

Brussels, 8 March 2023  
Case Nos: 86451 and 88796  
Document No: 1306514  
Decision No 044/23/COL

Ministry of Culture and Business Affairs  
Skúlagötu 4  
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Iceland

**Subject: Alleged State aid to Farice – Decision to open a formal investigation procedure**

## 1 Summary

The EFTA Surveillance Authority ('ESA') wishes to inform Iceland that, having preliminarily assessed the alleged aid to Farice ehf. ('Farice') for performing a seabed survey ('Measure 1') and for investment in a third submarine cable ('Measure 2'), it has doubts as to whether Measure 1 constitutes State aid within the meaning of Article 61(1) of the EEA Agreement and as to whether Measures 1 and 2 are compatible with the functioning of the EEA Agreement. ESA has therefore decided to open a formal investigation procedure pursuant to Articles 4(4), 6 and 13 of Part II of Protocol 3 to the Surveillance and Court Agreement ('Protocol 3'). ESA has based its decision on the following considerations.

## 2 Procedure

- (1) By letter dated 27 January 2021, the Icelandic authorities initiated pre-notification discussions with ESA concerning their plans to increase capital in Farice, in order to invest in a third submarine cable between Iceland and Europe ('the IRIS cable'), i.e. Measure 2 <sup>(1)</sup>.
- (2) On 23 February 2021, ESA received a complaint ('the complaint') from Sýn hf. ('Sýn') regarding Farice <sup>(2)</sup>. Sýn alleged that Farice received public service compensation from the Icelandic authorities in violation of the SGEI rules <sup>(3)</sup>, including compensation for costs related to surveys conducted in preparation for a possible third submarine cable. Sýn also alleged a violation of the standstill obligation as regards Farice's investment in the IRIS cable.
- (3) On 23 February 2021, ESA forwarded the complaint to the Icelandic authorities and invited them to provide comments by 25 March 2021 <sup>(4)</sup>.
- (4) On 23 March 2021, ESA received a formal notification from the Icelandic authorities regarding Measure 2 <sup>(5)</sup>. On 26 March 2021, ESA adopted Decision 023/21/COL on *Aid to Farice ehf. for investment in a third submarine cable*.

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<sup>(1)</sup> Document No 1176447.

<sup>(2)</sup> Document No 1182556.

<sup>(3)</sup> 'SGEI' stands for 'Services of General Economic Interest'.

<sup>(4)</sup> Document No 1182715.

- (5) By email dated 25 March 2021, the Icelandic authorities requested an extension of the deadline to provide comments on the complaint. ESA extended the deadline to 31 March 2021. On 31 March 2021, the Icelandic authorities provided ESA with their initial comments on the complaint <sup>(6)</sup>.
- (6) On 9 July 2021, Sýn lodged an application with the EFTA Court under Article 36 of the Surveillance and Court Agreement ('SCA'), seeking the annulment of Decision No 023/21/COL of 26 March 2021.
- (7) On 20 January 2022, ESA sent a request for information to the Icelandic authorities concerning the complaint <sup>(7)</sup>. On 16 March 2022, the Icelandic authorities provided their response to the request for information <sup>(8)</sup>.
- (8) On 1 June 2022, the EFTA Court annulled Decision No 023/21/COL <sup>(9)</sup>.
- (9) On 21 June 2022, ESA sent the Icelandic authorities a second request for information concerning the complaint <sup>(10)</sup>. The Icelandic authorities responded on 20 September 2022 <sup>(11)</sup>.
- (10) On 8 November 2022, ESA had a meeting with a representative of Sýn <sup>(12)</sup>.

### 3 Description of the measures

#### 3.1 Background

- (11) Farice is a private limited liability company established in Iceland. It was founded in 2002 by Icelandic and Faroese parties. According to its articles of association, the purpose of Farice is the wholesale of international data transfer between countries through a fibre optic cable, the operations of fibre optic cable systems, and the sale of services in relation to such activities. The Icelandic State acquired Farice in full in March 2019 following the classification of international submarine cables as infrastructure. All of Farice's long-term borrowing comes from the Icelandic Treasury
- (12) Farice operates two submarine cables running from Iceland to parts of Europe: FARICE-1 and DANICE. FARICE-1 connects Iceland with Scotland, with a branch unit to the Faroe Islands. DANICE connects Iceland with Denmark. FARICE-1 and DANICE are the only submarine cables running from Iceland to Europe and they intersect in the Atlantic Ocean. A third submarine cable, Greenland Connect, runs from Iceland to Canada via Greenland. Greenland Connect is owned and operated by Tele Greenland. It terminates in Iceland and its traffic is directed through FARICE-1 and DANICE on the way to Europe. It is possible to buy services from Tele Greenland to mainland Canada and from there to New York.
- (13) Between 2010 and 2012, the Icelandic authorities engaged in a series of measures for the restructuring of Farice, due to its financial difficulties. During the

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<sup>(5)</sup> Document No 1189996.

<sup>(6)</sup> Document No 1192410.

<sup>(7)</sup> Document No 1256678.

<sup>(8)</sup> Document No 1276074.

<sup>(9)</sup> Judgment of the EFTA Court in Case E-4/21 *Sýn hf. v EFTA Surveillance Authority* (not yet reported).

<sup>(10)</sup> Document No 1285878.

<sup>(11)</sup> Document No 1313840 and attachments.

<sup>(12)</sup> Document No 1326167.

same period, the Icelandic authorities submitted various State aid notifications to ESA. These were later withdrawn because the Icelandic authorities concluded that the SGEI Decision applied to these measures <sup>(13)</sup>. On 19 July 2013, ESA sent a comfort letter to the Icelandic authorities noting that Article 3 of the SGEI Decision exempted the Icelandic authorities from the prior notification obligation under Article 1(3) of Part I of Protocol 3 SCA <sup>(14)</sup>.

- (14) The first public service contract between Farice and the Telecommunications Fund ('the Fund'), representing the Icelandic authorities, was entered into on 12 April 2012.
- (15) In November 2018, the Minister for Transport and Local Government submitted a proposal to the Icelandic Parliament for a resolution on an electronic communications policy 2019 to 2033 ('the Telecommunication Policy'). The objectives of the policy are, *inter alia*, to promote accessible and effective communications and to guarantee the security of infrastructure. To achieve those objectives, the policy emphasises that three active submarine cables are needed to connect Iceland with the rest of Europe from different landing sites. As a geographically remote country, effective international connections are a prerequisite for the development of Iceland as a modern technology-based society. A serious disruption in international connectivity would cause major damage to the Icelandic economy, and society as a whole.
- (16) Between 2017 and 2020, the Ministry of Transport and Local Government, and the Ministry of Finance and Economic Affairs received several proposals from Sýn regarding the construction of a third submarine cable. The proposals included both an independent project and a collaboration with Celtic Norse AS. These proposals did not entail financing in full by private investors but required cooperation with the Icelandic State and/or Farice.
- (17) On 21 December 2018, Farice signed a new public service contract with the Fund regarding the Icelandic authorities' work on the Telecommunications Policy ('the 2018 PSO Contract'). Farice was engaged to start preparations for the possible construction of a new submarine cable between Iceland and Europe. Farice was compensated for the costs of the preparation work that it undertook on behalf of the Fund, which also included compensation for seabed research to be carried out by Farice in 2019, i.e. Measure 1. The Icelandic State's participation in further investment or costs for a third cable was neither secured nor structured at that time.
- (18) In January 2019, Sýn submitted a formal request for funding of seabed research in preparation for the introduction of the submarine cable project. In February 2019, the Fund refused to engage in any discussions with Sýn, referring to the public service contract concluded with Farice in December 2018, according to which Farice was entrusted with seabed research as an intermediary.
- (19) On 3 June 2019, the Icelandic Parliament approved the Telecommunications Policy.

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<sup>(13)</sup> Commission Decision 2012/21/EU on the application of Article 106(2) of the Treaty on the functioning of the European Union to State aid in the form of public service compensation to certain undertakings entrusted with the operation of services of general economic interest (OJ L 7, 11.1.2012, p. 3, and EEA Supplement No 43, 2.8.2012, p. 56).

<sup>(14)</sup> Document No 664512.

