

Case No: 63616  
Event No: 498592  
Dec. No: 787/08/COL

EFTA SURVEILLANCE AUTHORITY DECISION  
of 17 December 2008  
regarding the Danice project  
(Iceland)

THE EFTA SURVEILLANCE AUTHORITY<sup>1</sup>,

Having regard to the Agreement on the European Economic Area<sup>2</sup>, 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<sup>3</sup>, in particular to Article 24 thereof,

Having regard to Article 1(3) of Part I and Article 4(2) of Part II of Protocol 3 of the Surveillance and Court Agreement<sup>4</sup>,

Having regard to the Authority's Guidelines on the application and interpretation of Articles 61 and 62 of the EEA Agreement<sup>5</sup>,

Whereas:

## I. FACTS

### 1 Procedure

Pursuant to Article 1(3) of Part I of Protocol 3, the Icelandic authorities notified the so-called Danice project by letter of 21 November 2007 (Event No 453326).

By letters dated 18 January 2008 (Event No 461046), 16 April 2008 (Event No 468449) and 15 September 2008 (Event No 483006), the Authority requested additional information from the Icelandic authorities.

---

<sup>1</sup> Hereinafter referred to as the Authority.

<sup>2</sup> Hereinafter referred to as the EEA Agreement.

<sup>3</sup> Hereinafter referred to as the Surveillance and Court Agreement.

<sup>4</sup> Hereinafter referred to as Protocol 3.

<sup>5</sup> Guidelines on the application and interpretation of Articles 61 and 62 EEA and Article 1 of Protocol 3 to the Surveillance and Court Agreement, adopted and issued by the Authority on 19 January 1994, published in the Official Journal of the European Union OJ L 231 of 03.09.1994, p. 1 and EEA Supplement No 32 of 03.09.1994, p. 1. Hereinafter referred to as the State Aid Guidelines.

The updated version of the State Aid Guidelines is published on the Authority's website:

<http://www.eftasurv.int/fieldsOfWork/fieldstateaid/guidelines/>

By letters dated 18 February 2008 (Event No 465552), 26 May 2008 (Event No 478334), 12 June 2008 (Event No 481156), 18 July 2008 (Event No 486382) and 17 October 2008 (Event No 495494), the Icelandic authorities replied to the respective information requests. On 3 December 2008 (Event No 500837), the Icelandic authorities sent another letter.

The case was subject to discussions between the Icelandic authorities and the Authority in two meetings held in Brussels on 22 November 2007 and 4 March 2008 as well as during the Package Meeting that took place in Reykjavik on 24 October 2008.

By letter dated 14 April 2008 (Event No 474970), Hibernia Atlantic Cable Systems Limited (hereinafter referred to as Hibernia) lodged a complaint with the Authority alleging that the Danice project contains elements of incompatible state aid.

## **2 Description of the Danice project**

### **2.1 The construction of a telecommunications cable**

The Danice project concerns the construction of an undersea telecommunications cable between Iceland and Denmark.

From 2004 onwards, two cables, CANTAT-3 and Farice 1, have provided the main gateway for international connectivity in Iceland while satellite links have been primarily used for restoration. According to the information provided by the Icelandic authorities, CANTAT-3 had several failures in the past, is obsolete and will thus cease to operate in the near future. Farice hf. (the owner of the Farice 1 cable) has for some time been planning to lay a new undersea cable ensuring alternative international connectivity for Iceland.

Moreover, according to the information provided by the Icelandic authorities, the Icelandic Government had received requests from the IT sector, financial institutions, banking and government institutions to build a new undersea cable. In addition, server farms and data centres have shown an interest in establishing themselves in Iceland; on the condition that sufficiently broad and reliable connectivity is put in place.

