JUDGMENT OF THE COURT
26 June 2007

(Conditions for concession for acquisition of hydropower resources – scope of the EEA Agreement – free movement of capital – right of establishment – indirect discrimination – public ownership – security of energy supply – environmental protection – proportionality)

In Case E-2/06,

EFTA Surveillance Authority, represented by Niels Fenger, Director, and Per Andreas Bjørgan and Arne T. Andersen, Senior Officers, Legal & Executive Affairs, acting as Agents,

Applicant,

v

The Kingdom of Norway, represented by Fredrik Sejersted, Advocate, the Attorney General for Civil Affairs, and Ingeborg Djupvik, Adviser, the Ministry of Foreign Affairs, acting as Agents,

Defendant,

supported by **the Republic of Iceland,** represented by Sesselja Sigurðardóttir, First Secretary and Legal Officer, Ministry for Foreign Affairs, acting as Agent,

Intervener,

APPLICATION for a declaration that the Kingdom of Norway has infringed Articles 31 and 40 of the EEA Agreement by maintaining in force measures as laid down in Act No 16 of 14 December 1917 Relating to Acquisition of Waterfalls, Mines and Other Real Property etc. (*lov 14. desember 1917 nr. 16 om erverv av vannfall, bergverk og annen fast eiendom m.v.*), which grant to private undertakings and all undertakings from other Contracting Parties to the EEA

Agreement a time-limited concession for the acquisition of waterfalls for energy production, with an obligation to surrender all installations to the Norwegian State without compensation at the expiry of the concession period, whereas Norwegian public undertakings benefit from concessions for an unlimited period of time.

THE COURT,

composed of: Carl Baudenbacher, President, Thorgeir Örlygsson (Judge-Rapporteur) and Henrik Bull, Judges,

Registrar: Skúli Magnússon,

having regard to the written pleadings of the Applicant, the Defendant and the Intervener, and the written observations of the Republic of Poland, represented by Ewa Ośniecka-Tamecka, Secretary of the Committee for European Integration, acting as Agent, and the Commission of the European Communities, represented by Hans Stovlbaek and Michael Shotter, Members of its Legal Service, acting as Agents,

having regard to the Report for the Hearing,

having heard oral argument of the Applicant, represented by its Agents Niels Fenger and Per Andreas Bjørgan, the Defendant, represented by its Agent Fredrik Sejersted, the Intervener, represented by its Agent Sesselja Sigurðardóttir, the Kingdom of the Netherlands, represented by its Agent Pepjin van Ginneken, the Republic of Poland, represented by its Agent Marcin Nowacki, and the Commission of the European Communities, represented by its Agent Michael Shotter, at the hearing on 14 March 2007,

gives the following

Judgment

I Pre-litigation procedure

1 By a letter dated 8 March 2001, the Applicant requested information from the Defendant on certain aspects of Act No 16 of 14 December 1917 Relating to Acquisition of Waterfalls, Mines and Other Real Property etc. (hereinafter the "Industrial Licensing Act" or the "ILA"), including the reasons why only Norwegian public undertakings are granted concessions for acquisition of

waterfalls for an unlimited period of time. It also asked whether the Defendant considered those rules as being compatible with the EEA Agreement, in particular the rules on free movement of capital and freedom of establishment. The Defendant replied by a letter of 20 April 2001. It stated *inter alia* that public legal bodies were entrusted with the management of waterfalls on behalf of the State and that the authorities needed to be able to assess whether non-public concessionaires should be allowed to continue to manage the waterfalls. The Defendant did not find the Act to be in conflict with Article 31 or 40 EEA.

2 On 27 June 2001, the Applicant issued a letter of formal notice concluding that certain measures laid down in the ILA infringed Articles 31 and 40 of the EEA Agreement. The Applicant emphasised that, according to the ILA, undertakings from other EEA States, whether public or private, were never able to benefit from a concession for acquisition of waterfalls for hydropower production for an unlimited period of time, and were subject to the requirement of reverting property rights in relation to hydropower production to the State (hereinafter "reversion" or "system of reversion"). Conversely, a concession could be granted for an unlimited period of time to undertakings controlled by Norwegian public bodies, and without any reversion requirement. These rules, in the Applicant's view, constituted discrimination restricting freedom of establishment and free movement of capital which could not be justified. In addition, the Applicant pointed out *inter alia* that the State holds pre-emptive rights to shares in public undertakings. In the Applicant's view, this reinforced the obstacles met by private investors wishing to invest in this sector.

3 The Defendant replied to the letter of formal notice by a letter of 28 November 2001. It stated that the system of reversion had been introduced in order to achieve State ownership over developed waterfalls at the end of the concession period, while at the same time providing the private sector with incentives to develop natural resources in the interest of society as a whole. The rules at issue were an integral part of the management of natural resources falling outside the scope of the EEA Agreement. In any event, the Defendant found that the rules were covered by Article 125 EEA, and stated that this Article took precedence over conflicting provisions of the EEA Agreement.

4 Disagreeing with the arguments of the Defendant, the Applicant delivered a reasoned opinion on 20 February 2002, concluding with the same reasoning as that of the letter of formal notice, that Articles 31 and 40 EEA had been infringed. The Defendant replied to the reasoned opinion by a letter dated 19 April 2002, in which it upheld the views previously expressed in its reply to the letter of formal notice. The Defendant nevertheless stated that it had decided to harmonise the provisions on reversion between public and non-public actors. Therefore, it had decided to propose amendments to the ILA in order to establish a requirement of reversion to the State in all existing concessions.

5 On 29 November 2002, the Ministry of Oil and Energy sent out a hearing paper proposing such changes to the ILA. Due to fierce opposition to the hearing paper, the Government decided, in April 2003, to convene an independent committee

with a mandate to review the system of reversion as regards waterfalls and how it should be designed. The Committee delivered its report to the Ministry of Oil and Energy on 30 November 2004, NOU 2004: 26 (hereinafter "NOU 2004: 26").