- (20) In December 2019, Sýn and the Board of the Fund had a meeting during which Sýn presented its case for a third submarine cable between Iceland and Ireland. Sýn offered to build a submarine cable for remuneration and required a guarantee that Farice would change its operating model to a so-called 'carrier's carrier' model.
- (21) In March 2020, the Fund engaged an independent expert to evaluate the feasibility of Sýn's and Farice's third cable projects. The expert's report was delivered in April 2020. According to Sýn, the report concluded that the project proposed by Sýn was more cost effective. According to the Icelandic authorities, the expert was instructed not to make recommendations. However, the report included recommendations and relied on available, but allegedly unverified, data from Farice and Sýn.
- (22) By letter of 29 April 2020, the Ministry of Transport and Local Government shared the results of the report with Farice and stated that Farice would be responsible for the project and the envisaged owner and operator of the new submarine cable. The Ministry urged Farice to take account of the fact that Sýn's proposal had been considered more cost effective by the expert. The Ministry stated that it found Sýn's proposal to change the operational model of Farice unacceptable.
- (23) In May 2020, Sýn and Farice held a meeting to explore the details and validity of Sýn's proposal and to confirm pricing and quality from key suppliers. According to the Icelandic authorities, Sýn was not able to confirm the prices because the key suppliers had not been willing to confirm their prices. As the foundation for the discussions between Farice and Sýn was the project's cost effectiveness, which was based on the prices submitted, the discussions were terminated.
- (24) Later in May 2020, the Fund communicated to Sýn that it considered the expiry of the offers to be unacceptable. It further stated that it would therefore not engage in any further discussions with Sýn. It was further stressed that the Fund was not responsible for the project since its role was limited to the provision of funds.
- (25) On 23 February 2021, Sýn lodged a complaint with ESA. Sýn submitted that payments to Farice from the Icelandic State since 2013 had erroneously been classified as a public service compensation as the conditions to be considered as services of a general economic interest had never been met. It further submitted that there was an ongoing breach of State aid rules related to the introduction of a new submarine cable.
- (26) On 23 March 2021, the Icelandic authorities formally notified ESA of their intention to provide aid to Farice for investment in the third cable, i.e. Measure 2. On 26 March 2021, ESA adopted Decision No 023/21/COL approving the measure. That decision was later annulled by the EFTA Court.

### **3.2 Measure 1**

- (27) According to Article 1A of the 2018 PSO Contract between Farice and the Fund, the 'parties [to the agreement] agree that the Fund will compensate Farice for seabed research to be carried out in 2019 for a possible optic fibre cable between Iceland and Europe (Ireland) according to article 12 of this contract'.
- (28) In Article 12 of the same contract, it is further stated that '[t]he Fund intends to do a seabed survey on a route between Europe (Ireland) and Iceland for an optic

fibre cable to be possibly laid in the near future. Farice undertakes the execution of the projects as an intermediary. Preliminary time and cost schedule is described in annex 1. Farice shall aim to deliver a final marine route survey report to the Fund before December 31, 2019'. The temporal scope of the survey was later extended to 2021.

- (29) According to annex 1, the compensated costs related to the survey were: 1) a desk top study; 2) survey; 3) inshore survey; 4) main survey (excluding inshore survey); 5) reporting and maps; and 6) overhead costs. The costs were estimated at EUR 1.9 million.
- (30) In accordance with the contract, Farice undertook the survey in the years 2019, 2020 and 2021. Payments for third party works, for example the work performed by EGS<sup>(15)</sup> (the main survey contractor) were invoiced to the Fund based on costs incurred. Work performed by Farice employees was invoiced on the basis of an hourly rate. Additionally, Farice invoiced an administration fee for general administration costs in 2019.

### 3.3 Measure 2

- (31) In relation to the Icelandic authorities' work on the Telecommunications Policy, the Icelandic authorities selected Farice to build and operate a third submarine cable connecting Iceland and Europe, i.e. the IRIS cable. Measure 2 relates to the financing by the Icelandic State of the IRIS cable through an estimated EUR 50 million capital increase in Farice, which is wholly owned by the Icelandic State<sup>(16)</sup>.
- (32) According to the Icelandic authorities, Farice was chosen because it is the only entity that: (i) currently operates submarine cables from Iceland to Europe, (ii) has extensive experience in such operations, and (iii) was able to work fast in seeing the project through within the desired timeframe.
- (33) Farice is currently operated on commercial terms without financial support from the State<sup>(17)</sup> and offers services on two distinct markets: the market for international connectivity ('international data transfer market') and the data centre market ('DC market').
- (34) The primary objective of the measure and the IRIS cable project is to enhance security and reduce the vulnerability of international connectivity to and from Iceland. The secondary objective is to shorten the digital distance between Iceland and Europe, by reducing data latency.
- (35) The new submarine cable is in principle expected to complement the existing submarine cable infrastructure. According to the Icelandic authorities, the

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<sup>(15)</sup> EGS is an international group of companies with offices in Europe, the Americas, Asia and Australia. EGS provides global specialist multi-disciplinary marine survey support, and delivers solutions to the Telecommunications, Renewables, Oil and Gas, Charting and Marine Infrastructure market sectors. See also <http://www.egssurvey.com/>.

<sup>(16)</sup> For a more detailed description of Measure 2, see Section 3 of ESA's Decision No [023/21/COL](#).

<sup>(17)</sup> In 2013–2018, Farice received public service compensation from the Fund for offering electronic communications connectivity between Iceland and Europe through FARICE-1 and DANICE. The last payment on this basis was made on 4 October 2018.

interconnection to the new cable will be technologically neutral, provided that instructions and recommendations are followed <sup>(18)</sup>.

- (36) Moreover, according to the Icelandic authorities, Farice grants effective wholesale access to the system on an open and non-discriminatory basis and those access obligations will be enforced irrespective of any change in ownership, management or operation of the infrastructure.
- (37) The eligible costs of Measure 2 are the investment costs related to the new cable, costs relating to survey of the seabed and the optimal path of the cable <sup>(19)</sup>, construction of landing sites and project management. The costs are considered investment costs, including project management costs which are directly related to the investment project. The maximum aid intensity is 100% of the eligible costs. The board of directors of Farice authorised the capital increase for established costs in intervals during the construction period of the new cable. According to the Icelandic authorities, any overcompensation is controlled retroactively through a capital decrease, dividend payments or by other available means.
- (38) Farice signed a contract with SubCom LLC, a global undersea fibre optic cable system supply company, to lay the IRIS cable, after having elicited offers from three different suppliers. On 11 November 2022, SubCom formally handed over the IRIS cable, which is expected to be ready for service in the first quarter of 2023 <sup>(20)</sup>.

### 3.4 The Complaint

- (39) As previously mentioned, on 23 February 2021, Sýn submitted a complaint to ESA regarding alleged unlawful State aid measures in favour of Farice. In summary, the complaint concerns three measures:
1. The payment of compensation for services of general economic interest ('SGEI') from the Icelandic authorities to Farice for the public service obligation ('PSO') of providing international connectivity for electronic communication ('the SGEI measure');
  2. compensation paid to Farice for carrying out a seabed survey as an intermediary, i.e. Measure 1; and
  3. non-compliance with the stand-still obligation in relation to the roll-out of the third submarine cable between Iceland and Europe, i.e. Measure 2.
- (40) The SGEI measure, covered by Sýn's complaint, was not the subject of the annulled Decision No 023/21/COL, nor the judgment of the EFTA Court in Case E-4/21. Therefore, this measure is not the subject of this Decision, and is currently being processed separately in an open complaint case <sup>(21)</sup>. Conversely, Measures 1 and 2 are the subject of this Decision.

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<sup>(18)</sup> The new IRIS cable will be based on an open cable architecture which means that customers can be given an access to the infrastructure by using their own terminal equipment. Access to infrastructure can be granted by own fibre pair or fractional fibre pair (spectrum). Furthermore, the technology to use the submarine cable is standardised and based on Ethernet, which is the technology commonly used. A more advanced interface in the form of OTU2, OTU3 and OTU4 is also offered.

<sup>(19)</sup> This refers to different surveys than those covered by Measure 1.

<sup>(20)</sup> See Farice [press release](#) dated 11 November 2022.

<sup>(21)</sup> Case No 86451.

- (41) As regards Measure 1, Sýn submitted that Iceland had under the 2018 PSO Contract agreed to compensate Farice for seabed research to be carried out in 2019. The agreement was later extended (see section 3.2).
- (42) Sýn argued in its complaint that the compensation for the seabed research did not fulfil any of the SGEI criteria, whether under the Altmark conditions <sup>(22)</sup>, the SGEI Decision <sup>(23)</sup>, or the SGEI Framework <sup>(24)</sup>. In particular, Sýn argued that seabed research could not be qualified as a service of general economic interest, and even if it could be, no parameters for the calculation of compensation for such a service had been established.
- (43) As regards Measure 2, Sýn asserted in its complaint that the Icelandic authorities seemed to have entrusted Farice with the roll-out of a new submarine cable funded by the State. In Sýn's view this constituted a breach of the EEA State aid rules. Sýn was unaware that at the time they submitted the complaint, ESA and the Icelandic authorities were engaged in pre-notification discussion regarding the roll-out to the new submarine cable <sup>(25)</sup>.
- (44) Therefore, Sýn submitted that the actions of the Icelandic authorities related to the roll-out of a new submarine cable, including the payment for seabed research under the auspices of a public service obligation, constituted a breach of the EEA State aid rules, which called for action by ESA.

### 3.5 Comments of the Icelandic authorities

- (45) The Icelandic authorities have provided their views as regards Measures 1 and 2. These views were expressed during the notification procedure leading up to Decision 023/21/COL <sup>(26)</sup>, as well as in replies to questions sent to them by ESA in connection to the complaint <sup>(27)</sup>.

