

Case No: 77755
Doc. No: 755918
Decision No.: 061/16/COL

The logo of the EFTA Surveillance Authority, featuring the text "EFTA SURVEILLANCE AUTHORITY" in white on a dark blue background.

EFTA SURVEILLANCE AUTHORITY DECISION

of 16 March 2016

to close the formal investigation into alleged state aid through the lease of an optical fibre
previously operated on behalf of NATO

(Iceland)

The EFTA Surveillance Authority (“the Authority”),

HAVING REGARD to the Agreement on the European Economic Area (“the EEA Agreement”), in particular to Article 61 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 of Part I and Article 7(2) of Part II,

HAVING called on interested parties to submit their comments pursuant to those provisions,¹ and having regard to their comments,

Whereas:

I. FACTS

1. Procedure

- (1) By letter dated 16 July 2010 (Document No. 565828), Míla ehf. (hereinafter referred to as “Míla” or “the complainant”) submitted a complaint to the EFTA Surveillance Authority (“the Authority”) concerning alleged unlawful state aid granted by the Ministry for Foreign Affairs in Iceland through leases for the use and operation of two optical fibres, which were previously operated on behalf of the North Atlantic Treaty Organisation (“NATO”). Following its investigation, the Authority adopted Decision No. 410/12/COL on 21 November 2012 concluding that the lease by the Defence Agency of the Ministry for Foreign Affairs in Iceland with Og fjarskipti hf. (currently Fjarskipti hf., but hereinafter referred to as “Vodafone Iceland”

¹ Decision No. 299/14/COL of 16 July 2014 to initiate the formal investigation procedure into potential aid through the lease of an optical fibre previously operated on behalf of NATO, published in OJ C 366, 16.10.2014, p. 4.

or “Vodafone”)² of 1 February 2010 for the use and operation of an optical fibre did not involve state aid within the meaning of Article 61 of the EEA Agreement.³

- (2) On 19 February 2013, Míla lodged an application to the EFTA Court for the annulment of Decision No. 410/12/COL. By its judgment of 27 January 2014 in Case E-1/13, the EFTA Court annulled the Authority’s Decision.⁴
- (3) On 14 July 2014, the Authority adopted Decision No. 299/14/COL to initiate the formal investigation procedure provided for in Article 1(2) of Part I of Protocol 3 and invited the Icelandic authorities as well as interested parties to provide comments.
- (4) The Authority received comments by the Icelandic authorities (Documents No. 722921-722923) as well as third party comments by Míla (Document No. 729699), Vodafone (Document No. 723556) and a private individual (Document No. 729917). The third party comments were forwarded to the Icelandic authorities, who provided comments on them (Documents No. 744468-744471 and 753302-753303).

2. Description of the measure

2.1 Background – Invitation to tender for the lease of two optical fibres operated on behalf of NATO

- (5) On 15 August 2007, the Icelandic Government fully took over the operation of the Radar Agency (*Ratsjárstofnun*)⁵, which had until that time been operated under the auspices of the US authorities. The Radar Agency had previously operated three optical fibres in the approximately 1 850 km long, eight-fibre optical cable circling Iceland and its North-West region.⁶ This opened up opportunities for the Icelandic Government to put one or more of the three fibres to other use.
- (6) The Icelandic authorities decided to use one of the fibres for the Icelandic Air Defence System (“IADS”) and for secure governmental telecommunications. The authorities further decided that the State Trading Centre (*Ríkiskaup*) should carry out a tender award procedure for the use and operation of the other two fibres.⁷

² Vodafone Iceland (Fjarskipti hf.) is an Icelandic telecommunications company, providing fixed telephony, mobile and data transmission services in Iceland. Vodafone is currently the second largest telecom operator in Iceland, following the incumbent Skipti hf. and its subsidiaries Síminn and Míla. The company carries the Vodafone brand and trademark. However, the Vodafone Group owns no interest in the company, but rather franchises the brand and associated advertising styles to Fjarskipti. Fjarskipti was previously owned by the Icelandic Teymi Group. The Teymi Group was later split up, and Fjarskipti went through a financial restructuring process. In December 2012, Fjarskipti was listed on the Icelandic Stock Exchange.

³ For a detailed description of the investigation and the background to the case, see Decision No. 299/14/COL to initiate the formal investigation procedure.

⁴ Case E-1/13 *Míla ehf. v EFTA Surveillance Authority* [2014] EFTA Ct. Rep. 4.

⁵ With the entry into force of the Defence Act No. 34/2008 on 31 May 2008, the Radar Agency was closed. Certain functions of the Radar Agency were taken over by the Defence Agency (*Varnarmálastofnun*). By Act No. 98/2010, amending the Defence Act, the Defence Agency was closed on 1 January 2011 and certain functions taken over by other State agencies, including the Ministry for Foreign Affairs.

⁶ The remaining five fibres are the property of Míla, the complainant.

⁷ The Icelandic public procurement rules are laid down in Act No 84/2007. That Act implements the EU Public Procurement Directive into Icelandic law, i.e. Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts (OJ L 134, 30.4.2004, p. 114), incorporated as point 2 of Annex XVI

- (7) The details of the invitation to tender were set out in the project description drafted by Ríkiskaup.⁸ According to that document, Ríkiskaup, on behalf of the Defence Department of the Ministry for Foreign Affairs, invited tenders for the use and operation of two of the three optical fibres to be leased out to two unrelated parties, with the intention of negotiating a lease for the duration of ten years.
- (8) According to the tender, the optical cable is about 1 850 km in length, lies intact between the present 16 termination points (as of the date of the tender) and goes through telephone exchanges and other telecommunication installations on its way circling Iceland. Telephone exchanges and other telecommunications installations are, for the most part, owned by and under the supervision of Míla. According to point 2.3 of the tender, the proposed lease will not include any facilities for equipment of the lessee. The lessee will be responsible for obtaining necessary facilities for its equipment or any other facilities needed to use the fibres. The lessee is thus responsible for securing access to facilities and the termination points where it intends to connect its equipment to the fibre. In case the lessee needs to acquire or rent facilities for its equipment, additional connections or other items, the lessee will bear the costs. The lessee is responsible for all communications with the owners of facilities, the lessor being neither an intermediary nor the provider of facilities of any kind nor will the lessor guarantee that the lessee will have access to facilities at assembly points or elsewhere. The lessee may add new termination points to the optical fibre, but this must be done in consultation with the lessor and other co-owners of the fibre. The lessee will bear any costs associated with the adding of new termination points. Detailed requirements are set to secure that any access to the cable by the lessee and the addition of termination points are carefully prepared and executed in a professional manner so as to secure uninterrupted use of the cable by others.
- (9) As concerns the rental charge, the invitation to tender sets a minimum rental charge of ISK 19 000 000 per year for each fibre to ensure that the cost of operation and maintenance of the optical fibres would be covered.⁹ The closing date for submitting offers and for opening of offers was 19 June 2008.
- (10) The assessment of offers was based on the following criteria:

Matter of Judgment	Percentage points
Stimulation of Competition	40
Rental Charge	15
Commencement of Services	10
Supply of Services	10
Number of network termination points	15
One Tariff throughout the Country	10

Table 1: Award criteria in the tender.

- (11) The outcome of the tender was that five offers were received from four independent undertakings, as summarised in Table 2 below. Two of the offers were variant offers:

to the EEA Agreement by Joint Committee Decision No. 68/2006 (OJ L 245, 7.9.2006, p. 22 and the EEA Supplement No 44, 7.9.2006, p. 18), e.i.f. 18.4.2007.

⁸ Project No. 14477: Optical Fibres. Ministry for Foreign Affairs, April 2008 (Document No. 669632).

⁹ Point 1.2.4 of the description of Project No. 14477.

Name of company	Leasing price offered	Award criteria: total points scored	
		Main offer	Variant offer ¹⁰
Fjarski ehf.	ISK 20 000 000	92.18	
Vodafone	ISK 19 150 000	89.67	84.67
Hringiðan ehf.	ISK 24 006 900	88.60	
Gagnaveita Reykjavíkur	ISK 19 500 000		59.34

Table 2: Offers received in the tender.

- (12) The evaluation of received offers was made by Ríkiskaup, following an assessment conducted by the independent consulting firm *Mannvit*. According to information from Ríkiskaup and Mannvit, all four companies submitting bids were found to have met the required technical capacity to perform the project, as well as the general requirements set out in the invitation to tender regarding the personal and financial situation of the candidates for the project. However, Mannvit made a reservation regarding the proposal from Hringiðan. According to that proposal, the project was to be performed by an undertaking to be founded by Hringiðan. Mannvit did not consider it possible to assess the capacity – both financial and technical – of this undertaking, which at the time had not been established. According to the terms of the tender, Hringiðan’s offer could therefore be excluded. Mannvit simulated the effect of an exclusion of Hringiðan’s offer on the result of the tender, but found that there was no impact as Hringiðan’s offer was not amongst the top two bids and was therefore in any event unsuccessful.
- (13) As set out in Table 1, the two companies scoring the highest on the basis of the award criteria were Fjarski ehf. (92.18 points) and Vodafone (89.67 points). Negotiations were entered into with those two companies. Due to the financial crisis in Iceland, which began to take hold in the fall of 2008, negotiations did not take place until late 2009 and were subsequently finalised early 2010. Fjarski ehf., however, decided to pull out of the project. A lease contract was therefore negotiated with Vodafone and for only one of the two fibres.

