

Case No: 68875
Event No: 570134
Dec. No: 373/10/COL

EFTA SURVEILLANCE AUTHORITY DECISION

of 22 September 2010

to initiate the formal investigation procedure with regard to the recapitalisation of Sjóvá insurance company

(Iceland)

The EFTA Surveillance Authority (“the Authority”),

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

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

HAVING REGARD to Protocol 3 to the Surveillance and Court Agreement (“Protocol 3”), in particular to Article 1(3) of Part I and Articles 4(4), 6 and 13(1) of Part II,

HAVING REGARD to the Authority’s State Aid Guidelines on the application and interpretation of Articles 61 and 62 of the EEA Agreement, in particular Part VIII, Temporary Rules regarding Financial Crisis, and the chapter on aid for rescuing and restructuring firms in difficulty¹,

HAVING REGARD to the Authority’s decision No 77/10/COL of 10 March 2010 on an information injunction against Iceland to provide information on the state intervention in Sjóvá,

Whereas:

I. FACTS

1 Procedure

The Authority became aware of the Icelandic state intervention in the insurance company Sjóvá-Almennar tryggingar hf. (Sjóvá) in the summer of 2009 through the Icelandic media. Subsequently the Authority included this case in the agenda of an annual meeting on pending cases in the field of state aid between the Authority and the Icelandic authorities which was held in Reykjavik on 5 November 2009. At the meeting the

¹ Available at: <http://www.eftasurv.int/state-aid/legal-framework/state-aid-guidelines/>

Icelandic authorities provided brief information concerning the background and history of the case.

Due to the complexity of the intervention and the circumstances surrounding it, the Authority asked the Icelandic authorities at the meeting on 5 November 2009 to provide written detailed information.

In a letter to the Icelandic authorities dated 16 November 2009 (Event No 536644), the Authority summarised the points of discussion at the meeting on 5 November 2009 and repeated its request for detailed information in writing regarding the state intervention in Sjóvá. Moreover, the Authority invited the Icelandic authorities to put forward their views regarding possible state aid issues involved in the case. The Authority requested that this information be provided no later than 16 December 2009.

The Authority sent a reminder letter to the Icelandic authorities, dated 14 January 2010 (Event No 543092) requesting that the information be sent to the Authority by 29 January 2010.

No written information was received and subsequently the Authority adopted an information injunction decision, pursuant to Article 10(3) of Part II of Protocol 3, on 10 March 2010 (Event No 548842), requesting:

‘...all documentation, information and data necessary to permit the Authority to assess the existence of state aid in the state intervention in Sjóvá as well as its compatibility with the state aid rules of the EEA Agreement. In particular, but not exclusively, the Authority requires the Icelandic authorities to provide it with a detailed description of the capital injection in Sjóvá including copies of all relevant documents and moreover a detailed explanation of how the Central Bank of Iceland came into possession of the assets of Sjóvá.

Moreover, the Icelandic authorities are requested, also no later than 11 April 2010, to provide all information and data necessary to assess the compatibility of the measure with the state aid rules of the EEA Agreement.

The Icelandic authorities are invited to provide their comments and view regarding any possible and potential state aid issues involved in this case within the same deadline, i.e. 11 April 2010.’

On 11 April 2010, the Icelandic authorities submitted a reply (Event No 553315).

On 7 June 2010 the Authority received a complaint (Event No 559496) against alleged state aid granted when the State intervened in Sjóvá.

2 Description of the case

2.1 Background

Sjóvá is one of Iceland's leading insurance companies². The company was taken over by Glitnir Bank³ (Glitnir) in 2003 and its operations were merged with those of the bank. In 2005, the financial group Moderna/Milestone Finance⁴ bought 66.6% of Sjóvá's shares from Glitnir and acquired full ownership as from 2006. Sjóvá's operations were then separated from those of Glitnir.

2.2 The state intervention and the events leading to it

The events leading to the state intervention and the state intervention itself are rather complex and will be described below in chronological order according to information available to the Authority.

