necessary to provide an incentive effect for the investment, *i.e.* whether the aid actually contributes to changing the behaviour of the recipient so that the level of environmental protection is increased.<sup>30</sup> It is moreover important to verify that the aid in fact was needed and that the undertaking would not have made the investment had it not benefited from the aid.<sup>31</sup>
- (62) As a general rule, the Authority will consider that no incentive effect exists when the project has started before the submission by the recipient of an application requesting the aid.<sup>32</sup> However, the Authority does not exclude the incentive effect of aid to a project that has started when the grant of aid unequivocally ensures the completion of projects that would otherwise not have been completed or adding environmental protection that would otherwise not come to fruition.
- (63) In the case at hand, however, the Authority has doubts with regard to whether the aid provided Finnfjord with an incentive to fully complete the project without delays.
- (64) The incentive effect of the aid has to be verified on the basis of a full analysis of the economic circumstances of the counterfactual situation,<sup>33</sup> level of risk<sup>34</sup> and profitability<sup>35</sup>. These circumstances should be documented by the recipient's original and

<sup>24</sup> Points 167-168 of the EAG.

<sup>25</sup> Points 175-185 of the EAG.

<sup>26</sup> Points 186-188 of the EAG.

<sup>27</sup> Points 169-170 of the EAG.

<sup>28</sup> Points 171-173 of the EAG.

<sup>29</sup> Points 171-173 of the EAG as well as points 27-29.

<sup>30</sup> Point 142 of the EAG.

<sup>31</sup> Point 27 of the EAG.

<sup>32</sup> Point 143 of the EAG.

<sup>33</sup> Point 172(a) of the EAG.

<sup>34</sup> Point 172(f) of the EAG.

<sup>35</sup> Point 172(g) of the EAG.

revised business plans and other relevant documents such as profitability calculations for the project with and without the aid, project finance analysis, risk assessment and detailed account on how the relevant circumstances influenced the original business plan and required rate of return of the investment.

- (65) It appears that Finnfjord, when it applied for more aid from Enova in the spring of 2012, did not realistically consider stopping, reducing the scope or halting the project. This also appears to have been the case when Finnfjord formally applied for additional aid from Enova on 5 July 2012 and when it was faced with the further cost increases to NOK [730-760] million and NOK [740-790] million (and potentially up to [approximately NOK 800] million).
- (66) More specifically and with reference to the conclusions drawn in the board meeting of 25 September 2012, it appears that the company, due to the prohibitive cost involved, and as long as it could secure sufficient financing, did not seriously consider stopping or postponing the project, as a whole or in part, or reducing its scope. The extract of the board meeting protocol from 25 September 2012 indicate that Finnfjord intended to seek additional loan financing from SNN and additional aid from Enova and IN, and that any potential aid would be used to reduce the loan Finnfjord would seek to obtain from SNN.
- (67) IN has explained that on the basis of signals from SNN and IN itself during the ensuing negotiations, Finnfjord still considered it feasible to maintain its primary goal of full and timely completion of the energy recovery project. Finnfjord's board did therefore not formally decide on any alternate course of action and did not initiate in-depth studies of the consequences for a hypothetical failure to adequately securing the additional financing required. Based on the above, it is the preliminary view of the Authority, that Finnfjord appeared to be taking all measures within reason in attempting to finalise the aided project and Finnfjord viewed any additional aid, be it from Enova or IN, as an addition of the most welcome, but not absolutely necessary, kind.
- (68) Furthermore the Authority considers relevant the argument against the incentive effect set out by Enova in its rejection letter: that all the investments relating to the project had already been carried out and that most of the equipment had been delivered. In light of this the Authority questions what incentive there was left for the aid to provide.
- (69) However, the Authority does not exclude at this stage the incentive effect of the proposed aid. An incentive effect may be established for a given project to compensate for unforeseen cost increases. Especially when the scope of the unforeseen cost is substantial and linked to the fact that the project is innovative and that the costs thereby, by their very nature are difficult to estimate in advance – which indeed would appear to be the case for Finnfjord.
- (70) Under such circumstances, it could be argued that the incentive effect of all the aid for the project as one has to be assessed, the question would be whether Finnfjord, knowing all it eventually came to know about the cost increases, would have decided to go ahead with the project with only the NOK 175 million from Enova.
- (71) On the other hand, the Authority notes that Finnfjord in February 2011, when faced with the cost increase from NOK 511.66 million to NOK [680-720] million, decided to go ahead with the project without applying for any further aid. The Authority has not been provided with an explanation of why Finnfjord did not at that stage apply for more aid. It could perhaps be that the project in light of the revenue increases stemming from the increased electricity production would not be less profitable than the approved project and

thus not eligible for more aid using the Enova model. The Authority invites the Norwegian authorities and Finn fjord to explain why Finn fjord did not apply for more aid at that stage.