6 On the basis of *inter alia* NOU 2004: 26 and the former Norwegian Government's publicly stated intentions to change the disputed provisions, the Applicant decided to postpone any decision as to whether it should commence the infringement procedure before the Court. However, in April 2006, after a change of Government, the Applicant was informed by the Defendant that no changes would be proposed to the ILA. On that basis, the Applicant decided, on 26 April 2006, to bring the matter before the Court under Article 31(2) of the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice (hereinafter the "SCA").

II EEA law

7 Article 31(1) EEA reads:

> *Within the framework of the provisions of this Agreement, there shall be no restrictions on the freedom of establishment of nationals of an EC Member State or an EFTA State in the territory of any other of these States. This shall also apply to the setting up of agencies, branches or subsidiaries by nationals of any EC Member State or EFTA State established in the territory of any of these States.*
>
> *Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms within the meaning of Article 34, second paragraph, under the conditions laid down for its own nationals by the law of the country where such establishment is effected, subject to the provisions of Chapter 4.*

8 Article 33 EEA reads:

> *The provisions of this Chapter and measures taken in pursuance thereof shall not prejudice the applicability of provisions laid down by law, regulation or administrative action providing for special treatment for foreign nationals on grounds of public policy, public security or public health.*

9 Article 40 EEA reads:

> *Within the framework of the provisions of this Agreement, there shall be no restrictions between the Contracting Parties on the movement of capital belonging to persons resident in EC Member States or EFTA States and no discrimination based on the nationality or on the place of*

> *residence of the parties or on the place where such capital is invested. Annex XII contains the provisions necessary to implement this Article.*

10 Article 125 EEA reads:

> *This Agreement shall in no way prejudice the rules of the Contracting Parties governing the system of property ownership.*

11 Article 1(1) of Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty (OJ 1988 L 178, p. 5), referred to at point 1 of Annex XII to the EEA Agreement, (hereinafter "Directive 88/361") reads:

> *1. Without prejudice to the following provisions, Member States shall abolish restrictions on movements of capital taking place between persons resident in Member States. To facilitate application of this Directive, capital movements shall be classified in accordance with the Nomenclature in Annex I.*

12 Heading III A(1) and (3) of Annex I to Directive 88/361 read:

> *A - Transactions in securities on the capital market*
>
> *1. Acquisition by non-residents of domestic securities dealt in on a stock exchange (…)*
>
> *2. (…)*
>
> *3. Acquisition by non-residents of domestic securities not dealt in on a stock exchange (…)*

III Norwegian rules on acquisition of waterfalls – factual and legal background

13 According to the documents of the case, more than 99% of the electricity supply in Norway is based on hydropower, and electricity makes up nearly half of the country's total energy consumption. The average production capacity of Norway's hydropower stations is approximately 119 TWh. In 2004, the total power production in Norway was 110.4 TWh, while total gross consumption was 121.9 TWh. In principle, the total hydropower potential from Norway's waterways is estimated to be approximately 186 TWh, with 67 TWh still undeveloped. However, due to environmental and other concerns only a relatively small part of this is likely to be exploited in the foreseeable future.

14 According to the same information, approximately 88% of the total hydropower production capacity in Norway is presently in public ownership. Approximately 45% is owned by the State itself through Statkraft AS, and more than 42% is owned by municipalities and county municipalities. The remaining hydropower resources are owned by private undertakings (domestic and foreign). Some of the private waterfalls were harnessed before the introduction of the reversion

rules explained below and are therefore not subject to those rules. However, these waterfalls become subject to the reversion rules if they are sold to a non-public entity. Today, the rules on reversion apply to approximately 7% of the existing production capacity.

15 According to the documents of the case, there are approximately 175 undertakings involved in hydropower production in Norway. Out of these, approximately 115 are organised as limited undertakings. Most power producing undertakings are owned by county municipalities and municipalities. Public ownership in the hydropower sector was originally organised as part of the administration, governed by public entities under administrative law. In recent years this has changed and public hydropower ownership is now almost entirely organised along company lines, as separate undertakings. Most of these are 100% publicly owned, often by several municipalities or county municipalities, but some of them also have private minority owners.

16 Under Norwegian law, river systems have from the very beginning been subject to private ownership. This principle is now laid down in the first paragraph of Section 13 of Act No 82 of 24 November 2000 Relating to River Systems and Groundwater (*lov 24. november 2000 nr. 82 om vassdrag og grunnvann (vannressursloven))* where it is stated: "A river system belongs to the owner of the land it covers, unless otherwise dictated by special legal status." The private ownership rights are, however, limited by public law which *inter alia* subjects the exploitation and acquisition of waterfalls to concession requirements.

17 Rules on concessions for the acquisition of waterfalls for energy production were first introduced in Norway in the early 20th century. At that time, the country was experiencing a rapid increase in investment in waterfalls for energy production. The main rivers and waterfalls were then in private ownership. Due to lack of domestic financial resources, interested investors were primarily foreign and despite general rules restricting foreign investment in real estate in Norway, many waterfalls were acquired by foreign undertakings.

18 In 1906, in order to control foreign investment in waterfalls, Stortinget (the Norwegian Parliament) adopted two Acts which subjected all foreign private investors and all limited liability companies, both foreign and Norwegian, to a concession requirement.

19 In 1909, Stortinget introduced further limitations to the acquisition of waterfalls by Act No 4 of 18 September 1909 Relating to Acquisition of Waterfalls, Mines and Other Real Property. This Act introduced the reversion system into law. According to the explanatory notes to the legislative bill, it was considered important to limit "the foreign capital's future rights over … waterfalls" and ensure that the rules prevented "foreign capital's … unlimited acquisition of … natural resources." According to the explanatory notes, the aim was also to assert the "interest of the general public, the state and the local government in this natural wealth". In light of the general public interests involved, it was regarded desirable for the State to obtain a share in and "full control over the major

waterfalls that are acquired with Norwegian capital as well." Under the 1909 Act, the reversion system applied to foreign individuals and foreign and Norwegian undertakings, but not to Norwegian individuals.