2.2 Contract between the Icelandic Defence Agency and Vodafone

- (14) The contract, concluded on 1 February 2010 between Vodafone and the Icelandic Defence Agency (“*Varnarmálastofnun*”), provides for the use of an optical fibre belonging to the eight-fibre, about 1 850 km long optical cable circling Iceland. The annual lease is set at ISK 19 150 000 (excluding VAT), indexed according to the building cost index as from June 2008. The term of the contract is ten years.
- (15) The contract states that the fibre at issue was registered on NATO’s inventory list. Under Article 16 of the Defence Act No. 34/2008, the lessor was entitled, on behalf of the State and of NATO, to conclude a lease for the use of such facilities. However, in view of Iceland’s

¹⁰ The proposal from Gagnaveita Reykjavíkur was classified as a variant offer, as it did not meet the minimum number of network termination points and the number of municipalities covered. One of the two offers from Vodafone is also a variant offer, as it does not foresee that Vodafone will use the same tariff throughout Iceland. Other items in the offers from Vodafone are the same, including the leasing price to be paid to the State.

international commitments, it was necessary to include a clause authorising the lessor to take over the cited facilities without notice in times of war. Provisions to this effect are found in Article 8 of the contract.

- (16) The contract repeats the provision of the tender that it does not include any facilities for equipment of the lessee. The lessee will be responsible for obtaining necessary facilities for its equipment or any other facilities needed to be able to use the fibres. The lessee is thus responsible for securing access to facilities and the assembly points where it intends to connect its equipment to the fibre. In case the lessee needs to acquire or rent facilities for its equipment, additional connections or other items, the lessee will bear the costs. The lessee is responsible for all communications with the owners of the cable or facilities.

3. The complaint

- (17) Míla's complaint relates to the contract referred to above, concluded on the basis of the tender on 1 February 2010 between the Icelandic Defence Agency and the telecommunication operator Vodafone. The complainant claims that the awarded contract involves state aid in the form of a rent for the use of the optical fibre at a level significantly below what a market investor would have considered to be acceptable.
- (18) In support of this contention, Míla essentially argued as follows:¹¹
- At the time of the tender, Míla was the only party operating in the market and was therefore by definition unable to acquire 40% of the points used in the award criteria, i.e. the points awarded for stimulation of competition. Accordingly, the method of evaluation of the submitted tenders, as summarised in Table 1, effectively excluded Míla from the tender. However, Míla did not have any economic motive for taking part in the tender as it already had sufficient transmission capacity in its own fibres. It did therefore not submit any bid.
 - The rental prices offered in the tender were below what a market investor would have deemed an acceptable rent. In particular, these prices did not provide an appropriate contribution to fixed costs (*i.e.* the costs of construction, renewal and depreciation of the cable) and an adequate return on the capital investment for the Icelandic state as the owner of the fibres.
 - Míla estimated the market price for the lease right at over ISK 85 million per year, resulting in an alleged total aid amount of ISK 464.2 million over the estimated twenty year lifetime of the fibre to each of the two companies, based on a rental price of ISK 19.15 - 20 million per year.¹²
- (19) By letter dated 19 September 2012, the complainant submitted further information regarding its allegation of state aid to Vodafone. The complainant notably drew attention to a new tariff

¹¹ A more detailed description of the complaint can be found in Decision No. 299/14/COL.

¹² The complainant's assessment of the aid amount is based on a memorandum annexed to the complaint, containing Míla's calculations of the value of the alleged subsidy. The calculations are based on Míla's own costs of operating fibres in the same cable.

by the undertaking *Orkufjarskipti*¹³ for the rent of a fibre optic cable.¹⁴ The tariff specifies the rent for each fibre in a six-fibre optical cable in terms of monthly rent in ISK per kilometre in the cable.¹⁵ By multiplying the tariff with the length of the cable, according to the lease with Vodafone, about 1 850 km, the complainant concludes that the rent for a fibre of that length according to the tariff should be ISK 107 137 200 per year.

4. Position of the Icelandic authorities regarding the complaint

- (20) In response to the complaint, the Icelandic authorities submitted that the leasing out of the NATO optical fibres does not constitute state aid, as the award of the contract does not confer any economic advantage upon the lessee which goes beyond market conditions, does not entail the use of state resources, and does not distort or threaten to distort competition.
- (21) In this regard the Icelandic authorities refer to a Memorandum of the Ministry for Foreign Affairs, dated 7 May 2008, on the proposed lease-out of NATO optical fibres. The Memorandum explains in general terms the proposed tender procedure, including the modalities of the invitation to tender and the criteria for the selection of eligible lessees from among the bidders. The objectives of the project were to lower the maintenance and operating costs of NATO's optical fibres, to increase public broadband access and to encourage competition in data transmission on the domestic market. The Icelandic authorities consider that the lease-out of the two fibres was a non-aid measure. They further note that the project would benefit the implementation of government policies regarding electronic communication services and information society. It would also make infrastructure competition possible in the leased-lines market in areas where there was no competition at the time, which in turn would lead to more competition in downstream markets such as the market for high-speed broadband connection.
- (22) In view of the complainant's contention that the fibre was owned by the Icelandic State and that the rental price should have included fixed costs related to the construction, renewal and write-down of the cables, the Icelandic authorities provided clarifications on the ownership and costs of construction. They note that it was NATO, and not the Icelandic State, which financed the installation of the cable. Furthermore, the cable was registered on the inventory list of the organisation, and three out of eight fibres were reserved for use related to the operations of the American forces in Iceland. After the departure of the American forces from Iceland in 2006 and 2007, the Icelandic State took over the operation of the three fibres, as a so-called "host-nation, user-nation", on the basis of a written arrangement with NATO. Even though the Icelandic authorities have assumed operational management of the fibres, they remain subject to a number of exclusive NATO rights. The Icelandic State does not own the three fibres. As long as the Defence Agreement between Iceland and the US is in force, the three fibres are the property of NATO. NATO has the priority rights to the use of the fibres. Any rental income from the fibres can only be used for the operation and maintenance of NATO's assets.¹⁶ This

¹³ Orkufjarskipti is jointly owned by Landsvirkjun (the National Power Company) and Landsnet (operator of Iceland's electricity transmission grid). Orkufjarskipti operates and maintains telecommunication infrastructure in Iceland for its owners.

¹⁴ According to the complainant, the tariff entered into force on 1 August 2012, having been reviewed and accepted by the Post and Telecom Authority in Iceland following a regulatory procedure. By accepting the tariff, the Post and Telecom Authority has agreed that the tariff is based on a cost analysis.

¹⁵ The monthly rent per kilometre varies from ISK 4 826 for fibre 1 to ISK 7 507 for fibre 6.

¹⁶ Email of the Ministry for Foreign Affairs to the EFTA Surveillance Authority of 16 November 2012. A more detailed description of these arrangements can be found in Decision No. 299/14/COL.

means in particular that any income in excess of these costs cannot be retained by Iceland but has to be transferred to NATO.

- (23) NATO originally invested in and paid the cost of the installation of the fibre optic cable. The maintenance and operation of the fibres are a part of Iceland's obligations as a member of NATO and are not optional. According to the Icelandic authorities, the complainant is not correct when claiming that since two of the fibres were in active use for the IADS system, the State needed to invest ISK 250 million to make one of the fibres available and free for use by the successful bidder. The intention was initially to lease out two fibres. The cost assessment for making both fibres free for commercial use was ISK 20-65 million. As one of the two successful bidders withdrew its offer, only one fibre needed to be set free. The cost was therefore much lower than initially estimated and well below Vodafone's rent for the fibre. It is recalled that according to point 1.2.4 of the invitation to tender of April 2008, the Icelandic State's cost of operation and maintenance of each of the two fibres to be leased out was estimated at about ISK 19 000 000 per year.¹⁷
- (24) In the opinion of the Icelandic authorities, as a result of the successful call for tenders the measure does not involve any type of state financing. On the contrary, the measures produce revenue for the State from leasing out fibres which the State would otherwise have had to continue to maintain through state resources. Furthermore, the Icelandic authorities point out that the restrictions stemming from the ownership of NATO and NATO's priority of use during war times mean that the price may have been lower than if no such restriction had existed. This factor would have affected all the tenderers in the same way, and the market price had to adjust to that fact.¹⁸
- (25) The Icelandic authorities were of the opinion that neither the application of the award criterion on stimulation of competition nor the alleged effective exclusion of an undertaking holding a monopoly position on the market could, as such, lead to the conclusion that the measure distorts competition or confers an advantage upon an undertaking. According to the Icelandic authorities, the Government was fully authorised to use multiple award criteria. Moreover, the criteria were legitimate and pursued important objectives aimed at enhancing competition and ensuring good services to the general public.
- (26) Finally, the Icelandic authorities submitted that, in the event that the Authority would consider the measure to constitute state aid, such aid could be considered compatible with Article 61(3) of the EEA Agreement, by reference to the objectives of the measure, including the objective of increasing public broadband access in assisted areas. In this regard, the Icelandic authorities also invited the Authority to assess whether such aid should be considered to constitute the financing of services of general economic interest ("SGEI"), as referred to in Chapter 2.2.2 of the Authority's Broadband Guidelines.¹⁹

¹⁷ The maintenance service that the Icelandic State is committed to pay for ensures the functioning of the fibre at all times, i.e. all monitoring and testing, repairs and technical support. However, major repairs of the cable are not included in that commitment. The relevant proportion (3/8) of such costs is claimed from NATO on a case-by-case basis when they occur.

