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# *EFTA SURVEILLANCE AUTHORITY*

Doc. No. 00-4347-I  
Dec. No. 121/00/COL  
Ref. No. SAM 030.99001

## EFTA SURVEILLANCE AUTHORITY DECISION

OF 28 JUNE 2000

CONCERNING ALLEGED INFRINGEMENT OF  
THE COMPETITION AND STATE AID PROVISIONS OF THE EEA AGREEMENT  
OWING TO THE FRAMEWORK CONDITIONS  
FOR THE NORWEGIAN STATE HOUSING BANK  
(NORWAY)

THE EFTA SURVEILLANCE AUTHORITY,

HAVING REGARD TO the Agreement on the European Economic Area<sup>1</sup>, in particular to Articles 59, 61 to 63, 109 and Protocol 26 thereof,

HAVING REGARD TO the Agreement between the EFTA States on the establishment of a Surveillance Authority and a Court of Justice<sup>2</sup>, in particular to Article 24 and Article 1 of Protocol 3 thereof,

HAVING REGARD TO the EFTA Surveillance Authority's Decision of 9 July 1997 concerning alleged infringement of the competition and State aid provisions of the EEA Agreement owing to the framework conditions for the Norwegian State Housing Bank (Decision No. 177/97/COL),

HAVING REGARD TO the Judgment of the EFTA Court dated 3 March 1999 (Case E-4/97, *Norwegian Bankers' Association v EFTA Surveillance Authority*) concerning the application for annulment of Decision No. 177/97/COL of 9 July 1997 of the EFTA Surveillance Authority concerning alleged infringement of the competition and State aid provisions of the EEA Agreement owing to the framework conditions for the Norwegian State Housing Bank<sup>3</sup>,

WHEREAS:

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<sup>1</sup>Hereinafter referred to as the EEA Agreement.

<sup>2</sup>Hereinafter referred to as the Surveillance and Court Agreement.

<sup>3</sup> EFTA Court, Case E-4/97, *Norwegian Bankers' Association v EFTA Surveillance Authority* supported by The Kingdom of Norway [1999] Report of the EFTA Court, page 1. The Judgment is also available from the EFTA Court homepage ([www.efta.int](http://www.efta.int)).

## I. FACTS

### 1. The initial procedure

By letter dated 7 November 1995, received and registered on 8 November 1995 (Doc. No. 95-6439-A), *Den Norske Bankforening* (the Norwegian Bankers' Association, hereinafter "the Association") lodged a complaint with the EFTA Surveillance Authority (hereinafter "the Authority"), requesting it to assess whether the framework conditions for the Norwegian State Housing Bank (hereinafter "Husbanken") were in conformity with the EEA Agreement.

#### 1.1 The Complaint

The complaint concerns the competitive conditions between commercial and saving banks and mortgage companies on the one hand, and Husbanken on the other. The initial complaint claimed that owing to the special framework conditions, within which Husbanken operates, including annual subsidisation from the Government budget and an effective "monopoly" on providing subsidised lending for housing purposes, Husbanken is shielded against competition from banks and mortgage companies. The Association submitted that this represents distortion of competition, which is in breach of Norway's obligations under the EEA Agreement, in particular of the State aid rules of the EEA Agreement. The Association further contended that the framework conditions for Husbanken went beyond what is required by the interest of the population groups targeted by the subsidies and beyond the scope of necessity implicit in Article 59 of the EEA Agreement regarding public undertakings.

The initial complaint was supplemented by letters and faxes of 17.11.95, 27.11.95, 20.12.95, 22.02.96, 21.03.96, 25.03.96, 03.04.96, 18.04.96, 21.06.96, 28.06.96, 29.08.96, 02.10.96, 31.10.96, 13.11.96, 08.01.97 and 14.3.97. Additionally, on 25 June 1996 the Authority met with representatives of the Association in Oslo to discuss the case and exchange information. The Authority requested also information from the Norwegian authorities on 22 January 1996 and met with officials of the Royal Ministry of Local Government and Labour on 13 September 1996 in Oslo. The Authority received information from the Norwegian authorities by letters dated 1 March 1996 and 22 October 1996.

#### 1.2 Husbanken

Husbanken was established by an act of the Norwegian Parliament (*Storting*) on 1 March 1946 (Act No. 3 of 1 March 1946 on the Norwegian State Housing Bank, *Lov om Den Norske Stats Husbank*, hereinafter "the Act"). The primary capital of Husbanken was contributed by the State. An indemnity fund was established to cover losses on loans and guarantees, with the initial amount being contributed partly by the State and partly by local authorities. According to the Act, further deposits can be made to the fund, as determined by the Parliament, and Husbanken can receive funding from the Treasury. Husbanken borrows solely from the State.

### 1.2.1 The Norwegian housing policy and the role of Husbanken

Husbanken forms part of the Norwegian housing policy. Husbanken's role in the Norwegian housing policy is to assist underprivileged groups of the population to become established in the market as house owners and more generally to ensure good quality housing of moderate standards throughout the country. Furthermore, Husbanken contributes, *inter alia*, to the construction and improvement of dwellings for elderly and handicapped people and stimulates urban renewal and the development of good residential environments.

### 1.2.2 Husbanken's loan and grant/allowance schemes

Following an amendment to the Act in 1992, the only task of Husbanken has been the financing of housing. Husbanken provides loans to individuals for housing purposes, but also provides loans, *inter alia*, to nursery schools, sheltered housing, new nursing home places and other care facilities. Improvement loans are granted for the purposes of assisting people with special needs and for the purposes of urban renewal. First home loans and purchase loans are granted, following means testing, to underprivileged groups. In addition, Husbanken offers grants and allowances for some of the purposes mentioned above. Grants and allowances are typically restricted to under-privileged groups. It is open for anyone to apply for those loans, grants and allowances.

Husbanken's loans for new dwellings are granted without any means testing as regard income, i.e. Husbanken does not reject any loan applications for new dwellings, as long as these applications fulfil certain objective requirements and conditions. These objective requirements and conditions are for example limits on the costs of the project (price of the land), the size (maximum of 120 square meters), as well as functional or planning requirements. Husbanken requires, as a main rule, a first-priority mortgage on the dwelling for which the loan is granted. The Parliament decides on the total lending volume. Husbanken does not offer any loans for commercial buildings.

### 1.2.3 Interest rates for Husbanken's loans

Originally, interest rates for Husbanken were directly set by the Parliament by way of regulations. Since 1 January 1996, however, the lending terms of Husbanken have followed directly the interest rate on Government securities, with an added margin of 0.5%. Since 1996, Husbanken has provided loans either with fixed or floating interest rates. The floating rate is based on short-term Government securities (0-3 months' term) observed three months before implementation of a new interest rate, adjusted quarterly. The rate of fixed interest is based on Government bonds with a remaining term of approximately five years, observed one month before implementation, adjusted every month<sup>4</sup>.

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<sup>4</sup> The system of calculating the five year fixed rates was altered as of 1 January 2000. The observation period of Government bonds with a remaining term of approximately five years was reduced from six months to one month.

## **2. The Decision of the Authority of 9 July 1997**

On 9 July 1997, the Authority adopted a Decision (hereinafter the “Decision”) with respect to the complaint (Decision No. 177/97/COL). In the Decision it was, *inter alia*, concluded that matters raised by the complaint were affected by provisions of the EEA Agreement and that the framework conditions for Husbanken involved State aid within the meaning of Article 61(1) of the EEA Agreement. In this context the Decision stated:

*“Apart from a very small equity, consisting of risk and loss funds, Husbanken’s core activity of providing loans for housing purposes is based on borrowings, which are obtained exclusively from the State (...). Husbanken, being a government agency financed by the State, enjoys the borrowing terms and favourable credit rating of the State. (...) Husbanken also in other ways clearly enjoys the financial backing of the State Treasury, for instance by way of budget appropriations, if needed, to cover the losses it incurs on loans as well as administrative expenses. It is therefore clear that as a State institution, Husbanken enjoys financial advantages of a kind not afforded to other providers of credit for housing purposes (...)”.*

As regards the exemption clauses in Article 61(2) and (3) of the EEA Agreement, the Authority found that they were not applicable. However, the Authority concluded that the derogation in Article 59(2) of the EEA Agreement concerning services of general economic interest was applicable and that it justified the current Husbanken scheme. Consequently, the Authority decided to close the complaint case without further action.

## **3. The Judgment of the EFTA Court of 3 March 1999**

On 9 September 1997, the Association lodged an application with the EFTA Court for annulment of the Decision. In its judgment of 3 March 1999 (Case E-4/97), the EFTA Court, although being in favour of the Authority’s findings on many points, concluded that certain aspects in the Decision had not been considered to the extent necessary, and therefore decided to annul the Decision. However, the EFTA Court did not alter the Authority's findings on the following points:

- The framework conditions for Husbanken involve State aid within the meaning of Article 61(1) of the EEA Agreement.
- The aid is existing aid.
- The Authority was under no obligation to open formal proceedings.
- None of the exemptions in Article 61 are applicable, neither in Article 61(2)(a) nor in 61(3) of the EEA Agreement.
- Husbanken is an undertaking entrusted with the operation of services of general economic interest; this applies also to Husbanken's non-means tested loans for new dwellings. Accordingly, none of Husbanken's activities fall outside the scope of services of general economic interest.
- The Authority did not incorrectly interpret the EEA Banking Directives, in finding that these Directives did not apply to specialised house financing institutions such

as Husbanken, nor did the Authority underestimate the effects of harmonisation achieved through these Directives, as well as through primary and other secondary EEA legislation, when balancing the interests of the EEA vis-à-vis those of the Norwegian authorities.