20 The ILA, enacted in 1917, replaced the 1909 Act and eliminated the above mentioned distinction between foreign and Norwegian individuals. Over the years, the ILA has been subject to several amendments. For example in 1969, the rules on the reversion system were amended by the introduction of rules on early reversion, which were subsequently amended in 1993 with the introduction of the first paragraph of Section 41 of the ILA. Moreover, in 1993 amendments were made to the ILA with the intention to comply with the EEA Agreement.

21 Rules on concessions for acquisition of ownership or rights to utilise waterfalls are laid down in Section 1 of the ILA. If the acquirer is not the State, and the waterfall can be expected to produce more than 4,000 natural horsepower when harnessed, then, according to the first paragraph, the acquisition is as a main rule subject to a concession. If the acquired waterfall is not to be utilised for power production, then, according to the fifth paragraph, the King [i.e. the Government] may permit acquisition without applying the conditions set out in the fourth paragraph of Section 2 of the Act, including the time limitation and the requirement of reversion, described below.

22 Section 2 of the ILA lays down rules regarding the right to be granted a concession for acquisition of ownership rights to waterfalls, and the conditions for such a concession, for both Norwegian and foreign individuals and private undertakings.

23 According to the first paragraph of Section 2, a concession may be granted "under special circumstances". Sub-paragraph 17 of the fourth paragraph of Section 2 states that such a concession shall be for a specified period of time of up to 60 years from the time the concession is granted. The same sub-paragraph further states that when the concession period expires, the waterfall and related installations shall revert to the State with full ownership rights and without compensation. Related installations include all the facilities through which the course and bed of the water have been altered, the parcels of land and the rights acquired for the development and for the power plant, the power stations and appurtenant machinery and other equipment, as well as the housing built for workers and other buildings that belong to the power plant.

24 Sub-paragraph 22 of the fourth paragraph of Section 2 states that if a private party purchases a waterfall during the concession period, the conditions of the original concession, including the original time limitation, apply to the new owner.

25 Section 5 of the ILA states that "under special circumstances," Norwegian and foreign individuals and undertakings may be granted a concession to acquire a right to utilise, or long-term disposition rights to, waterfalls belonging to the State, municipalities, county municipalities or certain public undertakings. The

concession shall be for a specified period of time of up to 60 years from the time the concession is granted.

26 Rules relating to the right to be granted a concession and the conditions for a concession for certain fully State-owned undertakings, Norwegian municipalities and Norwegian county municipalities, as well as undertakings in which such public entities own at least two-thirds of the shares (hereinafter "public undertakings"), are laid down in Section 4 of the ILA. Such undertakings may, "when public interests do not weigh against it," be granted a concession to acquire ownership, rights to utilise or long term disposition rights to waterfalls. A concession pursuant to Section 4 may be granted for an indefinite period and, according to NOU 2004: 26, public undertakings have always been granted a concession without time limitations. Despite differences in wording between Section 2 and Section 4 as concerns the right to be granted a concession, according to NOU 2004: 26 in practice there have not been essential differences in the way the limitations for granting a concession have been applied to public undertakings and other undertakings (hereinafter "private" undertakings; unless otherwise indicated, the term "private" will include all foreign operators).

27 Under Section 4 of the ILA, the State holds rights of pre-emption to shares or interests referred to in that provision, should two-thirds of the capital and votes in undertakings no longer be owned by one or more municipalities or county municipalities. If the State does not assert its right of pre-emption, the undertaking concerned is subjected to the reversion condition. According to NOU 2004: 26, a situation where the preconditions for the application of this provision have been fulfilled has never arisen.

28 Section 41 of the ILA provides for the possibility of so-called "early reversion". When less than 25 years remain of a concession subject to a reversion requirement, the King may, with the consent of Stortinget, enter into an agreement with the concession holder to the effect that the waterfall and related installations shall revert to the State immediately. Pursuant to the first paragraph of Section 41, the concession holder is permitted at the same time to acquire the ownership of the reverted rights for a new period of 50 years or, pursuant to the second paragraph of Section 41, to acquire the right to utilise the waterfall and appurtenant installations at the expiry of the concession period. The concession holder shall normally have the right to enter into the latter type of agreement.

29 In NOU 2004: 26, it is stated that there are about ten cases of ordinary reversion where the waterfall and related installations have reverted to the State without compensation, and with full ownership rights, at the expiration of the set concession period. Subsequently, the State has either sold or leased out the reverted rights. In most of the cases, the reverted rights have been sold to public undertakings. In one case, however, the reverted rights were sold back to the private undertaking having held the original concession. In three cases, moreover, the reverted rights were subsequently leased to the original concession holders; and in one of these cases the power plant was later sold to a private undertaking after public tender. As concerns early reversion, NOU 2004: 26 also

lists ten cases. In the first five of the cases, the reverted rights were leased back to the original concession holders. These cases all occurred before Section 41 of the ILA was amended to the effect that the State in relation to early reversion may resell the ownership of the reverted rights to the original concession holder for a period of 50 years. The last five of the cases occurred after the said legislative amendments, and in all of these cases the State resold the reverted rights to the two original concession holders.

IV Arguments of the parties

The Applicant

30 The Applicant submits that the difference in treatment of, on the one hand, Norwegian public undertakings and, on the other hand, all undertakings from other EEA States as well as all other Norwegian undertakings, entailed in the ILA, constitutes discrimination based on nationality contrary to Articles 31 and 40 of the EEA Agreement. The Applicant also submits that the difference in treatment is neither objectively justified, nor falling within the ambit of Article 125 EEA.