According to the notification, E-Farice ehf.<sup>6</sup> will build a new cable linking the south of Iceland with Denmark, the so-called Danice cable. On the Icelandic side, the landing of the new cable will be in Landeyjar, where a new cable station facility will be built. The plan is to use Tele Denmark's (TDC) cable station facilities in west Denmark for the Danish end. To begin with, the capacity of the Danice cable will be 100GB/s, although the cable will be built to support up to 4 000GB/s. The terminal locations at either end of the cable will be in Reykjavik and Amsterdam. The intention is to lease managed capacity and/or dark fibre from competitive providers for the routes from the landing stations to the points of presence.<sup>7</sup>

Farice 1, which links Iceland with the Faroe Islands and Scotland, and the new Danice cable will be operated as one system. According to the information provided by the Icelandic authorities this will be a technically safe system with seamless redundant

---

<sup>6</sup> On the relationship between Farice hf. and E-Farice ehf. and the company structure, see Section 2.2.

<sup>7</sup> A point-of-presence (POP) is an artificial demarcation point or interface point between communications entities

connectivity if failure of one cable occurs.<sup>8</sup> For that reason, as part of the project, the Farice 1 cable will be upgraded to 100GB/s in order to ensure that Farice 1 can substitute Danice in case of breakdown. The land routes of Farice 1 within the UK and Iceland will also be upgraded.

## **2.2 Ownership structure of the companies Farice hf. and E-Farice ehf.**

Farice hf. was established to build and operate the Farice 1 cable, which has been in operation since 2004. The company was owned by Icelandic and Faroese shareholders. The Icelandic shareholders were the Icelandic State (42,3%), the incumbent telecoms operator, Síminn hf. (now Skipti hf.) (30,3%), and Og fjarskipti ehf. (Vodafone) (9,0%). Moreover, various minor shareholders hold 0,1 % of Farice hf's shares. The Icelandic shareholders established a holding company called E-Farice ehf. to take care of their interests in Farice hf.

In a letter dated 18 February 2008, the Icelandic authorities informed the Authority that following the capital increase necessary for the financing of the Danice project, E-Farice ehf. and Farice hf. were merged into one company, to be known as Farice hf.

Nonetheless, the Authority will assess the notified capital increase under the circumstances in which it took place, *i.e.* before the merger was completed.

## **2.3 The financing of the new cable**

According to the information provided by the Icelandic authorities, a consultancy firm, ParX Business Consulting, was engaged to evaluate the costs and the financing of the so-called Danice project. It estimated the capital expenditure of the new Danice undersea cable, including the cost of landing stations, to be EUR 54.6 million. Although the capacity from the Danish landing station to Amsterdam will most likely be leased from TDC, it was assumed that certain terrestrial fibre installations would be needed in Iceland, at a cost of EUR 2.6 million. The total cost of upgrading of the Farice 1 cable was estimated to be EUR 14 million. The total investment was therefore EUR 71.2 million. Annual operating costs of both cables, Farice 1 and Danice, were estimated to be EUR 4.1 million.

At the time of the notification, the Icelandic authorities stated that the project would be financed by an increase in equity in E-Farice ehf. (30%) and by long term loans (with a maturity of 18 years with equal annual payments) (70%). According to the information provided by the Icelandic authorities, the construction of the Danice cable and the necessary upgrading of the existing Farice 1 cable, would require that ISK 1 877 million in new capital be invested in E-Farice ehf.

At the time of the notification, the Icelandic State planned to participate in the increase in equity and inject ISK 391.2 million. Moreover, three new shareholders (the energy utilities Landsvirkjun, Orkuveita Reykjavíkur and Hitaveita Suðurnesja<sup>9</sup>) would buy into the company by injecting equity of ISK 495.3 million each so that the capital injection from the three new shareholders together would amount to ISK 1 486 million.

In a letter dated 18 February 2008, the Icelandic authorities stated that changes had been made to the notification regarding participation in the equity of E-Farice ehf. According to the Agreement on share-capital increase, signed by the parties to E-Farice ehf. on 17

---

<sup>8</sup> Redundant connectivity avoids interruption of the service. Seamless redundancy means that no data is lost even in the time period between the breakdown of one processor and the take over by the back-up.

<sup>9</sup> Hereinafter referred to collectively as the Energy Companies.

December 2007 (the Shareholders Agreement), together with the three new shareholders, two of the three original Icelandic shareholders would participate in the share capital increase: the Icelandic State and Og fjarskipti ehf. (Vodafone). The latter would invest ISK 207.5 million and the capital injection by the State would be reduced accordingly, to ISK 185.5 million.