- The Authority is not under an obligation to ensure that Norway selects the least distortive means for the achievement of its housing policy goals; the appropriate test is that the means must not be disproportionate. A reasonable relationship between the aim and the means employed is satisfactory in this context.

On the other hand, the EFTA Court found that the Authority did not adequately assess the effects on trade and the interests of the Contracting Parties in the context of Article 59(2) of the EEA Agreement. The EFTA Court's view on the flaws in the Decision are stated in paragraphs 67-70 of the judgment:

- “67. *The Court notes, as already mentioned in this judgment, that Article 59(2) EEA provides that the operation of undertakings entrusted with services of general economic interest must not affect the development of trade ‘to such an extent as would be contrary to the interest of the Contracting Parties’.* The services under consideration in the present case are financial in nature. There is no doubt that the word ‘trade’ in Article 59(2) EEA applies to them.
68. *In its Decision, the EFTA Surveillance Authority did not go into depth on this condition. It states in its Decision that even if it cannot ‘be excluded that the measures under consideration may affect trade between Contracting Parties, in practice such trade effects are likely to be only limited’.*
69. *The Court notes that the parties disagree as to which market is relevant in this case. It is also disputed whether there are alternative means less distortive to competition than those presently applied whereby the housing policy of the Norwegian State can be achieved. The Applicant has further argued that an analysis of the costs and benefits of the State aid cases referred to above, can be done in this case. The Court cannot conclude that these points have been considered to the extent necessary by the EFTA Surveillance Authority in its Decision. At least the Decision itself does not bear witness to that.*
70. *These questions call for complex analyses and assessments which the Court cannot carry out but which must be done by the EFTA Surveillance Authority. Article 59(2) EEA calls for an application of a proportionality test to assess whether the required balance has been struck between the common interests of the Contracting Parties to the EEA Agreement and the legitimate interest of Norway. The common interests require extensive freedom in the field of services whereas the interest of Norway could be said to be that the Government and Parliament must be permitted to regulate Norwegian housing policy according to the political goals set. In other words, the EFTA Surveillance Authority must strike a balance between the right of Norway to invoke the exemption and the interest of the Contracting Parties in avoiding distortions of competition. For these reasons, the Court concludes that the EFTA Surveillance Authority, by not carrying out the test described, wrongly*

*interpreted and applied Article 59(2) EEA. Accordingly, the Decision under scrutiny must be annulled”.*

#### **4. The Authority’s subsequent review**

Following the EFTA Court’s judgment, the Authority reviewed the case in the light of the EFTA Court’s findings and requested the Norwegian authorities by letter of 26 March 1999 (Doc. No. 99-2256-D) to provide certain information relating especially to the points which the EFTA Court considered had not been adequately reasoned in the Decision. The Norwegian authorities were, in particular, asked to provide statistical and other information on the following items:

- Structure of the Norwegian housing finance market;
- trade effects of aid to Husbanken;
- market presence in Norway of foreign banks in housing finance loans;
- cost-benefit analysis of aid to Husbanken; and
- balancing of EEA Contracting Parties’ interests.

Also by letter of 26 March 1999 (Doc. No. 99-2257-D), the Authority sent a copy of the above request to the Association and invited the Association to submit their comments.

##### **4.1 Procedural rights of the Association**

In the same letter to the Association, the Authority used the opportunity to respond to an earlier request from the Association, made by letter of 12 March 1999 (Doc. No. 99-2013-A). In that request the Association asked the Authority to confirm that the Association will be treated as a party in the proceedings, and that the Association will be given the right to access documents produced by the Norwegian authorities or other interested parties, as well as to have the right to be heard before a new decision is taken.

The Authority’s response to this request reads as follows:

*“Decisions by the EFTA Surveillance Authority in the field of State aid are addressed to the EFTA States concerned. Furthermore, the review of State aid pursuant to Article 1(1) of Protocol 3 to the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice is a procedure between the EFTA Surveillance Authority and the EFTA State concerned. Accordingly, the procedural rights of third parties in such proceedings are limited and not as far-reaching as in the case of undertakings which, under procedures specific for anti-trust cases (cf. Regulation 17), are themselves the object of an investigation and might be penalised by a decision of the Authority (right to a fair hearing and full disclosure of a case file). Nevertheless (...) it has been found appropriate in the present case to make available to the Association information from the case file (...). While it is hoped that this approach will be to your satisfaction, it must be underlined that it is at the same time without prejudice*

*to the Authority's further examination of the present case and to its conduct in general of the review procedure for State aid*".

## 4.2 Information received and meetings

The Norwegian authorities submitted information by letter of 28 May 1999 (Doc. No. 99-3890-A). The Association likewise submitted its comments by letter of 7 June 1999 (Doc. No. 99-4285-A). By letters of 11 June 1999 (Doc. No. 99-4208-D and 99-4209-D), the Authority sent the observations of the Norwegian authorities to the Association for comments and *vice versa*. Comments were received from the Norwegian authorities by letters of 5 July 1999 (Doc. No. 99-5642-A) and 7 July 1999 (Doc. No. 99-5266-A), as well as from the Association by letters of 5 July 1999 (Doc. No. 99-5102-A) and 21 July 1999 (Doc. No. 99-5581-A). The Association submitted subsequent comments by letter of 28 September 1999 (Doc. No. 7164-A) and the Norwegian authorities by letter of 25 November 1999 (Doc. No. 99-8982-A). On request of the Association, the Authority met with its representatives in Brussels on 25 February 2000<sup>5</sup>. Finally, on 29 March 2000 the Authority met with officials of the Norwegian authorities in Oslo to clarify some outstanding issues and to obtain up-dated statistical information. As a follow-up of this last meeting in Oslo, the Norwegian authorities submitted by letter of 9 May 2000 (Doc. No. 00-3621-A) their response to the issues raised at the meeting and provided up-dated statistical information. The main contributions of the Norwegian authorities and the Association will be described below.

### 4.2.1 Structure of the Norwegian housing finance market

#### *Information from the Norwegian authorities*

According to the Norwegian authorities, the relevant product market is the market for housing mortgage loans and the relevant geographical area is Norway. Under the definition used by the Norwegian authorities, Husbanken's mortgage loans for housing improvements and for disadvantaged people are included along with loans for new dwellings. However, as municipalities can obtain Husbanken loans without a mortgage, the Norwegian authorities have chosen not to include such loans in Husbanken's market share. The Norwegian housing finance market is statistically identified as mortgage loans for housing (see table 1).

#### **(1) Housing mortgage loans and Husbanken's market share\* Amounts in billion NOK**

	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Total	259,3	269,1	282,1	289,7	308,9	322,0	347,7	375,7	416,6	473,5	516,4
Husbanken	68,6	72,5	78,1	83,3	77,4	72,9	69,9	65,6	61,3	65,1	68,9
Other Norwegian operators	190,4	195,5	202,4	204,5	229,6	246,8	274,5	306,0	349,8	408,8	447,5
Foreign banks**	0,3	1,1	1,6	1,9	1,9	2,3	3,3	4,1	5,5	6,3	9,4
Husbanken's market share %)	26	26	27	28	25	22	20	17	14	14	13,3

<sup>5</sup> At that meeting the Association informed the Authority of its merger with the Norwegian Insurance Association at the beginning of 2000 to form the "Norwegian Financial Service Association".

\* Figures for 1989-90 comprise housing loans and other loans for housing purposes under amortised loans. As from 1991 a special code (mortgage loans) was used under amortised loans. Before 1996 and after 1990 lending for housing purposes consisted of the codes "mortgage lending" and "other loans for housing purposes". From 1996 on, lending for housing purposes consists solely of mortgage loans.

\*\* Foreign banks with branch offices in Norway and banks in Norway that are wholly or partly owned by a foreign bank.

[Sources: Norges Bank (the Central Bank of Norway) and Husbanken]

Since life insurance companies and foreign banks without branches in Norway do not explicitly report their mortgage lending, such loans were not, according to the Norwegian authorities, included in the above statistics. If these institutions were included, the overall market would be larger and Husbanken's market share would approximately decrease to 13.4% in 1998 and to approximately 13.1% in 1999.

Concerning the financing of new dwellings, the Norwegian authorities stated that since there are no official Norwegian statistics available, the lending for such purposes would have to be estimated. The best estimate of the market share could be arrived at by calculating the ratio between the number of dwellings, which actually received loans from Husbanken and the number of completed dwellings, since Husbanken loans are granted once the dwelling has been completed. Based on this calculation method the Norwegian authorities presented figures, whereby Husbanken had approximately a share for the financing of new dwellings of 48% in 1998 and approximately 55% in 1999. The Norwegian authorities emphasised that this share reflects the dwellings for which Husbanken had provided basic financing and thus is not indicative for Husbanken's percentage of the loan volume. Separate estimated figures were provided concerning Husbanken's share of the loan volume for new dwellings. According to these figures, Husbanken had a share of the loan volume for new dwellings of approximately 36% in 1998 and of approximately 41% in 1999.

