

Case No: 69969
Event No: 622201
Dec. No: 392/11/COL

EFTA SURVEILLANCE AUTHORITY DECISION

of 14 December 2011

on the power contract between Landsvirkjun and Íslenska kísilfélagið ehf.

(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 thereof,

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 Article 4(2) of Part II,

Whereas:

I. FACTS

1. Procedure

- (1) The Icelandic authorities notified for legal certainty a new power contract between Landsvirkjun and Íslenska kísilfélagið ehf. (“ISC”) pursuant to Article 1(3) of Part I of Protocol 3 by letter of 17 May 2011 (Event No 598580 and 598929).
- (2) By letter dated 13 July 2011 (Event No 603433), the Authority requested additional information. By letter dated 30 August (Event No 607430), the Icelandic authorities replied to the information request. Further clarifications were submitted by the Icelandic authorities by email on 24 November 2011 (Event No 616733) and on 29 November 2011 (Event No 616727) .

2. Description of the proposed measures

2.1 The parties to the power contract

2.1.1 Íslenska kísilfélagið ehf

- (3) Íslenska kísilfélagið ehf. (“ISC”)ISC was founded in 2009 according to the Icelandic company register. It is majority owned (85%) by the US-based Globe Speciality Metals Inc. (“GSM”) and the Icelandic company Tomahawk Development á Íslandi

ehf. (15%). GSM is publicly traded, listed on the NASDAQ since July 2009 and a leading producer of silicon products worldwide. According to the Icelandic authorities, Tomahawk is an Icelandic / Danish company.

2.1.2 Landsvirkjun

- (4) Landsvirkjun is a public partnership company regulated by Act No 42/1983 on Landsvirkjun (“the Landsvirkjun Act”). The company produces electricity from renewable hydro and geothermal sources. Landsvirkjun processes 75% of all electricity in Iceland and is the country's biggest electric generator. Landsvirkjun sells 85% of its electricity to power intensive industries.
- (5) The company was established as an enterprise, jointly owned by the State Treasury and the City of Reykjavík in equal parts, on the basis of Act 59/1965 on Landsvirkjun, by a Partnership Agreement of 1 July 1965 between the Government of Iceland and the City Council of Reykjavík. Laxá Power Station, a power company jointly owned by the Town of Akureyri and the State Treasury, was merged with Landsvirkjun with effect from 1 July 1983 and as a result Landsvirkjun became a national electricity company, whereas it had been operating only in parts of the country before.
- (6) The founding of Landsvirkjun in 1965 may be traced to the Icelandic government’s growing interest in increasing the utilization of hydroelectric energy resources by attracting foreign investors for power-intensive industry in Iceland. This happened following the Swiss aluminum producer Alusuisse interest in building an aluminum plant in Iceland; the Straumsvík Aluminium Plant, later purchased by Alcan Iceland Ltd.
- (7) Landsvirkjun is now governed by the provisions of Act No 42/1983, the Act on Landsvirkjun, as amended. The legal form of the company is a public partnership according to Art 1(1) of the Landsvirkjun Act with a joint liability, which means that the owners are liable for all of Landsvirkjun’s liabilities.
- (8) Following the liberalization of the electricity sector the Electricity Act was adopted in 2005 and 1 January 2005 the Landsvirkjun's Transmission Division became Landsnet, an independent limited liability company and a subsidiary of Landsvirkjun. Landsnet owns and operates the Icelandic transmission system.
- (9) As of 1 January 2007, the State Treasury took over the ownership shares of the Town of Akureyri and the City of Reykjavík in Landsvirkjun. The company remained a partnership company with joint liability of the owners. Landsvirkjun is now jointly owned by the State Treasury (99.9 %) and Eignarhlutir ehf. (0.1 %). The latter is a limited liability company wholly owned by the State Treasury. The state’s interests are controlled by the Ministry of Finance.
- (10) According to the Landsvirkjun Act, the company shall be financially independent. It is foreseen that Landsvirkjun shall pay dividends to its owners, determined on the basis of the performance of the company and the profits carried forward from preceding years.
- (11) Landsvirkjun’s board of directors is composed of five members and an equal alternate members, all appointed by the Minister of Finance. The board adopts their own Rules of Procedure and according to the information provided by the Icelandic authorities

the board functions like any other independent board of directors of a company engaging in competitive business operations.