2.2.1 Intervention by the Financial Supervisory Authority

Early in 2008, the Icelandic Financial Supervisory Authority (the FME) started an in-depth investigation into the financial position of Sjóvá on the basis of its annual report for the fiscal year 2007. It transpired that the company had insufficient capital reserves to meet the minimum required to continue insurance operations⁵ due to losses on its investment activities, which had grown substantially.

Following the investigation, from October 2008 to September 2009, Sjóvá was subjected to special supervision by the FME under Article 90 of the Act on Insurance Activities No 60/1994⁶. Furthermore, in December 2008, the FME appointed a special auditor to review Sjóvá's activities.

In March 2009, the FME referred "several issues relating to the business activities of the company" to the Special Prosecutor⁷. The Authority is not aware of the substance of the ongoing criminal investigation or whether it has any relevance to this case.

² According to a memorandum from the Financial Supervisory Authority (FME) dated 29 June 2009, the market shares of insurance companies in Iceland, based on their share in total premium income, was at the time as follows: Vátryggingafélag Íslands (VÍS) 35.3%, Sjóvá 29.5%, Tryggingamiðstöðin (TM) 27% and Vörður 8%.

³ Until 2006, the bank was named Íslandsbanki, when its name was changed to Glitnir banki. Following its collapse in October 2008, Glitnir has been managed by a Resolution Committee and has entered a winding-up procedure. In October 2008, a new bank was founded under emergency legislation to take over domestic assets and liabilities of Glitnir Bank. That bank was initially named Nýi Glitnir, but its name was changed to Íslandsbanki in February 2009.

⁴ Moderna Finance AB was a Swedish holding company owned by the Icelandic company Milestone hf. While Moderna Finance acquired financial undertakings in Sweden and Luxembourg, its biggest Icelandic assets were Sjóvá and the investment bank Askar Capital hf. The car financing company Avant is a subsidiary of Askar Capital. Milestone and affiliated companies were for a period among the major shareholders in Glitnir Bank, achieving their highest share of ownership of 16-18% of total shares in Glitnir in early 2007. Following Milestone's acquisition of Sjóvá and a major change of the ownership structure in Glitnir, Milestone's holdings in Glitnir declined. Milestone was also among the biggest borrowers from Glitnir. Further information on Sjóvá and Milestone and their ties with Glitnir Bank are available in the report of the Icelandic Parliament's Special Investigation Commission (SIC) available at <http://rma.althingi.is/> (Icelandic version) and <http://sic.althingi.is/> (Excerpts in English).

⁵ Minimum guarantee fund of 2 billion ISK as defined in the Icelandic legislation.

⁶ Now Article 86 of Act No 56/2010.

⁷ The role of the Special Prosecutor is to investigate suspicions of criminal actions in relation to the collapse of the Icelandic banks according to Act No 135/2008.

2.2.2 *Glitnir takes over Sjóvá - division of the company*

In March 2009, Sjóvá was taken over⁸ by its biggest creditor, Glitnir Bank (Glitnir). Glitnir had been under moratorium since 24 November 2008 and managed by a Resolution Committee appointed by the FME. Sjóvá's creditors had previously been managing the company since October 2008, when it had been put under the special supervision of the FME.

In April 2009, Glitnir and Íslandsbanki⁹ approached the Icelandic State requesting its assistance in refinancing and restructuring Sjóvá, having exhausted all alternative market solutions to rescue the company.

The Authority has received a presentation document prepared by Íslandsbanki in April 2009 and addressed to the Ministry of Finance. This document outlined a plan to restructure Moderna Finance AB, and its subsidiaries Askar Capital and Sjóvá. It furthermore contains plans to split up old Sjóvá by transferring insurance operation to a new company, leaving the less viable investment activities in the old company. After restructuring, the insurance company would then be sold to new investors.

During the summer of 2009, assets and liabilities were to be divided into 1) SA tryggingar hf., a new company to be incorporated, which would receive the insurance portfolio activities from old Sjóvá upon approval by the FME, and 2) SJ Eignarhaldsfélag (SJE), a holding company in which the toxic assets of old Sjóvá would be placed.