31 As concerns the discriminatory nature of the ILA, the Applicant mainly refers to the different conditions with regard to whether or not a concession for acquisition of waterfalls for hydropower production is time-limited, and whether or not such waterfalls and related installations shall be surrendered to the State without compensation at the end of the concession period. The Applicant also mentions other elements of the Act that, in the view of the Applicant, reinforce its discriminatory nature, such as the different criteria to be applied when assessing whether a licence should be granted, cf. Section 2 and 4 of the ILA; the conditions under which a waterfall may be rented out or leased, cf. Section 4 and 5 of the Act, and the pre-emptive rights of the State under Section 4 of the Act.

32 The Applicant explains that, mainly due to the negative effect on the economic value of a waterfall caused by time-limited concession and reversion, the difference in treatment creates a disincentive for investment. This is so even at the start of a concession period, and the difference in treatment will increase the less there is left of the concession period. The negative economic effect creates an obstacle with respect to both free movement of capital and the freedom of establishment.

33 The Applicant submits that Article 125 EEA corresponds to Article 295 EC. It infers from the case law of the Court of Justice of the European Communities (hereinafter "ECJ") on Article 295 EC that, although the Contracting Parties have the power under Article 125 EEA to define the rules governing the system of property ownership, the system and the exercise of the property rights remain subject to the fundamental rules of the Agreement. In that regard it is irrelevant, in the view of the Applicant, that the case at hand concerns natural resources. In the Applicant's view, a concession system, including rules on reversion, might as such be covered by Article 125 EEA. However, such a system must not, as the

rules at issue, result in discrimination based on the origin of the undertaking or investor concerned. The Applicant states that Article 125 EEA does not encompass preferential rights to public undertakings competing on an open market, and argues that under such circumstances, public undertakings have to be distinguished from the State and its exercise of regulatory power.

34 According to the Applicant, the ILA neither regulates who may own property nor restricts the exploitation of waterfalls to Norwegian public undertakings only. In its view, the Act only regulates ownership rights in a very broad sense, by laying down the obligations which may be imposed on a particular group of property owners wishing to exercise a specific liberalised economic activity. Finally, in relation to Article 125 EEA, the Applicant maintains that even if that Article permitted discrimination with regard to reversion, time limitations on concessions held by private undertakings could never be considered a regulation of property ownership.

35 The Applicant contends that the rules at issue are directly discriminatory and therefore only justifiable under Article 33 EEA. In the Applicant's view, what needs to be assessed under that Article is only public security and the Applicant maintains that security of energy supply is the only ground that is relevant in that respect. However, the Applicant questions the existence of a serious threat to public security and the suitability of the reversion system as a means of meeting such a threat. Moreover, it questions the necessity of making a distinction between Norwegian public undertakings and private undertakings. Therefore, the Applicant is of the opinion that the rules cannot be justified with reference to Article 33 EEA.

36 In case the Court should find that the rules at issue are not only justifiable under Article 33 EEA but also on the basis of mandatory requirements, the Applicant addresses other possible justificatory grounds advanced by the Defendant. It contests that public ownership, regardless of why it is sought, may serve as a justificatory ground. It also denies that the aim of effective collection of economic rent may constitute a legitimate public interest under EEA law.

37 With regard to all the aims referred to by the Defendant, the Applicant stresses that the core issue is not whether reversion as such is suitable and necessary to achieve these aims, but rather whether the difference in treatment with regard to reversion is necessary in order to achieve them. In the Applicant's view, that is not the case.

38 As an alternative to the rules at issue, the Applicant argues that a concession model with reversion for all undertakings would be less restrictive and at least equally effective in achieving the aims. In this respect, the Applicant rejects the relevance of whether or not the State needs, in light of the objective of public ownership, to require reversion of publicly owned waterfalls, and reiterates that a firm distinction must be drawn between the State as a regulator and as an economic operator. The Applicant also rejects the relevance of the Defendant's argument that the abolishment of the discriminatory elements may lead to public

undertakings selling out their ownership rights. It submits that it is entirely for the public authorities themselves to weigh the interests at stake and, based on that, to decide whether to sell or not. From this, the Applicant concludes that the differential treatment is not justified on the basis of mandatory requirements.

39 The Applicant adds that in any event, the considerations pertaining to public ownership do not justify the contested differential measures. The Applicant contests *inter alia* that public ownership allows for better management and control, and better protection of security of energy supply and environmental concerns, than steering via regulatory methods alone. The Applicant submits, *inter alia*, that neither have Norwegian public undertakings been entrusted with any special obligations relating to electricity supply and environmental concerns, nor are such undertakings subject to any more control in these fields than private undertakings. The Applicant also argues that it would run contrary to EEA law to presume that national public undertakings will behave differently and more reliably than private undertakings, and that there is no reason to believe that they will actually do so. In relation to the argument that public ownership allows for easier and more flexible control, the Applicant argues that advantages of a purely administrative nature are not sufficient under EEA law to justify a restriction on a fundamental freedom.

The Defendant

40 The Defendant argues that the application is unfounded, and in support of that plea advances four main submissions. Firstly, that the rules at issue fall outside the scope of the EEA Agreement. Secondly, that the rules do not constitute a restriction under Articles 31 and 40 EEA read together with Article 125 EEA. Thirdly, that the aim of maintaining and acquiring public ownership over essential energy resources is a legitimate justification under the EEA Agreement, and that the contested rules are suitable and necessary to this end. Fourthly, that the aim of maintaining and acquiring public ownership is a means of achieving other legitimate aims, such as public security, security of energy supply, environmental protection, and that the contested rules are suitable and necessary to achieve these objectives.