¹⁸ Written observations of the Icelandic Government of 2 July 2013 in Case E-1/13 *Míla ehf. v The EFTA Surveillance Authority*, p. 7.

¹⁹ The reference is to the Authority's broadband guidelines in force at the time when the complaint was submitted. By Decision No. 73/13/COL of 20 February 2013, OJ 8.5.2014 L 135/49, the Authority adopted new broadband guidelines, available at: <http://www.eftasurv.int/state-aid/legal-framework/state-aid-guidelines/>.

5. Decision No. 410/12/COL and the EFTA Court Judgment in Case E-1/13

- (27) On 21 November 2012, the Authority adopted Decision No. 410/12/COL concluding that the measure did not involve state aid within the meaning of Article 61(1) of the EEA Agreement. The Authority considered that the lease for the use and operation of the optical fibre did not involve state aid, as the lease contract was established by means of the use of an open tender capable of establishing market terms and therefore did not confer an economic advantage on Vodafone.
- (28) On 27 January 2014, the EFTA Court annulled the Authority's Decision No. 410/12/COL. The Court concluded that the Authority should have opened a formal investigation procedure, as the Authority had at its disposal information and evidence which should, objectively, have raised doubts or serious difficulties regarding whether the lease agreement conferred an economic advantage on Vodafone.²⁰
- (29) The Court considered that the Authority should have had doubts as to whether the price agreed as a result of the tender was a reflection of a true market price for the lease of such an asset. In particular, the Court held that the award criteria in the tender did not reflect what a private investor would consider relevant when tendering out a lease and that it was apparent that the Authority had not assessed all circumstances and consequences for the applicability of a market economy investor test. The award criteria other than price appeared to reflect public policy or regulatory considerations, which a private investor would not consider relevant. The tender procedure did not use price or leasing charge as a sole or main award criterion. The EFTA Court furthermore considered that the Authority had not assessed the likelihood of NATO using its priority rights to make use of the fibre and the probability that NATO would use its right of reversal.
- (30) On the basis of *inter alia* the above, the Court concluded that there existed consistent and objective evidence that the Authority had not examined in a complete and sufficient manner whether the lease contract involved state aid and, if so, whether the aid was compatible with the EEA Agreement.

6. Decision No. 299/12/COL to initiate the formal investigation procedure

- (31) On 16 July 2014, the Authority decided to initiate the formal investigation procedure into potential state aid granted through the lease of the NATO optical fibre. In its Decision, the Authority stated that based on the information submitted by the complainant and the Icelandic authorities, it could not exclude the possibility that the contract concluded on 1 February 2010 by the Icelandic Defence Agency with Vodafone Iceland might involve state aid within the meaning of Article 61(1) of the EEA Agreement. The Authority further stated that based on the available information it also had doubts as to the compatibility of the potential aid with the functioning of the EEA Agreement.

7. Comments by the Icelandic authorities to the opening decision²¹

- (32) In their reply to the opening of the formal investigation, the Icelandic authorities argue that the case concerns the opening up of a sector previously monopolised by a state-owned enterprise and later, after privatisation and sale, by Míla. The necessary network and infrastructure, i.e.

²⁰ Case E-1/13 *Míla ehf. v EFTA Surveillance Authority* [2014] EFTA Ct. Rep. 4, paragraph 101.

²¹ The comments of the Icelandic authorities summarised in this section are found in Documents No. 722921-722923, 744468-744471 and 753302-753303.

the optical fibre, could not have been realistically duplicated by any of the competitors of Míla. The sector is highly important to the general public and its access to information. The case also concerns access and provision of services to rural and sparsely populated areas in Iceland. The unique characteristics of the case relate to the complex ownership issues and the relevance of restrictions due to the role of the fibre in the defence mechanism and crisis management of Iceland and other members of NATO.

- (33) The main aim of the measures of the Icelandic authorities was to limit public expenditure relating to the operation of the fibre. Otherwise, all steps taken were aimed at contributing to increased competition in the sector. The measures were successful and the general public, as well as private and public entities that rely heavily on telecommunication throughout Iceland, now enjoy more competition and better service. Certain limitations were introduced to promote competition on equal ground, all with the final purpose of ensuring that the general public would receive as good and cheap service as possible.
- (34) The Icelandic authorities reiterate the view expressed previously that the measure does not involve state aid. In addition, they put forward the arguments outlined below.

State resources, the influence of the ownership of the cable and implication for advantage

- (35) While Iceland does not contest that state resources can be deemed to be transferred by other means than direct distribution of state-owned funds by the State itself to other entities, they underline that this must be assessed on a case-by-case basis.
- (36) In this context, the Icelandic authorities request the Authority to consider in particular that the “resource” (i.e. the fibre) is not owned by the Icelandic State or any of its entities. The resource was financed, constructed and is permanently owned by a third party, i.e. NATO. The arrangements between NATO and the Icelandic authorities are based on the no-cost no-gain principle. This means that any proceeds from the leasing of the fibre will first be used to pay for operational costs and minor repairs. Article 16 of the Icelandic Defence Act No 34/2008 reflects this arrangement and further explains that any assets falling under this category are subject to rules of security and priority rights of NATO. Moreover, if revenue exceeds those costs, any remainder is to be returned to the owner of the fibre, NATO. If costs exceed revenue, or in case of major repairs or replacements due to *force majeure* incidents, the Icelandic authorities are not liable for the relevant costs. Rather, the cost of repairs to the cable is shared between the fibres’ owners according to their respective number of fibres, i.e. Míla (5/8) and NATO (3/8). Hence, any private vendor test is not directly applicable to the present case, as the Icelandic authorities have no economic interest in achieving a rental income above the operation and maintenance costs of the fibre.
- (37) The tender documents stipulate that access to the fibre was contingent upon various other issues than the lease and the lease price. According to clause 2.3 it was for the lessee to obtain necessary facilities and assembly points to the fibre. The Icelandic State did not even guarantee that the lessee would have access to such facilities. Furthermore, clause 2.7 stipulated that the lessee shall return the fibre in principle in the same condition as when it received it, but where the lessee has made amendments, the lessors shall acquire such amendments free of charge at the end of the contract period. Access to the fibre had to be negotiated with Míla, which owned the facilities needed to operate the fibre. Eventually, the Icelandic Post and Telecom Administration (“PTA”) issued two rulings instructing Míla, as a dominant market operator, to grant Vodafone access to the connection points for a reasonable fee.

- (38) The Icelandic authorities submit evidence from Vodafone regarding Vodafone's additional costs in obtaining access to the fibre.²² Vodafone's investment costs in equipment, optic trunks and initial fees to Míla amount to ISK 130 million. In addition there are annual license fees for the equipment of ISK 7.5 million. This expenditure comes in addition to the annual rental charge of ISK 19.15 million, which is linked to a price index. Furthermore, Vodafone pays to the Icelandic Coast Guard ("LHG") a monthly fee of ISK 15 000 for each connection point beyond the ones covered in the existing agreement with LHG.
- (39) This demonstrates that the "resources" in this case are not owned by the state, the financial gain of the lease is shared with the real owner according to the no-cost no-gain principle and that the Icelandic authorities did not have authority to grant potential investors full access to the fibre. These facts are important: firstly for the assessment of whether state resources were transferred, secondly when considering the tender procedure and thirdly they affect the commercial drivers for the appropriate lease price. Finally, the facts demonstrate that the comparison between a hypothetical commercial actor on the market and the state is almost impossible, as no market participant could have been in a comparable situation. The NATO restrictions discussed below and the complex ownership and distribution of revenue would be completely alien to a normal market operator.

The NATO restrictions and probabilities of exercise

- (40) The Icelandic authorities submit that the probability of NATO use or revocation may vary during the tenure of the lease agreement and are beyond the control of Iceland or NATO. Nevertheless, the NATO restrictions, by their nature, have a significant and negative impact on the utilisation of the fibre for commercial purposes. The impact on the rental market price is negative, and the Icelandic authorities estimate the negative effect on price at 15-25%. No such restrictions exist as regards the fibres operated by Míla.