On 20 June 2009, Sjóvá on the one hand and Glitnir, Íslandsbanki, and SAT Eignarhaldsfélag hf. (a holding company wholly owned by Glitnir, hereinafter referred to as SAT Holding) on behalf of SA tryggingar hf.¹⁰ on the other hand signed an Asset Transfer Agreement, according to which all assets and liabilities of Sjóvá related to the company's insurance operations, including the insurance portfolio, were transferred to SA tryggingar hf., in accordance with Article 86 of the Act on Insurance Activities No 60/1994. Following the transaction the new company, SA tryggingar hf., was renamed Sjóvá.

According to its Articles of Association, dated 20 June 2009, the shareholders of the new company (Glitnir, Íslandsbanki and SAT Holding) were to contribute new equity of 16 billion ISK, required to continue insurance operations, as follows¹¹:

⁸ Together with other Icelandic subsidiaries of Moderna Finance AB: Askar Capital and its subsidiary, Avant.

⁹ The Authority assumes that Íslandsbanki became involved as it was also a major creditor of Sjóvá.

¹⁰ An unregistered company to be incorporated under Icelandic law.

¹¹ Subject to FME's approval, which was granted on 22 September 2009, see below.

Company	Amount	Form of payment	Share holding
Glitnir	ISK 2.8 billion	Bond issued by Avant with interest of REIBOR plus 3.75% with the following collaterals: <ul style="list-style-type: none"> • 3rd priority (in parallel with a bond issued by Askar Capital, see table in 2.2.3 below) in Avant's portfolio • 1st priority in Glitnir's claim against Milestone, equivalent of 54.9% of total claims against Milestone 	17.67 %
Íslandsbanki	ISK 1.5 billion	various bonds issued by 10 different companies and municipalities	9.30 %
SAT Holding	ISK 11.6 billion	bond issued by Askar Capital and bond issued by Landsvirkjun (the National Power Company) see table in 2.2.3 below	73.03 %

It is clear, however, that the recapitalisation of Sjóvá was not finalised on 20 June 2009, as the assets to be provided by SAT Holding, amounting to some 73% of the new equity, were at that time not owned by SAT Holding but by the State. The transaction was later finalised when the State decided to undertake the measures described below.

2.2.3 Description of the intervention by the State

On 27 June 2009 a meeting was held in the Ministry of Finance on the ongoing work on financial restructuring of Sjóvá¹². This meeting was followed by an agreement dated 8 July 2009 on the transfer of bonds¹³ ("Samningur um kröfukaup") owned by the Icelandic State to SAT Holding.

At this point Sjóvá's equity was 13.5 billion ISK in the negative. A minimum positive equity of 2 billion ISK was required according to law. In order to fulfil the minimum equity requirements, a capital injection of at least 15.5 billion ISK was therefore required.

¹² According to an FME memorandum dated 29 June 2009, the meeting took place on Saturday 27 June 2009. The Prime Minister and the Minister of Finance took part in the meeting together with their assistants. Other participants were the Chairman of the Board of Directors of FME and the two FME officials who wrote the memorandum. The Authority has no information concerning the extent to which the State had been involved before this date other than the presentation given to the Ministry of Finance in April 2009. Yet the FME memorandum refers to a close cooperation between Glitnir, Íslandsbanki and the Ministry of Finance and refers to a memorandum from the Minister of Finance dated 26 June 2009 and a memorandum dated 27 June 2009 on the insurance company. The Authority has not received these memoranda.

¹³ For the purpose of this decision, the assets transferred to SAT Holding by the State will be referred to as bonds.

The agreement between the State and SAT Holding covers the following two bonds that were in the possession of the State, valued by an external expert on 16 June 2009¹⁴:

Asset	Estimated value	Description and securities
Claim against Askar Capital	6 071 443 539 ISK	An indexed loan agreement with 3% interest. The loan had come into the possession of the State when it took over Central Bank collateral in 2008. The loan is secured by: <ul style="list-style-type: none"> • 3rd priority collateral in Avant's¹⁵ portfolio (in parallel with a bond issued by Avant to Glitnir, see table in 2.2.2 above, book value of the portfolio was 26 bn ISK and Landsbanki Íslands' 1st priority lien 16 bn ISK), and • 1st priority collateral in indexed bonds issued by Landsvirkjun (the National Power Company) of nominal value 4.7 billion ISK.
Bond issued by Landsvirkjun (the National Power Company)	5 558 479 575 ISK	Issued in 2005 payable in 2020, with state guarantee, indexed and 3% interest. The bond came into the possession of the State as collateral against lending made by the Central Bank to Landsbanki Íslands.

