JUDGMENT OF THE COURT

3 March 1999

(Action for annulment of a decision of the EFTA Surveillance Authority – State aid – Exceptions under Article 59(2) EEA – Procedures)

In Case E-4/97

Norwegian Bankers' Association, represented by Counsel Mr Jonas W. Myhre, Hjort Law Office, Akersgaten 2, 0105 Oslo, Norway,

applicant,

v

EFTA Surveillance Authority, represented by Mr Håkan Berglin, Director of the Legal and Executive Affairs Department, acting as Agent, 74 rue de Trèves, Brussels, Belgium,

defendant,

supported by the **Kingdom of Norway**, represented by the Office of the Attorney General (Civil Affairs), Mr Ingvald Falch, acting as Agent and Mr Morten Goller, acting as Co-agent, P.O. Box 8012 Dep., 0030 Oslo, Norway,

intervener,

APPLICATION for annulment of Decision No. 177/97COL of 9 July 1997 of the EFTA Surveillance Authority concerning alleged infringement of the competition and State aid provisions of the EEA Agreement owing to the framework conditions for the Norwegian State Housing Bank,

THE COURT

Composed of: Bjørn Haug, President, Carl Baudenbacher and Thór Vilhjálmsson (Rapporteur), Judges,

Registrar: Gunnar Selvik,

having regard to the written observations of the parties and the intervener and the written observations of the Commission of the European Communities, represented by Mr Francisco Santaolalla, Principal Legal Advisor and Mr Dimitris Triantafyllou and Mr Xavier Lewis, Members of the Commission's Legal Service, acting as Agents,

having regard to the revised Report for the Hearing,

after hearing oral argument from the parties and the intervener and the oral observations of the Government of Iceland, represented by Mr Einar Gunnarsson, Legal Officer in the Ministry of Foreign Affairs, acting as Agent, and of the Commission of the European Communities, at the hearing on 4 November 1998,

gives the following

Judgment

1 Husbanken, the Norwegian State Housing Bank (hereinafter "Husbanken") was established by an act of the Norwegian Parliament (Storting) on 1 March 1946 (Act No. 3 of 1 March 1946 on the Norwegian State Housing Bank (*Lov om Den Norske Stats Husbank*, hereinafter "the Act")). The primary capital of Husbanken was contributed by the State. An indemnity fund was established to cover losses on loans and guarantees, with the initial amount being contributed partly by the State and partly by local authorities. According to the Act, further deposits can be made to the fund, as determined by the Parliament, and the Bank can receive funding from the Treasury.

2 Following an amendment in 1992, the only task of Husbanken has been the financing of housing pursuant to the Act and a number of regulations laid down by the public authorities. Husbanken provides loans to individuals for the building of new dwellings. Loans are also provided *inter alia* to nursery schools, rental

housing, special-purpose and sheltered housing, new nursing home places and other care facilities. Improvement loans are granted for the purposes of assisting people with special needs and for the purposes of urban renewal. First home loans and purchase loans are granted, following means testing, to under-privileged groups. In addition, Husbanken offers grants and allowances for some of the purposes mentioned above.

3 It is open for anyone to apply for those loans and grants that are not means-tested. However, certain requirements and conditions are imposed, such as limits on cost and size and functional or planning requirements. An overview submitted by the Government of Norway concerning loans, grants and allowances given by Husbanken in 1996 shows that a little under one-third of loans for construction of new housing, including special care and day care centres, renovation loans and special first home loans, were means-tested (NOK 2434 million out of NOK 7777 million). Grants and allowances are typically restricted to certain groups, but are rarely means-tested. Husbanken requires, as a main rule, a first-priority mortgage in the dwelling for which the loan is granted.

4 Originally, interest rates for Husbanken were directly set by the Parliament in regulations. Since 1 January 1996, however, the lending terms of Husbanken have followed directly the interest rate on government securities, with an added margin of 0.5%, instead of being fixed yearly by political decisions. The Parliament decides the lending quota. Since 1996, Husbanken has provided loans either with fixed or floating interest rates. The floating rate is based on short-term government securities (0-3 months' term) observed six to three months before implementation of a new interest rate, adjusted quarterly. The rate of fixed interest is based on government bonds with a remaining term of approximately five years, observed nine to three months before implementation, adjusted every half a year.

5 *Den Norske Bankforening* (the Norwegian Bankers' Association, hereinafter variously "the Applicant" or "the Association") is an association of banks, mortgage institutions and other financial institutions which are entitled by law to carry on activities in Norway. By a letter of 7 November 1995, the Association lodged a complaint with the EFTA Surveillance Authority, asking it to assess whether the framework conditions for Husbanken were in conformity with the Agreement on the European Economic Area (hereinafter "EEA").

6 The complaint was based on Article 61 EEA on State aid and contended that the arrangement distorted competition to the detriment of credit institutions in competition with Husbanken and that the monopoly on subsidized lending constituted an economic barrier to free trade in financial services and affected cross-border trade. The Association further contended that the arrangement went beyond what was required by the interests of the population groups targeted by the

subsidies and beyond the scope of necessity implicit in Article 59 EEA regarding public undertakings.

7 The initial complaint was later supplemented by letters and faxes from November 1995 through March 1997. On 25 June 1996, officials of the EFTA Surveillance Authority met with representatives of the Association to discuss and exchange information. The EFTA Surveillance Authority requested information from the Norwegian authorities on 22 January 1996 and met with officials of the Royal Ministry of Local Government and Labour on 13 September 1996. Information from the Government of Norway was received in letters dated 1 March 1996 and 22 October 1996.