The ownership structure of E-Farice ehf., both before and after the capital increase, is shown in the table below (figures in ISK):

E-Farice ehf - shareholders	Capital before increase		New Capital		Total Capital after increase	
Icelandic State	552,1 m.kr.	51,8%	183,5 m.kr.	9,8%	735,6 m.kr.	25,0%
Skipti hf (Siminn)	395,5 m.kr.	37,1%	0,0 m.kr.	0,0%	395,5 m.kr.	13,4%
Og fjarskipti ehf (Vodafone)	117,8 m.kr.	11,1%	207,5 m.kr.	11,1%	325,3 m.kr.	11,1%
The three power companies	0,0 m.kr.	0,0%	1.486,0 m.kr.	79,2%	1.486,0 m.kr.	50,5%
<b>Total</b>	<b>1.065,3 m.kr.</b>	<b>100,0%</b>	<b>1.877,0 m.kr.</b>	<b>100,0%</b>	<b>2.942,3 m.kr.</b>	<b>100,0%</b>

### 3 Comments by the Complainant

Hibernia Atlantic (hereinafter Hibernia) submitted a complaint against Iceland to the Authority on 14 April 2008, alleging *inter alia* that the Danice project is in breach of the EEA rules on (i) public procurement, (ii) state aid, and (iii) competition.

According to Hibernia, in the absence of a public tender, the EEA rules on public procurement have been breached, notably as a result of the fact that the Danice project will be operated by the same actor as is operating the present cable, and thus distorts competition on the market. Indeed, the third point made by the complainant raises questions as to the compatibility of the project with the competition rules in the EEA Agreement.

Concerning the rules on state aid, the core issue, according to the complainant, is to establish whether the capital injection by the four entities in E-Farice ehf. (i.e. the Icelandic State, Landsvirkjun, Orkuveita Reykjavíkur and Hitaveita Sudurnesja) is in conformity with the so-called *market investor principle*. The complainant claims that there is state aid involved where fresh capital is contributed in circumstances that would not be acceptable to a private investor operating under normal market economy conditions, and refers, in particular, to Sections 6(b) and (c) of the State Aid Guidelines on Public authorities' holdings. In this respect, the complainant claims that the Energy Companies are 'public authorities' within the meaning of those guidelines, with the possible exception of Hitaveita Suðurnesja, 32% of which is owned by a private party.

With reference to the decision of the Authority from 2006 concerning the original Farice project, the complainant concludes that a capital increase in E-Farice ehf. by four public entities, in order to set up and operate an undersea telecommunications cable such as Danice, would constitute state aid within the meaning of Article 61 EEA.

In support of this conclusion, the complainant cites the absence of private participation in the project, although he then mentions the capital injection by Vodafone. The complainant also acknowledges that companies with a connection to the potential new business that the establishment of Data Centres will bring might be willing to invest some capital in the project, and cites Orkuveita Reykjavíkur as an example.

Finally, the complainant doubts that the aid can be declared compatible with the functioning of the EEA, notably because there are private operators (i.e. Hibernia) that are

ready to increase connectivity between Iceland and Europe, thus indicating that the injection of public funds is not necessary.<sup>10</sup>

#### **4 Comments by the Icelandic authorities**

The Icelandic authorities have stated that the measure under examination does not constitute state aid within the meaning of Article 61(1) EEA. In their view, the criterion relating to an “advantage” is not fulfilled in this case due to the fact that the involvement of the Icelandic State is based on the market investor principle. Nevertheless, they have notified the project for reasons of legal certainty.

The Icelandic authorities have mentioned paragraph (6) of the State Aid Guidelines on Public authorities’ holdings, and stated that there is no market reluctance towards the project and that the State is simply behaving like a private investor in the market, in line with the above mentioned paragraph. The facts show that the private investors’ holdings in the project have real economic significance.

If the increase in the share capital took place in a situation in which no private investor was increasing its share capital in the same proportion, this would constitute an advantage to E-Farice ehf. and a drain on state resources. However, in the view of the Icelandic authorities, contrary to the Farice project, this is not the case concerning the Danice project.