#### 3.5.1 Regarding Measure 1

- (46) The Icelandic authorities have maintained that the payments to Farice related to the seabed survey did not constitute compensation for a public service, even though contractual provisions related to the survey were included in the 2018 PSO contract <sup>(28)</sup>.
- (47) Instead, the Icelandic authorities have stated that the work related to the survey was allocated to Farice on market terms, in line with the market economy operator principle. Specifically, the Icelandic authorities contend that the award of the seabed survey did not grant Farice an economic advantage that an undertaking could not have obtained in the absence of State intervention, and that it was, in essence, a service assignment, for which Farice was paid the incurred costs. In

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<sup>(22)</sup> Judgment of 24 July 2003, *Altmark*, C-280/00, EU:C:2003:415, paragraphs 87-93.

<sup>(23)</sup> Commission Decision 2012/21/EU on the application of Article 106(2) of the Treaty on the functioning of the European Union to State aid in the form of public service compensation to certain undertakings entrusted with the operation of services of general economic interest (OJ L 7, 11.1.2012, p. 3, and EEA Supplement No 43, 2.8.2012, p. 56).

<sup>(24)</sup> Framework for State aid in the form of public service compensation (OJ L 161, 13.6.2013, p. 12 and EEA Supplement No 34, 13.6.2013, p. 1).

<sup>(25)</sup> See the Judgment of the EFTA Court in Case E-4/21 *Sýn hf. v EFTA Surveillance Authority*, paragraph 67.

<sup>(26)</sup> Cases 86220 and 86598.

<sup>(27)</sup> Case 86451.

<sup>(28)</sup> Document No 1276074, Section 6.1.

the view of the Icelandic authorities, this is demonstrated by the fact that the Fund, and not Farice, retains all ownership of survey results and that Farice did not *de facto* make a profit for administering the survey.

- (48) Moreover, the Icelandic authorities have submitted that Measure 1 did not distort or threaten to distort competition and did not have any effect on trade between the Contracting Parties.
- (49) Specifically, the Icelandic authorities stated that the measure did not grant Farice a stronger competitive position than it would have had if the survey had not been undertaken, and that Farice was not relieved of expenses it would otherwise have had to bear in the course of its day-to-day business operations. The Icelandic authorities had full discretion to utilise the seabed survey in any way they saw fit and no utilization guarantees were granted to Farice. Therefore, the Icelandic authorities contend that the award of the seabed survey did not strengthen the position of Farice as compared with other undertakings.
- (50) Finally, the Icelandic authorities are of the view that the Fund was exempt from the procurement rules when awarding a contract of carrying out the seabed survey, as it was an essential part of preparing the IRIS cable project and therefore a factor in providing a public communications network.
- (51) Consequently, the Icelandic authorities argue that Measure 1 does not constitute State aid.

### 3.5.2 Regarding Measure 2

- (52) The Icelandic authorities consider Measure 2 to constitute State aid, which is compatible with Article 61(3)(c) of the EEA Agreement, and that the measure falls outside the scope of the Guidelines for the application of State aid rules in relation to rapid deployment of broadband networks ('the 2014 Broadband Guidelines')<sup>(29)</sup>.
- (53) In this regard, the Icelandic authorities note that the measure contributes to a well-defined objective of common interest, i.e. to enhance the security of international connectivity to and from Iceland. The aid measure serves to significantly reduce the vulnerability of Iceland's international telecommunications network in case of major failures of the current systems.
- (54) Further, as regards the need for State intervention, the Icelandic authorities contend that market failure necessitates State participation in the IRIS cable project. Specifically, the Icelandic authorities note that Farice is the only operator of submarine cables connecting Iceland to Europe, and that despite some interest from private parties to lay similar cables in the past, none of those plans have materialised<sup>(30)</sup>. The Icelandic authorities argue that three main causes have adversely affected the feasibility of other submarine projects to the point where none of them materialized: First, laying a single cable to Iceland without having

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<sup>(29)</sup> ESA's Guidelines on the application of the State aid rules in relation to rapid deployment of broadband networks ([OJ L 135, 8.5.2014, p. 49](#) and [EEA Supplement No 27, 8.5.2014, p. 1](#)).

<sup>(30)</sup> The Icelandic authorities mention specifically earlier interest shown by [Emerald and Nordic Networks](#) in 2010-2016, and proposals from Sýn, both independently and in collaboration with Celtic Norse AS, in 2018-2020. These proposals were all dependant on some kind of financial participation by the Icelandic State. For further information see Section 3.2.4 in ESA's Decision No 023/21/COL.



secured redundancy in connections without material cost through another cable has proven problematic. Second, the small size of the Icelandic market is a natural hindrance. Third, the uncertainty of income from international data centre operators disincentivises investment.

- (55) Moreover, the Icelandic authorities point to the fact that Farice required public service compensation from 2012 to 2018 to operate the two existing cables, i.e. FARICE-1 and DANICE, and that Farice's current revenues do not support investment in the IRIS cable.
- (56) Consequently, in the absence of a realistic chance of private actors building the submarine infrastructure needed to secure international connectivity to Iceland, and since Farice's current revenues do not support investment in a third cable, the Icelandic authorities found it necessary to provide Farice with State aid to lay the IRIS cable.
- (57) Moreover, the Icelandic authorities contend that Measure 2 was proportional. In this regard, they note that only established costs were financed through the capital increase. Moreover, the *ex post* control, including a review of any expenses, will keep costs to the minimum necessary.
- (58) Furthermore, the Icelandic authorities have consistently argued that the IRIS project is not subject to public procurement rules, as it is exempt from the Procurement Act <sup>(31)</sup>, with reference to Article 10 of the Act, cf. Article 8 of the Procurement Directive <sup>(32)</sup>, as the Act and the Directive do not apply to contracts for the principal purpose of permitting the contracting authorities to provide or exploit public communications networks or to provide to the public one or more electronic communications services.
- (59) However, when choosing a subcontractor to lay the cable, Farice engaged in discussions with three suppliers, and selected the most economically efficient offer, having taken account of all relevant considerations.
- (60) As regards the expert report that concluded that the proposal of Sýn was more cost effective than the one from Farice, the Icelandic authorities argue that the cost estimate used by the expert was not verified. Further, that Sýn specifically notified the Icelandic authorities that the supposed offer from Vodafone International was no longer valid. Moreover, the conditions on the operational function of the new cable set by the Sýn, as well as concerns regarding national security and critical infrastructure contributed to the decision to entrust Farice with the building of the new submarine cable. Finally, the proposition of Sýn was based on a different business model, not only for the purposes of the new cable but also Farice's operation through the FARICE-1 and DANICE cables. Therefore, the business proposition of Sýn was not relevant for the purposes of the determination of proportionality of the aid measure. Consequently, the Icelandic authorities consider Measure 2 to be proportional.
- (61) Finally, as regards limited negative effects on competition, the Icelandic authorities note that the new infrastructure is principally expected to complement

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<sup>(31)</sup> The Act on Public Procurement [No 120/2016](#).

<sup>(32)</sup> Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC (OJ L 94, 28.03.2014, p. 65, and EEA Supplement No 73, 16.11.2017, p. 53).

the other connections by providing enhanced security for international connectivity favouring the general public and general economic activities in Iceland. Therefore, the Icelandic authorities consider the IRIS cable to not have a material impact on competitiveness of other European markets compared to Iceland. As regards any negative effects the measure might have on the market for international data transfer or the related DC market, the Icelandic authorities consider those effects vastly outweighed by the positive effects of the measure.

### 3.6 ESA Decision No 023/21/COL

- (62) On 26 March 2021, ESA adopted Decision No 023/21/COL, concluding that Measure 2, i.e. the capital increase to finance the investment in the IRIS cable, constituted State aid within the meaning of Article 61(1) of the EEA Agreement. However, as ESA found that no doubts were raised as to the compatibility of the measure with the functioning of the EEA Agreement, it decided not to raise objections to the implementation of the measure.
- (63) ESA noted that the compatibility of State aid for the introduction of broadband networks was normally assessed under the 2014 Broadband Guidelines. However, since the measure specifically targeted the security issues raised by the lack of geographical diversity, it fell outside the scope of the 2014 Broadband Guidelines. ESA stated that it would nevertheless apply the principles of the 2014 Broadband Guidelines by analogy to the extent that they were relevant, because those guidelines were the most detailed guidance available for assessing the compatibility of State aid to broadband infrastructure projects with the EEA Agreement.
- (64) Article 61(3)(c) of the EEA Agreement provides that ESA may declare compatible 'aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest'. Therefore, in order to declare aid compatible, first, the aid must be intended to facilitate the development of certain economic activities or of certain economic areas and, second, the aid must not adversely affect trading conditions to an extent contrary to the common interest<sup>(33)</sup>.
- (65) Under the first condition, ESA examines how the aid facilitates the development of certain economic activities or areas. Under the second condition, ESA weighs up the positive effects of the aid for the development of said activities or areas and the negative effects of the aid in terms of distortions of competition and adverse effects on trade (i.e. conducts a balancing test).
- (66) Concerning the first condition, ESA concluded that Measure 2 facilitated the development in the market for international data transfer services specifically and the markets for electronic communications services in general. Furthermore, ESA found that the selection of Farice, as owner and operator of the third cable, and the selection of a cable manufacturer and installer was exempted from the Icelandic Procurement Act. Further, ESA did not have reasons to believe that the measure was in breach of other relevant EEA provisions.