8 On 9 July 1997, the EFTA Surveillance Authority adopted the following decision (hereinafter the "Decision"): "The complaint initiated by letter of 7 November 1995 (Doc. No. 95-6439-A), concerning the framework conditions for the Norwegian State Housing Bank and their compatibility with the provisions of the EEA Agreement on State aid and competition, is closed without further action by the Authority. (...)" The Norwegian authorities, the Association and the Commission of the European Communities were informed of the Decision by means of a copy.

The contested Decision

9 In the Decision, the EFTA Surveillance Authority rejected the submission of the Government of Norway to the effect that privileges afforded to Husbanken as an instrument of the public housing policy were not governed by Articles 59 and 61 EEA. Regarding the assessment under Article 61 EEA, the contested Decision states the following:

> "...for a measure to constitute State aid in the meaning of Article 61(1) EEA it must
> 1. be granted through State resources;
> 2. distort or threaten to distort competition by favouring certain undertakings or the production of certain goods;
> 3. affect trade between Contracting Parties.
>
> It is clear that the first condition is fulfilled in the present case, as Husbanken's framework conditions are established by the State and its financial means are derived from State resources.
>
> Apart from a very small equity, consisting of risk and loss funds, Husbanken's core activity of providing loans for housing purposes is based on borrowings, which are obtained exclusively from the State(...) Husbanken, being a government

> agency financed by the State, enjoys the borrowing terms and favourable credit rating of the State. (...) Husbanken also in other ways clearly enjoys the financial backing of the State Treasury, for instance by way of budget appropriations, if needed, to cover the losses it incurs on loans as well as administrative expenses. It is therefore clear that as a State institution, Husbanken enjoys financial advantages of a kind not afforded to other providers of credit for housing purposes and which fulfil the condition referred to in point 2 above.(...) ...the Authority does not have reason to question the complainant's contention that potential distortions of competition have not been removed.
> (...)
>
> It ... cannot be ruled out that the financial advantages enjoyed by Husbanken may, at least potentially, affect trade between Contracting Parties to the EEA Agreement, although in practice such effects are likely to be limited."

10 As regards the derogation under Article 59(2) EEA, the Decision is worded as follows:

> "Article 59(2) in other words permits States parties to the EEA Agreement to confer on undertakings to which they entrust the operation of services of general economic interest, exclusive rights or other privileges which may hinder the application of the rules of the Agreement on competition and State aid, in so far as restrictions on competition, or even the exclusion of all competition by other economic operators, are necessary to ensure the performance of the particular tasks assigned to the undertakings concerned.
> (...)
>
> In view of the above facts and considerations, and given that there is no legislation at the EEA level providing a uniform definition of the boundaries of a social housing policy and public housing finance services, the Authority has no grounds to dispute that Husbanken is entrusted with the operation of services of general economic interest.
> (...)
>
> Husbanken is not a credit institution in the meaning of the relevant EEA legislation. It is not authorised to accept deposits from the public and therefore does not compete with credit institutions in that area. It does not engage in other financial services, e.g. payment intermediation, outside the scope of its core activity to provide credit for housing purposes.
>
> Given that the Norwegian authorities have entrusted Husbanken with the operation of loan schemes, whose interest rate terms are fixed by the Norwegian parliament, and these loans being considered to form an integral part of the Government's social housing policy, *inter alia* by virtue of their nation-wide and universal availability and on uniform terms, irrespective of the economic situation

of the recipients, the funding by the State to service these loan schemes must be deemed to be necessary for the performance of these services of general economic interest. This funding is earmarked to allow Husbanken to annually meet the lending quotas, also determined by the Norwegian parliament, of its individual loan schemes, which as stated above are not applied to go beyond Husbanken's core housing finance activity. The funding by the State Treasury is therefore genuinely needed to allow Husbanken to perform the particular tasks assigned to it and does not allow the undertaking to compete in lending activity outside its statutory functions.
(...)

In this context it must be acknowledged that in most developed countries, including most States parties to the EEA Agreement, governments, both at central and local level, intervene in housing and housing finance markets. This intervention takes different forms from one State to another, depending *inter alia* on certain realities in the housing markets, in particular the pattern of housing tenure, and the objectives of the housing policy of the governments concerned.
(...)

It shall furthermore be noted that the Authority is aware of no relevant case-law, according to which the EC Court of Justice has ruled on the compatibility with the State aid provisions of the EC Treaty of support granted through any of the numerous publicly supported housing finance institutions which exist in the EU Member States, or for that matter other types of institutions, which serve as instruments of public housing policy, nor is the Authority aware of any decision whereby the EC Commission has intervened to prohibit or limit the granting of such support.

As concerns assessment of whether restrictions or distortions of competition due to special measures in favour of public undertakings can be justified on the basis of the second paragraph of Article 59, the last sentence of that paragraph provides that "The development of trade must not be affected to such an extent as would be contrary to the interests of the Contracting Parties". This implies that the assessment of the derogation shall be done in an EEA context, i.e. it is subject to a proviso intended to safeguard the interests of other Contracting Parties. Whereas it clearly does not require that trade effects be non-existent, measures involving major trade effects are excluded. As has been concluded above the Authority considers that although it cannot be excluded that the measures under consideration may affect trade between Contracting Parties, in practice such trade effects are likely to be only limited.

For the above reasons the Authority does not in the present circumstances consider that restrictions or distortions of competition as a result of the framework conditions for the Norwegian State Housing Bank go beyond what is required to allow that undertaking to perform the services of general economic interest with which it has been entrusted."