#### *Comments from the Norwegian Bankers' Association*

The Association considers the market for first priority housing loans for new dwellings to be the most relevant market. However, the Association indicated that it would not oppose to assess also the effects of Husbanken's market share on the total market for housing mortgage loans. In this context, the Association stated that the calculations of Husbanken's market share on the total market for housing finance must be amended. Lending for housing purposes by insurance companies, which the Norwegian authorities excluded must for example be included.

The Association stated further that the Norwegian authorities were wrong in excluding from the figures lending by Husbanken to municipalities. According to the Association, municipalities are ordinary borrowers on the credit market and the credit institutions compete heavily with each other to provide loans to them. The Association submitted that Husbanken's loans to the municipalities are part of the market for housing finance, since the means are used for financing of dwellings, and that the end user of Husbanken's loans to the municipalities are households and not the municipalities themselves. Accordingly, the market share of Husbanken on the total market for housing finance would be some 23% in 1995 and about 17% in 1998.

The Association argued furthermore that there is no way of knowing whether a loan from a credit institution backed by a mortgage is actually used for housing purposes and suggests therefore that 25% of bank loans should not be counted for housing



purposes, which would further increase Husbanken's share to approximately 23% in 1998.

#### 4.2.2 Trade effects of aid to Husbanken

##### *Information from the Norwegian authorities*

The Norwegian authorities stated that Husbanken has never granted loans for the financing of dwellings outside Norway. Its activities are targeted exclusively towards promoting Norwegian housing policy. It was stressed that participation in cross-border lending would be contrary to the legislation.

The volume of housing mortgage loans provided by foreign credit institutions, which do not have a branch office in Norway, or own a Norwegian finance company is regarded to be insignificant. The Norwegian authorities were unable to find any statistics in this field.

##### *Comments from the Norwegian Bankers' Association*

The Association provided no specific comments on these issues, apart from allegations that the volume of housing mortgage loans provided by foreign credit institutions, which do not have a branch office in Norway, or own a Norwegian finance company, is increasing.

#### 4.2.3 Market presence in Norway of foreign banks in housing finance loans

##### *Information from the Norwegian authorities*

On the other hand, when it comes to foreign banks with branch offices in Norway or Norwegian banks that are wholly or partly owned by foreign companies, statistics are available. The market share on the Norwegian market for housing mortgage loans held by such foreign banks was according to the Norwegian authorities, in 1998 approximately 1%.

##### *Comments from the Norwegian Bankers' Association*

The Association argued that the Ministry had failed to appraise the effects of Fokus Bank being taken over by Den Danske Bank in the spring of 1999 and of Bergensbanken being taken over by Svenska Handelsbanken in autumn 1999. As a result of these changes, the market share of foreign institutions on lending for housing purposes would increase from 1.3% to approximately 5% in 1998. However, this calculation was based on loans secured on housing for all sectors and not only for households and local authorities.

#### 4.2.4 Cost-benefit analysis

##### *Information from the Norwegian authorities*

State appropriations for and revenues from Husbanken are included in the Government's annual accounts, cf. the two tables below:

#### **(2) Appropriations for Husbanken in the Government budget 1996-99** **Accounting figures. Amounts in million NOK.**

<b>Chapter, item</b>		<b>1996</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>
<b>2412.01,11,45</b>	<b>Administrative budget</b>	<b>191</b>	<b>199</b>	<b>209</b>	<b>206,9</b>
<b>2412.70</b>	<b>Losses on loans*</b>	<b>88</b>	<b>71</b>	<b>7</b>	<b>7,5</b>
<b>2412.72</b>	<b>Interest support</b>	<b>2,047</b>	<b>77</b>	<b>77</b>	<b>97</b>
<b>2412.90</b>	<b>Loans to Husbanken**</b>		<b>5,896</b>	<b>8,909</b>	<b>8,597</b>

\* Book losses.

\*\* New item introduced in connection with the restructuring of the funding system in 1997.

#### **(3) Reversals from Husbanken to the Government budget 1996-99** **Accounting figures. Amounts in million NOK.**

<b>Chapter, item</b>		<b>1996</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>
<b>5312.01,04</b>	<b>Fees and admin. Charges</b>	<b>29</b>	<b>28</b>	<b>30</b>	<b>27,9</b>
<b>5312.90</b>	<b>Instalments on loans*</b>		<b>7,425</b>	<b>4,038</b>	<b>4,904</b>
<b>5615.80</b>	<b>Interest from Husbanken*</b>		<b>3,749</b>	<b>3,326</b>	<b>5,176</b>

\* New item introduced in connection with the restructuring of the funding system in 1997

On the cost side it is submitted that in 1998 Husbanken's gross administrative costs totalled NOK 209 million and that the net administrative costs, after deducting reversed fees and charges, totalled NOK 179 million. The amount of net administrative costs remained for 1999 the same. It is stated that it is difficult to isolate the administrative costs of Husbanken's lending activities from the costs related to its other activities, such as for example grants and allowances, information and guidance services and directorate functions. However, the Norwegian authorities presented a calculation which is based on the "rough assumption" that the relative amount of working hours related to an activity can be used as an estimated share of the administrative costs related to the same activity. According to this calculation method, of a total of 206,9 NOK million in 1999, the gross administrative costs related to mortgage secured lending could be estimated to be 107 NOK million. The net costs are accordingly estimated to be 82 NOK million.

The Norwegian authorities stated that since 1997 Husbanken's borrowing costs have by definition equalled the interest income from loans. Thus, Husbanken has no funding benefit or net interest income of its own. However, the Norwegian authorities stated that the "technical borrowing" cost may be of interest with respect to the

competitive relationship between Husbanken and other credit institutions. To this end, the Norwegian authorities have relied on the 3-month NIBOR<sup>6</sup> rates as a term of reference and compared them with the rates of short-term Government certificates. The interest rates for short-term Government certificates indicated in the table below do, however, not include the added margin of 0.5%, which is charged to Husbanken.

**(4) Comparison in percentage points of 3-months NIBOR rates  
with rates of short term Government certificates**

	1997	1998	1999
NIBOR, 3-month, %	3.71	5.79	6.53
Rate for Government certificates, 0-3 months, %	3.51	5.52	6.17
Difference, %	0.20	0.27	0.36

[Sources: Norges Bank (the Central Bank of Norway)]

According to the Norwegian authorities, since the funding system was different prior to 1997, only the years 1997, 1998 and 1999 are relevant for this comparison.

As regards Husbanken's fixed interest rates, the Norwegian authorities provided interest rates of State bonds with a remaining term of approximately five years and interest rates of private bonds with the same duration. The interest rates for State bonds indicated in the table below do, however, not include the added margin of 0.5%, which is charged to Husbanken.

**(5) Comparison in percentage points of 5 year private bonds rates  
with rates of 5 year State bonds**

	1997	1998	1999
Private bonds, 5 years, %	5.46	5.88	6.09
State bonds, 5 years, %	5.11	5.33	5.37
Difference, %	0.35	0.55	0.72

[Sources: Norges Bank (the Central Bank of Norway)]

According to the Norwegian authorities, loans with floating rates account for approximately 13% of Husbanken's total lending volume. The share of loans with fixed rates is some 80%. The remaining 7% are based on special terms given before 1996.

Concerning possible tax benefits, the Norwegian authorities point out that the accounts of Husbanken are totally included in the Government Budget. The accounts are set up on a cost base and do not operate with a net profit or loss. For these reasons they consider it natural that Husbanken's activity is not taxed.

According to the Norwegian authorities, it might be argued that the housing allowances provided by Husbanken favour Husbanken loans. The historical reason for relating housing allowances to financing by Husbanken was to ensure that housing would become affordable for households with modest incomes. The average housing

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<sup>6</sup> Norwegian inter-bank offered rate.

allowance per household in 1998 was NOK 13,656<sup>7</sup>, mainly distributed to households with elderly and disabled members totalling 80,000 households. In 1998 only 20,000 other households, mainly single parents, were granted housing allowances. Besides being subject to dwelling-related requirements, the housing allowance is strictly means-tested.

Additionally, in order to secure affordability objectives, new Husbanken-financed dwellings are exempt from municipal property tax for the first three years. However, only 46% of Norwegian municipalities apply municipal property tax. The annual tax on average for new Husbanken-financed dwelling in these municipalities amounts to less than NOK 1,000. According to the Norwegian authorities, a draft bill for discontinuing this special property tax exemption is under consideration by the Government.