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<sup>(33)</sup> Judgment of 22 September 2020 in *Austria v Commission (Hinkley Point C)*, C-594/18 P, EU:C:2020:742, paragraphs 18–20.

- (67) Concerning the second condition, ESA concluded that the amount of aid granted through Measure 2 was limited to what was necessary to achieve its objective and therefore proportional. ESA reached this conclusion, *inter alia*, on the basis that the aid amount was limited to the actual costs of the measure and subject to *ex post* control.
- (68) Furthermore, ESA concluded that Measure 2 would not have a material impact on the competitiveness of other EEA markets compared to Iceland, as investment in the IRIS cable was, in and of itself, unlikely to materially alter the dynamics of intra-EEA trade on the relevant market.
- (69) As regards the potential effect on the DC market, ESA noted that the data centre market was not a single market of universal services, since the digital needs of businesses were highly dependent on the applications hosted and operated in the data centres. ESA also noted that, while data centres might be more inclined to invest in projects in Iceland, due to extended capacity and security of the international connection network following the construction of a third cable, that was only one of multiple factors that would influence such a decision. Other factors, such as electricity prices, start-up costs and regulatory environment also influenced such decisions. ESA found that those factors were not altered by the measure.
- (70) Consequently, ESA found that the Icelandic authorities had demonstrated that the socio-economic benefits of Measure 2 outweighed any potential adverse effects on competition or trade between the Contracting Parties, given the safeguards in place to minimise such adverse effects.

### **3.7 EFTA Court Judgment in Case E-4/21**

- (71) On 1 June 2022, the EFTA Court annulled ESA's Decision No 023/21/COL. The Court concluded that ESA should have opened a formal investigation procedure, as ESA had at its disposal information and evidence at the time, which should, objectively, have raised doubts or serious difficulties regarding whether the capital increase to finance the laying of the IRIS cable was compatible with the functioning of the EEA Agreement.
- (72) In particular, the EFTA Court found that ESA was aware of documents that called into question the information at its disposal and on which it relied in the contested decision, without going beyond a mere examination of the information submitted by the Icelandic authorities. These documents related, *inter alia*, to Sýn's complaint of 23 February 2022 and annexes thereto. Specifically, the Court noted a document comparing the proposals of Sýn and Farice, and an email dated 29 May 2020, regarding Sýn's inability to confirm the prices of its proposal. By not obtaining further information on whether Sýn was actually able to confirm its prices, or whether it had been given that opportunity, the Court concluded that ESA failed to satisfy its obligation to conduct a diligent and impartial examination of the notified measure so that it had at its disposal the most complete and reliable information.
- (73) Furthermore, the Court found that Sýn tried to enter the market for international connectivity services, according to the information available to ESA. Yet, in the contested decision, ESA did not consider factors such as potential competitors on the wholesale market for international connectivity, public consultation of stakeholders and entry barriers to that market.

- (74) Finally, the Court found that ESA did not adequately state its reasons for concluding that the notified measure fell outside the scope of the 2014 Broadband Guidelines, and that even though ESA stated in the contested decision that it would apply the guidelines by analogy, where relevant, the Court found little, if any, trace of the principles in the guidelines actually being applied.
- (75) On the basis of, *inter alia*, the above, the Court concluded that there was consistent and objective evidence that demonstrated that ESA adopted the contested decision despite the existence of doubts. Consequently, the Court annulled the Decision.

## 4 Presence of State aid

### 4.1 Introduction

- (76) 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’.
- (77) The qualification of a measure as aid within the meaning of this provision requires the following cumulative conditions to be met: (i) the measure must be granted by the State or through State resources; (ii) it must confer an advantage on an undertaking; (iii) favour certain undertakings (selectivity); and (iv) threaten to distort competition and affect trade.

### 4.2 Measure 1

- (78) In the following chapters, ESA will assess whether the payments from the Fund to Farice for carrying out a seabed survey involve State aid within the meaning of Article 61(1) of the EEA Agreement.

#### 4.2.1 State resources

- (79) According to Article 61(1) of the EEA Agreement, a measure must be granted by the State or through State resources to constitute State aid.
- (80) The Fund has the task of promoting the development of telecommunications in Iceland. The Fund was formed in 2006 on the basis of Act No 132/2005 on the Telecommunication Fund. The main role of the Fund is to allocate funds to: projects aimed at the development of telecommunication infrastructure; projects that contribute to the safety and competitiveness of society in the field of electronic communications; and other telecommunication projects <sup>(34)</sup>.
- (81) According to Article 1 of Act No 132/2005, the Fund is under the ownership of the Icelandic State and its administration falls under the authority of the Ministry of Higher Education, Science and Innovation.
- (82) ESA therefore preliminarily concludes that the payments from the Fund to Farice for carrying out a seabed survey constitute State resources.

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<sup>(34)</sup> <https://www.stjornarradid.is/verkefni/samgongur-og-fjarskipti/fjarskiptasjodur/>.

#### 4.2.2 Advantage

- (83) According to Article 61(1) of the EEA Agreement, a measure must confer an advantage upon an undertaking. An advantage, within the meaning of Article 61(1) of the EEA Agreement, is any economic benefit which an undertaking could not have obtained under normal market conditions <sup>(35)</sup>, thus placing it in a more favourable position than its competitors <sup>(36)</sup>.
- (84) The Icelandic authorities have argued that Measure 1 was concluded on market terms, in line with the market economy operator principle. In order to establish whether or not a transaction carried out by a public body is in line with normal market conditions, ESA will apply the market economy operator test ('MEO test'), comparing the behaviour of the public body to that of similar private economic operators under normal market conditions <sup>(37)</sup>.
- (85) In that respect, it is not relevant whether the intervention constitutes a rational means for the public bodies to pursue public policy considerations. Similarly, the profitability or unprofitability of the beneficiary is not in itself a decisive indicator for establishing whether or not the economic transaction in question is in line with market conditions. The decisive element is whether the public bodies acted as a market economy operator would have done in a similar situation <sup>(38)</sup>.
- (86) Moreover, whether a State intervention is in line with market conditions must be examined on an *ex ante* basis, having regard to the information available at the time the intervention was decided upon. If a State argues that it acted as a market economy operator it must, where there is doubt, provide evidence showing that the decision to carry out the transaction was taken on the basis of economic evaluations comparable to those which, in similar circumstances, a rational market economy operator (with characteristics similar to those of the public body concerned) would have had carried out to determine the profitability or economic advantages of the transaction <sup>(39)</sup>.
- (87) Concerning Measure 1, it is undisputed that the contractual provisions concerning the seabed survey and the payments for that survey were placed in the 2018 PSO Contract between the Fund and Farice, namely Article 1A, 12 and Annex 1. According to the Icelandic authorities, no other provisions of the 2018 PSO Contract applied to the seabed survey <sup>(40)</sup>.
- (88) ESA notes that the Icelandic authorities essentially argue that Articles 1A, 12, and annex 1 of the 2018 PSO Contract do not, in fact, form part of that contract, but are instead a separate service contract made on market terms. This fact raises doubts as to whether the Fund was operating as a market economy operator, when it charged Farice with performing the seabed survey, since such operators

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<sup>(35)</sup> ESA's Guidelines on the notion of State aid as referred to in Article 61(1) of the EEA Agreement ('NoA') ([OJ L 342, 21.12.2017, p. 35](#) and EEA Supplement No 82, 21.12.2017, p. 1), paragraph 66.

<sup>(36)</sup> See for instance Judgment of 5 June 2012, *Commission v EDF*, C-124/10 P, EU:C:2012:318, paragraph 90; Judgment of 15 March 1994, *Banco Exterior de España*, C-387/92, EU:C:1994:100, paragraph 14; and Judgment of 19 May 1999, *Italy v Commission*, C-6/97, EU:C:1999:251, paragraph 16.

<sup>(37)</sup> NoA, Section 4.2.1.

<sup>(38)</sup> NoA, paragraph 76.

<sup>(39)</sup> NoA, paragraph 79.

<sup>(40)</sup> Document No 1313844.

would in general conclude clear and concise contracts when purchasing a similar service.