Additionally, given that the Shareholders Agreement contains a clause with a required internal rate of return for the project, the Icelandic authorities consider that this support should be regarded as a non-aid measure in line with the market investor principle.

Finally, two expert reports evaluating the investments in E-Farice ehf. necessary to carry out the so-called Danice project have been presented and both conclude that the project is an interesting investment.

##### **4.1 The ParX evaluation**

The company ParX Business Consulting submitted a Memorandum to the Managing Director of E-Farice ehf. on the Danice project on 25 September 2007 assessing the general assumptions about investment, operation and financing of the new cable.<sup>11</sup> The financial plan for the Danice project is based on real cost figures from the Farice 1 project, offers from providers of equipment and services and advice from current service providers of Farice 1.

In the financial plan of the Danice project, revenues are estimated to cover payments of all loans, interests and dividends during the estimated duration of the cable (20 years), as well as the equity. Refinancing of the Farice cable is also included in the financial plan.

The ParX evaluation came to the conclusion that the return on equity for this investment could correspond to 18,7% taking into account a 4,66% Euribor with a mark-up of 200 basis points for interest rate on loans, inflation in the Eurozone corresponding to 2% and a weighted average cost of capital of 8,76%.

---

<sup>10</sup> Indeed, the complainant notes that he had announced plans to build and operate a cable to Iceland in August 2007, before the Icelandic Government made public its plans in relation to the Danice project.

<sup>11</sup> Annex 7 to the notification (Event No 453349).

The ParX calculation mentioned a potential future opportunity in the fact that the new Danice cable system could enable the offering of a new route across the Atlantic, connecting Scandinavia and Central Europe to North America together with Tele Greenland's "Greenland Connect" system. However, the potential benefits of this connection were not included in the project plans.

#### 4.2 The evaluation made by a second expert

The Icelandic authorities commissioned an additional assessment of the business case by a second expert, Arnthor Halldorsson. Mr. Halldorsson was asked to evaluate the Danice submarine cable project at the time the investment decision was adopted, i.e. prior to September 2007. The evaluation was submitted to the Authority by the Icelandic authorities in May 2008.<sup>12</sup>

The evaluation made by the second expert was based on the consolidated accounts of E-Farice ehf.<sup>13</sup> The expert used the discounted cash flow method and a credit analysis of the project and concluded that the project had overall very favourable results. Therefore, obtaining debt financing in accordance with the assumptions presented, i.e. financing approximately 75% of the Danice project cost (EUR 53.3 million) was considered realistic.

The expert estimated a weighted average cost of capital corresponding to 7,99% with a return on equity equal to 15%. Mr. Halldorsson carried out a sensitivity analysis considering the "Worst Case Scenario" (no data centre) and a "Bull Case Scenario" (two data centres) and came to the conclusion that "*the results are very good on all accounts*".

## II. ASSESSMENT

### 1 The presence of state aid

In order to reach the conclusion presented by the Icelandic authorities, that the notified capital injection by the Icelandic State does not amount to state aid, it has to be established whether the participation of the State in the capital increase in relation to E-Farice ehf. is in conformity with the market investor principle. In case the State's investment was not carried out in accordance with the market investor principle, the Authority will assess whether it constitutes state aid within the meaning of Article 61(1) EEA.

As mentioned above, the total capital injection in E-Farice ehf. was ISK 1 877 million. That capital injection came mainly from three new shareholders in the company: the electricity companies Landsvirkjun, Orkuveita Reykjavíkur and Hitaveita Sudurnesja. The three companies together provided nearly 80% of the new capital required for the Danice project and contributed ISK 1 485.9 million (i.e. each of the utilities invested ISK 495.3

---

<sup>12</sup> Event No 494184.