The Norwegian authorities refer to different requirements for Husbanken, which could be considered as a competitive advantage for Husbanken, such as for example that Husbanken does not have to earn returns on equity, subordinated loan capital, capital backing and yield to owners as compared to regular credit institutions. According to the Norwegian authorities, the credit institutions, which can be best compared with Husbanken, are mortgage institutions, as they primarily provide loans secured by mortgages in dwellings and base borrowings on securities. A comparison of relative revenues and expenses is set forth in the table below:

**(6) Results of Norwegian mortgage companies<sup>8</sup> vs. results of operations of the  
Husbanken system<sup>9</sup>  
Percentage of average loans outstanding in 1997**

	<b>Mortgage companies</b>	<b>Husbanken system*</b>
Net interest income	0.68	0.50
Other revenues	0.15	0.03
Other expenses	0.27	0.25
“Result” before loss	0.57	0.28
Losses on loans	-0.03	0.08
“Result”	0.60	0.20

\* Incl. Treasury mark-up

According to the Norwegian authorities, the mark-up on Treasury loans to Husbanken was 0.18 percentage points lower than the average net interest income of Norwegian mortgage companies (0.68 -0.50). The table shows that the results of the Husbanken

<sup>7</sup> Computed on the basis of average monthly housing allowances 2<sup>nd</sup> term 1998.

<sup>8</sup> *Economic Bulletin* 1998/1, p. 53, Norges Bank, “Financial Institutions in 1997” by Robin Nilsen, Snorre Evjen and Inger Anne Nordal.

<sup>9</sup> Assumptions regarding Husbanken:

- Average lending: NOK 78.166 billion, which is the mean of outstanding loans in 1997.
- Net interest income by definition equal to 0.5 percentage points charged by the Treasury.
- Other revenues from lending activity NOK 28.497 million (chap. 3574), cf. accounts.
- Other expenses: NOK 199.059 million administrative budget, cf. accounts.
- Losses on lending activity: NOK 70 million, cf. accounts.

system before loss is 0.29 percentage points lower than the result of mortgage companies (0.57 -0.28). Apart from the lower interest rates, this difference may largely be ascribed to lower fee-based revenues (other revenues) by Husbanken. The Norwegian authorities state that if the difference between 3-month NIBOR rates and rates for short-term Government was 0.20 percentage points in 1997 (see table 4 above) and a 0.29 percentage points difference in earnings were added to that, Husbanken's competitive advantage on the lending market would be about 0.50 percentage points compared to Norwegian mortgage companies.

The Norwegian authorities stated that there are no official statistics available for interest rates offered on the Norwegian market for housing mortgage loans. However, there is one company (Cicero Information A/S) which offers statistics of mortgage interest rates offered to private households in Norway and which could at least be used as an indication. The Norwegian authorities stated that Husbanken generally offers loans to private households in the range of 60% to 80% of the sales value (for example in 1999 the average loan was 60.8% of the sales value). The value of such a loan would, in general, exceed 500,000 NOK. Based on the rates from Cicero Information A/S, the Norwegian authorities stated that these rates would be best comparable to Husbanken's floating rates. The Norwegian authorities, however, emphasised that the provided rates, which are displayed below in table 7, should only be seen as a rough approximation or indications and should by no means reflect a precise comparison. In this context the Norwegian authorities stated that since there is no interest rate benefit for Husbanken's lending activities to municipalities, the figures provided only reflect the rates of loans to private households. Based on the figures provided by the Norwegian authorities, Husbanken's interest rate benefit to private borrowers in 1997, 1998 and 1999 looks as follows:

**(7) Interest rate benefit for Husbanken loans to private borrowers in 1997, 1998 and 1999**

	1997	1998	1999	Average
Average market rate*, %	5.2	7.0	8.0	6.7
Husbanken rate**, %	4.0	6.0	6.7	5.6
Interest rate benefit on Husbanken loans	1.2	1.0	1.3	1.1

\* Cicero Informasjon A/S, loans for amounts within 60% of appraisal value

\*\* Calculated on the basis of the average interest rate of government certificates (0-3 months), including the mark-up of 0.5%

Additionally, the Norwegian authorities stated that in order to achieve housing policy goals, Husbanken applies certain criteria regarding size and the design of the dwelling, maximum costs, building process and documentation that are different and more comprehensive than those applied by ordinary credit institutions. These requirements may be perceived by borrowers as an additional cost related to taking up a Husbanken loan, and must be weighed against a possible interest rate benefit. Furthermore, Husbanken does not provide bridging loans for construction or financing packages for purposes other than housing. According to the Norwegian authorities, the interest rate benefit derived for a loan with Husbanken is used to compensate the borrower for the additional costs of the above kind. If Husbanken's lending rates were the same as the

market rates, Husbanken would not be in a position to set additional housing policy requirements when awarding loans.

*Comments from the Norwegian Bankers' Association*

Concerning the calculation of Husbanken's borrowing costs (table 4 above), the Association disagreed with the irrelevance of figures prior to 1997. The Association made its own calculations, based on *effective* interest rates, and concluded that on average the difference was 0.6 percentage points for the period 1990-98. Apparently, the difference fluctuated from 1.15 percentage points in 1992 to 0.16 points in 1993. For the years 1997 and 1998, the Association finds that the difference was 0.30 and 0.49 points, respectively.

The Association also calculated the difference between interest rates on 5 years Government bonds and interest rates on 5 years mortgage bonds issued by mortgage institutions, as a proxy for the funding costs of credit institutions. The outcome would be an average interest rate difference in the period 1993-98 of 0.6 percentage points in favour of Husbanken.

The Association also disagreed with the calculations on the interest rate benefit for Husbanken loans. Firstly, it is questioned why municipalities should borrow in Husbanken if there was no interest rate benefit. Secondly, and more generally, it is argued that the Ministry has omitted to take into account the time lag in setting of Husbanken interest rates. According to the Association's adjusted calculations, the average difference between the interest rates of Husbanken's loans and the average market rates in the period 1996-98 was 1.8 percentage points, varying from 0.9 percentage points in 1996 to 3.1 percentage points in 1998.

Concerning other financial benefits, the Association refers to a report by the Office of the Auditor General in Norway on housing support. That report claims that many families in weak economic situations do not receive housing allowances as a result of the fact that if they had financed their dwelling by a loan in a private credit institution, they do not fulfil the conditions for obtaining support. As many as  $\frac{3}{4}$  of the number of families in the investigation with income levels below the income limits did not receive housing allowances under the scheme. The report questions the fact that it is the source of financing of the dwelling, which determines whether the family shall obtain housing support and not their economy.

4.2.5 Balancing of EEA Contracting Parties' interests

Neither the Norwegian authorities nor the Association have provided any information concerning the common interest of the Contracting Parties.

*Information from the Norwegian authorities*

The Norwegian authorities submitted arguments for providing general loans for new dwellings under the current system, in light of the goals of Norwegian housing policy. The Norwegian authorities state that for special groups of low-income households the mix of reasonable mortgage loans combined with means tested supplementary loans,

investment grants and housing allowances makes it possible for Husbanken in co-operation with the municipalities to tailor-make affordable housing. In the view of the Norwegian authorities, the introduction of means testing for Husbanken basic mortgage loan for new housing might create an additional tax incentive that would distort the labour market, as well as introducing a new housing segregation measure.

The Norwegian authorities submitted a detailed outline of the way loans contribute towards achieving the housing policy goals. Having explained the objectives and fulfilment of the current housing policy, the Norwegian authorities went on to discuss possible alternative models to organise the housing policy and referred in this context to a report<sup>10</sup> of the State Bank Committee (“the Committee”), which presented four alternative models for housing finance:

*“Model 1: status quo, i.e. the system practised prior to 1996. Husbanken continues to provide loans with interest support to general (non-means-tested) and selected (means-tested) target groups.”*

*Model 2: Husbanken continues to provide loans to general and selected target groups, but interest support is phased out and replaced by a grant aimed at priority housing policy goals and target groups. This is the current model.*

*Model 3: Husbanken loans are limited to use as a housing policy instrument in respect of selected groups.*

*Model 4: Husbanken does not provide loans, but instead provides guarantees for loans provided to selected target groups in the rest of the credit market.”*

On the basis of the Committee’s recommendations, the Government presented a report to the Parliament<sup>11</sup> based on Model 2. This was subsequently adopted by the Parliament and has formed the basis for the restructuring of Husbanken’s financial policy instruments since 1996.

The Norwegian authorities argued that if grants alone were to be used to achieve housing policy aims, the grant amounts would have to be larger than the value of the interest rate benefit of the loan, but by offering a combination of loans and grants, Husbanken achieves a co-ordination gain. This reasoning is based on the assumption that the borrower perceives the necessity of writing a new application and having to deal with several institutions, and the time spent waiting for the application to be processed by two institutions, as an extra administrative cost. Dealing with more than one institution means that more information must be sought, more forms must be filled out, more time is spent in the process and higher fees may have to be paid. Compensation must be provided for this cost so as not to prejudice the achievement of housing policy goals. However, the Norwegian authorities acknowledged that it is difficult to “put a value” on the gain achieved through co-ordination. In the view of the Norwegian authorities, a shift to Model 3 or 4 would entail significant extra

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<sup>10</sup> The State Banks under Changing Framework Conditions, NOU 1995:11, p. 114.