- (72) Additionally, the Authority has not been provided with an explanation of the extent to which Finn fjord, with the aid from Enova, was compensated for risks of budget overruns. The Authority notes that Finn fjord initially applied for NOK 200 million in aid, however, through negotiations with Enova the aid was reduced by NOK 25 million to the NOK 175 million finally granted. This effectively lowered the rate of return to 12.35% which was at the bottom of the range provided by Enova of what companies making investments outside their core area normally require, which according to Enova was 12% - 16%.<sup>36</sup> In light of these circumstances, the Authority questions the extent to which Finn fjord with the aid from Enova has been compensated for unforeseen costs and the risks related thereto. This should in the preliminary view of the Authority be assessed on the basis of the original budget of the project and the required rate of return.
- (73) IN has explained that Finn fjord needs additional aid to ensure that the internal rate of return (IRR) of the project does not drop to an unacceptably low level and make the investment unsustainable. On the basis of the cost increases, IN has re-calculated the level of the IRR by updating the spreadsheets used by Enova when calculating the initial 12.35% figure. According to IN the level is now [approximately 11%] without the additional NOK 16 million and [11.5-12%] with the aid. This difference appears marginal and appears as such to be a risk already covered by the profit margin of the original project. The project is furthermore still profitable with the estimated IRR of [approximately 11%] However, the Authority questions the accuracy of IN's updated calculations on the basis of the following. It appears to the Authority that IN has:
- i. based the calculations on a total budget of approximately NOK 695 million (and not on any of the later estimates),
  - ii. not taken account of the cash flow of the two last years of the project's lifetime,
  - iii. included the income from steam (although no longer aid-supported), and
  - iv. not adjusted correctly the volume of electricity produced.
- (74) In light of the above, the Authority invites the Norwegian authorities to comment on the Authority's findings listed in the paragraph above and to provide an updated spreadsheet.
- (75) The Authority has further doubts on the incentive effect and compatibility of the aid related to some more general considerations.
- (76) The Authority notes as a positive aspect of the Energy Fund Scheme that the aid under that scheme is given to trigger projects that would otherwise not be realised. The aid applicants are responsible for providing accurate information on costs and incomes and bear the risk of cost overruns or lower than estimated earnings. On the other hand, the aid applicants have a potential upside when higher earnings are realised. The competition for aid should prevent applicants from unduly inflating their cost estimates and required levels of return. Additionally, where a project turns out to be less costly than budgeted, Enova reduces the aid grant in a pro rata calculation. Enova does not guarantee a certain level of return. Enova restricts the aid to the amount necessary to trigger the investment.

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<sup>36</sup> See Decision No 39/11/COL p. 12-13.