<sup>13</sup> The following documentation was relied on for the purposes of the evaluation:

- E-Farice ehf. and Farice hf. annual statement for 2006
- A business case and memorandum prepared by ParX – IBM consulting
- Draft Shareholders Agreement outlining the terms of a new share issue in E-Farice ehf.
- Draft Pre-Contract between E-Farice ehf. and Verne Holding
- Agreement between Greenland Telecom and E-Farice ehf. for termination of the Greenland subcable in Iceland and access to London PoP through Danice
- Farice I Loan Agreement.

million). Following the capital increase, the Energy Companies own 50,5% of E-Farice ehf.

Og fjarskipti ehf. (Vodafone), one of the two original shareholders together with the Icelandic State, also participated in the capital increase with a fresh capital injection of ISK 207.5 million. This capital injection ensured that the company maintained the share of ownership it had in E-Farice ehf. before the capital increase (i.e. 11,1%).

Although the State's share in E-Farice ehf. amounted to 51,8 %, it only contributed ISK 183.5 million to the capital increase, which corresponds to approximately 9,8% of the total capital injected. Therefore, after the capital increase, the State's share in E-Farice ehf. fell to 25%.

The only existing shareholder in E-Farice ehf. which did not participate in the capital increase was Skipti hf. (Síminn hf.). Accordingly, its ownership share in E-Farice ehf. has decreased from 37,1% to 13,4%.

The question is therefore whether, in light of the other participants in the capital increase, the capital injection by the Icelandic State can be considered to have taken place on normal market terms.

The Chapter of the State Aid Guidelines on Public authorities' holdings describes the general approach of the Authority with regard to the acquisition of share holdings by public authorities.

Those guidelines recall the principle of impartiality with regard to the system of property ownership expressed in Article 125 EEA. This means that the Authority's action may neither penalise nor favour public authorities which provide companies with equity capital.

The guidelines distinguish between four types of cases in which public authorities may have occasion to acquire a holding in the capital of companies. The participation in an increase in share capital in a company is applicable to the case at hand, which concerns the participation by the Icelandic State in the capital increase in E-Farice ehf.

According to Section 6(b) of the guidelines, no state aid is involved where fresh capital is contributed to an undertaking in circumstances that would be acceptable to a private investor operating under normal market economy conditions. This can apply when public holdings in a company are to be increased, provided that the capital injected is proportionate to the number of shares held by the authorities and goes together with the injection of capital by a private shareholder. The private investor's holding must have real economic significance.

In the present case, the increase in capital provided by the Icelandic State in fact leads to a decrease in its shareholding overall because, in addition to fresh capital from Og fjarskipti ehf. (Vodafone), three new entities inject capital into E-Farice ehf. (the Energy Companies).

Looking first at Og fjarskipti ehf. (Vodafone), this private operator, despite initial reluctance<sup>14</sup>, decided to inject the capital necessary to maintain its former shareholding of 11,1%. Both proportionately and in real monetary terms, this is a greater contribution to

---

<sup>14</sup> When the Danice project was first notified to the Authority, no participation by Og fjarskipti ehf. (Vodafone), was envisaged.

the total capital increase than that made by the Icelandic State. It may also be concluded that ISK 207.5 million (which is equal to 176% of the capital previously invested by Og fjarskipti ehf. (Vodafone) and 11,1% of the new capital injected) cannot be said to be economically insignificant.

It therefore appears that the circumstances described in Section 6(b) of the State Aid Guidelines on Public authorities' holdings are present in relation to the Danice project and the injection of fresh capital does not amount to state aid.

However, the Icelandic authorities also refer to the significant participation by the Energy Companies in the capital increase. Thus, for the sake of completeness and given that the complainant alleges that these utilities are themselves public undertakings, the Authority will consider the significance of the capital injected by those companies.

As underlined by the complainant, Landsvirkjun is a state-owned utility in the form of a partnership. Orkuveita Reykjavíkur is a limited liability company owned by several municipalities. The third utility participating in the new capital injection, Hitaveita Suðurnesja, is a limited liability company owned mainly by the municipalities of the Reykjanes peninsula and the Icelandic State. However, in this company approximately one third of the shares are held by private entities.

Before the participation by these companies in the project can be used to support the conclusion that the capital injected by the Icelandic State was contributed in circumstances which would be acceptable to a private investor operating under normal market conditions, it must be verified that the funds from the Energy Companies do not themselves constitute state aid.