2.2 The notified power contract

- (12) According to the Icelandic authorities, Landsvirkjun entered into negotiations with GSM, ISC's parent company, early in 2010. A Memorandum of Understanding ("MOU") between the parties was signed on 5 February 2010.
- (13) The ensuing negotiations were handled on behalf of Landsvirkjun by a committee of four members, lead by its Executive Vice President for Marketing and Business Development. Formal negotiations between the parties took place during several meetings in 2010 and early in 2011. The parties reached a basic agreement on the purchase of electricity in February 2011.
- (14) On 17 February 2011, Landsvirkjun and ISC signed a power contract for a new 40.000 ton silicon metal production facility in Helguvik, Southwest Iceland.
- (15) According to the agreement Landsvirkjun will provide energy for ISC's new plant in Helguvik, which is expected to start production in mid-2013 and will require 65 MW of power. The contract has a duration of 18 years.
- (16) The agreement is structured in two phases. Initially, i.e. from 2013 onwards, Landsvirkjun will provide 35 MW of energy (298 GWh per year) and the remaining 30 MW will be supplied by HS Orka, a privately owned electricity company. From January 2016 onwards, Landsvirkjun will supply all of the energy to the smelter (550 GWh per year). According to the Icelandic authorities, HS Orka and ISC had already agreed on a three year contract before the negotiation between Landsvirkjun and ISC began. The Icelandic authorities submit that HS Orka wanted to only conclude a short term contract in order to have the 30 MW available again in 2016 for different uses.
- (17) As regards the contract under assessment, it is the first that Landsvirkjun enters into with the contract price in EUR. The base contract price is ≥ 20 EUR per MWh, which corresponds to approximately ≥ 30 USD per MWh at the rate of exchange for EUR and USD around the turn of the year 2010 to year 2011.
- (18) The contract price in the Power Contract is increased by [...] % annually, in order to keep the contract price level [...], and covering an estimated average annual inflation rate. The parties also agreed to have an additional increase of [...] % in price at year [...] of the contract period (year [...]) and at year [...] and [...] an additional increase of [...] % each year in addition to the [...] % annual inflation increase. This additional increase on top of the estimated inflation is equal to [...] % over the entire period. It means that the contract price will be EUR [...] in 2031.
- (19) Article 6 of the contract contains a "Take or Pay obligation" according to which ISC must pay at least for a fixed amount of energy per calendar year regardless of whether the actual consumption is less (during the first phase of the contract, ISC is obliged to pay for at least [...] GWh, and for [...] GWh during the second phase; this amount to [a considerable share] of the entire contract power).
- (20) This contract price does not include the cost of transmission, which will be paid by ISC to Landsnet hf., the Icelandic transmission system operator, according to a separate agreement with them.

- (21) According to the Icelandic authorities, the electricity that Landsvirkjun has agreed to provide is already available in its power system and thus no further construction of power plants will be needed. However, the additional 30 MW that Landsvirkjun will deliver from 2016 onwards mainly originate from the Búðarháls Hydro Power Project, which is currently under construction. The profitability of this project is assessed in the Authority's decision 391/11/COL on the Power Contract between the National Power Company in Iceland (*Landsvirkjun*) and Alcan for Straumsvík Aluminium Plant.
- (22) The contract is subject to several conditions being fulfilled by the parties. ISC has not fulfilled conditions, and hence the agreement is not finalised yet. The deadline for ISC to fulfil the outstanding conditions was recently extended to 15 December.

3. Comments by the Icelandic authorities

- (23) The Icelandic authorities submit that the power contract between Landsvirkjun and ISC, with a duration of 18 years, is shorter in duration than many of the power contracts that are currently being executed by Landsvirkjun, of which a duration of 20 years and more was common. However, Landsvirkjun has for some time aimed at shortening the contract periods in new power contracts towards no longer than fifteen years, which would facilitate the adjusting of the price for contract electricity to the price developments in more liquid electric power markets than that of Iceland.
- (24) In the Icelandic authorities' view it is at the same time evident that an investor setting up a new power intensive industry plant requires some certainty about the price of the electricity, which is a major cost factor that has a strong impact on the profitability of the investment, and its feasibility forecast. Against this background the result of the negotiation dialogue between Landsvirkjun and ISC is to be seen as a compromise that satisfies the interest of both parties.
- (25) The Icelandic authorities have informed the Authority that Landsvirkjun sees the contract also as an implementation of the company's new strategy that is aimed at increasing the diversity of its client base. Silicon metal represents a new industry in the company's portfolio, which it believes has good long-term prospects in Iceland where power is generated from renewable energy sources only.
- (26) The Icelandic authorities are of the view that the notified power contract does not entail an element of state aid.
- (27) They submit that the power contract was negotiated on normal market terms and provides an acceptable rate of return to Landsvirkjun, and that it hence does not confer an advantage on ISC. Moreover, they contend that there was no transfer of State resources, and that there is neither a distortion of competition nor an affectation of intra-EEA trade. These arguments are however not elaborated on any further.
- (28) The Icelandic authorities have provided more specific views on the issue of imputability, in particular as regards the involvement of Landsvirkjun's owners, i.e. the Icelandic state. The State was informed of the progress of discussions between Landsvirkjun and ISC while the negotiations were in progress, but according to the Icelandic authorities no formal approval was obtained from it, neither with regard to the methodology used or individual substantive provisions of the power contract. In essence, the Icelandic authorities seem to argue that the State did not exert any direct