41 In relation to its submission on the scope of the EEA Agreement, the Defendant puts forward three main arguments. It argues firstly that the rules at issue are a part of the basic ownership structure in the hydropower sector, and as such fall under Article 125 EEA. In the Defendant's view, Article 125 EEA must be understood to the effect that a State has sovereign rights to regulate the property rights over natural resources, and has the discretion to keep its undertakings nationalised or to privatise them. It submits that Article 125 EEA does not necessarily need to be interpreted in the same way as Article 295 EC, as the EEA Agreement's legal and political characteristics differ from those of the EC Treaty. Secondly, the Defendant argues that it must be taken into account, when assessing whether the rules fall under the EEA Agreement, that they govern ownership of essential natural energy resources. Thirdly, the Defendant argues

that it is an internal public affair how States choose to regulate and organise ownership within the public sphere, which is not subject to EEA law.

42 In the event the Court should not agree that the rules at issue fall outside the scope of the EEA Agreement, the Defendant submits that Article 125 EEA must be construed to the effect that the rules do not entail a restriction contrary to Article 31 or 40 EEA. However, should the Court find that the rules are restrictive, the Defendant maintains that they are not discriminatory. In that regard, the Defendant submits that the contested measures do not differentiate on the basis of nationality, but build on a legitimate distinction between national public undertakings and all other undertakings, and that these undertakings are not in a comparable situation. The aims pursued are legitimate and justify the difference in treatment. The Defendant submits that the legal form of the public undertaking, or whether the undertaking is owned directly by the State or other public entities, does not matter in this respect.

43 Should the Court find the rules at issue directly discriminatory, the Defendant maintains that they are justified under both Articles 125 and 33 EEA. In its view, the wording of Article 125 EEA supports the conclusion that public ownership of essential natural energy resources is a legitimate objective. As concerns Article 33 EEA, the Defendant maintains that public ownership is intended to ensure security of electricity supply, which in its view must be considered a public security ground.

44 In case the Court should find that the rules at issue constitute a non-discriminatory or indirectly discriminatory restriction, the Defendant maintains that, in addition to the express provisions of the EEA Agreement, they are justified on the basis of mandatory requirements. Firstly, the general aim of maintaining and securing public ownership over essential energy resources is, in the view of the Defendant, in itself a mandatory requirement. The Defendant submits that this is the necessary corollary of the discretion conferred on each Contracting Party under Article 125 EEA, to regulate its system of property ownership. The Defendant argues also that public ownership over hydropower resources in Norway serves the public security consideration of ensuring security of the electricity supply (covered by Article 33 EEA), management and control over natural resources, environmental concerns and taxation of economic rent, which are in its view all mandatory requirements.

45 In relation to effective public management, the Defendant argues that direct public ownership, in combination with regulatory powers, guarantee the authorities a level of actual and potential management and control which is not obtainable merely through public regulation. In relation to environmental concerns, the Defendant refers to the control over limited resources such as waterfalls, making it possible to balance the need for energy supplies with future requirements for environmental protection, and states that it provides a framework for ensuring sustainable development.

46 The Defendant contests the Applicant's submission that ensuring effective collection of economic rent cannot be regarded as a legitimate objective in itself. The Defendant compares it with taxation, which inevitably serves economic aims, but may still be justified. The Defendant further maintains that this objective is in any event not the primary objective of the rules at issue.

47 The Defendant maintains that the rules at issue are both suitable and necessary for the attainment of the objectives referred to above. The Defendant argues that in the assessment of suitability, the combined effect of the rules on reversion, concessions and pre-emptive purchase rights, as well as the effects of the contested differentiation, must be taken into account. The rules consistently ensure both short and long term control, which is suitable to maintain strong public ownership, and thereby also suitable for the achievement of the other aims referred to above. It states that the main effect of the contested rules today is that they create a "lock-in" effect, which makes it economically very unattractive to sell public waterfalls to private undertakings, since the resources will have a far higher value in public ownership than in private hands. In the view of the Defendant, the current strong public ownership over hydropower resources in Norway clearly shows that the contested measures are suitable to ensure public ownership.

48 As concerns the necessity of the contested measures with regard to the aim of ensuring public ownership over hydropower resources, the Defendant expresses the view that there are no alternative regimes which will achieve this aim as effectively as the contested rules. As concerns the aim of ensuring public security (security of energy supply), environmental protection and effective collection of economic rent, the Defendant expresses the view that there are no alternative regimes which will achieve these aims as effectively as the rules at issue. The residual competence inherent in public ownership supplements the control that can be achieved through command and control regulation, and the combination ensures a higher degree of control than exclusive reliance on regulatory tools allows for. Furthermore, public ownership ensures a more efficient collection of economic rent than other alternatives, e.g. taxation. The Court must conduct a general and overall necessity review in relation to all these public interest requirements at stake, assessed as a whole.

The Intervener and others

49 The Republic of Iceland intervenes in support of the Defendant. It submits that regulation of property ownership falls outside the scope of the EEA Agreement and that it was a pre-condition for the Agreement, on behalf of both Iceland and the Defendant, that ownership over energy resources would remain unaffected by it. In this context, the Intervener refers to Article 125 EEA and states that it should be interpreted differently from Article 295 EC, as argued by the Defendant. In relation to the rules at issue, the Intervener contends that they are an inherent part of the reversion system and are a means to achieve the aim of maintaining public ownership over hydropower resources. In its view, it is

irrelevant, in light of the objective of public ownership, to what kind of public body or what level of government the ownership rights belong.

50 The Kingdom of the Netherlands interprets Article 125 EEA to the effect that States have the sovereign right to choose whether to privatise or nationalise undertakings, or maintain any such status. In its view, the Defendant is fully entitled to pursue a public ownership objective, provided it does so in a manner compatible with the fundamental rules of the EEA Agreement. It states that the rules at issue do not seem to discriminate on the basis of nationality, but finds that the concession requirement restricts the freedom of establishment and the free movement of capital. The Kingdom of the Netherlands is of the opinion that the rules at issue can be justified on the basis of the overriding goal of acquiring public ownership of hydropower resources, and that the rules at issue are proportionate in light of that goal, and therefore do not infringe Articles 31 and 40 EEA.