<sup>11</sup> Report No. 34 (1994-95) to the Parliament on Husbanken’s interest terms and subsidy profile.

expenses for the State for grants, losses and administration if the achievement of housing policy goals continues as before. The State would incur these additional costs as a result of:

- larger grants to compensate for the lost interest rate benefit for the borrower;
- larger grants to compensate for the loss of the co-ordination gain achieved by the present system of offering a combination of loans, grants and guidance; and
- larger grants to motivate borrowers to apply for a grant in Husbanken in addition to applying for a loan.

If Husbanken were to furnish guarantees for the loans provided by other credit institutions, extra expenses would also be incurred in connection with:

- increased administrative costs related to the operation of the guarantee scheme, e.g. guarantee approvals and monitoring procedures;
- increased overall administrative costs due to the duplication of processing;
- increased losses on loans resulting from a lack of incentive to reduce losses and to ensure that activities are optimal from a socio-economic point of view.

To explain the background for choosing model 2, the Norwegian authorities stated that unlike many other countries, Norway has a largely unsegregated housing market and that this can be largely attributed to Husbanken. Turning housing finance entirely over to the private market would increase the risk of a more segregated housing market. On the other hand, the model favoured by the Government entailed that Husbanken's market share decreased substantially.

Additionally, choosing model 3 or 4 would imply abandoning the general policy followed so far. Husbanken would no longer be able to use its loans to exert the same influence as before on long-term housing investments in terms of the use of resources, housing environment design, quality standards, etc. Furthermore, the Norwegian authorities stated that selective lending would require changes in the use of resources and the administrative organisational structure. Husbanken's current modest administration in relation to target groups and activities is based on co-ordination with other policy instruments and on the principle that means-testing is primarily carried out locally in municipalities and in private banks in connection with possible supplementary financing. For the public sector, Husbanken's general lending activity is a cost-effective way of achieving Norway's main housing policy goals and forms the basis for the overall focus on advisory services, educational functions and selective, economic measures.

#### *Comments from the Norwegian Bankers' Association*

The Association submitted an alternative market-based model to replace the present system. This model was developed in co-operation with the Norwegian Savings Banks Association. The model is based on interest rate setting on the ordinary credit market. The State support would be aimed at borrowers who satisfy the housing and social priorities, by an explicit reduction of the loan interest rate. Public support



would be made available, in accordance with the Norwegian authorities' priorities, via the credit institutions.

According to the Association, a rejection of an application for finance from a market-based credit institution could either be due to the borrower's total household income being considered too low under normal criteria to service a housing loan of the size applied for, or the construction project would be located in a part of the country where the housing market is weak. For these situations it is proposed to set up a special scheme. Under this special scheme such projects - where the authorities wish these projects to be carried out - will either receive a means-tested Husbanken loan or be supported by a state guarantee to facilitate a loan in the ordinary credit market. Alternatively the Association suggests that the credit institution, where the client has chosen to place his loan, receives a grant from the State through Husbanken, for instance by quarterly payments. The grant would be used to lower the interest rate on the housing loan. The Parliament could at any time decide by how much the interest rate on such loans should be reduced compared to the banks' ordinary terms, for instance by 1%, as was the assumption when the existing system was designed. The Parliament could also decide whether the grant should run for the full term of the loan, or only for a certain period.

The Association also suggests a possible alternative formula for the way the grant is awarded, namely that the credit institution would receive at the time when the final loan is granted a once and for all grant from the State, via Husbanken, which corresponds to a discounted flow of interest subsidies over the term of the loan. When a loan is transferred from one credit institution to another, the remaining subsidy would also be transferred to the new institution. It would be a clear advantage with such an arrangement that the subsidy for a particular project is given once and for all. Husbanken's resources otherwise required to follow up ongoing loans could therefore be used for other purposes.

The Association stated that Model 3 and 4, would lead to an improvement of the competitive situation in the credit market. The Association went on to discuss the housing policy under the present scheme and provided details of an application process to Husbanken for a typical housing project.

According to the Association, the main advantages of the new market-based model for new dwellings would be that the clients will be able to gain from competition in the credit market, both by being able to choose the credit institutions where they want to apply for a loan - and possibly co-ordinate this with other loans and services - and besides being able to transfer the loan through the whole term to another institution, and thereby being able to secure the best available conditions. Linking the interest rate with market terms would also imply that the rates would fluctuate more over the business cycle than under the present scheme. The rates would vary with the borrowing costs of credit institutions and their need for interest margin, and these would normally fluctuate more over the business cycle than the State's borrowing costs, which form the basis for Husbanken's interest terms. However, the Association believes that also this property cannot be regarded as any major disadvantage compared to the present scheme, when account is taken of the fact that a great majority of Husbanken's borrowers are not significantly different from clients with

regular housing loans. The support in relation to market rates would be unchanged over the whole period of the loan.

According to the Association, there is reason to believe that the total costs of the current regime are at any rate not smaller than the interest subsidy to borrowers of 1%, which is proposed as an estimate by the Association. The difference between a market based model and the present regime lies, *inter alia*, in the fact that, in the former alternative, the State's costs are made transparent through the granting of interest support. The implications for the state budget will be quite secondary compared to the social costs and improvements, which can be achieved through the new scheme.

#### *The response of the Norwegian authorities*

In response to the proposed model by the Association, the Norwegian authorities stated that in March 1999, the Norwegian Parliament had a broad discussion on housing policy, based on a White paper from the Government<sup>12</sup>, where the role and management of Husbanken were debated and confirmed by the majority as highly satisfactory. The Norwegian authorities highlight the following problem areas in the model proposed by the Association:

- double work and differentiated treatment of borrowers;
- distributional policy consequences whereby customers will be faced with differentiated interest conditions according to creditworthiness;
- a large gap in interest rates between borrowers in a relatively weak financial position, but who still qualify for loans on the ordinary credit market and those who are refused loans and offered financing by Husbanken;
- lack of incentives for lenders to pass subsidies on to the borrowers; and
- increased subsidies and extra administrative expenses for the Government.

It is claimed that the effects of the proposed model would be negative for borrowers living in sparsely populated areas or in difficult financial position, since they would be exposed to an application process where they must apply for a loan with another institution and receive a refusal before they can apply for a loan in Husbanken. Whereas it has been a principal aim of the of Norwegian housing policy to treat applicants equally and not to discriminate against customers in a difficult position, these groups could experience the process as discriminatory. The Norwegian authorities claim that there are reasons to expect that under the proposed model many applicants would be refused financing because the project was not partly financed by Husbanken.

It is also submitted that the model favoured by the Association would tend to weaken the State finances by

- loss of interest margin for the borrowers who move their loan to another bank;
- interest subsidies for borrowers changing banks; and

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<sup>12</sup> St. meld. nr. 49 (1997-98), st. meld. nr. 14 (1998-99), Innst. S. nr. 100 (1998-99), Innst. S. nr. 98(1998-99).

- administration of a new interest subsidy arrangement.

The Norwegian authorities argued that it is difficult to agree with the Association that the State would reduce its credit risk by handing over the best borrowers to other banks. The Norwegian authorities emphasised that the current system has proved to be an inexpensive and efficient instrument in fulfilling the long-term objectives of Norwegian housing policy and that the abolition of the system would be seen as a drastic change in the structure of the housing policy.

## II. APPRECIATION

### 1. Introduction

Article 38 of the Surveillance and Court Agreement states that “[i]f a decision of the EFTA Surveillance Authority has been declared void...the EFTA Surveillance Authority shall take the necessary measures to comply with the judgment”. Following the EFTA Court’s judgment, the Authority reviewed the case in the light of the EFTA Court’s findings and requested for its review additional information from the Norwegian authorities and the Association. It needs to be stressed that the Authority considers the problems identified by the EFTA Court in its judgment of 3 March 1999 to be limited in nature. To this end, the Authority requested only particular information, which it deemed to be necessary in order to address adequately the identified problems of its previous Decision. These problems relate in particular to the question whether the Authority had assessed in sufficient detail all the necessary conditions for the application of the derogation in Article 59(2) of the EEA Agreement. In the light of the EFTA Court’s findings, this Decision will consequently only focus on the flaws identified by the EFTA Court in the Authority’s Decision of 9 July 1997 and will in particular deal with the effects on competition, trade and the interests of the Contracting Parties in the context of the application of Article 59(2) of the EEA Agreement.

### 2. The presence of State aid

In line with its previous Decision of 9 July 1997 and in the light of the EFTA Courts findings, the Authority maintains its assessment that the framework conditions for Husbanken constitute State aid under Article 61(1) of the EEA Agreement. As regards the declared objectives of the State’s financing of Husbanken, the Authority reiterates its view expressed in its Decision of 9 July 1997 that none of the exemptions provided for under the third paragraph of Article 61 of the EEA Agreement would appear to be relevant in the present case, and that the same applies to indents (a), (b) and (c) under the second paragraph of Article 61 of the EEA Agreement.

### 3. Derogation under Article 59(2) of the EEA Agreement

The derogation under Article 59(2) of the EEA Agreement permits States parties to the EEA Agreement to confer on undertakings to which they entrust the operation of services of general economic interest, exclusive rights or other privileges which may hinder the application of the rules of the EEA Agreement on competition and State

aid, in so far as restrictions on competition, or even the exclusion of all competition by other economic operators, are necessary to ensure the performance of the particular tasks assigned to the undertakings concerned.