The purchase price was 11.6 billion ISK and SAT Holding was to pay for the bonds within 18 months, *i.e.* before year-end 2010, and no interest was to be charged during that period. In other words, the State granted a period of grace of 18 months.

As a security for the payment of the purchase price of the bonds, the State was granted 1st priority collateral in SAT Holding's shares in Sjóvá.

The agreement provided for the option of payment by the delivery of SAT Holding's original 73.03% shareholding in Sjóvá to the State, which would be considered payment in full. SAT Holding could exercise this option without prior consent of the State.

2.2.4 *Glitnir sells its shares in Sjóvá to its subsidiary SAT Holding*

The FME considered that Glitnir, in moratorium and undergoing winding-up proceedings, was not eligible to own a qualifying holding in Sjóvá. Subsequently, on 16 September 2009, Glitnir sold its 17.67% shareholding in Sjóvá to Glitnir's subsidiary, SAT Holding.

Following the above transaction, shareholders in Sjóvá were:

Company	Ownership (%)
Íslandsbanki	9.30%
SAT Holding	90.70%

¹⁴ The Icelandic authorities have not yet provided the Authority with a copy of the valuation, referred to in the agreement.

¹⁵ See footnote 4 above.

On 22 September 2009, the FME finally issued an insurance operation licence to Sjóvá and lifted the special supervision Sjóvá had been under since October 2008. The portfolio transfer appears to have taken place on 1 October 2009.

2.2.5 *The State becomes Sjóvá's biggest shareholder through an option exercised by SAT Holding*

At year-end 2009, the management of claims owned by the Ministry of Finance and the Central Bank of Iceland (CBI) was merged, and transferred to a new entity; CBI asset management (ESI). From that time, ESI took over management of the claims.

On 3 May 2010, SAT Holding exercised the option to transfer 73.03% of shares in Sjóvá to the State in lieu of repaying the debt. From that point in time, shareholders in Sjóvá are:

Company	Ownership (%)
Íslandsbanki	9.30%
SAT Holding	17.67%
ESI (the State)	73.03%

3 Position of the Icelandic authorities

The Icelandic authorities are of the view that the Icelandic state has behaved as a private market investor/creditor when contributing to the rescue of Sjóvá. They claim that the State's decision was taken following commitments by Glitnir and Íslandsbanki to contribute equity to Sjóvá amounting to 2.8 billion ISK and 1.5 billion ISK, respectively, or a total of 4.4 billion ISK, which they consider to be a substantial private investor participation amounting to 28% of the total recapitalisation of Sjóvá.

Furthermore, the Icelandic authorities submit that the assets provided by the State were collateral that it had obtained against loans made to Landsbanki Íslands, and: *“As such the assets were rooted in the collapse of the financial system and there was no new capital to be contributed as equity.”* The Icelandic authorities further claim that: *“Given how the claims against Askar and Landsvirkjun came into the possession of the State, and the conditions for release of such claims on the current market, by its use in the restructuring of Sjóvá, the State was acting in the same capacity and under the same conditions as a private investor. The use of the assets in question was consistent with the conduct of a private investor, endeavouring to put assets to use under prevailing market uncertainties.”*

In the Icelandic authorities' opinion, the measures undertaken by Glitnir, Íslandsbanki and the Icelandic State were an attempt to prevent a serious disruption and loss for the Icelandic economy, which would have resulted from the bankruptcy of Sjóvá.

With reference to Article 61(3)(b) and (c) of the EEA Agreement, the Icelandic authorities have furthermore submitted, should the Authority consider that the state participation in the recapitalisation of Sjóvá contained elements of state aid, that the measures are compatible with the functioning of the Agreement. They claim that the grant of aid was an emergency measure to save a financial institution whose bankruptcy would have had

“immense spill-over effects for insurance markets as well as the economy as a whole, and [was] likely to result in economic losses for the state“. Furthermore the Icelandic authorities claim that the intervention was based on the implementation of a restructuring plan suitable to restore the long-term viability of Sjóvá.