The tender process

- (41) The Icelandic authorities maintain that the 2008 tender process qualified as a proper method to establish market price. In particular, given the ownership structure, the restrictions in relation to the NATO defence function and the nature of the asset at stake, no private vendor, having to take into consideration all these relevant factors, would have considered a process in which the only criteria would have been the lease price.
- (42) The Icelandic authorities claim that the six different award criteria of the tender are fully justified and do not agree with the view expressed by the Authority in its opening decision that the criterion of stimulation of competition might be to the disadvantage of the incumbent operator. They note in particular that Míla had no commercial interest in the NATO fibre. Accordingly, any argument by Míla that it could hypothetically have made a higher offer should be disregarded. Any bid by Míla would not have been a good faith commercial offer. The Icelandic authorities argue that they would have had the right to exclude such a bid following the judgment in Case T-244/08 *Konsum Nord v Commission*.²³
- (43) The Icelandic authorities contest the view expressed by the complainant that the setting of a minimum price in the tender had discouraged bidders from competing on prices. A minimum price criterion does not limit competition for price. The bidders would go as high as they deem

²² Letter of Advel law firm of 6 February 2015 to law firm Landslög (Document No. 744468).

²³ Judgment in *Konsum Nord ekonomisk förening v Commission*, T-244/08, EU:T:2011:732.

commercially viable. The removal of the minimum price could only encourage lower bids than were actually obtained in the process and the price range would only increase downwards. The fact that most of the bids were within a narrow price range can only indicate reluctance by the market to go above the minimum price due to commercial reasons.

- (44) The Icelandic authorities highlight that the tender actually contained not only one but two separate price components. Besides the rental price, the bidders were also competing on the number of network termination points they committed to install. Each such termination point requires substantial investments that will not be recovered by the lessee at the end of the lease, but rather increase the value of the NATO fibre.

The expert valuation study by Mannvit

- (45) In paragraph 87 of the Authority's opening Decision No. 410/12/COL, the Icelandic authorities were requested to submit an independent expert evaluation of the market price of the rental charge. It was the initial understanding of the Icelandic authorities that this request was contingent upon the Icelandic authorities withdrawing arguments relating to the tender process and the actual rental charge being an appropriate proxy for such market price. As these arguments were in the view of the Icelandic authorities upheld, no valuation study was included in the initial comments prepared by the Icelandic authorities. However, in response to the third party comments and notably the arguments put forward by Míla regarding the alleged market value of the lease right in question, the Icelandic authorities requested and provided a valuation study by the expert consultant Mannvit.²⁴ Mannvit is an international consultancy firm in the fields of engineering, technical services and innovation, and had already advised the Icelandic authorities on the tender process in the present case.
- (46) As a starting point, Mannvit compares the NATO fibre leased by Vodafone with the offer for the product (trunk leased lines) quoted by Míla in its complaint (see paragraph (56) below for the most recent calculation). Mannvit explains a number of relevant differences:
- Míla's regulated tariff for fibre leased line services only applies to services between existing termination points with existing transmission equipment. The fibre leased by Vodafone, however, required the installation of transmission equipment at 30 locations. Mannvit estimates the average cost of installing this equipment at ISK 4 million per connection point, with a depreciation of 15% per year, an estimated operating expenditure ("Opex") of 20% of capital expenditure ("Capex") and a weighted average cost of capital ("WACC") of 8.5% of Capex.²⁵ In total, Mannvit calculates an annual cost of ISK 52 million for the investments required to make the lease price paid by Vodafone comparable to Míla's offer.
 - Míla's calculation uses as a basis the actual length of the NATO fibre, namely 1 850 km. However, it calculates its own offer on a point-to-point basis, i.e. as a direct lines between the relevant termination points. When applied to the termination points on the NATO fibre at the time of the transaction, this point-to-point method results in a total length of only 1 283 km.

²⁴ Document No. 753303.

²⁵ In deciding these values, Mannvit refers in particular to the cost analysis in the PTA's Decision No. 14/2011, available here (in Icelandic): http://www.pfs.is/upload/files/Ákv_14-2011_M13-14_Leigulínur.pdf.

- Míla's calculation assumes a discount of 15%, which is the maximum Míla can grant under its regulated offer for a contract duration of three years. However, at the time of the lease contract, Míla offered a discount of 25% for customers renting a similar length of fibre. In addition, the duration of 10 years should also result in a higher discount than 15%, which applies to a three-year contract. Mannvit therefore assumes a discount of 25%.
 - Mannvit further questions whether Míla's current regulated tariff (ISK 7 609 per km/month, which entered into force on 1 August 2011) provides a good benchmark to determine the market price. The regulated tariff is set by the PTA based on an analysis of the historic costs of Míla's whole fibre network, including all of Míla's relevant termination points, Míla's operating expenditure in each of these locations, Míla's general utilisation rates, etc. A number of these cost factors do not apply in the context of the NATO fibre at hand, which is much simpler and has fewer connection points. Míla's tariff is thus cost-based and relevant only to Míla's own situation which differs greatly to that of other market operators. Mannvit also points out that at the time of the tender, market participants were not given the opportunity to lease optical fibres from Míla, save in exceptional cases. Those who requested it were simply told that no optical fibres were available. In those circumstances it is not appropriate to refer to the prices of Míla as market prices. Mannvit therefore proposes to rather use the most recent wholesale tariff (ISK 5 020 per km/month, which entered into force on 1 January 2014) of another operator, *Orkufjarskipti*, as the basis for calculating the market price. This operator also provides a 15% discount for three-year contracts.
 - The price estimate provided by Míla, as well as the *Orkufjarskipti* tariff set out above, refer to today's prices. In order to be meaningful, they have to be compared to the rent Vodafone pays today, which amounts to ISK 28 million per year.
- (47) Mannvit thus estimates as a starting point that a market rent for the NATO fibre (before investments) should be calculated based on the point-to-point distance of 1 283 km and *Orkufjarskipti*'s tariff of ISK 5 020 per km/month with a 25% discount, resulting in a value of ISK 57 965 940 per year.
- (48) In order to compare the above value with the rental charge paid by Vodafone, account needs to be taken of the fact that Vodafone was faced with a variety of costs to make the fibre operational and fulfil its obligations under the lease contract. Mannvit estimates these costs as ISK 52 million per year. Added to the rental price paid by Vodafone, which currently is ISK 28 billion per year, this amounts to a total of ISK 80 million per year or well above the price of about ISK 58 million estimated on the basis of the tariff of *Orkufjarskipti*. Mannvit therefore concludes that the rent for leasing the NATO fibre actually exceeds the market value.
- (49) Mannvit did not assess the impact of the restrictions due to the role of the fibre in the defence mechanism and crisis management of Iceland and other members of NATO on the market value. However, the Icelandic authorities estimate that these restrictions might have negatively affected the price by 15-25%.

Compatibility of potential aid

- (50) The Icelandic authorities submit that, in the event the measure is considered to constitute state aid, such aid should be considered compatible with the functioning of the EEA Agreement with reference to Article 59(2) and/or Article 61(3)(c).
- (51) The Icelandic authorities have on previous occasions pointed out that the measure could be considered to constitute the financing of SGEI, in line with the principles enshrined in Chapter 2.2.2 of the Authority's Broadband Guidelines, applicable at the time the measure was assessed.
- (52) The Icelandic authorities also argue that, alternatively, the measure could be declared compatible on the basis of Article 61(3)(c) of the EEA Agreement. They note that the objectives of the measure, including the objective of increasing public broadband access in assisted areas, have previously been demonstrated by the Icelandic authorities to be in the common interest. They propose to apply the principles of the current broadband guidelines, to the measure at issue, and argue that the measure fulfils all the substantive compatibility conditions.

8. Comments by interested parties to the opening decision

8.1 Míla²⁶

- (53) In its comments to the opening decision, Míla reiterates and elaborates on the submissions already made in the complaint and in its application to the EFTA Court.
- (54) On the question of state resources and ownership of the fibre, Míla maintains in principle that the ownership lies with the Icelandic Government. In support of this claim, Míla refers firstly to a report of a special committee for the privatization of the state-owned telecom operator Landssími Íslands hf. (later Síminn hf. and Míla ehf.) from 2001. Secondly, Míla refers to an agreement between the Icelandic Government and Síminn hf. dated 27 March 2001 regarding the ownership, operations and maintenance of the fibres. Míla considers that both documents confirm that the ownership of the fibres rests with the Icelandic Government. However, Míla also states that irrespective of whether the formal ownership of the fibre lies with the Icelandic Government or with NATO, the measure was granted through state resources.
- (55) Míla argues that the procurement for the lease of the fibres failed to establish a market price, allowing Vodafone to pay a leasing price below what it considers to be the market value; as a consequence, Vodafone gets an advantage compared to its competitors. Accordingly, the contract with Vodafone involves state aid.
- (56) Míla also provides an updated estimate of the market price for the NATO fibre. Based on the regulated tariff (in force from 1 August 2011) for access to a single fibre of 7 609 ISK per km/month and a discount of 15% for a contract duration of three years, the market price for a 1 850 km fibre should be ISK 143 589 600 per year.
- (57) As concerns the question of compatibility, Míla submits that the Authority should come to the conclusion that the measure does not meet the relevant criteria set out in the Broadband Guidelines and is therefore not compatible with Article 61(3)(c) of the EEA Agreement.
- (58) As concerns possible compatibility under Article 59(2) of the EEA Agreement as a compensation for SGEI, Míla submits that the EFTA States cannot attach specific public service obligations to services that are already provided by undertakings operating under

²⁶ The comments of Míla summarised in this section can be found in Document No. 729699.

normal market conditions. As Míla was already providing the same fibre service in Iceland from before the time the contract was entered into with Vodafone, the Authority's conclusion should be that the Icelandic Government measure may not be defined as an SGEI. Consequently, state aid may not be provided in the case at hand with reference to Article 59(2) of the EEA Agreement.