In that respect, the judgment of the European Court of Justice (hereinafter referred to as the Court) in *Stardust Marine*<sup>15</sup> is instructive. According to the Court, it has to be determined whether the undertakings in question are under the control of the State and have to be regarded as public undertakings. Article 2 of the Transparency Directive<sup>16</sup> defines a “public undertaking” as any undertaking over which the public authorities may exercise directly or indirectly a dominant influence by virtue of their ownership of it, their financial participation therein, or the rules which govern it. A dominant influence on the part of the public authorities shall be presumed when these authorities, directly or indirectly in relation to an undertaking: (i) hold the major part of the undertaking's subscribed capital; or (ii) control the majority of the votes attaching to shares issued by the undertakings; or (iii) can appoint more than half of the members of the undertaking's administrative, managerial or supervisory body.

Landsvirkjun is 100% state-owned.<sup>17</sup> It is organised as a so-called jointly owned enterprise (*sameignarfyoirtæki*) and is governed by Act 42/1983, as amended by Act 154/2006. According to Article 5 of the Landsvirkjun Act, the Minister of Finance appoints the board of directors in the General Assembly. The five members of the board shall safeguard only the interests of Landsvirkjun when serving on the board.

---

<sup>15</sup> Case C-482/99 *France v Commission* [2002] ECR I-4397.

<sup>16</sup> The Act referred to at point 1a of Annex XV to the EEA Agreement, *Commission Directive 2006/111/EC of 16 November 2006 on the transparency of financial relations between Member States and public undertakings as well as on financial transparency within certain undertakings* (Codified version), published in the OJ L 318 of 17.11.2006, p. 17. Published in the OJ L 266 of 11.10.2007, p. 15 and EEA Supplement No 48 of 11.10.2007, p. 12.

<sup>17</sup> The City of Reykjavik sold its shares to the State and as of 1 January 2007 Landsvirkjun is jointly owned by the State (99,9%) and Eignarhlutir ehf. (0,1%), a limited liability company wholly owned by the State.

Orkuveita Reykjavíkur is also a jointly owned enterprise, created following the merger of various municipality utilities and operated on the basis of Act 139/2001. According to Article 3 of that Act and Article 6 of the Partnership Agreement, a board of six directors elected for one year at a time manages the company between the General Assemblies. Five board members are elected by the City Council of Reykjavík and one by the municipality of Akranes. The City Council of Reykjavík elects the chairman and vice-chairman.

Hitaveita Suðurnesja<sup>18</sup> is a limited liability company. As of 2007, the shareholders in Hitaveita Suðurnesja hf. were the Town of Reykjanes (34,75%), Geysir Green Energy (GGE, an investment company founded in 2007) (32%), Orkuveita Reykjavíkur (16,58%), Town of Hafnarfjörður (15,42%) and others (1,25%). The board is comprised of seven members: three from the Town of Reykjanes, two from GGE, one from Orkuveita Reykjavíkur and one from the Town of Hafnarfjörður.

On the basis of this information, the Authority considers that the three Energy Companies can be considered as public undertakings within the meaning of the Transparency Directive.

Nevertheless, even if the State is in a position to control a public undertaking and to exercise a dominant influence over its operations, actual exercise of that control in a particular case cannot be automatically presumed.<sup>19</sup> A public undertaking may act with more or less independence, according to the degree of autonomy left to it by the State. Therefore, the mere fact that a public undertaking is under state control as regards its ownership is not sufficient for measures taken by that undertaking, such as the participation in the share capital increase in E-Farice ehf. in question in this case, to be imputed to the State. Rather, it is necessary to examine whether, in fact, the public authorities must be regarded as having been involved, in one way or another, in the adoption of those measures.

On that point, it cannot be demanded that it be demonstrated, on the basis of a precise inquiry, that in the particular case the public authorities specifically incited the public undertaking to take the measures in question.<sup>20</sup> Indeed, it will, as a general rule, be very difficult for a third party, precisely because of the privileged relations existing between the State and a public undertaking, to demonstrate in a particular case that aid measures taken by such an undertaking were in fact adopted on the instructions of the public authorities. For those reasons, it must be accepted that the imputability to the State of a measure taken by a public undertaking is to be inferred from a set of indicators arising from the circumstances of the case and the context in which that measure was taken.