Procedure and forms of order sought by the parties

11 By an application of 9 September 1997, received at the Court Registry on the same day, the Association brought the present action for annulment, under Article 36 of the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice (hereinafter the "Surveillance and Court Agreement")

12 On 24 November 1997, the Government of Norway lodged an application to intervene in support of the EFTA Surveillance Authority, pursuant to Article 36 of Protocol 5 to the Surveillance and Court Agreement. By a letter of 14 January 1998, the Court informed the Government of Norway of its decision to allow the intervention. A Statement in Intervention was received at the Court Registry on 6 February 1998.

13 On 9 December 1997, the EFTA Surveillance Authority lodged at the Court Registry a request pursuant to Article 87 of the Rules of Procedure of the EFTA Court, asking for the application to be dismissed as inadmissible. After hearing oral argument from the parties on 30 April 1998 on the question of admissibility, the Court, in a decision of 12 June 1998, declared the application admissible and decided to reserve the decision on costs.

14 The Court decided to open the oral procedure without any measures of enquiry. However, by a letter of 7 September 1998, the Court requested supplementary information on certain issues from the intervener, the Government of Norway, and asked the parties to give supplementary or rebuttal information regarding the information from the intervener, as the parties found necessary. The supplementary information from the Government of Norway was received at the Court Registry on 16 September 1998, and remarks to the supplementary information from the Association were received at the Court Registry on 1 October 1998.

15 The Applicant claims that the EFTA Court should:

- annul the Decision of the EFTA Surveillance Authority of 9 July 1997 (Dec. No. 177/97COL), and
- order the EFTA Surveillance Authority to bear the costs.

16 The EFTA Surveillance Authority claims that the EFTA Court should:

- dismiss the application as unfounded, and
- order the Applicant to pay the costs.

17 The Government of Norway, intervener in support of the EFTA Surveillance Authority, contends that the EFTA Court should:

- dismiss the application.

Pleas in law

18 The *Applicant* bases the application for annulment on three pleas: that the EFTA Surveillance Authority wrongfully did not commence formal proceedings concerning State aid; that the EFTA Surveillance Authority infringed essential procedural requirements by not providing adequate reasons as required by Article 16 of the Surveillance and Court Agreement; and, finally, that the EFTA Surveillance Authority wrongfully interpreted and applied Article 59(2) EEA.

Opening of proceedings under Article 1(2) of Protocol 3 to the Surveillance and Court Agreement

19 The *Applicant* claims that the EFTA Surveillance Authority has infringed a procedural requirement by not opening the formal proceedings under Article 1(2) of Protocol 3 to the Surveillance and Court Agreement (hereinafter "the Protocol").

Article 1 of the Protocol reads as follows:

> "1. The EFTA Surveillance Authority shall, in co-operation with the EFTA States, keep under constant review all systems of aid existing in those States. It shall propose to the latter any appropriate measures required by the progressive development or by the functioning of the EEA Agreement.
>
> 2. If, after giving notice to the parties concerned to submit their comments, the EFTA Surveillance Authority finds that aid granted by an EFTA State or through EFTA State resources is not compatible with the functioning of the EEA Agreement having regard to Article 61 of the EEA Agreement, or that such aid is being misused, it shall decide that the EFTA State concerned shall abolish or alter such aid within a period of time to be determined by the Authority.

> If the EFTA State concerned does not comply with this decision within the prescribed time, the EFTA Surveillance Authority or any other interested EFTA State may, in derogation from Articles 31 and 32 of this Agreement, refer the matter to the EFTA Court directly.
>
> On application by an EFTA State, the EFTA States may, by common accord, decide that aid which that State is granting or intends to grant shall be considered to be compatible with the functioning of the EEA Agreement, in derogation from the provisions of Article 61 of the EEA Agreement, if such a decision is justified by exceptional circumstances. If, as regards the aid in question, the EFTA Surveillance Authority has already initiated the procedure provided for in the first subparagraph of this paragraph, the fact that the State concerned has made its application to the EFTA States shall have the effect of suspending that procedure until the EFTA States, by common accord, have made their attitude known.
>
> If, however, the EFTA States have not made their attitude known within three months of the said application being made, the EFTA Surveillance Authority shall give its decision on the case.
>
> 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. If it considers that any such plan is not compatible with the functioning of the EEA Agreement having regard to Article 61 of the EEA Agreement, it shall without delay initiate the procedure provided for in paragraph 2. The State concerned shall not put its proposed measures into effect until this procedure has resulted in a final decision."

20 The Applicant claims that the EFTA Surveillance Authority should have opened formal proceedings under Article 1(2) of the Protocol, given the complexity of the case and because the EFTA Surveillance Authority considered the derogation under Article 59(2) EEA in the case. Alternatively, the Applicant maintains the view that the aid was "new aid" for which notification should have been given. The Applicant argues that the EFTA Surveillance Authority should have opened the formal proceedings to investigate the legality of the "new aid".

21 The *EFTA Surveillance Authority* adheres to the view that the possibility of opening a formal investigation under Article 1(2) of the Protocol applies both with regard to new aid and existing aid; however, the conditions for opening the proceedings are different.

22 The EFTA Surveillance Authority argues that the aid in question, which is made up of the financing arrangements for Husbanken established in the context of the national and fiscal budgets of 1980 and 1981, is existing aid. In particular, it submits that the changes introduced on 1 January 1996 concern the lending terms for loans and not the financing arrangements for Husbanken, and do not alter the

category of the aid. The EFTA Surveillance Authority, supported by the *Government of Norway* and the *Commission of the European Communities*, maintains that, under those circumstances, it was not within the powers of the EFTA Surveillance Authority to open formal proceedings without first addressing appropriate measures to the State concerned, a decision which lies entirely within the discretion of the EFTA Surveillance Authority and which third parties are not in a position to require.