8.2 Vodafone²⁷

- (59) Vodafone is primarily of the view that its agreement with the Icelandic authorities does not entail state aid. In any event, the agreement would be in conformity with the *Altmark* principles on SGEI. Second, should an element of aid be identified in the case, Vodafone submits that the exemption provided for in Article 61(3)(c) of the EEA Agreement is applicable.
- (60) As concerns compatibility, Vodafone considers the Broadband Guidelines to be relevant to the assessment of the measure in question. Vodafone underlines that the existence of a network operator in a given area does not necessarily imply that no market failures or cohesion problems exist. To the contrary, the monopoly position of Míla in the relevant market has affected both the quality of service and the price at which services are offered to the citizens. There were limited if any prospects that third parties would build an alternative infrastructure. The leasing of the NATO fibre optic cable was therefore well suited to remedy the absence of infrastructure competition and reduce the current problems arising from the monopoly position of Míla.
- (61) Previous application of regulatory measures had not been successful in providing a level playing field in the market. As a result, competition in the market remained ineffective. It is noted in particular that Míla had been successful in preventing Vodafone's entrance in the relevant market by refusing access to essential facilities.
- (62) The conclusion of the disputed agreement resulted in a significant improvement of competition, mainly in rural areas, and thus increased welfare for consumers. By way of example, in the municipality of *Öræfasveit*, Vodafone was able to provide internet connections in a remote and rural area where the complainant had previously announced that it would not provide any such services.
- (63) The lease agreement was an essential element for Vodafone to build up and start to provide services in this part of the country. Míla had employed stalling tactics by refusing Vodafone access to colocation facilities. Vodafone had to request a formal decision from the PTA on the access issue, which was published on 1 November 2010. As a result of the disputed lease agreement, Vodafone was able to increase wholesale offers to include more than 30 different services.

8.3 Private individual²⁸

- (64) The comments by a private individual set out experiences when working on the introduction of fibre-optic broadband infrastructures in three small and remote municipalities: *Öræfasveit*, *Kirkjubæjarklaustri* and *Mýrdal*. All three systems are linked to Vodafone's operation of the fibre optic cable. When requested, only Vodafone was prepared to engage in providing the services to the inhabitants and companies in those municipalities. Other telecom operators did not respond to the inquiry of the inhabitants. Once the broadband in *Öræfasveit* became a reality, two further municipalities decided to invest in laying a fibre-optic cable to all

²⁷ The comments of Vodafone summarised in this section can be found in Document No. 723556.

²⁸ The comments summarised in this section can be found in Document No. 729917.

inhabitants, i.e. *Skeiða- og gnúpverjahreppur* and *Hvalfjarðarstrandarhreppur*. The private individual is of the view that without Vodafone's lease of the NATO optical fibre, there would have been much less progress in the provision of telecommunication services in remote regions of Iceland.

II. ASSESSMENT

1. The presence of state aid

1.1 Introduction

- (65) In the following chapters, the Authority will assess whether the contract between the Icelandic Defence Agency and Vodafone for the lease by the latter of an optical fibre previously operated on behalf of NATO involves state aid within the meaning of Article 61(1) of the EEA Agreement.
- (66) A measure constitutes state aid within the meaning of Article 61(1) of the EEA Agreement if the following conditions are cumulatively fulfilled: the measure (i) is granted by the state or through state resources; (ii) confers an economic advantage on an undertaking; (iii) is selective; and (iv) is liable to distort competition and trade between Contracting Parties.

1.2 State resources

- (67) According to Article 61(1) of the EEA Agreement, a measure must be granted by the state or through state resources in order to constitute aid.
- (68) Míla is of the principal view that the ownership of the fibre lies with the Icelandic Government. However, irrespective of whether the formal ownership lies with the Icelandic Government or with NATO, the measure was granted through state resources.
- (69) The Icelandic authorities have clarified that the ownership of the fibres rests with NATO, cf. section I.4 and I.7 above. The resource (i.e. the three fibres) is not owned by the Icelandic State or any of its entities. The resource was financed, constructed and is permanently owned by NATO. The arrangements between NATO and the Icelandic authorities are based on the no-cost no-gain principle, as confirmed in the Icelandic Defence Act No 34/2008, see Articles 5, 15 and 16 thereof. The Government of Iceland nevertheless has a wide-ranging right of use and other exploitation rights, including the right to lease out the fibres and use the proceeds for their maintenance and other running costs.²⁹ This right of use, however, is subject to rules of security and priority rights of NATO. Moreover, NATO receives any revenues exceeding operational costs of the fibres. NATO will also pay for any major repairs or replacements due to *force majeure* incidents.³⁰
- (70) With reference to the submission of the Icelandic authorities, the Authority considers that the fibre in question is not the property of the Icelandic State. However, the question of the ownership of the fibre is not decisive for the Authority's assessment. It is uncontested that the Icelandic State enjoys rights of control that enable it to exploit a lease right. In order to constitute state resources, it is sufficient, as correctly pointed out by Míla, that the resource in question, i.e. the lease right, was under public control and at the disposal of the national authorities,³¹ even though it was not the property of the public authority.³²
- (71) As regards state resources, the objective of the tender procedure and the leasing out of the fibre outlined in section I.2 was not to provide subsidies to interested lessees but on the contrary to

²⁹ See Article 16 of the Icelandic Defence Act No 34/2008.

³⁰ See section I.4 above for a more detailed description of the arrangements between Iceland and NATO.

³¹ See, for example, judgments in *Essent Netwerk Noord*, C-206/06, EU:C:2008:413, paragraph 70; *France v Ladbroke Racing and Commission*, C-83/98, EU:C:2000:248, paragraph 50.

³² Judgment in *Air France v Commission*, T-358/94, EU:T:1996:194, paragraphs 65-67.

alleviate the Icelandic State of costs that it was committed to pay for the operation and maintenance of the NATO fibres at its disposal. As set out in paragraph (36) above, the Icelandic authorities have explained that their arrangements with NATO are based on the no-cost no-gain principle. This means that any proceeds from the leasing of the fibre will first be used to pay for operational costs and minor repairs. If revenue exceeds those costs, any remainder is to be returned to the owner of the fibre, NATO. If costs exceed revenue, or in case of major repairs or replacements due to *force majeure* incidents, the Icelandic authorities are not liable for the relevant costs. Rather, the cost of repairs to the cable is shared between the fibres' owners according to their respective number of fibres. Reflecting these arrangements, the tender set a minimum reserve price corresponding to Iceland's payment obligation for operation and maintenance. Thus, the tender was designed to prevent any drain on state resources resulting from the lease right that was tendered out. In the Authority's view, it is a relevant consideration whether under the specific circumstances of the case at hand, an arrangement of this kind, which aims at preventing a drain on state resources in a situation where any further income would need to be passed on to a third party under an international obligation, can be considered to meet the requirement under Article 61(1) of the EEA Agreement that the measure is granted by the state or through state resources. However, given the conclusion that the measure did not result in an economic advantage (see section 1.3 below), the Authority does not need to assess this point any further.

1.3 Advantage

1.3.1 General

- (72) In order to constitute state aid within the meaning of Article 61(1) of the EEA Agreement, the measure must confer an advantage upon an undertaking.
- (73) Undertakings are entities engaged in an economic activity, regardless of their legal status and the way in which they are financed. Economic activities are activities consisting of offering goods or services on a market. The alleged beneficiary of the measure is Vodafone Iceland. The company is active on the electronic communications market, providing fixed telephony, mobile and data transmission services in Iceland. Accordingly, any aid involved in the leasing by the state of the NATO optical fibre would be conferred upon an undertaking.
- (74) An advantage, within the meaning of Article 61(1) of the EEA Agreement, is any economic benefit which an undertaking would not have obtained under normal market conditions, thus placing it in a more favourable position than its competitors. For it to constitute aid, the measure must confer on Vodafone advantages that relieve it of charges that would normally be borne from its budget. If the transaction was carried out under favourable terms, in the sense that Vodafone was paying a rental charge below market price, the company would be receiving an advantage within the meaning of the state aid rules.
- (75) To examine this question, the Authority applies the "*private vendor test*"³³ whereby the conduct of states or public authorities when selling or leasing assets is compared to that of private economic operators. The Authority considers that contrary to the view of the Icelandic authorities, this test can be applied in the present case even though Iceland does not own the fibre in question, given that the contract with Vodafone concerns a lease right which Iceland

³³ For the application of the "*private vendor test*", see Case E-12/11 *Asker Brygge* [2012] EFTA Ct. Rep. 536 and judgment in *Land Burgenland and Others v Commission*, C-214/12 P, C-215/12 P and C-223/12 P, EU:C:2013:682. These cases concern the sale of an outright property right in land. However, they also provide guidance for the sale of other rights in land, including the lease right in the present case.

has the right to exploit. However, the specific conditions applicable to this lease right will have to be taken into account in the assessment, in particular the fact that the Icelandic authorities could only offer for lease the fibre in the condition as it was used for defence purposes with only few connection points available for commercial purposes as well as the special NATO termination rights in case of war. The Authority also notes that the lease right which Iceland is entitled to dispose of is subject to a contractual obligation pursuant to which any rental income above the operation and maintenance costs of the fibre has to be transferred to NATO.