In concluding that a measure taken by a public undertaking is imputable to the State, the Court has stated that the following indicators might be relevant: *“its integration into the structures of the public administration, the nature of its activities and the exercise of the latter on the market in normal conditions of competition with private operators, the legal status of the undertaking (in the sense of its being subject to public law or ordinary company law), the intensity of the supervision exercised by the public authorities over the management of the undertaking, or any other indicator showing, in the particular case, an involvement by the public authorities in the adoption of a measure or the unlikelihood of*

---

<sup>18</sup> According to the information available to the Authority, on 1 December 2008, the shareholders in Hitaveita Suðurnesja hf. decided to divide the company into two different companies: HS Orka hf. and HS Veitur hf. Thus, Hitaveita Suðurnesja hf. no longer exists as a single company.

<sup>19</sup> Case C-482/99 *France v Commission*, cited above at footnote 15, paragraph 52.

<sup>20</sup> Case C-482/99 *France v Commission*, cited above at footnote 15, paragraph 53.

*their not being involved, having regard also to the compass of the measure, its content or the conditions which it contains.”<sup>21</sup>*

According to the information available to the Authority, none of the Energy Companies are integrated into the structures of the public administration but are independently organised as either a partnership<sup>22</sup> (in the case of Landsvirkjun and Orkuveita Reykjavíkur) or a limited liability company, subject to common Icelandic company law (in the case of Hitaveita Sudurnesja).

The nature of the activities carried out by the three Energy Companies is mainly the sale of electricity although some of them are also active in other sectors such as telecommunications in the case of Orkuveita Reykjavíkur<sup>23</sup> or engineering and energy related activities in the case of Landsvirkjun<sup>24</sup> and Hitaveita Sudurnesja<sup>25</sup>. The sale of electricity constitutes an economic activity which is carried out on a liberalised market throughout the EEA. Such an activity cannot be considered as related to the duties of the State as an administration and is carried out on the basis of purely economic considerations.

In the Authority’s view, based on the information provided in the case at hand, nothing indicates that there was any direct involvement of either the State or any of the municipalities owning any of the three Energy Companies concerned. On the contrary, in a letter forwarded by the Icelandic authorities, the three utilities explain that they became interested in the Danice project in early 2007 when the concept of building large scale data storage facilities in Iceland became a viable opportunity. They explained that it had become apparent that Iceland needed new investment in an undersea cable, “*a critical and essential infrastructure*”, to make Iceland a viable alternative to other international locations competing for such business: “*Not only did the Energy Companies see the need for a new submarine cable to facilitate Foreign Direct Investment but also as a profitable undertaking in its own right*”.<sup>26</sup>

In the negotiations with E-Farice ehf., the Energy Companies inserted a condition that they, collectively, hold a majority stake in E-Farice ehf. and that they would thereby

<sup>21</sup> Case C-482/99 *France v Commission*, cited above at footnote 15, paragraph 56.

<sup>22</sup> Both are established by special laws: Landsvirkjun is a jointly owned enterprise according to Art 1(1) of Act No 42/1983 and Orkuveita Reykjavíkur is a jointly owned enterprise operated on the basis of Act No 139/2001.

<sup>23</sup> Orkuveita Reykjavíkur wholly owns Gagnaveita Reykjavíkur which provides the electronic communications services through its fibre optic network, see <http://www.gagnaveita.is/>. Orkuveita Reykjavíkur also provides geothermal water for heating, and cold water for consumption and fire fighting. See <http://www.or.is/English/About/>

<sup>24</sup> Landsvirkjun owns a significant amount of shares in companies such as Þeistareykir ehf.(32,0%) which is active in geothermal activities, and Netorka hf. (40,8%), which furnishes comprehensive information and market services to power users in Iceland and elsewhere through the internet or other electronic media. In early 2007, in partnership with Landsbanki, Landsvirkjun established the limited liability company HydroKraft Invest, an investment company specialised in the renewal, restructuring and construction of power plants in the field of hydropower and other renewable energy sources abroad. In 2007, Landsvirkjun sold its 24,3 % share in Enex hf., a company engaged in research, development and use of energy resources and the distribution and sale of energy.