II. ASSESSMENT

1 The recipients of the potential aid

With transfer of bonds issued by Landsvirkjun and Askar Capital, Sjóvá and SAT Holding benefitted from a capital contribution from the State.

2 The market economy investor principle

As described above, the State provided a capital contribution to Sjóvá through a transfer of bonds (issued by Landsvirkjun and Askar Capital). This capital contribution was channelled through Glitnir’s subsidiary, SAT Holding, as the bonds first were transferred to SAT Holding, which subsequently used them as an equity contribution in Sjóvá.

If the transaction was carried out in accordance with the market economy investor principle, i.e., if the State transferred the bonds to SAT Holding on conditions that would have been acceptable for a private seller, the transaction would not involve the grant of state aid.

Considering that Glitnir Bank and Íslandsbanki approached the State after having “*exhausted alternative market solutions to rescue the insurance operations of Sjóvá*”, it was clear that corresponding market solutions were not available for Sjóvá to obtain necessary recapitalisation.

The conditions under which the bonds were transferred; payment in 18 months without interests or, alternatively, transfer of 73.03% shareholding in Sjóvá, do not in the Authority’s preliminary view correspond to what would normally have been available on the market. The Authority recalls that at the time of the agreement, in July 2009, Iceland was undergoing a severe financial crisis. Companies in Iceland were not able to raise capital on the market. Neither SAT Holding, a subsidiary of a bank under winding-up procedure, nor a company that was in as severe financial difficulties as Sjóvá was, would have been able to raise the necessary funding on the market under the conditions the State agreed to. In principle, it is very difficult to apply the market economy investor principle to companies in difficulties¹⁶. The Icelandic authorities have themselves acknowledged that Sjóvá was in severe financial difficulties. The company was short of 15.5 billion ISK that was required to comply with regulatory requirements of minimum equity.

Regarding the investment in new equity in Sjóvá, the Icelandic authorities have argued that there was a substantial private participation in the recapitalisation of the company, the private investors in this case being Glitnir Bank (through SAT Holding) and Íslandsbanki. However, it shall be noted first of all that at the time of conclusion of the asset transfer

¹⁶ See the Authority’s guidelines on aid for rescuing and restructuring firms in difficulty. See amongst others, Commission Decision C 4/10 (ex NN 64/09) – France, aid in favour of Trèves.

agreement on 20 June 2009 and the agreement on the transfer of bonds on 8 July 2009, Íslandsbanki was fully state-owned¹⁷. Furthermore, it is the Authority's understanding that Glitnir and Íslandsbanki were among the main creditors of Sjóvá. The State was not as such a creditor of Sjóvá. The State was not acting to protect its own assets, as it was not among the company's creditors¹⁸. Therefore the actions of the State in those circumstances cannot be compared with a private market investor or creditor seeking settlement of outstanding claims. Even in cases with an apparently genuine private investor behaviour from the State, the Commission has taken the view that the circumstances surrounding the financial crisis are so unusual that in general the market investor principle cannot be applied¹⁹.

For these reasons, the Authority preliminarily concludes that the market economy investor principle cannot be applied to the State's transfer of bonds for the recapitalisation of Sjóvá.

3 The presence of state aid

Article 61(1) of the EEA Agreement reads as follows:

“Save as otherwise provided in this Agreement, any aid granted by EC Member States, EFTA States or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Contracting Parties, be incompatible with the functioning of this Agreement.”

3.1 Presence of state resources

In this case the State contributed to the recapitalisation of Sjóvá by transferring to SAT Holding two bonds in its possession valued by an external expert to 11.6 billion ISK (approx. €76 million) with a period of grace, to be used as equity in Sjóvá. State resources were thus involved.

3.2 Favouring certain undertakings or the production of certain goods

Firstly, to constitute state aid, a measure must confer advantages that relieve undertakings of charges that are normally borne from their budgets. Secondly, the measure must be selective in that it favours *“certain undertakings or the production of certain goods”*.