- (76) The purpose of the private vendor test is to assess whether a sale or leasing of assets carried out by a public body involves state aid, by examining whether a private vendor, under normal market conditions, would have acted in the same manner. The public authority must disregard public policy objectives and instead focus on the single objective of obtaining a market rate of return or profit on its investments and a market price for the sale or lease of assets.³⁴ The Authority notes, however, that this assessment normally has to take into account any special rights or obligations attached to the asset concerned, in particular those that could affect the market price.
- (77) Compliance with market conditions, and whether the agreed price in a transaction corresponds to market price, can be established through certain proxies. Organising an open, transparent and unconditional bidding procedure is generally an appropriate means to ensure that the sale or lease by national authorities of assets is consistent with the private vendor test and that a fair market value has been paid for the goods and services in question. However, this does not automatically mean that the absence of an orderly bidding procedure or a possible flaw in such a procedure justifies a presumption of state aid. Public procurement law and state aid law exist in parallel and there is no reason that the violation of, for example, a public procurement rule should automatically mean that state aid rules have been infringed.³⁵
- (78) On the other hand, as stated in the *Land Burgenland* case, cited in paragraph 97 of the EFTA Court judgment in Case E-1/13, “*where a public authority proceeds to sell an undertaking belonging to it by way of an open, transparent and unconditional tender procedure, it can be presumed that the market price corresponds to the highest offer, provided that it is established, first, that the offer is binding and credible and, secondly, that the consideration of economic factors other than the price is not justified.*”³⁶ The same principle must apply in the case of lease of assets. A private operator leasing his assets would normally try to obtain the best offer with an emphasis on price, and, for example, not consider elements that would relate to the intended use of such assets, unless they might affect the value of the assets after the lease period. Therefore, provided that the said pre-conditions are met, it can be presumed that the market price is the highest price which a private operator acting under normal competitive conditions is ready to pay for the use of the assets in question.³⁷
- (79) It follows from the above that a sale or lease of assets may involve state aid even when it is effected through a competitive procedure. This may occur in particular when obligations

³⁴ Judgment in *Land Burgenland and Others v Commission*, C-214/12 P, C-215/12 P and C-223/12 P, EU:C:2013:682.

³⁵ Judgment in *SIC v Commission*, T-442/03, EU:T:2008:228, paragraph 147. By analogy, see judgment in *Matra v Commission*, C-225/91, EU:C:1993:239, paragraph 44.

³⁶ See judgment in *Land Burgenland v European Commission*, C-214/12 P, C-215/12 P and C-223/12 P, EU:C:2013:682, paragraph 94.

³⁷ See, for example, judgments in *Banks*, C-390/98, EU:C:2001:456, paragraph 77; and *Germany v Commission*, C-277/00, EU:C:2004:238, paragraph 80.

imposed on the buyer result in a lower price. The kind of obligations which have such an effect are those that are imposed for the pursuit of public policy objectives and reduce the expected profit of the buyer. Such obligations would normally not be imposed by a private operator because they reduce the maximum amount of revenue that can be obtained from the sale or lease of the asset.

1.3.2 *The tender process and the award criteria*

- (80) In light of the above considerations, the Authority must examine whether the tender procedure and the award criteria were adequate and well-suited to establish a market price. In order to verify this, the Authority must consider whether the State, when preparing the tender and establishing the award criteria, acted as a private operator, or whether public policy and regulatory considerations were more prevalent.
- (81) The tender process and the arguments made regarding the use of the chosen award criteria are described in detail in section I.2.1 above as well as in Decision No. 299/14/COL. As set out in Table 1, the multiple award criteria consisted of six separate items to be evaluated, each with the weight of 10% or 15%, except for the criterion of stimulation of competition, which had the weight of 40%.
- (82) The Icelandic authorities have now clarified that in addition to the rental price (representing 15% of the award criteria), the tender criterion relating to the number of network termination points (a further 15% of the award criteria) should also be considered a price component as termination points are indispensable for the service and the value of the service is positively linked to the number of termination points. Each termination point requires substantial investment in equipment (see the estimate of the Mannvit study in section I.7 above), which will accrue to the lessor at the end of the lease, thus affecting the value of the lease right in question after the lease period.³⁸ The Authority thus considers that the tender criteria related to price in total amounted to 30% of the award criteria. However, non-price considerations in relation to the stimulation of competition (40%), a single tariff throughout the country (10%) as well as the supply (10%) and the commencement of services (10%) still outweigh the price components.
- (83) At the time of the tender, Míla owned and operated most telecommunication facilities in the different areas of Iceland. In order for the NATO fibres to become operational, the operators of those fibres would need to invest in assembly points. In the Authority's view, the criteria on the commencement of services (10%) and supply of services (10%) would thus appear to favour Míla. In other words, the award criteria consisted of two price related items and four non-price related items. Of the non-price related items, one item, with the highest weight, is likely to have been to the disadvantage of the incumbent network provider, Míla, while two items are likely to have favoured Míla, to the detriment of potential new entrants.
- (84) The private vendor test sets the principle that as a main rule the market price corresponds to the highest price which a private operator acting under normal competitive conditions is ready to pay. However, this principle is not without exception. Exceptions relate, firstly, to instances where it can be established that the offer in question is not binding or credible, or not comparable to a lower offer. Secondly, as stated in *Land Burgenland*, paragraph 94, the presumption is subject to the reservation that “*the consideration of economic factors other than*

³⁸ This increase in value is relevant in the present case, as Iceland has to return any profits from the rental fee to NATO under the no-cost no-gain principle.

the price is not justified'. An example of such a justification can be found in Case T-244/08, *Konsum Nord v Commission*.³⁹ In that case, a municipality in Sweden had sold a plot of land to a supermarket chain at a price below the price offered by the highest bidder. The General Court held that the market value of the sale of land in question could not be established based solely on the presence of a higher bid without considering the particular circumstances invoked by the Swedish authorities. Further, the Court of Justice held in Case C-39/14, *BVVG* that a rule of national law enabling a public authority to reject a tender offer for agricultural land that is disproportionately high and of a speculative nature does not entail state aid, provided that it results in a price that is as close as possible to the market value of the land in question.⁴⁰

- (85) This case law is not directly applicable to the case at hand, given that Míla did not submit a bid. Nevertheless, the Icelandic authorities argue that its choice of award criteria were justified in the present case. They argue that in particular the disputed criterion on promotion of competition was designed to address the alleged monopolistic feature of the relevant market dominated by the incumbent provider, Míla. The Authority also notes that Míla itself declared that it had no economic reason for participating in the tender, given that it already had ample transmission capacity on its own fibres.
- (86) However, in the present case the particular circumstances invoked by the Icelandic authorities are not sufficient to demonstrate that a private vendor in the same situation would have designed the tender in a similar way. The EFTA Court in Case E-1/13 held that the award criteria other than price appeared to reflect public policy or regulatory considerations, which a private investor would not consider relevant. The Authority also considers that the non-price criteria in the tender partly reflected public policy or regulatory considerations, such as the promotion of competition, improvement of public broadband access and regional cohesion, which a private investor would not consider relevant. These award criteria outweigh the criteria related to price.
- (87) The Authority therefore concludes that the award criteria of the tender do not meet the requirements of the private vendor test. Accordingly, the outcome of the tender cannot provide a reliable proxy for establishing the market price for the lease right in question.

1.3.3 Expert valuation of the lease right

- (88) As stated above, the absence of a sufficient tender process does not exclude the possibility of the Authority applying the private vendor test. However, the Authority will need to examine the substance of the transaction in question, and in particular compare the agreed price to the market price. For this purpose, the Authority normally refers to an independent expert valuation study as a proxy for the market price. Such a study should ideally be prepared at the time of the transaction. However, the Authority can also rely on an *ex post* valuation study in its assessment.⁴¹
- (89) The Icelandic authorities have provided a valuation study by Mannvit, an international consultancy with a focus on Iceland, which regularly provides expert advice on infrastructure projects. The study is dated 30 January 2015.

³⁹ Judgment in *Konsum Nord ekonomisk förening v European Commission*, T-244/08, EU:T:2011:732.

⁴⁰ Judgment in *BVVG*, C-39/14, EU:C:2015:470, paragraph 42.

⁴¹ Case E-12/11 *Asker Brygge* [2012] EFTA Ct. Rep. 536, paragraph 81.