<sup>25</sup> Hitaveita Suðurnesja hf. handles production and sale of hot water and electric power supply to consumers, freshwater retention for the inhabitants of Sudurnes and the Westman Islands, in addition to selling geothermal steam to industry (see Annual Report 2007, p. 85). Hitaveita Suðurnesja hf. owns 29,3% of Blue Lagoon Ltd, which operates the Blue Lagoon geothermal seawater combined with a wellness and beauty center and sells skin care products (see Annual Report of Hitaveita Suðurnesja hf. for 2007, p. 101 and <http://www.bluelagoon.com/About-Us/>).

<sup>26</sup> Letter to the Ministry of Finance, dated 6 June 2008. This letter was forwarded to the Authority on 12 June 2008 (Event No 481156).

change the role of the company from serving only the Icelandic and Faroe Islands telecommunications markets to become a company that would have a broader purpose and mandate to operate as a profitable venture independent of the business interests of individual shareholders. For the Energy Companies to ensure that E-Farice mandate was to generate a profitable business was a necessary step as they are competing in the market of selling energy and hence uncertain whether they would generate other business in relation to the construction of data centres in Iceland. Thus, the requirement that E-Farice ehf. should generate profits independently of the owners.

The utilities concluded their letter stating that they “*unanimously consider a participation in E-Farice a sound investment with a projected return of the order 15-20 %. At the time of the decision, the risks associated with the investment were considered acceptable*”.

In light of the considerations above, the Authority does not consider the participation of the Energy Companies in the capital increase in E-Farice ehf. to be imputable to the State. It may therefore be concluded that the decision of these companies to participate in the Danice project amounts to a normal investment decision.

When the new capital injection of the Icelandic State is compared to those of the Energy Companies, it is evident that the latter are greater (both in isolation as well as when the three companies are taken together) and indeed constitute the greater part of the investment in pure monetary terms (ISK 1 486 million out of ISK 1 877 million, or 80% of the new capital injected).

Finally, any concern that the motivation for the investment by these companies rests principally on the hope of a future increase in energy sales (an incentive which could not be applied to the capital injection by the Icelandic State) is rendered redundant not only by the statements from the Energy Companies themselves but also by the two expert opinions assessing the viability of the so-called Danice project.

Both experts came to the conclusion that the investment would be objectively profitable. Since both reports came to similar conclusions independently of each other, the Authority has not considered it necessary to request a third independent opinion to evaluate the merit of the investment.<sup>27</sup> In the Authority’s view, the expert reports submitted by the Icelandic authorities support the conclusion that participation by the Icelandic State in the share capital increase in E-Farice ehf. was in conformity with the market investor principle and that the capital injected therefore does not constitute state aid within the meaning of Article 61(1) EEA.

## 2 Conclusion

On the basis of the foregoing assessment, the Authority considers that the notified capital injection by the Icelandic State in E-Farice ehf. does not constitute state aid within the meaning of Article 61(1) EEA.

---

<sup>27</sup> See, by analogy, Case T-366/00 *Scott SA v Commission* [2007] ECR II-797, paragraph 135; Case T-106/95 *FFSA & Others v Commission* [1997] ECR II-229, paragraph 102; and Joined Cases T-371/94 and T-394/94 *British Airways and Others and British Midland Airways v Commission* [1998] ECR II-2405, paragraph 72.

HAS ADOPTED THIS DECISION:

Article 1

The EFTA Surveillance Authority considers that the notified capital injection by the Icelandic State in E-Farice ehf. does not constitute state aid within the meaning of Article 61 EEA.

Article 2

This Decision is addressed to the Republic of Iceland.

Article 3

Only the English version is authentic.

Done at Brussels, 17 December 2008

For the EFTA Surveillance Authority,

Per Sanderud  
President

Kristján Andri Stefánsson  
College Member