51 The Republic of Poland maintains that the rules at issue are justified on the basis of the public security ground of ensuring security of energy supply, and states that the contested measures are not discriminatory, and are both suitable and necessary for the achievement of this objective. In its view, Article 125 EEA applies to the rules at issue. Poland maintains that the transfer of ownership rights which the rules pursue is legitimate under that Article.

52 According to the Commission of the European Communities, Article 125 EEA must be interpreted as having the same meaning as Article 295 EC. The Commission states that the mere fact that a national rule might govern the system of property ownership does not exempt such a rule from the fundamental rules of the Treaty. Thus, the rules at issue are covered by the EEA Agreement. The placing of a time limit on any private ownership can, in the view of the Commission, be seen as an inherent part of the objective of bringing hydropower resources into public ownership. Under such circumstances, there would be no reason to place a time limit on public undertakings. The Commission interprets Article 125 EEA to the effect that States have the sovereign right to choose whether to privatise undertakings, nationalise or maintain such a status. Accordingly, the Defendant is in principle fully entitled to pursue the aim of public ownership, provided that it does so in a manner confirming with the fundamental rules of the EEA Agreement.

53 The Commission finds that the concession system at issue constitutes in itself a restriction within the meaning of Articles 31 and 40 EEA. In its opinion, the rules are not discriminatory since public and private undertakings are not in a comparable situation. Applying a system of expropriation over time to only private undertakings does not, without evidence to the contrary, seem disproportionate in light of the aim of public ownership. However, the Commission raises questions in relation to the rules on early reversion, which prolong private ownership rights and thereby weaken the effectiveness of the rules. It also questions the proportionality of the different requirements that apply

to public and private undertakings with respect to the right to be granted a concession.

V Findings of the Court

General

54 The case before the Court concerns firstly the rules of the Norwegian Industrial Licensing Act (ILA) which provide that public undertakings are granted concessions for acquisition of waterfalls for energy production without time limitation whereas others, including all foreign undertakings, are granted such a concession with time limitation. Secondly, it concerns the provisions of the ILA, according to which property rights to waterfalls utilised for energy production and related installations are transferred from private undertakings to the State at a certain time without compensation, i.e. the system of reversion.

55 In its submissions, the Applicant refers to further provisions of the ILA, such as the rules on the pre-emptive rights of the State and the rules which preclude private undertakings from renting out a waterfall, that in the Applicant's view reinforce the difference of treatment entailed in the above mentioned rules. These rules do not, however, form part of the declaration sought by the Applicant and therefore the Court will not make a ruling on their conformity with the EEA Agreement.

56 According to the Defendant, the contested rules concern the system of property ownership under Article 125 EEA and aim at securing public ownership over the property rights in question. The Applicant does not question that the EEA Agreement is neutral with respect to which system of property ownership a State chooses. Neither does the Applicant dispute the Defendant's right to introduce different classes of concessions, nor its right to have a system of reversion, as long as such systems are designed and applied in a non-discriminatory manner. In essence, what the parties disagree on is whether the rules at issue fall under the scope of the EEA Agreement and, if so, whether the differentiation entailed in the rules is in conformity with Articles 31 and 40 EEA.

Scope of the EEA Agreement and Article 125 EEA

57 The Defendant, supported by the Intervener, submits that the application is unfounded since the contested rules fall outside the scope of the EEA Agreement. In that regard the Defendant refers mainly to Article 125 EEA which it construes to the effect that rules governing the system of property ownership fall outside the scope of the EEA Agreement. In this context, it is argued that the EEA Agreement does not govern rules on management of essential natural energy resources.

58 Article 125 EEA states that the EEA Agreement shall in no way prejudice the rules of the Contracting Parties governing the system of property ownership. The

wording of Article 125 EEA corresponds to the wording of Article 295 EC. The Defendant maintains that despite their identical wording, these Articles have a different scope of application due to fundamental differences between the EC Treaty and the EEA Agreement. Moreover, it is argued that this understanding was reflected in the EEA negotiations and in subsequent parliamentary procedures in Norway and Iceland.

59 The principle of homogeneity enshrined in the EEA Agreement leads to a presumption that provisions framed identically in the EEA Agreement and the EC Treaty are to be construed in the same way. There are certain differences in the scope and purpose of the EEA Agreement as compared to the EC Treaty which may under specific circumstances lead to a different interpretation (see Case E-3/98 *Rainford-Towning* [1998] EFTA Ct. Rep. 205, at paragraph 21). Unilateral expressions of understanding of the kind claimed to have been made by Norway and Iceland cannot constitute such circumstances.

60 The Defendant argues that when assessing whether the contested rules fall under the EEA Agreement it must be taken into account that they govern the management of essential natural energy resources. In that regard, the Court notes that such an interpretation is not supported by the provisions of the EEA Agreement. No provision exempts such rules from the scope of the Agreement. On the contrary, Article 73(1)(c) EEA provides that the Contracting Parties shall in their actions relating to the environment pursue the objective of ensuring a prudent and rational utilisation of natural resources.

61 There are no specific circumstances in the case at hand which would warrant an interpretation of Article 125 EEA different from the interpretation of Article 295 EC. Since Articles 125 EEA and 295 EC are identical in substance for the purpose of the case at hand, the case law of the ECJ on Article 295 EC is of relevance when interpreting Article 125 EEA.

62 It follows from the case law of the ECJ on Article 295 EC that Article 125 EEA is to be interpreted to the effect that, although the system of property ownership is a matter for each EEA State to decide, the said provision does not have the effect of exempting measures establishing such a system from the fundamental rules of the EEA Agreement, including the rules on free movement of capital and freedom of establishment (see for comparison Cases C-452/01 *Ospelt* v *Schlössle Weissenberg* [2003] ECR I-9743, at paragraph 24; C-302/97 *Konle* [1999] ECR I-3099, at paragraph 38 and 182/83 *Fearon* [1984] ECR 3677, at paragraph 7).