influence on the contract or the negotiations, and that therefore the measure is not imputable to the State.

II. ASSESSMENT

1. The presence of state aid

(29) Article 61(1) EEA Agreement 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.”

(30) This implies that a measure constitutes state aid within the meaning of Article 61(1) of the EEA Agreement if the following conditions are cumulatively fulfilled: the measure (i) is granted by the State or through state resources; (ii) confers an economic advantage to the beneficiary; (iii) is selective; (iv) has an impact on trade between Contracting Parties and is liable to distort competition.¹

1.1 Presence of state resources

(31) To be qualified as state aid, the advantage must be granted by the State or through state resources. The advantage can also be granted through a public undertaking provided there is imputability to the State². The European Court of Justice held in *Stardust Marine*³ that

“...“Art. 87 (1) EC covers all the financial means by which the public authorities may actually support undertakings, irrespective of whether or not those means are permanent assets of the public sector. Therefore, even if the sums corresponding to the measure in question are not permanently held by the Treasury, the fact that they constantly remain under public control, and therefore available to the competent national authorities, is sufficient for them to be categorised as State resources. [...]

The State is perfectly capable, by exercising its dominant influence over such undertakings of directing the use of their resources in order, as occasion arise, to finance specific advantages in favour of other undertakings. [...] the position of a public undertaking cannot be compared with that of a private undertaking. Through its public undertakings, the State may pursue objectives other than commercial ones, [...].”

¹ According to settled case-law, classification as aid requires that all the conditions set out in the provision should be fulfilled, see Case C-142/87 *Belgium v. Commission* (“*Tubemeuse*”) [1990] ECR I-959.

² Case C482/99 *France v Commission (Stardust Marine)* [2002] ECR I-4397, paragraphs 50-59 and Article 1 of the Transparency Directive.

³ Case 482/99 *France v Commission (Stardust Marine)*, cited above, paragraph 57.

(32) In this judgment the Court of Justice however also clarified that the mere fact of the company giving out public funds does not suffice to establish the presence of State resources. According to the Court the decisive elements are, on the one hand, whether the State is in a position to control the public undertaking and exercise a dominant influence over its operations and, on the other hand, whether it actually does exercise this right of control over the undertaking paying out the funds. At the same time the Court clarified that

“it cannot be demanded that it be demonstrated, on the basis of a precise inquiry, that in the particular case the public authorities incited the public undertaking to take the aid measure in question”.⁴

(33) As a consequence, imputability to the State may be inferred from a set of indicators arising from the circumstances of the case and the context in which that measure was taken. The judgment also contains a non-exhaustive list of such indicators, including

- a. the legal status of the undertaking (in the sense of its being subject to public law or ordinary company law);
- b. any other indicator showing, in the particular case, an involvement by the public authorities in the adoption of a measure or the unlikelihood of their not being involved, having regard also to the compass of the measure, its content or the conditions which it contains.

(34) In his opinion on the case, Advocate General Jacobs also provided a similar non-exhaustive list of possible indicators, including “a general practice of using the undertaking in question for ends other than commercial ones or of influencing its decisions”⁵.

(35) This list of indicators and the Court’s general formulation, according to which the public authorities must be regarded as having been involved “in one way or another”, seems to suggest that any kind of conduct (active or passive) of the public authorities could suffice to establish imputability. Likewise “the unlikelihood of [the public authorities] not being involved having regard also to the compass of the measure, its content or the conditions which it contains” shows that imputability could be established merely on the basis of some characteristics of the measure at stake, i.e. when they are such as to render unlikely the non-involvement of the State.