Article 59(2) of the EEA Agreement reads as follows:

*“Undertakings entrusted with the operation of services of general economic interest (...) shall be subject to the rules contained in this Agreement, in particular to the rules on competition, in so far as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them. The development of trade must not be affected to such an extent as would be contrary to the interests of the Contracting Parties”.*

In respect of the application of Article 59(2) of the EEA Agreement to the current case, the Authority maintains its opinion, which was upheld by the EFTA Court, that Husbanken can be considered to be an undertaking in the sense of Article 59(2) of the EEA Agreement, which is entrusted with the operation of services of general economic interest. However, in order to benefit from the derogation in Article 59(2) of the EEA Agreement, the principle of proportionality has to be respected. This proportionality test is twofold. It requires firstly that the compensation for the obligation to render a service of general economic interest must be based on the cost of such specific service. The European Court of First Instance held in this context that:

*“...the grant of State aid may, under [ex] Article 90(2) of the Treaty, escape the prohibition laid down in [ex] Article 92 of that Treaty provided that the sole purpose of the aid in question is to offset the additional costs incurred in performing the particular task assigned to the undertaking entrusted with the operation of a service of general economic interest and that the grant of the aid is necessary in order for that undertaking to be able to perform its public service obligations under conditions of economic equilibrium(...). Determining whether the aid is necessary entails a general assessment of the economic conditions in which the undertaking in question performs the activities in the reserved sector, without taking account of any benefits it may draw from the sector open to competition”.*<sup>13</sup>

Secondly, the proportionality test involves an assessment whether the specific service in question affects the development of trade to an extent contrary to the interests of the Contracting Parties.

In other words, if Husbanken’s costs to render the service of general economic interest are not overcompensated, are limited to what is necessary for Husbanken to perform the specific service in question and as long as the development of trade is not affected by the Husbanken system to an extent contrary to the interests of the Contracting

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<sup>13</sup> CFI, Case T-106/95 *Fédération française des sociétés d’assurances (FFSA) v Commission* [1997] ECR II-229 (at paragraph 178). See in this context also: CFI, Case T-95/94 *Chambre Syndicale Nationale des Entreprises de Transport de Fonds et Valeurs (Sytraval) and Brink’s France SARL v Commission* [1995] ECR II-2651; ECJ, Case C-367/95 P, *Commission v Chambre Syndicale Nationale des Entreprises de Transport de Fonds et Valeurs (Sytraval) and Brink’s France SARL* [1998] ECR I-1719.

Parties, the compensation may be accepted under Article 59(2) of the EEA Agreement.

The question whether Husbanken's services are not overcompensated and are limited to what is necessary to perform the service in question will be dealt with in detail in the subsequent section 3.1. The question whether the Husbanken system affects the development of trade to an extent contrary to the interests of the Contracting Parties will be dealt with in detail in section 3.2 of this Decision.

### **3.1 "Cost-benefit analysis" of aid to Husbanken**

In its judgment of 3 March 1999, the EFTA Court endorsed the Association's argument that the Authority failed in its Decision of 9 July 1997 to analyse the costs and benefits of the Husbanken system. This section will therefore focus on the question, whether the compensation (benefits) received by Husbanken for performing the services of general economic interest exceeds the costs incurred by such a public interest task and whether the benefits are limited to what is necessary to perform the service in question.

#### **3.1.1 Financial relations**

Since the accounts of Husbanken are fully integrated in the State budget, it may be useful at the outset to clarify the financial relations between the Treasury, Husbanken and Husbanken's clients.

To cover its general borrowing needs, stemming from Husbanken and all other State financed activities, the Treasury raises money at rates it is able to achieve in the credit market. To cover its lending activities, Husbanken borrows from the Treasury at these rates plus 0.5 percentage points. It lends on to its clients at exactly the same rates (i.e. the Treasury borrowing rate plus 0.5%). Thus, Husbanken has no added interest margin or mark-up in relation to its lending. By definition, Husbanken's interest payments from its clients equal its interest payment to the Treasury.

#### **3.1.2 Costs and benefits**

##### *Husbanken's borrowing and lending rates*

To the extent Husbanken is able to be funded at lower costs than competing financial institutions, a benefit may be said to accrue to Husbanken. Correspondingly, to the extent it is obliged to lend at lower rates than competing institutions, costs may be said to be incurred. In such a case Husbanken is forced to abstain from revenue.

As tables 4 and 5 show, Husbanken's funding costs for the years 1997 to 1999 were on average, when the Treasury's 0.5% margin is added, very close to costs for money raised by private institutions, in particular when Husbanken's borrowing and lending portfolios are taken into account. It is, therefore, hard to maintain that Husbanken received any particular funding benefit in this period.

On the other hand, by being obliged to lend at the same rates as it borrows, Husbanken is foregoing revenue.

According to the Norwegian authorities, the average difference from 1997 to 1999 between Husbanken's interest rates and the interest rates of private banks to final consumers was approximately 1.1% (see table 7 above). The Association calculated for the period from 1996 to 1998 on average a difference of 1.8%. In other words, Husbanken could have charged on average a between 1.1% to 1.8% higher interest rate. These costs, in form of reduced revenue, stem from Husbanken's obligation to provide services of general economic interest, namely to provide non-means tested reasonable loans to households.

In general terms, funding benefits of Husbanken can be expressed as the difference between funding costs of competing financial institutions and funding costs of Husbanken. Likewise, foregone revenue on Husbanken's lending can be expressed as the difference between competing institutions interest revenue and Husbanken's corresponding revenue. If private financial institutions borrow at a rate,  $r'(P)$  and Husbanken at a rate  $r'(H)$ , the funding benefit of Husbanken can be expressed as  $r'(P) - r'(H)$ . If private financial institutions lend at a rate  $r(P)$  and Husbanken at a rate  $r(H)$ , the costs or foregone revenue for Husbanken can be expressed as  $r(P) - r(H)$ . If the benefits are deducted from these costs, net costs can be expressed as  $(r(P) - r(H)) - (r'(P) - r'(H))$ . As Husbanken's lending rate equals its borrowing rate,  $r(H) = r'(H)$ , this expression of Husbanken's net costs boils down to  $r(P) - r'(P)$ . As this margin naturally is positive, net interest costs of Husbanken's funding and lending operations are by definition positive and correspond to the interest margin of private financial institutions.

#### *Administrative expenses*

According to the Norwegian authorities, the net administrative costs in 1998 totalled NOK 179 million. The Norwegian authorities have arrived at this figure by subtracting from the gross administrative costs of NOK 209 million in 1998 the fees and administrative charges of NOK 30 million in the same year. The amount of net administrative costs remained for 1999 approximately the same. It is stated that it is difficult to isolate the administrative costs of Husbanken's lending activities from the costs related to its other activities, such as for example grants and allowances, information and guidance services and directorate functions. However, the Norwegian authorities presented a calculation which is based on the "rough assumption" that the relative amount of working hours related to an activity can be used as an estimated share of the administrative costs related to the same activity. According to this calculation method, of a total of 206,9 NOK million in 1999, the gross administrative costs related to mortgage secured lending could be estimated to be 107 NOK million. The net costs are accordingly estimated to be 82 NOK million. Husbanken receives from the State compensation for its administrative expenses, no more, no less.

#### *Losses on loans*

Since Husbanken is generally under an obligation to provide loans to everyone (if the housing project fulfils certain condition), it involves the risk that in certain cases

Husbanken might not be able to recover the full amount of a loan (plus interest) if the lender's economic situation is weak. In order to cover for these cases, Husbanken receives from the State compensation for losses on loans. The compensation for losses on loans amounted in 1998 to NOK 7 million and in 1999 to NOK 7,5 million. This amount, however, serves only to compensate for incurred losses, i.e. it equals the amount of costs involved by the losses on loans.

#### *Direct Interest support*

Husbanken incurred costs in relation to lower interest rates amounting to NOK 77 million in 1998 and NOK 97 million in 1999. Husbanken received interest support from the State in 1999 amounting to NOK 97 million. This support is equal to interest support granted by Husbanken in relation to loans provided before the change of the system in 1996. However, the interest support as such will be phased out, since Husbanken's interest rate system changed in 1996 from direct interest support to a system, whereby the lending terms of Husbanken follow directly the interest rates on Government securities and Government bonds, with an added margin of 0.5%.

#### *Possible "regulatory" costs ?*

The Norwegian authorities stated that in order to achieve housing policy goals, Husbanken applies certain criteria regarding size and the design of the dwelling, maximum costs, building process and documentation that are different and more comprehensive than those applied by ordinary credit institutions. These requirements may be perceived by borrowers as an additional cost related to taking up a Husbanken loan, and must be weighed against a possible interest rate benefit. Furthermore, it was stated that Husbanken does not provide bridging loans for construction or financing packages for purposes other than housing. According to the Norwegian authorities, the interest rate benefit derived from a loan with Husbanken is used to compensate the borrower for the additional costs of the above kind. If Husbanken's lending rates would correspond with market rates, Husbanken would not be in a position to set additional housing policy requirements when awarding loans. These disadvantages might have an economic impact, however, these are "additional costs" to the consumers, are difficult to quantify and cannot be used for the purpose of this assessment, since they do not constitute any real costs to Husbanken.