- (89) Indeed, it appears that the Fund contracted Farice to perform a service, without including in the contract any provisions concerning cost overruns, specifics regarding the scope of the survey, contingencies for failure to perform the obligations of the contract, or specifics regarding what costs could be covered by the service contract. According to documentation from and statements made by the Icelandic authorities, the temporal scope of the survey was later extended, and final costs ran over the cost estimate in annex 1.
- (90) Moreover, ESA has asked the Icelandic authorities to provide all documentation of expert evaluations or independent studies of the cost of carrying out the seabed survey, if any such evaluations or studies were carried out prior to the start of the 2018 PSO Contract. However, according to the Icelandic authorities, no such evaluation exists. Additionally, the Fund does not seem to have considered alternative providers. Therefore, ESA has doubts as to whether the Fund's decision to carry out the transaction was taken on the basis of economic evaluations comparable to those which, in similar circumstances, a rational market economy operator would have taken, as it appears that the Fund committed to paying Farice for a service, without making an evaluation of eventual costs and alternative providers.
- (91) Furthermore, the Icelandic authorities have stated that Farice did not *de facto* make a profit from performing the survey for the Fund. Moreover, it is unclear to ESA whether the Fund derived any economic value from its ownership of the survey results. In fact, since the survey forms part of the preparatory works for a submarine cable, which the Icelandic authorities themselves consider a security measure, it would appear that the purpose of the survey was not economic in nature. Therefore, ESA doubts that the Fund acted as an economic operator, since it rather seems to have been pursuing public policy aims when commissioning the survey.
- (92) Finally, as the Icelandic authorities have already stated that the payments to Farice for the performance of the subsea survey did not entail compensation for a public service obligation, ESA does not see the need at this time to specifically examine whether Measure 1 fulfils the Altmark criteria, or the provisions of the SGEI Decision or Framework.
- (93) Consequently, ESA has doubts whether Measure 1 was concluded on market terms and cannot exclude that an advantage may have been granted in favour of Farice. Accordingly, the Icelandic authorities are invited to comment on this and submit relevant evidence.

#### 4.2.3 Selectivity

- (94) In order for a measure to involve State aid it must be selective in that it favours 'certain undertakings or the production of certain goods'. Measure 1 concerns a contract between the Fund and Farice. Therefore, Farice is the only potential beneficiary. Other undertakings have not concluded similar contracts with the Fund or the Icelandic State. Accordingly, the alleged advantage of Measure 1 would be a selective advantage, as it only concerns one particular undertaking.

- (95) It is therefore ESA's preliminary view that it cannot be excluded that a selective economic advantage was granted to Farice.

#### 4.2.4 *Distortion of competition and effect on trade between Contracting Parties*

- (96) To qualify as State aid within the meaning of Article 61(1) of the EEA Agreement, a measure must be liable to distort competition and affect trade between the Contracting Parties to the EEA Agreement. According to settled case-law, the mere fact that a measure strengthens the position of an undertaking compared with other undertakings competing in intra-EEA trade is considered to be sufficient, in order to conclude that the measure is likely to distort competition and affect trade between the Contracting Parties <sup>(41)</sup>.
- (97) The Icelandic authorities have argued that the measure in question did not distort or threaten to distort competition and did not have any effect on trade between the Contracting Parties, as the measure did not grant Farice a stronger competitive position than it would have had if the survey had not been undertaken. Moreover, they argue that Farice was not relieved of expenses it would otherwise have had to bear in the course of its day-to-day business operations. Therefore, the Icelandic authorities contend that the award of the seabed survey did not strengthen the position of Farice as compared with other undertakings, neither financially nor in other aspects.
- (98) On this point ESA notes that it is not obliged to establish the real effect of the aid on the market, but is only required to show that the aid is liable to distort competition and affect trade. Therefore, for all practical purposes, a distortion of competition within the meaning of Article 61(1) of the EEA Agreement is generally found to exist when the State grants a financial advantage to an undertaking in a liberalised sector where there is, or could be, competition <sup>(42)</sup>.
- (99) Measure 1 concerns payments made to Farice for a seabed survey. The costs covered by those payments included subcontracting costs, as well as Farice's overhead costs, including hourly rates for Farice staff and a general administration fee. Therefore, Measure 1 seems to have placed Farice in a better financial position than it would have been in the absence of Measure 1.
- (100) Moreover, there are multiple undertakings active in the EEA that provide seabed survey services. This is also demonstrated by the fact that Farice itself subcontracted a large portion of the survey.
- (101) Consequently, ESA has doubts as to whether it can be excluded that Measure 1 was liable to distort competition and affect trade within the EEA. The Icelandic authorities are invited to comment and submit relevant evidence on this.

#### 4.2.5 *Conclusion*

- (102) In light of the above, ESA cannot exclude that Measure 1 entailed State aid.

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<sup>(41)</sup> Judgment of the EFTA Court in Case E-6/98 *Norway v EFTA Surveillance Authority* [1999] Ct. Rep. 76, paragraph 59, where it is stated that '[w]hen State financial aid strengthens the position of an undertaking compared with other undertakings competing in intra-Community trade the latter must be regarded as affected by that aid'.

<sup>(42)</sup> NoA, paragraph 187.

### 4.3 Measure 2

- (103) It is uncontested between Sýn and the Icelandic authorities that Measure 2, i.e. the capital increase in Farice to facilitate the investment in the IRIS cable, constitutes State aid within the meaning of Article 61(1) of the EEA Agreement<sup>(43)</sup>.
- (104) ESA therefore preliminarily concludes that Measure 2 constitutes State aid within the meaning of Article 61(1) of the EEA Agreement.

## 5 Aid scheme or individual aid

- (105) ESA notes that Measures 1 and 2 were not granted on the basis of a scheme<sup>(44)</sup>. Measure 1, if found to be aid, would therefore be individual aid. Measure 2 constitutes individual aid.

## 6 Lawfulness of the aid

- (106) Pursuant to Article 1(3) of Part I of Protocol 3 to the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice ('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'.
- (107) The Icelandic authorities did not notify Measure 1 to ESA. ESA therefore concludes that, in the event that Measure 1 is deemed to involve aid, the Icelandic authorities have not respected their obligations under Article 1(3) of Part I of Protocol 3. In this event, Measure 1 would be unlawful aid.
- (108) The Icelandic authorities implemented Measure 2 after ESA approved it by Decision 023/21/COL. However, with the annulment of ESA's approval decision by the EFTA Court, Measure 2 became unlawful.

## 7 Compatibility of the aid

### 7.1 Introduction

- (109) In derogation from the general prohibition of State aid laid down in Article 61(1) of the EEA Agreement, aid may be declared compatible if it can benefit from one of the derogations enumerated in the Agreement.
- (110) Article 61(3)(c) of the EEA Agreement provides that ESA may declare compatible 'aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest'. Therefore, in order to declare the aid compatible, first, the aid must be intended to facilitate the development of certain economic activities or of certain economic areas and, second, the aid must not adversely affect trading conditions to an extent contrary to the common interest<sup>(45)</sup>.

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<sup>(43)</sup> The EFTA Court, in its judgment in Case E-4/21, did not suggest anything to the contrary.

<sup>(44)</sup> See Article 1(e) of Part II of Protocol 3 to the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice ('Protocol 3').

<sup>(45)</sup> Judgment of 22 September 2020, *Austria v Commission (Hinkley Point C)*, C-594/18 P, EU:C:2020:742, paragraphs 18–20.



(111) Under the first condition, ESA examines how the aid facilitates the development of certain economic activities or areas. Under the second condition, ESA weighs up the positive effects of the aid for the development of said activities or areas and the negative effects of the aid in terms of distortions of competition and adverse effects on trade.

## 7.2 Compatibility of Measure 1

(112) The Icelandic authorities have maintained that Measure 1 does not constitute State aid (see Section 3.5.1). Further, they have also stated that despite the fact that the contractual obligations concerning Measure 1 were included in the 2018 PSO Contract between the Fund and Farice, the measure does not constitute compensation for a public service obligation.

(113) Therefore, it would appear that the compatibility of Measure 1, should it be found to constitute aid, could not be examined under Article 59(2) of the EEA Agreement and even if it were, ESA has doubts that the Measure 1 is in line with the provisions of the SGEI Decision or Framework. The Icelandic authorities have not, at this stage, brought forward any other arguments as regards the potential compatibility of the measure.

(114) Therefore, following a preliminary assessment, ESA has doubts at this stage as to whether Measure 1 is compatible with the EEA Agreement. Consequently, ESA invites the Icelandic authorities to provide arguments and evidence to demonstrate that Measure 1 could be considered compatible under the EEA Agreement.

## 7.3 Compatibility of Measure 2

### 7.3.1 Introduction

(115) The Icelandic authorities have invoked Article 61(3)(c) of the EEA Agreement as the basis for the assessment of the compatibility of Measure 2.

(116) On this point, ESA notes that the compatibility of aid for the roll-out of broadband networks, for the purposes of securing coverage, access or connectivity, is normally assessed under the 2014 Broadband Guidelines. On 8 February 2023, ESA adopted new Broadband Guidelines ('the 2023 Broadband Guidelines')<sup>(46)</sup>.

(117) ESA will follow the principles and guidelines set out in the 2023 Broadband Guidelines for the compatibility assessment of all notified aid to broadband networks in respect of which it is called upon to take a decision after 8 February 2023 when the 2023 Broadband Guidelines entered into force. Unlawful aid to broadband networks will be assessed in accordance with the rules applicable on the date on which the aid was awarded<sup>(47)</sup>.

(118) The 2023 Broadband Guidelines were not in effect at the time when Measure 2 was enacted, and therefore cannot serve as a basis for the compatibility assessment of the measure. Therefore, ESA will apply the 2014 Broadband Guidelines, should Measure 2 be considered to fall within their scope. However, the 2023 Broadband Guidelines are based on existing case-law and decision-making practice of the European Commission. Therefore, the 2023 Broadband

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<sup>(46)</sup> See ESA Decision No 004/23/COL *amending the substantive rules in the field of State aid by introducing new Guidelines on State aid for broadband networks* (not yet reported).