(36) Against this background it becomes clear that the Authority cannot exclude that the conclusion of the notified power contract is imputable to the State. Not only is Landsvirkjun fully owned and controlled by the Icelandic state, it has, at least in the past, evidently been used by the State to attract foreign investment by means of offering power contracts of long duration⁶. It would seem arguable that this would be

⁴ Case 482/99 *France v Commission (Stardust Marine)*, cited above, paragraph 53.

⁵ See Opinion of Advocate General Jacobs, Case C-482/99 *French Republic v Commission (Stardust)* [2002] ECR I-4397, at paragraph 58.

⁶ Cf. Opening speech of the former minister of Industry and Commerce Ms. Valgerdur Sverrisdóttir, International Aluminium and Power Conference, 4-5 March 2004, available at <http://eng.efnahagsraduneyti.is/minister/speeches/nr/1385>: “For now over 40 years it has been the policy of all governments to promote the utilisation of the country’s clean and renewable hydro and geothermal energy resources for sustainable power development. [...] By promoting the utilisation of these resources, we are diversifying the industrial activity and economy and improving the living standard of the people. We further aim to expand merchandise exports and stimulate foreign investments, such as in the primary aluminum industry. Intensive energy marketing efforts initiated by the Ministry for Industry and Commerce, particularly in the last 15 years, have brought about large

exactly what AG Jacobs had thought of when he mentioned “a general practice of using the undertaking for ends other than commercial ones” in his opinion on *Stardust*.

- (37) Moreover, and perhaps most compelling, the legal status of Landsvirkjun, as mentioned by the Court in *Stardust*, which makes the State fully liable for all of Landsvirkjun’s liabilities, appear to be on its own a very strong indicator for imputability.
- (38) A prudent owner of a limited liability company – as the State was in *Stardust*, and is in fact in most cases of public ownership in companies - would in all likelihood already closely monitor the negotiation and conclusion of contracts of such economic significance as the contract at hand, which would already indicate imputability.
- (39) Whereas a (fictitious) limited liability company owner could at most lose his entire investment, i.e. the capital that he injected in the company, Landsvirkjun’s owner, the Icelandic State, is subject to an all-encompassing obligation to guarantee the company’s liabilities. Therefore, it cannot but be expected to pay even more attention to and possibly exert its influence in situations as the one under assessment, as agreeing on contracts of such importance will not only have economic repercussions for almost 20 years, but could entail liabilities far exceeding the capital position of the State in Landsvirkjun. The financial risk of an owner of a company with a legal status such as Landsvirkjun is thus of such magnitude that the absence of any (at least passive) influence appears virtually impossible.
- (40) Overall, the Authority is therefore, in light of the legal status of Landsvirkjun, the past evident use of Landsvirkjun as a tool to attract foreign investment and the general circumstances described above unable to exclude that the measure is imputable to the State, and that it entails State resources if and to the extent it confers an advantage on ISC. Whether the contract confers an advantage on ISC, which would be a further strong indicator of imputability, is assessed below.

1.2 Favouring certain undertakings or the production of certain goods

- (41) When governments make financial transactions and investments, the European Court of Justice has stated that in order to confirm whether a state measure constitutes aid, it is necessary to establish whether the recipient undertaking receives an economic advantage, which it would not have obtained under normal conditions.⁷ In doing so, the Authority has to apply the market economy investor test⁸, which in essence provides that state aid is granted whenever a state makes funds available to an undertaking which in the normal course of events would not be provided by a private investor applying ordinary commercial criteria and disregarding other considerations of a social, political or philanthropic nature⁹.
- (42) The measures at hand – a power contract, with a publicly owned company as a seller, could thus entail an element of state aid if its terms are such that they would not have

investments in the power and energy intensive industry, which gradually have put Iceland on the world map as a serious alternative location for light metal production”.

⁷ Case C-39/94, *SFEI v La Poste*, 2006 ECR I/3547, at paragraph 60.

⁸ This principle is explained in the Authority’s guidelines Part IV Rules on public service compensation, state ownership of enterprises and aid to public enterprises, Application of state aid provisions to public enterprises in the manufacturing sector.

⁹ Cf. for example Opinion of Advocate General Jacobs, Joined Cases C-278/92, C-279/92 and C-280/92 *Kingdom of Spain v Commission* [1994] ECR I-4103, at paragraph 28.

been acceptable to a private market investor and that the sale of electricity could not have been expected to be sufficiently profitable for a private operator.

