

► questions and answers

Event no: 731624

Investigation of PCC power contracts

What is state aid?

State aid is any kind of support granted by public entities that gives an enterprise an advantage which would not be obtained under normal market conditions.

What is the role of ESA?

The state aid rules are enforced by ESA regarding Norway, Iceland and Liechtenstein. All plans to grant state aid must be notified to ESA prior to implementation. ESA assesses whether such plans constitute state aid and whether such aid is eligible for exemption.

To enforce the rules, ESA has the power to require EFTA States to provide relevant information, and to order the recovery of any aid paid in breach of the EEA Agreement.

The rules of the game

The EEA agreement, just as the EU treaties, contains a general ban on state aid to prevent distortions of competition and negative effects on EEA trade. The rules are meant to ensure a level playing field for companies across the EEA and prevent protectionism in the form of government assistance.

There are many exceptions which means that state aid can be allowed when necessary to uphold a well functioning economy, for regional development or investment in R&D or to protect the environment among other things. Nevertheless all state aid must be kept in check and is only allowed if it complies with the strict requirements. Aid for the everyday operating cost of companies (operational aid) is rarely allowed.

Why is ESA assessing these contracts?

Iceland notified a 15 years power contract between Landsvirkjun and PCC for legal certainty. The majority of long-term power contracts with energy-intensive users in Iceland have been notified and assessed by ESA since the entry into force of the EEA Agreement. The PCC contract relates to the sale of 58 megawatts of power which will mainly come from a new geothermal power plant to be constructed in the North-East of Iceland, where the silicon metal plant will be located.

ESA has looked into the profitability calculations of the power plant and has raised doubts as to whether it is profitable, given the revenues expected to be generated by the power contract.

ESA will also investigate whether exemptions in a connection agreement entered into between Landsnet and PCC for transmitting the electricity will relieve PCC from paying costs for connecting the plant. That possible advantage would be financed by extra costs

of the existing users of the grid. The total investment is approximately EUR 32 million in transmission facilities.

ESA already approved aid to the silicon plant – why turn around now?

In March 2014 ESA approved aid granted by the State to PCC as regional investment aid. That aid was notified and assessed under rules that allow aid to be granted for development and job creation in sparsely populated regions under certain conditions. ESA found that these measures could be justified as investment aid, as they had the objective of increasing jobs, the aid was proportional and it was necessary for the construction of the silicon metal plant.

In contrast, operating aid is normally not allowed under the state aid rules. Operating aid merely relieves the beneficiary of the day-to-day expenses and does not create an incentive to invest. The Icelandic authorities are of the view that no state aid is involved in the sale of electricity to PCC and have argued that these are normal business transactions.

To the extent that ESA may conclude that state aid is involved in the sale and transmission of electricity, it would have to be assessed whether the aid could be justified on the basis of the exemptions in the EEA Agreement.

Does this investigation imply that the silicon metal plant cannot be built?

The Authority's decision from March 2014 to approve state aid for the construction of the silicon metal plant still stands, and is not affected by the investigation into the power contracts.

How come these cases were not assessed together?

The Icelandic authorities decided to notify the investment aid for the silicon plant separately and informed ESA that the power contract would be notified for legal certainty once it had been concluded. It was therefore not within the power of ESA to assess the power contract in March 2014.

In what way can these contracts entail state aid?

Publicly owned companies, like Landsvirkjun, enter into business transactions like any other businesses. They must however make sure that these transactions are made on market terms. This can be done by offering the electricity through an open, transparent and non-discriminatory tender procedure, or by ensuring that the investment entered into will be profitable and the expected revenues will cover the estimated costs plus a reasonable profit. In this case, Landsvirkjun plans to build a power plant to be able to provide the required electricity to the silicon metal plant. The expected revenues from the power contract must recoup the investment in the power plant.

Electricity is an important cost-component in the production of silicon metal. If PCC gets the electricity below the cost of producing it, this will constitute an advantage which PCC could not obtain under normal market conditions. Hence, it is state aid, provided the transaction was imputable to the state. Landsvirkjun is fully owned by the state. Yet it must be assessed on a case-by-case basis whether the transactions were imputable to the state. In this regard, ESA will in the formal investigation also assess the circumstances of the case and whether indeed Landsvirkjun's decision in this particular case is imputable to the Icelandic State.

ESA has also doubts as to whether the investment needed in the transmission grid to connect the planned silicon mental plant is in line with the statutory rules in Iceland and might not entail an advantage in favour of PCC financed through extra costs of the existing users.

Landsvirkjun is state owned – is that the problem?

No. EEA law is neutral when it comes to the ownership of companies, but it is not allowed to use state owned companies to give an undue economic advantage to companies which they would not have obtained under normal conditions, thereby distorting competition.

Are other parties involved?

Landsnet is the transmission system operator in Iceland, and is a subsidiary of Landsvirkjun. Landsnet has entered into a connection agreement with PCC and this agreement is inseparable from the sale of electricity.

Is the case based on a complaint?

The case is based on the notification from the Icelandic authorities and not on a complaint.

What is a formal investigation?

ESA assesses whether public state aid plans are in line with EEA law. If notified of planned state aid, ESA investigates whether intended support constitutes state aid and if it does, whether such aid is legal under EEA law. EFTA States are obliged to notify all planned state aid to ESA but it is their prerogative to decide how, what and when to notify. ESA also has independent investigative powers and can look into possible state aid cases by own initiative or due to a complaint.

Process:

- Notification/Complaint
- Preliminary Examination (request for information)
 - Aid or no aid
 - Compatible or non-compatible
- In-depth investigation (when deemed state aid and doubts about compatibility)
 - Preliminary assessment sent to EFTA State
 - Comments by EFTA State and interested parties
- Final decision
 - **Positive:** investigation closed
 - **Conditional:** monitoring
 - **Negative:** recovery

How long does it take?

There is no legal deadline for a formal investigation but ESA will endeavour to adopt a final decision within 12 months from its launch.

What is the status and what are the possible outcomes?

The contracts have not taken effect. The Icelandic authorities cannot put the contracts into effect while they have not been approved by ESA.

Should the formal investigation conclude that state aid was involved in the contracts, ESA would have to assess whether the aid could be justified by reference to the exemptions provided in the EEA Agreement. Operating aid is normally not allowed. Even if the aid could be classified as investment aid, there would be limited scope for granting such aid as regional aid, since the aid to PCC already granted by the investment agreement approved

by ESA in March 2014 is close to the maximum allowable ceiling. Other possible justifications, such as environmental aid, have not been considered.

Should ESA find that there is incompatible state aid involved, the contracts could not be executed.

What can Iceland do now in order to get ESA's clearance?

If the Icelandic authorities put forward evidence that convinces ESA that the electricity was sold to PCC on market terms, or that the decisions taken by Landsvirkjun were not influenced by explicit or implicit directions of the State, no state aid would be involved. Landsvirkjun could also sell the power from the power plant to a different buyer and could also renegotiate the terms with PCC to make the investment profitable and hence the prices would be market prices and free of state aid. An open and unconditional tender procedure could also make the transactions free of state aid.

Should the Icelandic authorities not succeed in convincing ESA that the investment and operating costs of the envisaged electricity infrastructure for PCC would not cause extra costs for the existing users of the grid, the Icelandic statutory rules on connection charges for new power plants and energy-intensive users could be revised, clarified and made more cost-reflective, non-discriminatory and transparent for the future contracts to be free of state aid.