- (77) The Authority also questions whether the practice of awarding additional aid to ensure that the a certain level of return is maintained risks undermining the workings of the Energy Fund Scheme and, in particular, its mechanism for competition for aid. With the initial IRR of 12.35%, Finn fjord was arguably sufficiently compensated for the risk involved in the project. If Finn fjord were to be compensated when that risk, that was and is inherent in the project, materialises, it would be difficult to see the justification for the 12.35% IRR in the first place.
- (78) The Norwegian authorities have explained that the aid of NOK 16 million was part of a financing package to secure the necessary NOK [80-95] million as referred to above. SNN and IN, after negotiations, decided to grant short term loans of NOK [65-80] million, [45-60] and 18 million respectively, collateralised *pari passu* with pre-existing loans of NOK [300-325] million and NOK 100 million respectively. The notified grant of NOK 16 million would together with the new loans cover the unforeseen cost increases of NOK [80-95] million that was necessary to ensure a timely completion of the project.
- (79) It is the Authority's preliminary understanding that the Norwegian authorities thereby submit that the grant was necessary in order to ensure additional financing in the market, which again was necessary for the timely and full completion of the project. Thus, that the grant seen in conjunction with the total financing of the unforeseen cost increases need provided the necessary incentive effect for the timely completion of the project.
- (80) The Authority would for the purposes of assessing the incentive effect of the aid not exclude that the aid may be seen in conjunction with and as a necessary element to secure financing for unforeseen cost increases. The Norwegian authorities have, however, not explained why in the particular circumstances of this case, the grant of NOK 16 million was a necessary condition for SSN and IN to grant the new short term loans. In this regard it is recalled that the two existing lenders, SNN and IN, accepted to grant new loans of NOK [65-80] million without additional collateral. The Authority therefore questions on what basis the additional NOK 16 million was a necessary condition for the loans.
- (81) The Authority furthermore questions whether the NOK 16 million grant was the appropriate instrument<sup>37</sup> and why IN could not instead have provided the capital as a loan.
- (82) Additionally, the Authority notes that the Norwegian authorities have not clearly explained how the aid amount of NOK 16 million was determined. What is clear is that the proposed aid from IN to Finn fjord has not been awarded on the basis of a competitive call for projects similar to the procedures under the Energy Fund Scheme. Given that the aid would be an appropriate instrument and have incentive effect, the Authority still questions whether a lower amount of aid could have produced the same effects. The Authority therefore has doubts as to whether the aid is proportionate.<sup>38</sup>
- (83) In sum, and on the basis of the above, the Authority has doubts about the appropriateness, necessity and incentive effect of the proposed aid.
- (84) Finally, the Authority notes that IN and Enova, both acting on behalf of the Kingdom of Norway, have presented seemingly conflicting views on whether the additional aid to Finn fjord provides the company with an incentive to change its behaviour and thereby achieves a greater level of environmental protection than it would have without the aid. Although it is not a circumstance that would by its very nature automatically lead to the

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<sup>37</sup> Points 169-170 of the EAG.

<sup>38</sup> Point 174 of the EAG.

opening of a formal investigation procedure, the fact remains that when the Authority is faced with seemingly conflicting views from different representatives of the same Contracting Party on an issue that has a decisive impact on the question of the compatibility of the notified aid, it will in those cases likely harbour doubts about the compatibility of that aid. When faced with doubts, the Authority must open the formal investigation procedure.

## **6. Conclusion**

- (85) Based on the information submitted by the Norwegian authorities, the Authority has concluded that the proposed NOK 16 million cash grant from IN to Finnfjord constitutes state aid within the meaning of Article 61(1) of the EEA Agreement. After a preliminary examination, the Authority, for the reasons set out above, has doubts that this aid is compatible with the functioning of the EEA Agreement. Consequently, and in accordance Article 4(4) of Part II of Protocol 3, the Authority is obliged to open the formal investigation procedure provided for in Article 1(2) of Part I of Protocol 3. The decision to open a formal investigation procedure is without prejudice to the final decision of the Authority, which may conclude that the measure in question is compatible with the functioning of the EEA Agreement.
- (86) Accordingly, the Authority, acting under the procedure laid down in Article 1(2) of Part I of Protocol 3, invites the Norwegian authorities to submit their comments within one month of the date of receipt of this Decision; and in particular to take into account the seemingly conflicting views of Enova and IN.
- (87) Further, within one month of receipt of this decision, the Authority request the Norwegian authorities to provide all documents, information and data needed for assessment of the compatibility of the proposed NOK 16 million direct grant from IN to Finnfjord.
- (88) The Authority requests the Norwegian authorities to forward a copy of this decision to Finnfjord immediately.

HAS ADOPTED THIS DECISION:

### *Article 1*

The formal investigation procedure provided for in Article 1(2) of Part I and Article 4(4) of Part II of Protocol 3 is opened into the NOK 16 million direct grant to Finnfjord notified by the Norwegian authorities.

### *Article 2*

The Norwegian authorities are invited, pursuant to Article 6(1) of Part II of Protocol 3, to submit their comments on the opening of the formal investigation procedure within one month from the notification of this Decision.

### *Article 3*

The Norwegian authorities are requested to provide within one month from notification of this decision, all documents, information and data needed for assessment of the compatibility of the aid measure.

### *Article 4*



This Decision is addressed to the Kingdom of Norway.

*Article 5*

Only the English language version of this decision is authentic.

Decision made in Brussels, on 13 November 2013.

*For the EFTA Surveillance Authority*

Oda Helen Sletnes  
*President*

Sverrir Haukur Gunnlaugsson  
*College Member*