- (90) The Authority notes that Mannvit had already advised the Icelandic authorities on the tender process. Furthermore, the valuation study was requested by the Icelandic authorities in response to the price estimate put forward by the complainant. The Authority has not found any indications that these circumstances have affected the objectivity of the expert consultants. However, under these circumstances the Authority considers it necessary to examine the valuation study in detail.
- (91) In this regard, the Authority first notes that the assessment of the market value of the lease right at issue is particularly complex, given the specific nature of the asset (including the NATO termination rights) and the existence of regulation in the sector. Furthermore, the existence of two price elements, namely the rental fee and the investments in termination points, has to be taken into consideration.
- (92) The Mannvit study is based on a comparison between two different scenarios for gaining access to the fibre cable around Iceland: An operator could either lease the NATO fibre (as Vodafone has done) or, alternatively, procure access from Míla, which offers a regulated wholesale product (trunk leased lines) at a regulated price. Given this choice, a market operator looking for access to the fibre cable would not be prepared to pay more than the price for the regulated wholesale access product offered by Míla. The regulated wholesale price thus acts as a price ceiling for the pricing of the NATO fibre lease, although it might not directly reflect the market price of the lease right due to the elements described in the following paragraphs. The Authority considers this approach based on a price comparison to be reasonable, given the existence of the two alternative ways of obtaining access to parallel fibres in the same cable.⁴²
- (93) The price comparison in the Mannvit study as well as the most recent one provided by the complainant are not based on prices at the time of the tender. However, the Authority considers that under the specific circumstances of the case at hand, the price references provided still offer a good proxy for the market price at the time of the transaction.
- (94) The regulated wholesale prices used as a comparison are based on historic costs and usually remain unchanged over a number of years.⁴³ For instance, Míla's regulated tariff of ISK 7 609 per km/month is based on a cost analysis prepared in 2010 and finalised in May 2011.⁴⁴ The tariff has been in force unchanged from 1 August 2011 until 2015. This demonstrates that the regulated wholesale tariffs used in the price comparison usually remain stable over time, and that the Míla tariff in particular is based on a cost analysis undertaken at around the same time as the contract of 1 February 2010 with Vodafone. Moreover, the rent payable by Vodafone is adjusted by the building cost index as from June 2008 (i.e. at the time of the tender). Once this indexation has been taken into account, the calculation provided based on today's prices can thus provide a good indication of whether the lease right had been granted on market terms at the time of the transaction.

⁴² The Authority highlights that under the regulatory system, Míla has an obligation to provide wholesale access to its fiber network. The reported difficulties in obtaining access from Míla do not render this price comparison invalid, given that a remedy is available in the form of the PTA ordering Míla to provide effective access, which it has done on a number of occasions.

⁴³ According to PTA's Decision No. 14/2011, page 7, Míla's proposal to continuously update its tariff based on inflation were rejected by the PTA. The PTA's Decision is available here: http://www.pfs.is/upload/files/Ákv_14-2011_M13-14_Leigulfnur.pdf.

⁴⁴ See the PTA's Decision No. 14/2011, page 18.

- (95) As explained in section I.7 above, Mannvit highlights a number of differences between the regulated wholesale product offered by Míla and the NATO fibre that should be taken into account when comparing prices.
- (96) First, the Authority considers it reasonable when Mannvit adjusts the length of the NATO fibre to be taken into account for the price calculation, as prices are usually calculated on a point-to-point basis (i.e. as direct lines between the relevant termination points). When applied to the existing termination points on the NATO fibre at the time of the transaction, the Mannvit study concludes that the total length to be taken into account is 1 283 km.
- (97) Mannvit then assesses which wholesale price and discount would be most appropriate to be applied in the case at hand.
- (98) The study highlights that Míla's regulated tariff (ISK 7 609 per km/month) might not be the right benchmark to determine the market price, as the regulated tariff is based on the costs and utilisation ratio of Míla's whole fibre network, including all of Míla's relevant termination points, and not only a fibre network comparable to that of the NATO fibre. Mannvit points out that the NATO fibre is simpler and has much fewer termination points, which indicates that the appropriate cost basis should be lower. Mannvit therefore proposes to rather use the wholesale tariff of another operator, Orkufjarskipti, as the basis for calculating the market price. The tariff of Orkufjarskipti is ISK 5 020 per km/month.
- (99) The Mannvit study also examines discount rates and concludes that a discount of 25% should be applied to the wholesale price, instead of the maximum of 15% currently available for three-year contracts. Mannvit justifies this adjustment by pointing out that the lease term is ten years, which is well in excess of the duration contemplated in the regulated tariffs of Míla and Orkufjarskipti. It is further justified by the existence of a 25% discount Míla offered to customers renting a similar length of fibre as the NATO fibre at the time of the tender.
- (100) The Authority concurs that the regulated tariff of Míla for trunk leased lines does not provide an appropriate market price comparison in the case at hand. In particular, Míla's tariff is based not only on the investment and operating costs of fibres in the same cable as the NATO fibre (which have most likely been amortised already) but also on newer investments in other fibres. However, the Authority notes that the tariff of Orkufjarskipti put forward by Mannvit does not provide the ideal point of reference either, given that it is based on the individual cost structure of that operator, a utility company. The Authority recognises that there appears to be no perfect price comparison possible as there are no available market prices that apply specifically to the NATO fibres as well as the parallel fibres in the same cable.
- (101) The Authority has similar concerns regarding the discount to be applied. The currently available wholesale offers foresee a mere 15% discount for a three-year contract. It is however likely that a market operator would grant more significant discounts for a longer-term contract and very high quantities. The Authority notes that a 25% discount was previously available from Míla for a very similar purpose.⁴⁵

⁴⁵ In Decision No. 14/2011, PTA states on page 6 that it has agreed to Míla's proposal on new system discounts. The new discounts depend on the length of contracts. A discount of 5% is granted for a one year contract, 10% for 2 year contracts and 15% for 3 year contracts. No reference is made, though, to contracts of longer duration. While it may be reasonable that the percentage rise in discount rates is not fully linear according to time (as Míla

- (102) Given the above, the Authority considers that it is appropriate to express the market price estimate for the lease right of the NATO fibre as a price range, based on the wholesale access price and discount assumptions discussed above.

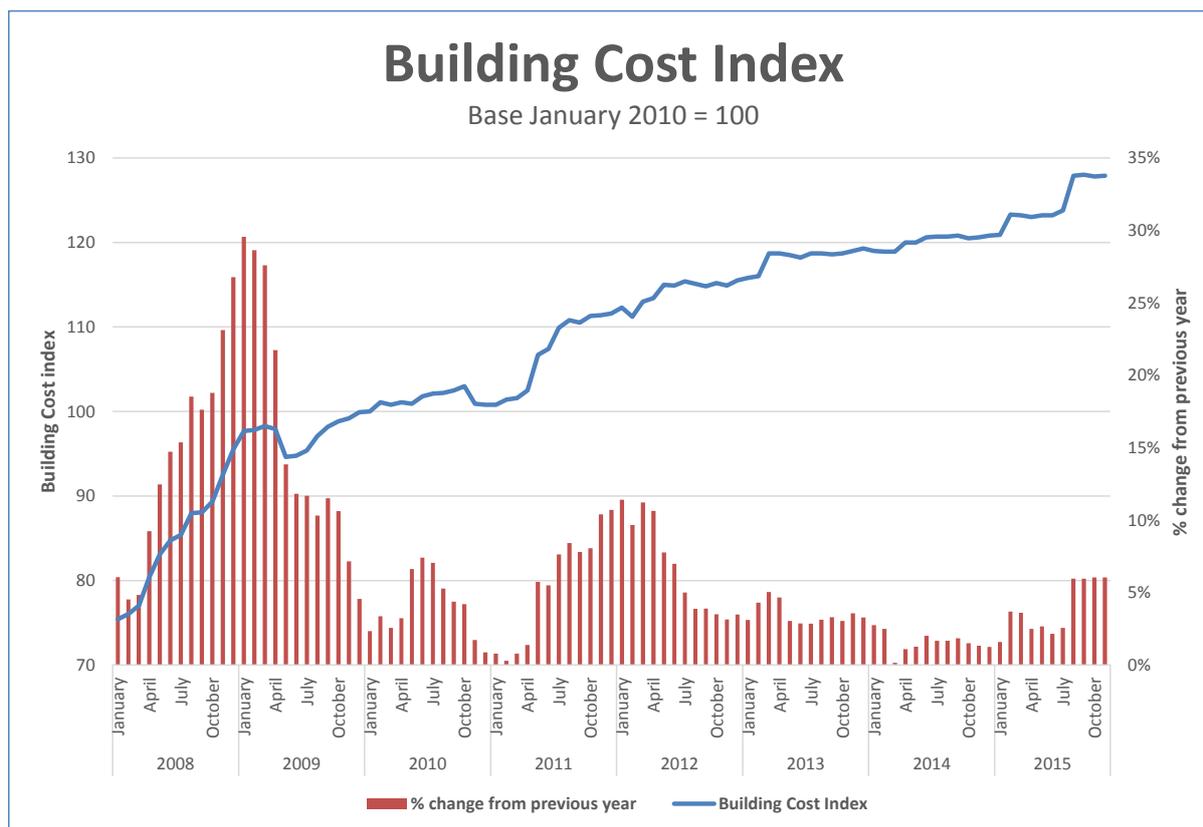
Price per km/month	-15% discount (*1 283km*12)	-25% discount (*1 283km*12)
Míla (7 609 ISK)	ISK 99.6m	ISK 87.9m
Orkufjarskipti (5 020 ISK)	ISK 65.7m	ISK 58.0m
<i>Average per discount</i>	<i>ISK 82.7m</i>	<i>ISK 73.0m</i>
<i>Total average</i>	<i>ISK 77.9m</i>	