- (43) However, in making that assessment the Authority cannot replace the seller's judgment with its own, which implies that the seller of electricity must enjoy a wide margin of judgment. Whilst the Authority fully recognises the right for public companies such as Landsvirkjun to operate on the market on commercial terms, it nevertheless must consider carefully whether similar agreements would have been concluded by a private market investor.¹⁰ Moreover, the Authority must base its assessment of the price and terms of the contracts between Landsvirkjun and ISC on the information available at the time of the conclusion of the contracts.
- (44) Ordinarily, when a sale by a public company or a public authority is assessed, the market price for the good under assessment can be used as a relevant benchmark. In the case at hand, however, a market price is not readily available, given the peculiarities of the Icelandic electricity market. A large majority of all electricity is sold to a few customers, which all have concluded long term agreements with the domestic power providers. Furthermore, the Icelandic market is isolated from the rest of the world, as currently no power can be transmitted elsewhere. The abundant potential to produce electricity in Iceland and this isolation can be assumed to be the main reason for the large difference of the price of electricity in Iceland and elsewhere in the EEA.
- (45) Assessed against this background it appears that the contract at hand is more advantageous for Landsvirkjun than the existing agreements with power-intensive customers as it is less risky and provides a stable, reliable income. First, the base price paid by ISC is higher than the [...] price paid by other large users. In fact, it is approximately as high as the [...] price recorded by Landsvirkjun in the period between [...] and [...]. In addition to that, the "take or pay obligation" for [a considerable share] of the contract power ensures that there will be a constant stream of revenue, regardless of the business success of ISC.
- (46) Second, the contract contains [...] annual increases, which should at least make up for inflation, and does not entail linkages to world market prices of the product made at the plant to which the power is sold anymore, as was customary in the past. This removes a major business risk for Landsvirkjun from this agreement that was present in former contracts.
- (47) Third, the duration is shorter than that of the average existing contract with power intensive users in Iceland, and should allow Landsvirkjun to adjust its prices to market developments elsewhere better than was possible in the past.
- (48) Fourth, the fact that the price for the additional 30 MW that Landsvirkjun will deliver from 2016 onwards is higher than the electricity price on the basis of which the Authority demonstrated the profitability of the Búðarháls Hydro Power plant in its decision 391/11/COL on the power contract between the Landsvirkjun and Alcan, is another indicator for the contract to be on market terms.

¹⁰ See the Authority's guidelines, Part IV Rules on public service compensation, state ownership of enterprises and aid to public enterprises, Application of state aid provisions to public enterprises in the manufacturing sector, paragraph 5(1).

(49)

- (50) For the above reasons, the Authority concludes that the terms of the contract fall within the margin of discretion that public companies enjoy in running their business. On the basis of the information provided by the Icelandic authorities, the Authority can conclude that conditions of the power contract does not entail an advantage for ISC.

1.3 Conclusion on the presence of aid

- (51) As the power contract does not entail an advantage for ISC, and the criteria laid down in Article 61(1) EEA are cumulative, the Authority will not assess in this decision whether the remaining conditions for a measure to be state aid are met.

2. Procedural requirements

- (52) Pursuant to Article 1(3) of Part I of Protocol 3, “the EFTA Surveillance Authority shall be informed, in sufficient time to enable it to submit its comments, of any plans to grant or alter aid (...). The State concerned shall not put its proposed measures into effect until the procedure has resulted in a final decision”.
- (53) By submitting a notification of the power contract with a letter dated 17 May 2011 (Event No 598580 and 598929), the Icelandic authorities have complied with the notification requirement.
- (54) The Authority can therefore conclude that Icelandic authorities have respected their obligations pursuant to Article 1(3) of Part I of Protocol 3.

3. Conclusion

- (55) On the basis of the foregoing assessment, the Authority considers that the notified power contract does not constitute state aid within the meaning of Article 61(1) of the EEA Agreement.

HAS ADOPTED THIS DECISION:

Article 1

The EFTA Surveillance Authority considers that the notified power contract between Landsvirkjun and ISC does not constitute state aid within the meaning of Article 61(1) of the EEA Agreement.

Article 2

This Decision is addressed to the Republic of Iceland.

Article 3

Only the English language version of this decision is authentic.

Decision made in Brussels, on 14 December.

For the EFTA Surveillance Authority

Oda Helen Sletnes
President

Sverrir Haukur Gunnlaugsson
College Member