According to the agreement dated 8 July 2009, described above under I.2.2.3, SAT Holding was granted a period of grace of 18 months and could pay the State for those bonds without being charged any interests for the delayed payment. More significantly,

¹⁷ The change of ownership of Íslandsbanki took place on 13 October 2009, when the Glitnir Resolution Committee decided, on behalf of its creditors, to exercise the option provided for in its agreement with the Icelandic State and take over 95% of share capital in Íslandsbanki.

¹⁸ It should be noted that both a press release issued by the Resolution Committee of Glitnir on 8 July 2009 (www.glitnirbank.com) and a press release published by Sjóvá on the same day (www.sjova.is) explicitly state that the State was protecting its own claims against Sjóvá: *“With its participation, the government intends to protect the state's claims against Sjóvá, as well as the interests of a large number of insurance customers”*. However, in an email which the Icelandic authorities sent to the Authority on 25 March 2010 (Event 551375) it was clarified that the Icelandic State never had any claims against Sjóvá, but only against Askar Capital.

¹⁹ See *inter alia* Commission Decision N 69/09 Sweden - Recapitalisation scheme for fundamentally sound banks.

the agreement provided for the option of payment by the transfer of SAT Holding's 73.03% shareholding in Sjóvá to the State. Prior consent of the seller was not required to exercise this option.

Furthermore, the provisions of the agreement are such that it is not only an agreement on transfer of the bonds but ultimately an agreement that the State would inject new equity to Sjóvá amounting to the value of the bonds sold, as SAT Holding could exercise the option at any time. Intervention by the State in Sjóvá's recapitalisation in July 2009 must therefore also be viewed as a decision by the State to inject new equity to Sjóvá and become its biggest shareholder.

It is the Authority's understanding that alternative funding could not have been obtained from the market. Therefore, on the basis of the information at its disposal, the Authority considers that the State's participation in the recapitalisation of Sjóvá through the transfer of bonds involved an advantage within the meaning of Article 61(1) of the EEA Agreement to the extent it made financing available and/or it reduced the financial costs for SAT Holding as well as Sjóvá.

The Authority's view is reinforced by the fact that public policy considerations, taken together with the needs of Sjóvá, appear to have determined the State intervention, rather than the possible return for the State as an investor.

A further potential state aid measure could arise, according to the information currently available to the Authority. The presentation document prepared by Íslandsbanki in April 2009 and described above under I.2.2.2 contains Glitnir's proposal to "close the gap" in Sjóvá by, as the first step, requesting the Ministry of Finance to accept that Glitnir's security in the loan to Avant will be upgraded to 2nd priority. According to the document, this was considered necessary for the FME to accept Glitnir's contribution to Sjóvá's equity. However, this appears to contradict other information from the Icelandic authorities and Sjóvá's Articles of Association dated 20 June 2009 (see I.2.2.2 above), which refer to 3rd parallel security in Avant portfolio for both Glitnir's and the State's claims. Consequently, the Icelandic authorities are invited to clarify whether and how Glitnir's proposal regarding the upgrade of its claim against Avant was actually enforced. If that was not the case, it should be clarified whether FME's acceptance of Glitnir's claim on Avant as an equity contribution to Sjóvá was based on different securities. The Icelandic authorities are also invited to submit any relevant information on other issues considered relevant for the assessment of this case.

3.3 Distortion of competition and effect on trade between the Contracting Parties

The measures under assessment involve undertakings active on markets where there is competition and trade between parties in EEA States. The measures are therefore likely to distort competition and affect trade between the Contracting Parties.

3.4 Conclusion on the presence of state aid

Based on the above, the Authority has come to the preliminary conclusion that the State's contribution to the recapitalisation of Sjóvá through the transfer of bonds involves state aid within the meaning of Article 61(1) of the EEA Agreement.

4 Procedural requirements

The Icelandic authorities did not notify the state intervention to the Authority. The Authority therefore is of the preliminary view that the Icelandic authorities have not respected their obligations pursuant to Article 1(3) of Part I of Protocol 3.