23 In order to determine which procedural rules were applicable to the proceedings of the EFTA Surveillance Authority, it is necessary for the *Court* to consider the substantive matters that are relevant for such determination. It would not be compatible with the Court's review function if it were to be entirely bound by the findings of the EFTA Surveillance Authority in its consideration of the procedure.

24 The first factor decisive for the determination of applicable procedural rules is whether or not the funding of Husbanken constitutes State aid within the meaning of Article 61 EEA.

25 The EFTA Surveillance Authority considered the funding of Husbanken to be State aid contrary to Article 61 EEA and proceeded on that basis to consider whether such aid could be upheld under Article 59(2) EEA. The Applicant was in agreement with this.

26 The Government of Norway, supported by the *Government of Iceland*, submits principally that the system does not constitute aid contrary to Article 61(1) EEA. Husbanken is not an "undertaking" favoured by State resources within the meaning of Article 61 EEA, but rather is part of the State itself. The organization of the public sector, including transactions within that sector, is a prerogative of the Government. Thus, it is the loans granted by Husbanken to private consumers – and not the funding of Husbanken – which might be subject to an assessment under Article 61 EEA.

27 The Government of Norway argues that the interpretation provided by the EFTA Surveillance Authority, according to which the application of Article 61(1) EEA is dependent on the "nature of the service" (page 12 of the Decision), is not supported either by the wording of Article 61 EEA or by case law. When the Court of Justice of the European Communities (hereinafter "ECJ"), in its judgment in Case 78/76 *Steinike und Weinlig* v *Germany* [1977] ECR 595, stated at paragraph 18 that Article 92 of the Treaty Establishing the European Community (hereinafter "EC"), which corresponds to Article 59 EEA, covers "all private and public undertakings and all their productions", it did not offer a definition of the term "undertaking". Furthermore, at paragraph 21 of that judgment, the ECJ went on to state:

> "The prohibition contained in Article 92(1) covers all aid granted by a Member State or through State resources without its being necessary to make a distinction whether the aid is granted directly by the State or by public or private bodies established or appointed by it to administer the aid."

According to the Government of Norway, this implies that aid does not escape Article 92 EC simply by being granted through a public body – such as Husbanken – established for that purpose. However, the statement also indicates that it is the aid given by the public body, not the aid received by that body, that is subject to scrutiny under Article 92 EC.

28 For this reason, according to the Government of Norway, the EFTA Surveillance Authority should have closed the case on the grounds that no infringement was found of Article 59(1) EEA, read in conjunction with Article 61 EEA. Nevertheless, the Government of Norway finds that the Decision is valid and must be upheld, since the conclusion was correct that no infringement took place, although it was based on different reasoning.

29 The *Court* notes that the Governments of Norway and Iceland have not fully argued their submissions on this point. Moreover, the Applicant, the EFTA Surveillance Authority and the Commission of the European Communities have not submitted written or oral arguments regarding this issue.

30 The Court sees no reason to decide what the correct procedural route would be if the submissions of the two governments were to be approved. It finds that they cannot be accepted. Husbanken is a State institution set up by law, having its own directors and board of directors and a board of controllers, its own offices and its own annual accounts. This leads to the conclusion that it is an undertaking within the meaning of Articles 61 and 59 EEA. This conclusion is not altered by the fact that the policy and resources of Husbanken are decided on by the Government and the Parliament of Norway. Further, with regard to the argument of the Government of Norway that private consumers and not Husbanken are the recipients of the aid, the EFTA Surveillance Authority has, in its Decision, correctly considered that the derogation in Article 61(2)(a) EEA is not applicable, as the aid is not neutral with respect to operators in the credit market. Therefore, as already noted at paragraph 25 of the Court's decision of 12 June 1998 on admissibility, the Court finds that the case must be viewed as a State aid case to be dealt with pursuant to Article 61 EEA and the Protocol.

31 In reviewing cases concerning State aid, it is necessary, in order to determine what procedural rules are applicable, to consider whether the alleged State aid

constitutes “existing aid” or “new aid” within the meaning of Article 1 of the Protocol, since the procedural rules are different.

32 As regards existing aid, Article 1(1) of the Protocol requires the EFTA Surveillance Authority to keep all such aids in the EFTA States under constant review and to propose to the EFTA State concerned “any appropriate measures required by the progressive development or by the functioning of the EEA Agreement”. If the EFTA Surveillance Authority considers that an existing aid is incompatible with the EEA Agreement, it must first present the EFTA State concerned with a specific proposal to correct the situation. There is no requirement that formal proceedings be opened before such a proposal is presented. The proposal is not legally binding, but non-compliance enables the EFTA Surveillance Authority to proceed with the contentious procedure provided for in the first paragraph of Article 1(2) of the Protocol.

33 As regards proposed new grants of aid by the EFTA States, Article 1(2) and (3) of the Protocol establish a procedure which must be followed before any aid can be regarded as lawfully granted. Under the first sentence of Article 1(3) of the Protocol, the EFTA Surveillance Authority is to be notified of any plans to grant or alter aid before those plans are implemented. The EFTA Surveillance Authority then conducts an initial review of the planned aid. If, at the end of that review, it considers a plan to be incompatible with the functioning of the EEA Agreement or is in serious doubt about the compatibility of such new aid, it must initiate without delay the procedure under the first paragraph of Article 1(2) of the Protocol. Accordingly, in the context of the procedure laid down by the Protocol, the preliminary stage of the procedure for reviewing new aid under Article 1(3) of the Protocol, which is intended merely to allow the EFTA Surveillance Authority to form a *prima facie* opinion on the partial or complete compatibility of the aid in question with the State aid provisions, must be distinguished from the examination under Article 1(2) of the Protocol, which is designed to enable the EFTA Surveillance Authority to be fully informed of all the facts of the case, see the judgments of the ECJ in Case C-198/91 *Cook* v *Commission* [1993] ECR I-2487, at paragraph 22, and Case C-225/91 *Matra* v *Commission* [1993] ECR I-3203, at paragraph 16.