<sup>(47)</sup> *Ibid*, Article 1(2).

Guidelines could still be relevant, should Measure 2 fall under the scope of the 2014 Broadband Guidelines, provided they do not place stricter conditions on the beneficiary.

- (119) In general, the 2014 Broadband Guidelines' primary objective is to ensure widespread availability of broadband services to end users or access to higher speed internet. The 2014 Broadband Guidelines state that '[t]hese guidelines summarise the principles of [ESA's] policy in applying the State aid rules [...] to measures that support the deployment of broadband networks in general (Section 2). They explain the application of these principles in the assessment of aid measures for the rapid roll-out of basic broadband and very high speed, next generation access (NGA) networks (in Section 3). [ESA] will apply the guidelines in the assessment of State aid for broadband' <sup>(48)</sup>. This objective has not changed with the adoption of the 2023 Broadband Guidelines, which state that '[t]hese Guidelines provide guidance on how ESA will assess [...] the compatibility of State aid for the deployment and take-up of fixed and mobile broadband networks and services' <sup>(49)</sup>.
- (120) Therefore, the 2014 Broadband Guidelines apply to aid measures that target situations where the market does not provide sufficient broadband coverage or where access conditions are not adequate <sup>(50)</sup>. Conversely, the 2014 Broadband Guidelines do not mention international connectivity, security, international data transfer, or subsea cables, and do not specifically lay down compatibility conditions for measures targeting security issues raised by the lack of geographical diversity and robustness of international connectivity services. Therefore, a measure like the one under assessment, where the objective is increased redundancy, security, and robustness of international connectivity services already available to end customers at high speeds, seems to differ from the general type of measure covered by the 2014 Broadband Guidelines, namely measures concerning the expansion or introduction of broadband networks and services.
- (121) ESA notes that the European Commission, in its Baltic Cable Decision <sup>(51)</sup>, applied the 2014 Broadband Guidelines in its assessment. However, ESA also notes that the measure under assessment in that decision differed significantly from Measure 2. Specifically, it concerned capacity concerns caused by the expected dramatic increase in traffic that could not be supported by the existing infrastructure. Therefore, in addition to security benefits comparable to the ones present in the case at hand, the Baltic Sea Cable targeted (longterm) broadband availability specifically <sup>(52)</sup>. Conversely, Measure 2 does not specifically concern broadband networks or availability.

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<sup>(48)</sup> See the 2014 Broadband Guidelines, paragraph 4.

<sup>(49)</sup> See the 2023 Broadband Guidelines, paragraph 14.

<sup>(50)</sup> See the 2014 Broadband Guidelines, paragraphs 34–35. See also the pre-requisites for defining a service as an SGEI in paragraph 16.

<sup>(51)</sup> Commission Decision SA.36918 (Finland), Baltic Sea Backbone Cable ([OJ C 422, 8.12.2017, p.1](#)).

<sup>(52)</sup> *Ibid*, paragraph 91: 'Thus, the measure facilitates the development of certain economic activities, i.e the provision of **electronic communications services and networks, including the provision of international connectivity**, and indirectly the provision of **broadband services**'. (emphasis added).

(122) However, in its judgment in Case E-4/21, when assessing ESA's conclusion that Measure 2 fell outside the scope of the 2014 Broadband Guidelines, the EFTA Court stated that the conclusion: '[...] is not supported by a sufficient analysis of the scope of application of the Broadband Guidelines. [...] Although the contested decision states that '[t]he Broadband Guidelines' primary objective is ensuring widespread availability of broadband services to end users or access to higher speed internet' and '[t]he particularities of the measure and investment at hand demonstrate that the Guidelines target different types of measures than the one under assessment', it fails to set out what impact these statements should have on the scope of application of the Broadband Guidelines. Accordingly, [...] ESA encountered serious difficulties in its preliminary examination' <sup>(53)</sup>. The Court then further noted 'that irrespective of whether the notified measure in the present case was outside of the scope of the Broadband Guidelines, those guidelines still may provide useful guidance on considerations that are relevant to the assessment of compatibility in general' <sup>(54)</sup>.

(123) Consequently, ESA cannot conclude at this stage to what extent the 2014 Broadband Guidelines apply to the compatibility assessment of Measure 2, and therefore invites the Icelandic authorities to provide further arguments in this regard.

(124) In the event that the Broadband Guidelines do not apply to the measure at hand, Article 61(3)(c) of the EEA Agreement provides that ESA may declare compatible 'aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest'. Therefore, in order to declare the aid compatible, first, the aid must be intended to facilitate the development of certain economic activities or of certain economic areas and, second, the aid must not adversely affect trading conditions to an extent contrary to the common interest.

(125) Under the first condition, ESA examines how the aid facilitates the development of certain economic activities or areas. Under the second condition, ESA weighs up the positive effects of the aid for the development of said activities or areas and the negative effects of the aid in terms of distortions of competition and adverse effects on trade.

### 7.3.2 Facilitation of development of certain economic activities or areas

#### 7.3.2.1 Economic activities or areas supported

(126) Under Article 61(3)(c) of the EEA Agreement, in order to be considered compatible, a measure must contribute to the development of certain economic activities or areas.

(127) The primary objective of the measure is to enhance security and reduce the vulnerability of international connectivity to and from Iceland by building a third submarine cable from Iceland to Europe. The secondary objective is to shorten the digital distance between Iceland and Europe allowing Icelandic people and businesses to make better use of international digital services available in Europe.

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<sup>(53)</sup> Judgment of the EFTA Court in Case E-4/21 *Sýn hf. v EFTA Surveillance Authority*, paragraph 72.

<sup>(54)</sup> *Ibid*, paragraph 73.

- (128) ESA generally considers the construction of a telecommunication infrastructure with a view to its future commercial exploitation to constitute an economic activity<sup>(55)</sup>. Furthermore, the telecommunications market in general constitutes an economic activity. The measure facilitates development in the market for international data transfer services specifically and the markets for electronic communications services in general.
- (129) In view of the above, ESA preliminarily concludes that the measure constitutes aid to facilitate the development of certain economic activities, as required by Article 61(3)(c) of the EEA Agreement.

#### 7.3.2.2 Incentive effect

- (130) State aid is only compatible with the functioning of the EEA Agreement if it has an incentive effect and so effectively facilitates the development of certain economic activities. To establish whether the measure has an incentive effect, it must be demonstrated that it changes the behaviour of the undertaking concerned in such a way that it engages in an activity which it would not carry out without the aid or which it would carry out in a restricted or different manner.
- (131) In Section 6.2.2 of ESA's Decision No 023/21/COL, ESA stated that Measure 2 had an incentive effect. ESA stated that: 1) Farice had historically proven to be unprofitable; 2) the operation of submarine cables in the region was generally unprofitable; 3) the investment in the IRIS cable was unlikely to achieve a profit; 4) the main objective of the cable was to provide enhanced security, which was an externality that did not heavily factor into investment decisions; and 5) few stakeholders had signalled interest in operating submarine cables without State support in the past.
- (132) In light of this, ESA is generally inclined to conclude that Measure 2 had an incentive effect, as it incentivised Farice to make an investment it would not have entered into otherwise. However, the Icelandic authorities are invited to provide further information and reasoning on the incentive effect of the measure.

#### 7.3.2.3 Compliance with relevant EEA law

- (133) The Icelandic authorities consider that the selection of Farice, as owner and operator of the IRIS cable, as well as the selection of cable manufacturer and installer, is exempt from the procurement rules, with reference to Article 10 of the Procurement Act (see also Article 8 of the Procurement Directive).
- (134) Specifically, Article 8 of the Procurement Directive states: 'This Directive shall not apply to public contracts and design contests for the principal purpose of permitting the contracting authorities to provide or exploit public communications networks or to provide to the public one or more electronic communications services. For the purposes of this Article, "public communications network" and "electronic communications service" shall have the same meaning as in Directive 2002/21/EC of the European Parliament and of the Council'. Furthermore, ESA notes that in accordance with Article 2(m) of Directive 2002/12/EC, 'provision of an electronic communications network' means the establishment, operation, control or making available such network.

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<sup>(55)</sup> NoA, paragraphs 202 and 216, and the 2014 Broadband Guidelines, paragraph 7.