5 Compatibility of the aid

The Icelandic authorities have submitted that their intervention, if considered to be state aid, complies with Article 61(3)(b) of the EEA Agreement as well as to the exemption in Article 61(3)(c) and the Authority's Guidelines on aid for rescuing and restructuring firms in difficulty, which are based on the latter exemption. They consider that the measures are "*appropriate, as they are targeted and well designed to ensure Sjóvá's swift return to viability by the exit of all non-core business pursued by its predecessor...*" The Icelandic authorities have asserted that the financial restructuring of Sjóvá has already been completed. They argue that the company's financial difficulties were brought about by its involvement in non-insurance related activities such as investment operations. These activities will not be pursued by the new, restructured company, which will focus on insurance operations. However, the Icelandic authorities did not notify the capital contribution and they did not provide a restructuring plan for the company. Thus, the Authority is not in the position to assess the measure under the Guidelines on aid for rescuing and restructuring firms in difficulty.

The Icelandic authorities have submitted that Sjóvá was in serious financial difficulties at the time of the state intervention. The Authority does not doubt that and understands that these difficulties were linked to those of the Milestone/Moderna Finance group. While state aid to undertakings in difficulties is normally assessed under Article 61(3)(c) of the EEA Agreement, the Authority may, under Article 61(3)(b) of the Agreement allow state aid "*to remedy a serious disturbance in the economy of an EC Member State or an EFTA State*".

Historically, it is clear from case law that the exemption in Article 61(3)(b) of the EEA Agreement needs to be applied restrictively²⁰. However, following the onset of the global financial crisis in the autumn of 2008, EU governments have made available unprecedented amounts in state aid through a combination of national schemes and ad hoc interventions in financial institutions²¹. This aid was assessed under a set of temporary guidelines regarding the financial crisis²², adopted by the European Commission, and subsequently by the Authority:

²⁰ Case law stresses that the exemption needs to be applied restrictively and must tackle a disturbance in the entire economy of a Member State (and not a sector or a region), cf. Joined Cases T-132/96 and T-143/96 *Freistaat Sachsen and Volkswagen AG Commission* [1999] ECR II-3663, p. 167. Followed in Commission Decision in case C- 47/1996 *Crédit Lyonnais*, OJ 1998 L 221/28, point 10.1, Commission Decision in case C 28/2002 *Bankgesellschaft Berlin*, OJ 2005 L 116, page 1, points 153 et seq and Commission Decision in Case C 50/2006 *BAWAG*, point 166. See Commission Decision of 5 December 2007 in Case NN 70/2007, *Northern Rock*, OJ C 43 of 16.2.2008, p. 1, Commission Decision 30 April 2008 in Case NN 25/2008, *Rescue aid to WestLB*, OJ C 189 of 26.7.2008, p. 3, Commission Decision of 4 June 2008 in Case C 9/2008 *SachsenLB*, OJ C 71 of 18.3.2008, p.14.

²¹ Between October 2008 and April 2010, EU governments made available €4.131 trillion in crisis aid through a combination of national schemes and ad hoc interventions – an amount equivalent to 32.5% of EU-27 GDP, see State Aid Scoreboard, Table 1 and Annex 3. The figure only includes aid to financial services sector, not general aid measures designed to stimulate the "real" economy.

²² Here, referred to together as the "financial crisis guidelines".

- the Banking Guidelines (“on the application of state aid rules to measures taken in relation to financial institutions”) adopted by the Authority 29 January 2009;
- the Recapitalisation Guidelines (“on the recapitalisation of financial institutions in the current financial crisis”) adopted by the Authority on 29 January 2009;
- the Impaired Assets Guidelines (“the Treatment of Impaired Assets in the EEA Banking Sector”) adopted by the Authority on 22 April 2009; and
- the Restructuring Guidelines (“the return to viability and the assessment of restructuring in the financial sector in the current crisis under the State aid rules”) adopted by the Authority 25 November 2009²³.