#### *Corporate tax exemptions*

The fact that Husbanken is not subject to corporate tax could constitute a benefit. However, Husbanken generates no profits on which such tax could be charged.

#### *Benefit of not being a "regular credit institution"*

It is stated that the fact that Husbanken is not required to run its business like a "regular credit institution", which for example would have to earn returns on equity, and to provide funds to ensure its financial security would constitute another benefit for Husbanken. As Husbanken is not allowed to have any income on its own, but to pass the State's borrowing costs plus 0.5% margin on to its customers, there is no basis for dividends or other allocations of profits.

### *Allowances and grants*

Furthermore, it is stated that the system of housing allowances and grants might provide a benefit for Husbanken. Any applicant who fulfils certain criteria may apply for such additional housing benefits. However, the possibility that this system favours Husbanken loans cannot be fully excluded. Nevertheless, it is first of all very difficult to quantify such a benefit; neither the Norwegian authorities nor the Association have presented any estimations, calculations or information, which could be used in this context. Secondly, any grant or allowance is in the first place a benefit to the household and not to Husbanken directly. Even under the assumption that the grant and allowance system would help Husbanken to increase its lending volume and consequently its interest revenues, such a benefit would flow back to the State for the compensation of operating the system and would not materialise as a real financial benefit with Husbanken.

### *Property tax exemption*

Additionally, it was submitted that in certain municipalities Husbanken financed dwellings are exempted from property tax for the first three years, which could be considered as a benefit for Husbanken. It needs to be noted that only 46% of Norwegian municipalities apply municipal property taxes. The tax advantage for a period of three years would on average per dwelling be NOK 3,000. In the light of this “relatively small amount”, the fact that not all municipalities offer these exemption and given the fact that neither the Norwegian authorities nor the Association have provided any calculations how a benefit for Husbanken should be quantified in this context, it is not possible to conclude or at least estimate a financial benefit for Husbanken. Additionally, such a tax exemption is in the first place a benefit for the household. Even if the tax exemption would help Husbanken to increase its lending volume and thus increase the interest revenue, this “benefit” would flow back to the State and would not materialise with Husbanken. Furthermore, it needs to be recalled that this scheme will be discontinued and that a draft bill is already under consideration by the Government. Hence, the tax benefit will consequently not have a significant impact on the future market.

### 3.1.3 Conclusion

The compensation for the obligation of Husbanken to render the above mentioned service is based on the costs which are necessary to perform this specific service. Considering the above funding system, it is indeed difficult to locate any form of overcompensation of costs, which are incurred by operating the current Husbanken system. The costs are limited to what is necessary for Husbanken to perform the service in question. The Husbanken funding system is a closed one, not allowing Husbanken to use the compensation for anything else than loans. Husbanken receives benefits, which it passes on to consumers or otherwise transfers net income to the Treasury. It has also to be noted in this context that Husbanken is not present on markets outside the scope of its service of general economic interest; i.e. there is no risk of cross-subsidisation, which could have an impact on other markets.



### 3.2 Balancing of EEA Contracting Parties' interests

Article 59(2) of the EEA Agreement calls for an application of a proportionality test to assess whether there is a balance between the common interests of the Contracting Parties to the EEA Agreement and the legitimate interest of Norway. As the EFTA Court held in this context in its judgment of 3 March 1999:

*“Article 59(2) EEA calls for an application of a proportionality test to assess whether the required balance has been struck between the common interests of the Contracting Parties to the EEA Agreement and the legitimate interest of Norway. The common interests require extensive freedom in the field of services whereas the interest of Norway could be said to be that the Government and Parliament must be permitted to regulate Norwegian housing policy according to the political goals set. In other words, the EFTA Surveillance Authority must strike a balance between the right of Norway to invoke the exemption and the interest of the Contracting Parties in avoiding distortions of competition” (paragraph 70).*

#### 3.2.1 Norway's right to regulate housing policy

On the one hand, it is Norway's right to regulate housing policy according to the political goals. In this context, the Association suggested an alternative model, which it claims would be less distortive on competition and trade than the current Husbanken system. Although the model suggested by the Association may have certain advantages, the legal situation is, however, such that a Contracting Party to the EEA Agreement is free to organise services of general economic interest in the way it sees fit, provided that it respects the conditions of Article 59(2) of the EEA Agreement. The Authority is not entitled to prescribe the least distortive solution, if a solution preferred by the State concerned respects the requirement under Article 59(2) of the EEA Agreement. Hence, the Authority is not under an obligation to ensure that Norway selects the least distortive means for the achievement of its housing policy goals; the appropriate test is that the means must not be disproportionate. A reasonable relationship between the aim and the means employed is satisfactory in this context.

However, the Authority considered the alternative model, which was presented by the Association, and has the following observations: It seems that the proposed market based model may risk the situation of applicants with a relatively weak financial position. It also seems that it would not safeguard applicants living in regions of Norway where property values are low, who would find it more difficult to obtain financing of their projects. According to the Association, a rejection of an application for finance from a market-based credit institution would either be due to the borrower's total household income being considered too low under normal criteria to service a housing loan of the size applied for, or the construction project would be located in a part of the country where the housing market is weak. To cover these situations the Association suggests a similar system to the one currently in operation, i.e. it seems that there would be no real change to the system where house financing gets difficult on the market.

It can also not fully be excluded that the suggested model may at least potentially involve State aid elements contrary to Article 61 of the EEA Agreement, if the result would be that *de facto* only certain established Norwegian banks would benefit from a new system. This is in particular relevant, given the fact that foreign banks currently only have a market share of approximately 1.8% and that there are no significant cross-border transactions in this field. The problem of a potential subsidisation could create even a greater impact on trade between the Contracting Parties, since these private Norwegian banks are active in cross-border financing and other financial service sectors, which implies the risk of cross-subsidisation.

Additionally, the Norwegian authorities have listed some problem areas in the model suggested by the Association, which cannot be dismissed. It cannot not be excluded that the alternative model would increase subsidies and inflict extra administrative expenses, whereas the current system works on the basis to cover the costs to the Government and generates even a certain surplus with the mark-up of 0.5%.

Furthermore, the Association did not provide any estimation of the kind of costs the alternative model would involve. The Association has not presented any socio-economic cost benefit analysis related to their proposed model, which would discredit the current system as being an overcompensating and uneconomical model, which disproportionately interferes with the trade between the Contracting Parties. As mentioned above, the current compensation for the obligation of Husbanken to render the service is based on the costs, which are necessary to perform this specific service (see above section 3.1).

### 3.2.2 Interests of the Contracting Parties

On the other hand, the common interests of the Contracting Parties need to be assessed, which are compliance with the rules on competition and extensive freedom in the field of services. At the outset it needs to be stressed that due to different national credit rules and practices and the absence of effective harmonisation or mutual recognition at EEA level, there continue to be considerable obstacles to effective cross-border operations in this area. In most developed countries, including most States parties to the EEA Agreement, Governments, both at central and local level, intervene in housing and housing finance markets. This intervention takes different forms from one State to another, depending, *inter alia*, on certain realities in the housing markets, in particular the pattern of housing tenure, and the objectives of the housing policy of the Governments concerned. There is for instance likely to be a relationship between the extent to which private individuals' home ownership is an objective of public housing policy and the scope of intervention by the Government concerned in housing finance; a Government who sees it as an important objective of its housing policy that as many households as possible own their own dwelling, like in Norway, is likely to want to support the financing of such investments on a broad scale. In other countries, including some countries within the EEA, the share of owner-occupied dwellings of the total housing stock is relatively low (down to about 40% in certain countries), which in some cases also coincides with a relatively high share of publicly owned and rented houses (up to 40%). In the latter circumstances

housing policies tend to take different forms, with more direct provision of subsidised housing rather than subsidised housing finance.

However, whether the Husbanken system affects the development of trade to an extent contrary to the interests of the Contracting Parties will be assessed in the following paragraphs:

#### *Structure of the Norwegian housing finance market*

A starting point to assess the above question would be to identify the relevant market. Generally, a distinction can be made in the banking sector between the savings and the loan market. Husbanken is not a credit institution in the meaning of the relevant EEA legislation. It is not authorised to accept deposits from the public and therefore does not compete with credit institutions in that area. It does not engage in other financial services, e.g. payment inter-mediation, outside the scope of its core activity to provide loans for housing purposes.

The lending market could be divided into mortgage loans and other loans. The mortgage loans could further be divided into mortgage loans for commercial and individual purposes. The latter product is mainly related to the financing of housing. Husbanken does not compete with regular operators in the credit market outside the scope of its housing finance business. It does not for instance provide any lending for general commercial purposes or to economic operators such as contractors in the construction industry or property developers. The financing arrangement for Husbanken is a closed system and does not allow Husbanken to expand its position into areas outside its statutory field. Husbanken has for example not provided any loans for financing of housing outside Norway. Thus, the scope of Husbanken's core lending activity is limited to housing finance in Norway.