34 The Court notes that, from the information available to it, it must be concluded that the aid in question is existing aid, the origin of which predates the signature of the EEA Agreement. The system in its present form dates back to 1981 and thus represented existing aid when the EEA Agreement entered into force. As regards changes to the rules made in 1996, the committee reports and proposals to the Parliament show that the main purpose and effect of the changes was to adjust the support given, for better implementation of the social policy program. The

changes are summed up as follows in a publication called *The Norwegian State Housing Bank*, issued by Husbanken in June 1996:

> "The Housing Bank's role as the government's main instrument in carrying out national housing policy was confirmed in Governmental Report to Parliament # 34, 1995. However, the government proposed significant changes in the Bank's instruments for carrying out this policy.
> These changes were implemented in the national budget for 1996. Subsidized interest rates, which were generally available for new construction in previous years, have been replaced with a system of grants and supplementary loans given for desirable housing and environmental qualities and to certain disadvantaged groups. Supplementary loans and grants for specific housing qualities are more directly aimed at influencing housing standards where the free market alone would not provide sufficient stimulus. Housing grants enable disadvantaged groups who would not receive loans from private credit institutions to establish themselves in a satisfactory home.
> In addition, the percentage of new construction to be financed by the Housing Bank has been lowered so that private credit institutions will be responsible for financing a larger share of new housing than has been the case in the recent past. The Housing Bank is expected to finance approximately 10,000 of an estimated 21 – 22,000 new homes in 1996."

Thus, from the information available to it, the Court concludes that the changes referred to by the Applicant did not constitute new aid but rather a decrease in the aid then existing. Accordingly, this change did not cause the State aid under scrutiny here to become new aid for which notification had to be given to the EFTA Surveillance Authority.

35 As regards existing aid, the Protocol does not explicitly require the EFTA Surveillance Authority to open formal proceedings. Nor is such a requirement established through the case law of the ECJ. The Court finds that there are indeed relevant differences between existing and new aid which speak in favour of different solutions with regard to the obligation to open formal proceedings. Firstly, the EFTA Surveillance Authority has a different role in supervising existing and new aid: the former is an ongoing process while the latter is a preventive control. Secondly, there are differences with regard to the consequences following from a decision to initiate formal proceedings. Thirdly, there are differences regarding the involvement of interested parties with regard to proposed new aid in comparison with existing aid.

36 The Court finds that the EFTA Surveillance Authority was under no obligation to open formal proceedings on the basis of the complaint from the Association. On the contrary, as pointed out by the EFTA Surveillance Authority, the appropriate approach under Article 1(1) of the Protocol is to subject the State aid system to

closer examination and analysis and, where warranted, propose to the State involved such appropriate measures as are found to be "required by the progressive development or by the functioning of the EEA Agreement". The EFTA Surveillance Authority enjoys broad discretion in both the prescribed review of existing aid and the appropriate measures it decides to propose.

37 The first plea of the Association must therefore be dismissed as unfounded.

Error in law and error in assessment

38 The third plea of the *Applicant*, which the Court finds should be discussed next, is that the EFTA Surveillance Authority wrongfully interpreted and applied Article 59(2) EEA, which reads:

> "Undertakings entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly shall be subject to the rules contained in this Agreement, in particular to the rules on competition, in so far as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them. The development of trade must not be affected to such an extent as would be contrary to the interests of the Contracting Parties."

39 The arguments of the parties may be considered in light of the elements brought out by Article 59(2) EEA: firstly, the question whether the services entrusted to Husbanken are services of general economic interest within the meaning of Article 59(2) EEA; secondly, if so, whether the application of the rules of the EEA Agreement would obstruct the performance, in law or in fact, of the particular tasks assigned to Husbanken; thirdly, the condition that the development of trade must not be affected to an extent contrary to the interests of the Contracting Parties by the application of the derogation. In connection with the second and third points, special attention has to be paid to the question of proportionality, in particular the question of whether social housing policy may be achieved through less distortive means.

40 The *Court* notes generally that, according to established case law of the ECJ, the Court cannot substitute its own assessment for that of the EFTA Surveillance Authority in a case such as the present one, which involves assessments of an economic and social nature which must be made within an EEA context (Case C-225/91 *Matra* v *Commission* cited above, paragraph 24). In reviewing the substantive issues of the case, the Court must confine itself to verifying whether the facts on which the contested finding was based have been accurately stated by the EFTA Surveillance Authority and whether there has been any manifest error of

assessment or a misuse of powers (see *inter alia* Case C-56/93 *Belgium* v *Commission* [1996] ECR I-723.)

Services of general economic interest

41 The *Applicant* maintains that there is to be a strict definition of those undertakings that may take advantage of the derogation under Article 90(2) EC and Article 59(2) EEA and that the relevant test includes whether the services in question show "special characteristics" as compared with other economic activities. The Applicant further contends that it is for the government claiming the derogation to show that such special characteristics exist. The fact that the government in question finds the services to be of general economic interest or that the public authorities have entrusted the services in question to a particular undertaking will not suffice.

42 The Association argues that the EFTA Surveillance Authority has erred in not distinguishing the broad housing policy issues from the issue relevant for the application of Article 59(2) EEA. The offering of first-priority mortgage loans, without means-testing, for new dwellings does not, in the submission of the Association, exhibit special characteristics compared with similar services offered by most banks and mortgage institutions.

43 The Association further submits that the only truly public service obligation performed by Husbanken is the providing of means-tested loans and grants to people in a weak financial position. The only purpose of the State aid as regards the non-means-tested loans is to put Husbanken permanently in a more advantageous position in the commercial market of offering first-priority mortgage loans.