Table 3: Estimated market price ranges (rental price per year) based on available tariffs and discount assumptions

- (103) Table 3 above shows a price range from ISK 58 million, the market price estimate of the Mannvit study, to a maximum of about ISK 100 million. The average market price estimate is about ISK 78 million.
- (104) According to the contract of 1 February 2010, Vodafone pays a rental charge of ISK 19 150 000 (excluding VAT), indexed as from 19 June 2008 according to the building cost index, for the lease right, payable on 1 July of each year. The Authority notes that tariffs of Míla and Orkufjarskipti are not subject to indexation. Accordingly, the effect of the indexation must be taken into account in the comparison.
- (105) Vodafone's rental payments are indexed using the building cost index.⁴⁶ According to the statistics, building costs increased strongly following the financial crisis in the autumn of 2008 and during 2009, up to a rate of 30% per annum, but have since then increased moderately, with a small hike at the end of 2011 and beginning of 2012. Between June 2008 and July 2010, when the first rental payment was due, the index had already risen by 20.5%.
- (106) The movement of the index since January 2008 and the percentage change from the previous year are illustrated by the graph below:

and the PTA have agreed is the case for the first three years), a 25% discount for a contract of 10 years appears realistic.

⁴⁶ The Building Cost Index is prepared by Statistics Iceland and available on its website. See <http://www.hagstofa.is/en/statistics/business-sectors/industry/building-cost-index/>.



Graph 1: Building cost index from January 2008, source: Statistics Iceland

- (107) The contract of 1 February 2010 foresaw a rental charge of ISK 19 150 000 before indexation. By mid-2010, the effect of the indexation had increased this to about ISK 23 million. Today, Vodafone pays a rental charge of about ISK 28 million, which corresponds approximately to the mid-term of the 10-year lease contract. Provided that the building cost index continues to increase gradually as it has over the last 4-5 years, this price also represents a reasonable average for yearly rental charge when considered over the lifetime of the contract.
- (108) The Authority therefore considers that the rental charge of ISK 28 million used by Mannvit represents a reasonable approach for the price comparison in the case at hand. However, the rental charge for the NATO fibre can only be compared with tariffs of commercially used facilities if appropriate account is taken of the substantial investment in transmission equipment required by the operator of the NATO fibre, Vodafone, to make the fibre fit for commercial use. Mannvit estimates an annual cost of ISK 52 million for the investments required to make the lease price paid by Vodafone comparable to Míla's offer and to comply with the terms of the tender offer, i.e. the required investment in new termination points.⁴⁷ The Authority notes that the amount estimated by Mannvit accounts for both technical equipment to make the NATO fibre operational and the price element identified in the tender related to the investment

⁴⁷ According to the Mannvit study, the average cost of installing the required transmission equipment is ISK 4 million per termination point (of which there are 30), with a depreciation of 15% per year, an estimated operating expenditure of 20% of Capex and a WACC of 8.5% of Capex. The Authority notes that Mannvit uses the WACC assumptions from the PTA's cost analysis in Decision No. 14/2011, and models the other parameters on the discussions in the PTA's cost analysis. The Authority considers it appropriate to use the same WACC assumptions as in the PTA's Decision on which the Míla prices used in the comparison are based. The Authority further considers that assuming an economic lifetime of 6.7 years for technical equipment is appropriate given the rapid technological changes in the sector, and that Opex of 20% of Capex is appropriate due to the mostly remote locations and the nature of the technical installations.

in new termination points. The Authority has cross-checked the expert's estimate of the investment costs in termination points (totalling ISK 120 million) against the actual investments to be carried out by Vodafone, which total ISK 130 million. The Authority notes that in addition, Vodafone has to pay an annual license fees for the equipment of ISK 7.5 million, which Mannvit did not take into account.

- (109) Based on the above, the annual financial contributions by Vodafone in the form of the rental payments and investment costs total about ISK 87.5 million (including the annual license fee). Compared to the market price estimates of the rental right in Table 3, Vodafone's financial contributions exceed the total average market price estimate of ISK 78 million as well as the average prices based on a 15% and a 25% rebate. They are also substantially higher than the price estimate based on the Orkufjarskipti tariff (whether 15% or 25% discount) and very close to the Míla tariff based on a 15% rebate.
- (110) The Authority notes that the market price comparison set out above does not take into account the impact of the special cancellation rights due to the NATO ownership of the fibre. The Icelandic authorities have estimated the impact on price of these rights at a range of 15-25%. Applying this range to the financial contributions of Vodafone, the respective underlying market value of the contributions without consideration of these NATO rights would be ISK 94 to 107 million, vastly exceeding the average market price estimates in Table 3.
- (111) Furthermore, the Mannvit study does not take into account the obligation for Iceland to transfer any rental income above the operation and maintenance costs of the fibre to NATO. The Authority considers that although this obligation may affect the incentives of the Icelandic authorities not to maximise the rental income (and for instance to prefer other criteria in the tender process, see above), it does not affect the market value of the lease right, which has been estimated above with reference to actual tariffs of telecommunication operators. In contrast to the special cancellation rights discussed in the paragraph above, the agreement between Iceland and NATO on how any income from the lease right is distributed has no impact on the user of that right (i.e. Vodafone).
- (112) For the sake of completeness, the Authority notes that this assessment is not affected by Míla's allegations that the design of the tender process had an effect on price. The Authority has not been presented with any evidence that the setting of a reserve price – which is a common occurrence in tenders – could have reduced the incentives for bidders to compete on price. The Authority also notes that in the tender, four independent contestants submitted five bids, where all bidders scored fully (40%) on the criterion of promotion of competition. Accordingly, price-related criteria for the bidders in practice accounted for 50% (i.e. 30 of the remaining 60 points). Similarly, there has been no evidence that in the absence of the competition criterion in the tender, a potential bid of Míla's – which was not interested in further transmission capacity – could have resulted in higher offers from the actual bidders. The Authority notes in particular that Míla's capacity on the NATO cable was publicly known and that any potential bid by Míla would have only served to protect its market position from a new entrant.⁴⁸
- (113) Based on the above, the Authority considers that the lease to Vodafone did not take place below market price.

⁴⁸ According to the judgment in *BVVG*, C-39/14, EU:C:2015:470, paragraph 40, the Icelandic authorities could in any event have had the right to reject such a bid on the basis of its manifestly speculative nature.

- (114) Finally, the Authority also notes that the tender process took place in June 2008, i.e. shortly before the onset of the financial crisis in Iceland. During the financial crisis, the process was halted. The contract with Vodafone was only finalised in February 2010, by which time Fjarski (the highest-rated bidder under the tender) was unable or unwilling to lease the second available fibre on the basis of its offer from June 2008. In early 2010, it was according to the Icelandic authorities no longer possible to accept offers from other bidders in the 2008 process as their offers had expired and it was obvious that market conditions had changed dramatically to the worse after the financial crisis. Despite the financial crisis and the ensuing changes in the economic situation in Iceland, Vodafone was willing to go ahead with the lease agreement under the conditions agreed upon following the tender in 2008. The Authority has not received any information indicating that following the financial crisis, other operators were still interested in obtaining a lease right in either of the two available fibres. The Authority considers that in a similar situation, a private vendor would also have entered into the lease agreement with Vodafone, as it offered the only opportunity to recoup operating costs of, and generate value from, an unused asset (i.e. the idle fibre).
- (115) In light of the above, the Authority concludes that Vodafone did not receive an economic advantage from the transaction.

1.4 Selectivity, distortion of competition and effect on trade between Contracting Parties

- (116) In order to qualify as state aid within the meaning of Article 61(1) of the EEA Agreement, the measure must be selective as well as liable to distort competition and affect trade between the Contracting Parties to the Agreement. However, given that no economic advantage was granted in the present case and the cumulative conditions for the existence of state aid are therefore not fulfilled, the Authority does not need to make any further assessment in this regard.

2. Conclusion

- (117) On the basis of the above, the Authority concludes that the measure does not involve state aid within the meaning of Article 61(1) of the EEA Agreement.

HAS ADOPTED THIS DECISION:

Article 1

The lease by the Defence Agency of the Ministry for Foreign Affairs in Iceland with Og fjarskipti of 1 February 2010 for the use and operation of an optical fibre does not involve state aid within the meaning of Article 61 of the EEA Agreement.

Article 2

This Decision is addressed to Iceland.

Article 3

Only the English language version of this Decision is authentic.

Done in Brussels, 16 March 2016

For the EFTA Surveillance Authority

Sven Erik Svedman
President

Helga Jónsdóttir
College Member

[Status]