63 In light of the above, the Defendant's submission that the contested rules do not fall within the scope of the EEA Agreement must be rejected.

Restriction under Articles 31 and 40 EEA

64 Article 31 EEA prohibits all restrictions on the freedom of establishment within the European Economic Area, whereas Article 40 EEA prohibits all restrictions on the free movement of capital in the area. National measures liable to hinder or

make less attractive the exercise of fundamental freedoms guaranteed by the EEA Agreement, such as the contested rules, are an encroachment upon these freedoms requiring justification (see for comparison Case C-55/94 *Gebhard* [1995] ECR 4165, at paragraph 37).

65 The differentiation entailed in the contested rules has, as argued by the Applicant, a negative effect on the value of the investment of private and foreign investors in hydropower production, due to the fact that they have shorter time to get a return on their investment as compared to Norwegian public owners of hydropower resources. The negative effect increases the less there is left of the concession period. This is not disputed by the Defendant. The differentiation is liable to operate to a particular disadvantage for foreign investors, since the rules in fact exclude them from benefiting from the more favourable provisions applying to Norwegian public owners.

66 The Court notes that Section 4 of the ILA does not set out that an undertaking must be Norwegian in order to obtain a concession for an indefinite period and therefore without a reversion requirement. Section 4 does, however, set out that Norwegian public entities must own at least two-thirds of the shares of the undertaking. The Court therefore concludes that the ILA on this point entails indirect discrimination (see for comparison Case 3/88 *Commission* v *Italy* [1989] ECR 4035, at paragraphs 8 and 9).

67 The differentiation in treatment at issue restricts the free movement of capital under Article 40 EEA, cf. heading III A(1) and (3) of Annex I to Directive 88/361. It also restricts the freedom of establishment under Article 31 EEA depending on the size of the private ownership interest in a hydropower undertaking (see for comparison Case C-524/04 *Test Claimants in the Thin Cap Group Litigation* v *Commissioners of Inland Revenue,* judgment of 13 March 2007, not yet reported, at paragraph 27).

68 With reference to the above, the contested rules fall under the scope of both Articles 31 and 40 EEA. In the situation of the case at hand, they are to be examined in parallel.

69 The Defendant's submission that obstacles inherent to rules of property ownership do not constitute restrictions on the right of establishment under Article 31 and on the free movement of capital under Article 40 EEA must be rejected since Article 125 EEA does not, as stated in paragraph 62 above, have the effect of exempting such rules from the fundamental rules of the EEA Agreement.

70 Next, it needs to be examined whether the restrictions at issue are objectively justified.

Legitimacy of the aims pursued by the contested rules

71 With regard to the legitimacy of the aims pursued by the contested rules, the Defendant mainly submits that the goal of acquiring and maintaining public ownership over essential energy resources is in itself a legitimate justification under the EEA Agreement. This is contested by the Applicant. In the alternative, the Defendant submits that the aim of acquiring and maintaining public ownership over hydropower resources and related installations is a means of achieving other legitimate aims under EEA law, namely public security through security of energy supply, public management and control over hydropower resources, environmental concerns and effective collection of economic rent. In the Applicant's view, effective collection of economic rent is an economic aim which cannot serve as a justificatory ground under EEA law.

72 The Court holds that Article 125 EEA is to be interpreted to the effect that an EEA State's right to decide whether hydropower resources and related installations are in private or public ownership is, as such, not affected by the EEA Agreement. The corollary of this is that Norway may legitimately pursue the objective of establishing a system of public ownership over these properties, provided that the objective is pursued in a non-discriminatory and proportionate manner.

73 However, for the Norwegian concession regime, with reversion to the State as an essential part of it, to qualify as aiming at establishing a "system of property ownership" within the meaning of Article 125 EEA, that regime must aim at attaining a situation where, as a matter of principle, the assets at issue are owned by public entities. A regime which merely brings or keeps this class of assets predominantly under public ownership, while at the same time leaving it to the discretion of the relevant authorities whether private ownership of the assets should be re-established, cannot be said to aim at establishing a system of property ownership under Article 125 EEA. Rather, such a regime aims at achieving a certain level of public control of the relevant sector of the economy – by means of securing public ownership of most of the relevant assets.

74 In this regard, the Court notes that, according to the ILA, not only public undertakings, but also private undertakings may obtain a concession for acquiring new hydropower resources for development. Moreover, in spite of certain differences in the wording of the relevant provisions, there are in practice no essential differences with respect to the requirements for a concession to be granted to private and public undertakings respectively. Concessions are granted to private as well as to public undertakings, if it is not contrary to public interest considerations to do so.

75 The authorities may resell reverted rights to private undertakings following a normal reversion, and have in fact done so on several occasions. Moreover, according to the so-called early reversion rules of the ILA, Norwegian authorities

have wide discretion to prolong private ownership over properties that are subject to the reversion system. In practice, Norwegian authorities have, in the cases of early reversion that have arisen after the legislative amendments in 1993, transferred the ownership rights back to the private undertakings.

76 Finally, the ILA does not in principle preclude private investors from obtaining more than one-third of the shares in a public undertaking in the relevant sector and thereby change its legal status from public to private within the meaning of the ILA. In such circumstances, the State may use its pre-emptive rights under the ILA. That is subject to the discretion of the competent authorities at any given time. If private ownership is allowed to surpass one-third, the hydropower resources and related installations are subject to reversion. This, however, merely makes private ownership of more than one-third of the shares in such an undertaking economically less attractive and therefore less likely to occur.

77 For the reasons set out above, the contested rules, as they exist today, cannot be said to aim at establishing a "system of property ownership" within the meaning of Article 125 EEA. Rather, the contested rules are aimed at achieving a certain level of public control of the relevant sector of the economy.

78 Acquiring public control does not, as such, qualify as a mandatory requirement. However, acquiring public control may be a means of attaining other goals which may qualify as legitimate aims, potentially justifying restrictions on free movement. The documents of the case show that environmental protection and security of energy supply, as well as effective collection of economic rent, are concerns which through the years have gained importance in relation to management and control of hydropower resources.