- (135) The primary objective of the measure in question is to increase security of international connectivity in Iceland by building a third submarine cable, which in turn will provide the public with more electronic communication services. Therefore, the investment in the submarine cable seems to permit Farice to 'provide or exploit public communications networks', as defined in Article 2(a) of Directive 2002/21/EC. However, ESA cannot conclusively conclude at this stage whether all conditions for the application of the exemption are fulfilled.
- (136) Moreover, according to paragraph 74(c) of the 2014 Broadband Guidelines, '[w]henver the granting authorities select a third party operator to deploy and operate the subsidised infrastructure, the selection process shall be conducted in line with the spirit and the principles of the Public Procurement Directives. It ensures that there is transparency for all investors wishing to bid for the implementation and/or management of the subsidised project. Equal and non-discriminatory treatment of all bidders and objective evaluation criteria are indispensable conditions'.
- (137) However, despite this provision, footnote 91 to paragraph 74(c) states: '[t]he situation is different when the public authority decides to deploy and manage the network directly (or through a fully owned entity) [...] In such cases, [...] (i) the publicly owned network operators shall limit their activity on the pre-defined target areas and shall not expand to other commercially attractive regions; (ii) the public authority shall limit its activity to maintain the passive infrastructure and to grant access to it, but shall not engage in competition on the retail levels with commercial operators and (iii) to have an accounting separation between the funds used for the operation of the networks and the other funds at the disposal of the public authority'.
- (138) Therefore, the applicability of procurement rules in the context of an assessment under the 2014 Broadband Guidelines seems to depend on whether or not the conditions, listed in footnote 91, are fulfilled. The Icelandic authorities have not provided sufficient information in this regard.
- (139) Consequently, ESA has doubts as to whether or not Measure 2 falls under the exemption from procurement rules described above, and as to whether the provisions of the 2014 Broadband Guidelines have effect in this regard. Therefore, ESA invites the Icelandic authorities to provide further information and rationale in this regard.

### *7.3.3 Whether the aid adversely affects trading conditions to an extent contrary to the common interest*

#### 7.3.3.1 Introduction

- (140) ESA has not only identified positive effects of the planned aid for the development of the abovementioned economic activities and economic areas, but also possible negative effects that it may have in terms of distortions of competition and adverse effects on trade. These positive and negative effects must then be weighed up.

#### 7.3.3.2 Markets affected by the aid

- (141) The measure mainly has an effect on the wholesale market for international connectivity and the telecommunication market, both national and international. Additionally, the measure may have an effect on the DC market.

#### 7.3.4 Positive effects of the aid

- (142) Measure 2 contributes to the development of a submarine cable between Iceland and Europe, thereby enhancing both redundancy and the security of the submarine cable network that Iceland relies on to participate in the global economy. This is in line with the Icelandic Government's Telecommunications Policy, whose objective is, *inter alia*, to promote accessible and effective communications and to guarantee the security of telecommunications infrastructures.
- (143) To achieve those objectives, the Icelandic authorities have emphasised that three active submarine telecommunications cables will connect Iceland with Europe from different landing sites. As a geographically remote country, effective international connections are a prerequisite for the development of Iceland as a modern technologically based society. A serious disruption in international connectivity would cause major damage to the Icelandic economy and society as a whole.
- (144) According to the Icelandic authorities, the main vulnerabilities of the current international connections relate to human error, malfunctions, accidents, natural disasters and other unforeseen events. The Icelandic authorities have provided ESA with a detailed description of the various and multiple disruptions that have happened in the past and disrupted the functionality of the two existing submarine cables <sup>(56)</sup>. ESA considers these vulnerabilities both realistic and probable.
- (145) Furthermore, the absolute lengths of the submarine cables from Iceland to Europe increase the probability of incidents compared to shorter cables going from Scandinavia and the UK to mainland Europe. Moreover, other countries in the EEA are connected to major international network connection points via diversified networks of multiple land and/or submarine cables while Iceland is wholly dependent on only two submarine cables.
- (146) By implementing the measure and adding a third submarine cable to the network, the Icelandic authorities expect the security of international connectivity increases *circa* tenfold. In particular, a third submarine cable will: (i) increase the projected uptime to 99.9993%, (ii) reduce the probability of a total outage in a 10-year period to 0.2–1.5%, and (iii) diversify the land routes in Iceland, decreasing risks associated with a single route failure <sup>(57)</sup>.
- (147) In addition to enhanced security, the Icelandic authorities contend that the addition of a third submarine cable will also improve the competitiveness of Iceland as a whole, as the Icelandic digital market will become 'closer' to major network hubs in Europe. Data latency in communications between Iceland and Europe will be reduced as a result of shorter cable length and simpler network structure than is available through the current system connecting Reykjavík with Europe. ESA considers this factor positive, as it contributes to the development of the Icelandic economy as a whole.

##### 7.3.4.1 Limited negative effects of the aid

###### 7.3.4.1.1 Introduction

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<sup>(56)</sup> See Section 3.2.3 of ESA's Decision No 023/21/COL for details.

<sup>(57)</sup> See ESA's Decision No 023/21/COL, paragraph 22.

(148) Article 61(3)(c) of the EEA Agreement requires an assessment of any negative effects on competition and on trade. The aid must not adversely affect trading conditions to an extent contrary to the common interest.

#### 7.3.4.1.2 Necessity of the aid

(149) To assess whether State aid is effective to achieve its objective, it is necessary to first identify the problem that needs to be addressed. A State aid measure is necessary if it is targeted towards situations where aid can bring about a material improvement that the market cannot deliver itself, for example by remedying a well-defined market failure.

(150) A market failure exists if markets, left to their own devices, without intervention fail to deliver an efficient outcome for society. This may arise, for instance, when certain investments are not being undertaken even though the economic benefit for society exceeds the cost<sup>(58)</sup>.

(151) The Icelandic authorities have explained that Farice would not have undertaken the investment in the IRIS cable in the absence of aid, as it cannot support such an investment with its own funds. This, *inter alia*, is an indication of the market failure associated with providing international connectivity services in Iceland.

(152) However, the fact that a specific company may not be capable of undertaking a project without aid does not mean that there is a market failure. For instance, the decision of a company not to invest in a project with low profitability or in a region with limited market demand and/or poor cost competitiveness may not be an indication of a market failure, but rather of a market that functions well<sup>(59)</sup>.

(153) Concerning the ability of the market to deliver an efficient outcome for society, the Icelandic authorities have pointed to the fact that Iceland was, prior to the IRIS cable project, only connected to Europe through two submarine cables. Furthermore, over the past decade, few stakeholders signalled interest in investing in international data connectivity services between Iceland and Europe or America. These projects did not materialise primarily due to problems with constructing a sound business case for such an investment. Furthermore, these planned and aborted projects by market actors would have been dependent on financial participation by the State (see paragraph (54)).

(154) However, while it is a fact that no privately funded subsea cables from Iceland have been built in the last 10 years, it is also clear that Sýn approached the Icelandic State with plans to build a subsea cable. Negotiations and discussions between the State and Sýn continued over two years, but were then terminated. Therefore, while it is unclear to ESA whether Sýn's offer was comparable to the IRIS cable project, or if it indicates an attempt to enter the market for international data connectivity services, ESA cannot exclude the possibility that the market could have delivered the outcome sought by Measure 2.

(155) Consequently, ESA must preliminarily conclude that it has doubts as to the necessity of Measure 2. The Icelandic authorities are invited to provide further arguments and information relating to this point.

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<sup>(58)</sup> See 2014 Broadband Guidelines, paragraph 33.

<sup>(59)</sup> See 2014 Broadband Guidelines, footnote 45.

#### 7.3.4.1.3 Appropriateness of the aid

- (156) EFTA States can make different choices with regard to policy instruments, and State aid control does not impose a single way to intervene in the economy. However, State aid under Article 61(1) of the EEA Agreement can only be justified by the appropriateness of a particular instrument to contribute to the development of the targeted economic activities or areas.
- (157) ESA normally considers a measure appropriate where the EFTA State can demonstrate that alternative policy options would not be equally suitable, and that alternative, less distortive, aid instruments would not deliver equally efficient outcomes.
- (158) Due to the general unprofitability of submarine cable infrastructure investments and projects from Iceland to Europe, ESA is inclined to conclude that an alternative policy instrument, such as regulations, would neither trigger investment in the IRIS cable project, nor other similar investment projects. Further, ESA is equally inclined to conclude that a loan or guarantee would not be a more appropriate aid instrument <sup>(60)</sup>.
- (159) Therefore, ESA preliminarily concludes that State aid in the form of a capital increase is the appropriate instrument to facilitate the development of the economic activities that the measure concerns. However, the Icelandic authorities are invited to elaborate on this point.

#### 7.3.4.1.4 Proportionality of the aid

- (160) State aid is proportionate if the aid amount per beneficiary is limited to the minimum needed to incentivise the additional investment or activity in the area concerned.
- (161) Measure 2 constitutes a capital increase in Farice. The board of directors of Farice were authorised to increase the capital in intervals during the construction period of the new cable. The financing needs of the recipient were assessed at each interval and only established costs were granted through the capital increase. The granting authority reviews any expenses and controls overcompensation retroactively. This aid granting method and claw-back mechanism contributes to the proportionality of the aid. Moreover, when seeking subcontracting offers, Farice engaged in a competitive selection procedure whereby it selected a contractor who will manufacture and lay the IRIS cable. The selection procedure resulted in Farice opting to contract with the lowest bidder.
- (162) However, according to paragraph 74 of the 2014 Broadband Guidelines, multiple conditions must be fulfilled in order to demonstrate the proportionality of a measure. Failure to meet any of those conditions would in most cases require a detailed assessment <sup>(61)</sup>. These conditions include mapping an analysis of coverage, public consultation, and a competitive selection process.
- (163) ESA is not aware of any mapping analysis or public consultation performed by the Icelandic authorities prior to the implementation of Measure 2. Moreover, as Iceland selected an 'in house entity', namely Farice, to own and operate the infrastructure, it is clear that no competitive selection process was followed in

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<sup>(60)</sup> See ESA Decision No 023/21/COL, Section 6.3.4.3.