It remains to be determined in the course of the investigation initiated by this decision whether and to what extent guidelines based on Article 61(3)(b) of the EEA Agreement in relation to the financial crisis are relevant in the case of an ailing insurance company such as Sjóvá. The Icelandic authorities have not put forward any information specific to this case to substantiate their view that the measure should be assessed as a measure to remedy a serious disturbance in the economy. They have limited their reasoning to referring to the widely documented and evidenced effects of the financial difficulties of Iceland, and referred to an assessment of the FME on the grave consequences of not rescuing the insurance part of Sjóvá, without this assessment being provided to the Authority.

The Icelandic authorities have not submitted information to demonstrate that the systemic effects that might have resulted from a bankruptcy of Sjóvá could have reached a size constituting “a serious disturbance in the economy” of Iceland within the meaning of Article 61(3)(b) of the EEA Agreement. Limited information has been submitted regarding the operations of Sjóvá; on the causes of the difficulties and the restructuring itself. This information is not sufficient to enable the Authority to assess the measure under Article 61(3)(b) and the financial crisis guidelines.

In the case at hand, neither an exemption under Article 61(3)(b) nor (c) of the EEA Agreement, and application of the relevant guidelines based on these provisions, can be excluded at this stage. However, the information provided by the Icelandic authorities so far is too limited to allow the Authority to assess whether the measure would be compatible under these exemptions.

Based on the above, the Authority is not in a position to establish whether the State participation in recapitalising Sjóvá involves measures that can be approved under Article 61(3)(b) or (c) of the EEA Agreement.

With reference to the considerations above, the Authority invites the Icelandic authorities to submit any information and documentation relevant to determine whether the aid in question can be assessed on the basis of Article 61(3)(b) and the financial crisis guidelines or Article 61(3)(c) and the Guidelines on aid for rescuing and restructuring firms in difficulty.

²³ The full text of the Guidelines can be found at <http://www.eftasurv.int/state-aid/legal-framework/state-aid-guidelines/>

6 Conclusion

Based on the information submitted by the Icelandic authorities, the Authority has come to the preliminary conclusion that the Icelandic State's participation in the recapitalisation of the insurance company Sjóvá constitute aid within the meaning of Article 61(1) of the EEA Agreement. Furthermore, the Authority has doubts as to whether these measures comply with Article 61(3) of the EEA Agreement, in conjunction with the requirements laid down in the financial crisis guidelines and the Rescue and restructuring aid guidelines. The Authority, therefore, has doubts as to whether the above measures are compatible with the functioning of the EEA Agreement.

Consequently, and in accordance Article 4(4) of Part II of Protocol 3, the Authority is obliged to open the formal investigation procedure provided for in Article 1(2) of Part I of Protocol 3. The decision to open a formal investigation procedure is without prejudice to the final decision of the Authority, which may conclude that the measures in question are compatible with the functioning of the EEA Agreement.

In light of the foregoing considerations, the Authority, acting under the procedure laid down in Article 1(2) of Part I of Protocol 3, invites the Icelandic authorities to submit their comments, as well as all documents, information and data needed for assessment of the compatibility of the state participation in the recapitalisation in Sjóvá, within one month of the date of receipt of this Decision.

In light of the foregoing considerations, within one month of receipt of this decision, the Authority request the Icelandic authorities to provide all documents, information and data needed for assessment of the compatibility of the state intervention in Sjóvá.

The Authority requests the Icelandic authorities to immediately forward a copy of this decision to the potential recipients of the aid.

The Authority must remind the Icelandic authorities that, according to Article 14 of Part II of Protocol 3, any incompatible aid unlawfully granted to the beneficiaries will have to be recovered, unless, exceptionally, such recovery would be contrary to a general principle of EEA law.

HAS ADOPTED THIS DECISION:

Article 1

The formal investigation procedure provided for in Article 1(2) of Part I of Protocol 3 is opened into the participation of the Icelandic State in the recapitalisation of Sjóvá insurance company.

Article 2

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

Article 3

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

Article 4

This Decision is addressed to the Republic of Iceland.

Article 5

Only the English language version of this decision is authentic.

Decision made in Brussels, on 22 September 2010

For the EFTA Surveillance Authority

Per Sanderud
President

Sverrir Haukur Gunnlaugsson
College Member