44 The *EFTA Surveillance Authority* emphasizes that Member States remain free, in principle and where no common policy is established, to designate which services they consider to be of general economic interest and to organize these services as they see fit, subject to the rules of the EEA Agreement, and the specific conditions laid down in Article 59(2) EEA. Consequently, the EFTA Surveillance Authority has expressly limited its scrutiny. The *Commission of the European Communities* argues in a similar vein, *viz.* that the competence to define such services lies with the Member States, subject to scrutiny by the Community institutions, which essentially must be conducted on a case-by-case basis.

45 The EFTA Surveillance Authority further submits that it may be concluded that an undertaking entrusted by the State with the performance of economic activities which the State considers to be in the interest of the general public is an

undertaking "entrusted with the operation of services of general economic interest" within the meaning of Article 59(2) EEA, provided only that the activities exhibit special characteristics related to the public interest involved and distinguishing them from economic activities in general. Characteristics of the loans operated by Husbanken, in particular the obligation to keep the loans available on equal and preferential terms and the monitoring tasks linked to the operation of the loans, were clearly sufficient to distinguish them from loans generally offered on the market.

46 The *Government of Norway* claims that the housing sector must be regarded as exhibiting special characteristics as compared with the general economic interests of other economic activities and as being of direct benefit to the public. The Government of Norway further emphasizes that the tasks conferred on Husbanken have been entrusted to the Bank by acts of the public authorities, as required pursuant to Article 59(2) EEA.

47 The *Court* notes that, in the application of Article 59(2) EEA, it is primarily for the EFTA Surveillance Authority to assess whether certain services are "services of general economic interest" within the meaning of Article 59(2) EEA. In this assessment, the nature of the undertaking entrusted with the services is not of decisive importance, nor whether the undertaking is entrusted with exclusive rights, but rather the essence of the services deemed to be of general economic interest and the special characteristics of this interest that distinguish it from the general economic interest of other economic activities (See Case C-179/90 *Merci Convenzionali Porto di Genova*, [1991] ECR I-5889, at paragraph 27 and Case C-266/96 *Corsica Ferries France SA and Others* [1998] ECR I-3949, at paragraph 45). With regard to the discretion of the EFTA Surveillance Authority in this area, the Court cannot substitute the Authority's finding with its own assessment or annul the Decision on these grounds, provided that the outcome of the assessment is not manifestly wrong. It must also be kept in mind that it has been accepted by the Community judicature that Member States cannot be precluded from taking account of objectives pertaining to their national policy when defining the services of general economic interest which they entrust to certain undertakings (See Case C-202/88 *France* v *Commission* [1991] ECR I-1223, at paragraph 12 and Case C-159/94 *Commission* v *France* [1997] ECR I-5815, at paragraph 56).

48 The Court notes that the present housing policy in Norway dates back more than 50 years and is based on a political goal, which is to give priority to house building based on certain special presumptions or conditions by channelling capital to that sector and lending it to borrowers on more advantageous terms than are available on the open, general Norwegian capital market. For this reason, Husbanken may be considered as an undertaking entrusted with the operation of a service of general economic interest, because the service of general economic

interest is specifically defined by Norway. However, Norway, as a Contracting Party to the European Economic Area, has committed itself to following certain economic policies. The rules on these policies may direct, in a manner binding on Norway, what measures in the field of State aid and competition in general may be implemented.

49 Further, the facts presented to the Court show that the loans system operated by Husbanken is limited to certain categories of houses (which are not to exceed 120 m^2 for individuals), care facilities and projects relating to urban renewal, special needs of identified population groups, etc., and that the system applies to the entire territory of Norway, including sparsely populated areas, where asset evaluations are likely to differ compared to more densely populated areas.

50 Based on the foregoing, and taking into account the requirement of the system that loans must, in principle, be available to everyone on an equal basis, the Court does not find that the EFTA Surveillance Authority has manifestly erred in its assessment that the services in question are services of general economic interest, distinguishable from the economic interest of other economic activities, within the meaning of Article 59(2) EEA.

Obstruction of the performance of the particular tasks

51 The second argument raised by the *Applicant* under the plea of errors in law relates to the requirement that undertakings entrusted with the operation of services of general economic interest shall be subject to the rules contained in the EEA Agreement, in particular the rules on competition, in so far as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them. The Association submits that no evaluation of this has been made in the Decision. The Association further argues that the Government of Norway must show that the performance of the particular tasks assigned to Husbanken cannot be achieved with due application of the State aid rules, another point which is not set out or dealt with in the Decision. The Association refers in particular to Case C-320/91 *Corbeau* [1993] ECR I-2533 and Case T-106/95 *FFSA and Others* v *Commission* [1997] ECR II-229, at paragraph 178, for the nature of such a test and the necessary elements to be considered.

52 The *EFTA Surveillance Authority* maintains that the question of necessity must be examined on the basis of the tasks actually entrusted to Husbanken. The EFTA Surveillance Authority argues that it is not even suggested by the Association that the funding exceeds what is needed for Husbanken to carry out the functions entrusted to it. Rather, the Association’s arguments turn on the necessity of entrusting Husbanken with these tasks, which is not of relevance for the evaluation

at hand. The EFTA Surveillance Authority maintains that, as Husbanken is to operate loan schemes with interest rate terms fixed by the Norwegian Parliament, and the funding by the State is earmarked to allow Husbanken to meet the lending quotas set by the Parliament, the funding is genuinely needed to allow Husbanken to perform the particular tasks assigned to it. The EFTA Surveillance Authority has further emphasized that, since Husbanken is not authorized to accept deposits from the public and does not engage in financial services outside house financing, there is no risk of cross-subsidization to other tasks of a competitive nature.