The Norwegian housing finance market is statistically identified as mortgage loans for housing, totalling a volume of approximately NOK 516 billion in 1999, of which the relevant share of Husbanken was approximately NOK 68,9 billion or 13.3% in that same year. The total lending volume does, however, not include life insurance companies and foreign banks without branches in Norway, since these institutions do not report their mortgage lending. If these institutions had been included, Husbanken's market share would approximately decline to approximately 13.1% in 1999. The Association argued that Husbanken's loans to municipal housing projects and the fact that many loans from credit institutions, which are secured by a mortgage, are not used for housing purposes would increase Husbanken's market share in 1998 to 23%. However, the Association did not provide any figures or at least reconcilable calculations in this context, which would support the estimation of this market share.

Concerning the market for the financing of new dwellings, there are no official statistics available. Hence, any calculations would be based on pure estimations. Quite apart from these considerations, it needs to be recalled that Husbanken also provides mortgage loans for other housing purposes, such as for housing improvement, the purchase of already constructed houses and for disadvantaged people. Therefore, Husbanken is not limited in its activities to the financing of only new dwellings. The fact that Husbanken recruits a great part of its clients for the purpose of financing new

dwellings, is not sufficient to limit the market to just this segment. This is particularly relevant, since Husbanken is not free to finance all types of new dwellings, but only those which fulfil certain criteria (such as the price of the land, the size, etc.).

On the other hand, the market for mortgage loans for housing can be distinguished by its financial product, which are loans secured by mortgage on the borrowings for housing property in general.

In the light of the above, as well as the comments in the following sections, and for the purpose of this assessment, the Authority therefore considers the Norwegian market for housing mortgage loans to be the relevant market.

#### *Trade effects of aid to Husbanken*

Husbanken has never granted any loans for the financing of dwellings outside Norway. Its activities are, as stated by the Norwegian authorities, targeted exclusively towards promoting Norwegian housing policy.

It needs to be stressed in this context that the granting of loans to individuals for financing their purchase of residential accommodation is a financial service which, in the present market circumstances, is predominantly of a local character and normally does not involve any direct cross-border transactions. Distortions of competition arising from financial advantages accorded to a State agency operating such services have therefore only limited direct trade effects.

The EEA Agreement establishes, *inter alia*, the general principles, both applicable to financial services, of the right of establishment for nationals of EEA States and their freedom to provide services within the territory of the Contracting Parties. However, the secondary legislation which, under the EC Treaty and the EEA Agreement, has been adopted to make these basic provisions effective, does not extend to mortgage credit institutions or specialised housing finance institutions of the kind which Husbanken is<sup>14</sup>. Consequently, such institutions are at present not able to benefit from the principles of mutual recognition and home country control contained in the banking legislation of the EEA Agreement. Therefore, due to different national credit rules and practices and the absence of effective harmonisation or mutual recognition at EEA level, there continue to be considerable obstacles to effective cross-border operations in this area. This is in a way demonstrated by the fact that the Norwegian authorities were unable to “record” any significant housing mortgage loans provided to borrowers in Norway by foreign credit institutions, which do not have branch offices in Norway or own a Norwegian finance company. The Association did not present any information in this context, which would lead to a different conclusion.

#### *Market presence in Norway of foreign banks in housing finance loans*

On the other hand, it can be said that the State supported activity of Husbanken tends to limit the opportunity of regular private credit institutions operating on the

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<sup>14</sup> The EC Commission has on more than one occasion presented proposals for a directive to regulate mortgage credit activities, but legislation in this field has not yet been adopted.

Norwegian market to acquire a diversified loan portfolio by reducing their share of relatively secure loans. To the limited extent that branches of foreign banks operating in Norway are active in the provision of loans to households<sup>15</sup>, the effects last referred to are likely to be substantially the same for them as for other financial institutions on the Norwegian market, and thus to make the establishment of such branches or the expansion of their activity less attractive than would otherwise be the case. It therefore cannot be ruled out that the advantages enjoyed by Husbanken may, at least potentially, affect trade between Contracting Parties to the EEA Agreement, although in practice such effects are limited.

The limited extent to which trade is currently affected is demonstrated by the fact that the share on the Norwegian housing mortgage loan market held by foreign banks was in 1998 only 1.3% and in 1999 approximately 1.8% (see table 1 above). The Association argued that the share in 1998 should actually increase up to 5%, due to the take over of Fokus Bank by Den Danske Bank and the take over of Bergensbanken by Svenska Handelsbanken. However, the Association did not present any information in this context, which would support this calculation. The calculation was further based on loans secured on housing for all sectors and not only for households and local authorities. In the light of these uncertainties, it can be generally assumed that the current market share of foreign banks established on the Norwegian housing mortgage loan market remains very small.

It is the Authority's view that the Husbanken system does not create any trade barriers for foreign banks to expand their mortgage secured housing loan operations in Norway, which could be considered to be contrary to the common interest of the Contracting Parties. This is demonstrated by the information provided in table 1 above, according to which foreign banks have expanded their lending volume of housing mortgage loans from NOK 0,3 billion in 1989 to NOK 9,4 billion in 1999. Whereas between 1989 and 1999 the total lending volume of housing mortgage loans in Norway almost doubled, the market share of foreign banks in the same period increased by more than 30 times. Also the recent take-overs, which were reported by the Norwegian authorities and the Association, show that the Husbanken system does not hinder foreign investors to acquire Norwegian banks, which do have activities in the house financing market.

Additionally, the changes of the principles for setting the interest rates on Husbanken's loans, which were implemented as from 1 January 1996, are in the long run reducing the level of direct interest subsidisation and thus will limit the distortive effects on the market for housing mortgage loans. In this context it needs to be noted

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<sup>15</sup> According to information submitted by the Association (by telefax of 28.06.96), foreign providers of credit were at the end of 1995 responsible for little less than 19% of total credit supply in Norway, while domestic credit institutions provided the rest. The great majority of loans provided by foreign credit institutions are loans to industry. Households have so far availed themselves of little credit finance from foreign banks. The foreign banks, which have established activities in Norway are partly banks competing with Norwegian banks in special niches of the market, and partly universal banks participating in ordinary lending activities. The group of banks last referred to will be offering housing loans in competition with other operators on the market. The Association's information also confirms that foreign banks operating on the Norwegian market have so far had only a relatively small share of loans to private individuals.

that after the introduction of the new system Husbanken's share on the Norwegian market for housing mortgage loans decreased from 20% in 1995 to 13% in 1999 (see table 1 above).

### 3.2.3 Conclusion

In the light of the above, the Authority takes the view that the Husbanken system does not appear to be inappropriate for the realisation of the housing policy objectives and concludes that there seems to be a reasonable relationship between the aim and the means. There are no indications, which would suggest that the current Husbanken system confers a benefit to Husbanken, which overcompensates for the incurred costs of operating the system, which would put Husbanken in an unchallengable position towards its competitors. There exist numerous obstacles to the development of trade due to the absence of effective harmonisation or mutual recognition in the EEA. Therefore, at the current stage in the development of the EEA market for housing mortgage loans there are no indications that the Husbanken system affects the development of trade to an extent contrary to the interests of the Contracting Parties in the meaning of Article 59(2) of the EEA Agreement.

## **4. Compatibility with Article 54 of the EEA Agreement**

The Association submitted in its initial complaint that "*the Housing Bank arrangement must be viewed not only in the light of the rules governing state support but also in a broader perspective of competition law*". It was also briefly stated that owing to the framework conditions within which Husbanken operates, it would enjoy a market dominance. However, the Association did not explicitly allege that an abuse of a dominant position has occurred, which is required for Article 54 of the EEA Agreement to be applicable, nor has it submitted any clear evidence to substantiate a claim that this Article has been infringed. Furthermore, the Authority's examination of the facts available to it has not given any reason to suspect that Husbanken has acted in infringement of the provisions in Article 54 of the EEA Agreement. The Authority has therefore seen no reason to examine the allegation any further.

## **5. Conclusion**

For the above reasons the Authority does not in the present circumstances consider that restrictions or distortions of competition as a result of the framework conditions for Husbanken go beyond what is required to allow that undertaking to perform the services of general economic interest with which it has been entrusted. Consequently, the Authority does not see a reason to take any further action with respect to the matters raised by the Association. However, this does not preclude that the Authority may at a later stage find reason to intervene, for instance as a result of changes in the market situation, introduction of new legislation at EEA level or in response to changes of the Norwegian authorities' policy with regard to the scope of Husbanken's lending activities.

**HAS ADOPTED THIS DECISION:**

1. The complaint initiated by letter of 7 November 1995 (Doc. No. 95-6439-A), concerning the framework conditions for the Norwegian State Housing Bank and their compatibility with the provisions of the EEA Agreement on State aid and competition, is closed without further action by the Authority.
2. The Norwegian authorities, the complainant and the European Commission shall be informed by means of a copy of this decision.

Done at Brussels, 28 June 2000

For the EFTA Surveillance Authority

Knut Almestad  
President

Bernd Hammermann  
College Member