79 The Court notes first that environmental concerns are legitimate public interests under the EEA Agreement and therefore can serve as a justificatory ground in the case at hand (see for comparison Case C-2/90 *Commission* v *Belgium* [1992] ECR I-4431, at paragraphs 30-32). Moreover, ensuring security of energy supply may constitute a public security concern and therefore a legitimate aim capable of justifying a restriction on free movement (see for comparison Case 72/83 *Campus Oil* [1984] ECR 2727, at paragraphs 34 and 35 and Case C-503/99 *Commission* v *Belgium* [2002] ECR I-4809, at paragraph 46).

80 The aim of the collection of economic rent is of an economic nature and therefore cannot in itself serve as justificatory ground (see Case E-1/04 *Fokus Bank* [2004] EFTA Ct. Rep. 11, at paragraph 33). However, as stated above, the legislation at issue genuinely pursues several different objectives. Therefore, the presence of such an economic aim does not in itself invalidate other legitimate justificatory grounds.

81 In light of the above, the Court concludes that the contested rules are based on legitimate aims under EEA law in so far as the aims of ensuring security of energy supply and protection of the environment are concerned. It thus needs to

be examined whether the rules satisfy the requirements of suitability and necessity under the principle of proportionality.

Proportionality

82 In order to be justified, the contested rules must be suitable for achieving the intended objectives, and they must not go beyond what is necessary in order to attain the legitimate objectives which they pursue (see Case E-10/04 *Piazza* v *Schurte* [2005] EFTA Ct. Rep. 76, at paragraph 39).

83 With regard to hydropower resources in private ownership, the Court cannot see that reversion is suitable for safeguarding the security of energy supply, or ensuring that hydropower production meets environmental concerns, in the period prior to reversion. In this period, the reversion does not give the State any control measures which it does not already enjoy in its regulatory capacity.

84 As to hydropower resources and related installations in public ownership for which the reversion system entails a "lock-in effect", the Court notes that public ownership may in principle be suitable for giving the State effective control over the actions of the undertaking concerned. However, the Defendant has failed to demonstrate that ownership control is necessary in order to meet the aims of security of energy supply or environmental protection.

85 As pointed out by the Applicant, under normal circumstances neither private nor public undertakings in the hydropower sector have special obligations concerning energy supply. In crisis situations, the central authorities have the power to instruct all producers, whether they are subject to concessions or not, to implement necessary contingency measures. The Defendant has not demonstrated that private ownership would make full implementation of such measures less likely.

86 Most public undertakings in the hydropower sector are governed by normal company law, entailing *inter alia* equal treatment of shareholders and a requirement that the companies, within the limits laid down in the concessions, are run according to sound business practices. As the Defendant itself points out, these companies are participating in a fully liberalised market where the operators sell power on a common Nordic exchange (Nord Pool). Given that the electricity bought and sold may therefore come from Norway or from any other Nordic country, it is not likely that an individual hydropower producer would decide to adjust production in order to secure national supply of electricity. It seems that such a measure would in most cases have little effect on the total energy supply available on the Nordic market.

87 With respect to environmental concerns, the Court notes that a public undertaking producing hydropower in a given area is not necessarily owned by public entities in that area. The State-owned undertaking Statkraft AS owns approximately 45% of the total production capacity. Thus, this undertaking influences environmental conditions in a number of municipalities across the

country. Also, numerous municipalities own power stations situated at a distance from their own area. For this reason, and also taking into account the ownership structure on the Norwegian hydropower market, as described in paragraphs 14 and 15 above, it is difficult to see why public undertakings should be more inclined than private undertakings to act based on non-commercial environmental considerations.

88 Furthermore, in order for the exercise of ownership rights by public entities to be a necessary means of attaining a legitimate public interest objective, it is not sufficient that this exercise is an easier way of making the undertaking act in a certain way. It must be demonstrated that other forms of control, even if administratively more burdensome, may not achieve the relevant public interest objectives in an equally effective way. The Defendant has not demonstrated that this is the case with regard to actions which may have an impact on the environment.

89 Finally, the fact that Norwegian law allows and has allowed private and foreign ownership of hydropower resources for more than a hundred years illustrates that public security or environmental concerns cannot require Norwegian public ownership.

90 In light of the above, the Court holds that the Kingdom of Norway has infringed Articles 31 and 40 of the EEA Agreement by maintaining in force measures as laid down in the Industrial Licensing Act which grant to private undertakings and all undertakings from other Contracting Parties to the EEA Agreement a time-limited concession for the acquisition of waterfalls for energy production, with an obligation to surrender all installations to the Norwegian State without compensation at the expiry of the concession period, whereas Norwegian public undertakings benefit from concessions for an unlimited period of time.

VI Costs

91 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 that the Defendant be ordered to pay the costs. Since the latter has been unsuccessful, it must be ordered to pay the costs. The costs incurred by the Intervener and those who submitted observations are not recoverable.

On those grounds,

THE COURT

hereby:

1. **Declares that the Kingdom of Norway has infringed Articles 31 and 40 of the EEA Agreement by maintaining in force measures as laid down in Act No 16 of 14 December 1917 Relating to Acquisition of Waterfalls, Mines and Other Real Property etc., which grant to private undertakings and all undertakings from other Contracting Parties to the EEA Agreement, a time-limited concession for the acquisition of waterfalls for energy production, with an obligation to surrender all installations to the Norwegian State without compensation at the expiry of the concession period, whereas Norwegian public undertakings benefit from concessions for an unlimited period of time.**

2. **Orders the Kingdom of Norway to pay the costs of the proceedings.**

Carl Baudenbacher Thorgeir Örlygsson Henrik Bull

Delivered in open court in Luxembourg on 26 June 2007

Skúli Magnússon
Registrar

Carl Baudenbacher
President