53 The *Government of Norway* submits that Husbanken would generally not be able to offer terms and interest rates better than private banks can offer if Husbanken was forced to operate on terms equal to those under which private banks operate. Husbanken would also be forced to raise prices in unprofitable parts of the market in order to compete in the profitable parts. Thus, the restriction imposed on competition by the State aid to Husbanken is genuinely needed in order to ensure the performance of the particular tasks assigned to Husbanken.

54 The *Court* finds that the Applicant has not been able to substantiate its plea that the EFTA Surveillance Authority erred in its assessment of whether the aid in question was necessary for Husbanken to perform the tasks entrusted to it. However, it is for the Court to examine this matter and it will be further dealt with in the framework of the assessment of the proportionality.

Development of trade and the interest of the Contracting Parties

55 As regards the effect on trade between the Contracting Parties, the *Applicant* submits that the EFTA Surveillance Authority is wrong in interpreting this condition as involving only major effects on trade. The Applicant maintains that at least the potential cross-border activity is greatly underestimated by the EFTA Surveillance Authority, and emphasizes the difficulties foreign banks have in penetrating the market and the possible isolation of markets. The Association distinguishes the situation at hand from the one at issue in Case C-159/94 *Commission* v *France*, cited above, regarding electricity and gas, on the grounds that these activities were not harmonized, unlike the field of financial services.

56 In this context, the Applicant claims that the EFTA Surveillance Authority has underestimated the distortion of competition in the relevant market, partly by applying a wrong definition of the relevant market, which the Applicant maintains is the market for non-means-tested, first-priority mortgage loans. The Applicant submits that a proper analysis of the relative strength given to Husbanken in the relevant market as compared to its competitors would have led to even stronger conclusions under Article 61 EEA with respect to effect on trade, and also to a

finding that the effect on trade is contrary to Article 59(2) EEA. The Applicant maintains that an examination of the relevant market is appropriate under Article 59(2) EEA (Joined Cases 296 and 318/82 *Netherlands and Leeuwarder Papierwarenfabriek* v *Commission* [1985] ECR 809, at paragraph 24; Joined Cases T-371/94 and T-394/94 *British Airways and Others* v *Commission* [1998] ECR II-2405, at paragraph 273).

57 The Applicant also claims that the EFTA Surveillance Authority erred in its interpretation of First Council Directive 77/780/EEC of 12 December 1977 on the coordination of the laws, regulations and administrative provisions relating to the taking up and pursuit of the business of credit institutions (hereinafter "the First Banking Directive") and of Second Council Directive 89/646/EEC of 15 December 1989 on the coordination of laws, regulation and administrative provisions relating to the taking up and pursuit of the business of credit institutions and amending Directive 77/780/EEC (hereinafter the "Second Banking Directive"), in finding that Husbanken is excluded from the scope of the Directives. The Applicant maintains that the EFTA Surveillance Authority erroneously found that mortgage credit institutions do not fall within the scope of the Directives and thus also underestimated the scope and effect of the actual and/or potential competition on the relevant market and the effect on trade between the Contracting Parties.

58 The *EFTA Surveillance Authority* maintains that the balancing of interests required under the second sentence of Article 59(2) EEA implies that any effect on trade must be assessed in the light of the relevant interests of the Contracting Parties and the state of development of intra-EEA trade in the sector concerned. Moreover, a reasonable balance must be struck between the various interests involved. The EFTA Surveillance Authority submits that its finding that the aid involved had limited effects on trade and was not contrary to the interests of the Contracting Parties is well-founded. In particular, the EFTA Surveillance Authority refers to the following factors in supporting its conclusion: the fact that Husbanken does not engage in other activities and that, consequently, there is no room for cross-subsidization; the fact that house financing markets in most EEA States are characterized by the presence of government intervention (central and local); the fact that no precedents of the ECJ rule out the compatibility of the State aid provisions with any of the numerous publicly supported house financing institutions in the European Union; the fact that there is no harmonization of this field in the EEA, which results in obstacles to cross-border operations with regard to mortgage credits; and the fact that loans for house financing are predominantly of a local character.

59 The *Government of Norway* submits that the relevant question under the last sentence of Article 59(2) EEA is whether credit investments by foreign credit

institutions would be considerably higher in Norway if Husbanken was deprived of the State aid. It estimates that the most likely scenario would be that branches of foreign credit institutions would cover a similar share of Husbanken's "vacant" portfolio as in the credit market for households in general, which in 1995 was under 19% of the total credit supply in Norway. It concludes that foreign credit institutions are only marginally affected. Furthermore, as the State interest involved is considerable, the effect on intra-State trade must, in the submission of the Government of Norway, be correspondingly substantial before the derogation under Article 59(2) EEA is precluded.

60 The Government of Norway emphasizes that an analysis of the relevant market may be a factor to be considered under Article 61 EEA as part of the assessment of whether or not Husbanken distorts competition. However, as the Applicant does not contest the finding of the EFTA Surveillance Authority with regard to Article 61 EEA, the Court is not invited to decide upon the application of Article 61 EEA and the legal relevance of this analysis to the case at hand is therefore not shown. The Government of Norway argues that the only relevance of an analysis of the relevant market concerns the assumed effects on inter-State trade. In this context, the relevant market is loans to private persons backed by mortgages in private dwellings.

61 The *Commission of the European Communities* submits that it is legitimate to take into account not just the segment of the banking sector engaged in housing loans but also other lending activities in assessing whether the aid gives rise to a disproportionate restriction on the provision of credit services. If housing loans form but a relatively small portion of the total lending business, any restrictions resulting from the aid granted to Husbanken will be so much the less for the other undertakings active on the market.