<sup>(61)</sup> Similar conditions can also be found in the 2023 Broadband Guidelines, Section 5.2.4.



relation to Measure 2. However, ESA notes that there is no need for a competitive selection process if the State chooses to manage a network directly (or through a wholly owned entity).

- (164) Nevertheless, where the aid is granted without a competitive selection procedure, to a public authority that deploys and manages a broadband network at wholesale level directly, or through an in-house entity, the State must justify its choice of network and technological solution.
- (165) Moreover, according to paragraph 74(d) of the 2014 Broadband Guidelines, granting authorities should generally select the most economically advantageous offer. However, this only applies within the context of a competitive tender, and not when the State selects a wholly owned entity to own and operate the network.
- (166) As described in Section 3.1, the Icelandic authorities were approached by Sýn with an offer to build the third submarine cable, which following an examination by an independent expert, was considered to be cost effective than Farice's offer. The Icelandic authorities have argued that the independent report was based on unconfirmed prices, and when asked to confirm prices, Sýn was unable to do so. Discussions between the Icelandic State and Sýn were terminated as a result. Sýn has argued that it was not given any time or opportunity to renew offers and provide confirmation on prices <sup>(62)</sup>.
- (167) On this point, the EFTA Court stated that: 'ESA has not touched upon this issue at all or disputed that it was aware of this information, as alleged by Sýn. ESA has merely reiterated that Sýn's proposal relied on "unverified figures" without explaining why, if it considered that the figures were unverified, it did not seek to verify them by obtaining further information from Sýn, which had already submitted a complaint to ESA' <sup>(63)</sup>. The EFTA Court then concluded that 'it must be held that Sýn has established that ESA was aware of documents that called into question the information at its disposal and on which it relied in the contested decision, without going beyond a mere examination of the information submitted by the Icelandic authorities. By not obtaining further information on whether Sýn was actually able to confirm its prices, or whether it had been given that opportunity, ESA failed to satisfy its obligation to conduct a diligent and impartial examination of the notified measure so that it had at its disposal the most complete and reliable information' <sup>(64)</sup>.
- (168) Therefore, while the Icelandic authorities might not have been required to conduct a competitive tender, nor select the most economically advantageous offer, ESA must preliminarily conclude that the existence of an allegedly more economically viable offer from Sýn puts into doubt the proportionality of Measure 2, as the Icelandic authorities have not sufficiently explained the price differences between Sýn's offer, and the eventual cost of the IRIS cable project.
- (169) Consequently, as ESA has doubts as regards the proportionality of Measure 2 and invites the Icelandic authorities to further elaborate on the proportionality of the measure, and, in particular, to provide arguments and information explaining the aid amount in comparison to Sýn's allegedly more economical offer.

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<sup>(62)</sup> Judgment of the EFTA Court in Case E-4/21 *Sýn hf. v EFTA Surveillance Authority*, paragraph 64.

<sup>(63)</sup> *Ibid*, paragraph 66.

<sup>(64)</sup> *Ibid*, paragraph 68.

#### 7.3.4.1.5 Limited negative effect on intra-EEA trade

- (170) As ESA preliminary considers Measure 2 to constitute State aid, the measure has an effect on intra-EEA trade. However, in order to be compatible, a measure should limit those effects.
- (171) As stated previously, the primary objective of the measure is to enhance the security of international connections in Iceland, and while a third submarine cable will increase capacity, ESA notes that the capacity of the current network is not fully utilised; the new infrastructure is principally expected to complement the other connections currently in operation. Therefore, the addition of a third cable does not materially alter the structure of the market for international connectivity, but rather enhances the security of the infrastructure already present.
- (172) Moreover, even though a third cable will allow Iceland to be better connected to Europe, it will not change the fact that Iceland remains an island approximately 1 200 km from the nearest European country and 2 000 km from the European continent. The improved communication to Iceland will not bridge the natural data latency gap that exists between communication on the European continent compared with communication from the continent to Iceland. Therefore, ESA finds it hard to see how the IRIS cable will have a material impact on the competitiveness of other EEA markets compared to Iceland. Therefore, the third cable, in and of itself, should not materially alter the dynamics of intra EEA-trade on the relevant market.
- (173) ESA notes that there are no other companies, established in the EEA, that currently operate, or have shown concrete plans to operate without State support, a submarine cable similar to the IRIS cable. Therefore, market participants have not to date demonstrated any concrete plans to invest in a submarine cable between Iceland and Europe prior to the implementation of the measure.
- (174) However, as mentioned in paragraph (54), one of the factors that lead to reduced investment in subsea cables from Iceland to Europe is the need to secure redundancy. An undertaking wishing to establish its own subsea cable network needs to build two cables, or secure redundancy using an existing cable. Since Farice is the only operator of subsea cables from Iceland to Europe, it is most likely that any possible new entrant would opt to secure redundancy through one of Farice's existing cables, in lieu of building two cables at once. ESA does not have information regarding whether Farice offers redundancy services. However, if Farice does not provide such services, it could call into question the limited negative effects of the measure on competition in general due to potential entry barriers.
- (175) Moreover, paragraph 74 of the 2014 Broadband Guidelines lists a number of conditions aimed at limiting distortion of competition and trade, including the need for detailed mapping and public consultation. Failure to comply with any of the conditions is likely to trigger the need for a detailed analysis by ESA. Therefore, regardless of the eventual scope of the 2014 Broadband Guidelines, the apparent omission of the Icelandic authorities to comply with at least some of the conditions listed in paragraph 74 of the 2014 Broadband Guidelines when implementing Measure 2 leads ESA to doubt the overall limitation of negative effects on competition and trade.

#### 7.3.4.1.6 Conclusion on limited negative effects

(176) With reference to the foregoing, ESA has doubts that the effects of the measure on intra EEA-trade are sufficiently limited to a minimum. Therefore, ESA invites the Icelandic authorities to provide further arguments and information in this regard.

#### 7.3.4.2 Balancing positive and negative effects of the aid

(177) For the aid to be compatible with the functioning of the EEA Agreement, the limited negative effects of the aid measure in terms of distortion of competition and adverse impact on trade between Contracting Parties must be outweighed by positive effects, in terms of contribution to the facilitation of the development of economic activities or areas. It must be verified that the aid does not adversely affect trading conditions to an extent contrary to the common interest.

(178) As follows from the above, ESA is preliminarily inclined to conclude that Measure 2 has directly facilitated the economic activities of Farice and that it has had many positive effects.

(179) However, in respect of the negative effects, ESA doubts whether the negative effects of Measure 2 on competition and trade are sufficiently limited. Specifically, ESA doubts whether the market failure addressed by the measure is clearly present, and whether the aid was on the whole proportional. Moreover, the effects of the measure on the markets it affects need to be further examined.

(180) At this stage, ESA therefore doubts that the positive effects of the measure outweigh its possible distortion of competition and adverse impact on trade.

## 8 Conclusion

(181) As set out above, ESA has doubts as to whether Measure 1 constitutes State aid within the meaning of Article 61(1) of the EEA Agreement. Further, if the measure is found to involve aid, ESA also has doubts as to whether the measure would be compatible with the functioning of the EEA Agreement.

(182) Furthermore, ESA has doubts as to whether the Measure 2 is compatible with the functioning of the EEA Agreement.

(183) Consequently, and in accordance with Article 4(4) of Part II of Protocol 3, ESA hereby opens the formal investigation procedure provided for in Article 1(2) of Part I of Protocol 3. The decision to open a formal investigation procedure is without prejudice to the final decision of ESA, which may conclude that Measures 1 and 2 do not constitute State aid or are compatible with the functioning of the EEA Agreement.

(184) ESA, acting under the procedure laid down in Article 1(2) of Part I of Protocol 3, invites the Icelandic authorities to submit their comments by 14 April 2023, and to provide all documents, information and data needed for the assessment of the measures in light of the State aid rules.

(185) The Icelandic authorities are requested to immediately forward a copy of this decision to the aid recipient.

(186) The Icelandic authorities have confirmed that this opening decision does not contain any business secrets or other confidential information that should not be published.

(187) Finally, ESA will inform interested parties by publishing a meaningful summary in the Official Journal of the European Union and the EEA Supplement thereto. All interested parties will be invited to submit their comments within one month of the date of such publication. The comments will be communicated to the Icelandic authorities.

For the EFTA Surveillance Authority,

Yours faithfully,

Arne Røksund  
President  
Responsible College Member

Stefan Barriga  
College Member

Árni Páll Árnason  
College Member

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*This document has been electronically authenticated by Arne Roeksund, Melpo-Menie Josephides.*