62 According to the Commission of the European Communities, it must be established that the performance of the service of general economic interest does not affect competition and unity of the common market in a disproportionate manner. The test is of a negative nature: it examines whether the measure adopted is not disproportionate, but it is not a requirement that the measure adopted be the least restrictive possible. A reasonable relationship between the aim and the means employed is satisfactory. The *Court* concurs with these views.

63 The Court does not find that the EFTA Surveillance Authority incorrectly interpreted Directives 77/780 and 89/646, the First and Second Banking Directives, in finding that those provisions of secondary legislation did not apply to specialized house financing institutions such as Husbanken, nor that the effects of harmonization achieved through these Directives, as well as through primary and other secondary EEA legislation, have been underestimated by the EFTA

Surveillance Authority in its balancing of the interests of the EEA vis-à-vis those of the Norwegian authorities.

64 As to whether the social policy objectives of the Government of Norway in the housing sector could be achieved by means less distortive to competition than the existing rules, the Applicant argues that there are several possibilities, some of which are already set out in official documents. The main one, in the submission of the Applicant, is a system in which the borrower may choose finance options freely from among competing bids from different financial institutions, through which the authorities might provide a loan or a direct subsidy. Other possibilities pointed out by the Applicant are the so-called Models 3 and 4 in the Report from the Norwegian Commission on State banks, NOU 1995:11, The State Banks Under Amended Framework Conditions.

65 The EFTA Surveillance Authority stresses the freedom of States to define their policies and organize general interest services, leaving it no power to take a position on the organization and scale of the service or the expediency of political choices made (See Case T-106/95 *FFSA and Others* v *Commission*, cited above). The EFTA Surveillance Authority submits that the Applicant's claim on this point is manifestly unfounded and that the circumstances do not lend themselves to the conclusion that there was an error on the part of the EFTA Surveillance Authority.

66 The Commission of the European Communities submits that, even if it were successfully shown that the scheme in question was not an optimally efficient one, this alone would not lead to the conclusion that the EFTA Surveillance Authority had made a manifest error in stating that the distortive effects are not disproportionate to the goals assigned. The choice of the means belongs exclusively to the national authorities, within the boundaries set by the EEA law.

67 The Court notes, as already mentioned in this judgment, that Article 59(2) EEA provides that the operation of undertakings entrusted with services of general economic interest must not affect the development of trade "to such an extent as would be contrary to the interests of the Contracting Parties". The services under consideration in the present case are financial in nature. There is no doubt that the word "trade" in Article 59(2) EEA applies to them.

68 In its Decision, the EFTA Surveillance Authority did not go into depth on this condition. It states in its Decision that even if it cannot "be excluded that the measures under consideration may affect trade between Contracting Parties, in practice such trade effects are likely to be only limited."

69 The Court notes that the parties disagree as to which market is relevant in this case. It is also disputed whether there are alternative means less distortive to

competition than those presently applied whereby the housing policy of the Norwegian State can be achieved. The Applicant has further argued that an analysis of the costs and benefits of the State aid, as has been required by the ECJ in judgments in some of the State aid cases referred to above, can be done in this case. The Court cannot conclude that these points have been considered to the extent necessary by the EFTA Surveillance Authority in its Decision. At least the Decision itself does not bear witness to that.

70 These questions call for complex analyses and assessments which the Court cannot carry out but which must be done by the EFTA Surveillance Authority. Article 59(2) EEA calls for an application of a proportionality test to assess whether the required balance has been struck between the common interests of the Contracting Parties to the EEA Agreement and the legitimate interests of Norway. The common interests require extensive freedom in the field of services whereas the interests of Norway could be said to be that the Government and Parliament must be permitted to regulate Norwegian housing policy according to the political goals set. In other words, the EFTA Surveillance Authority must strike a balance between the right of Norway to invoke the exemption and the interest of the Contracting Parties in avoiding distortions of competition. For these reasons, the Court concludes that the EFTA Surveillance Authority, by not carrying out the tests described, wrongly interpreted and applied Article 59(2) EEA. Accordingly, the Decision under scrutiny must be annulled.

Statement of reasons

71 *The Applicant* has submitted that it is an independent basis for annulment that the Decision is not reasoned as required by Article 16 EEA. Those appearing before the Court have set out their views on this submission. The *Court* has already found that the Decision must be annulled on the basis of the arguments set out above which are, in part, closely linked to the arguments concerning the statement of reasons. The Court finds that it is not necessary to deal further with whether the reasoning is sufficient.

Costs

72 Under Article 66(2) of the Rules of Procedure, the unsuccessful party is to be ordered to pay the costs if they have been applied for in the successful party's pleadings. The Applicant has asked for the EFTA Surveillance Authority to be ordered to pay the costs of the Applicant in both the admissibility proceedings and the substantive proceedings. Since the latter has been unsuccessful in its defence, it must be ordered to pay the costs. The costs incurred by the Government of Norway as intervener, the Government of Iceland and the Commission of the European Communities, which have submitted observations to the Court, are not recoverable.

On those grounds,

THE COURT

hereby

1. Annuls Decision No. 177/97COL of 9 July 1997 of the EFTA Surveillance Authority.

2. Orders the EFTA Surveillance Authority to bear the costs of the Applicant in both the admissibility proceedings and the substantive proceedings. The Government of Norway as intervener, the Government of Iceland and the Commission of the European Communities shall bear their own costs.

Bjørn Haug Thór Vilhjálmsson Carl Baudenbacher

Delivered in open court in Luxembourg on 3 March 1999.

Gunnar Selvik
Registrar

Bjørn Haug
President