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Brussels, 20 February 2018
Case No: 80996
Document No: 892186

EFTA SURVEILLANCE AUTHORITY

The Norwegian Ministry of Finance
The Financial Markets Department
P.O. Box 8008 Dep
NO-0030 Oslo
Norway

Dear Sir or Madam,

Subject: Own-initiative case against Norway concerning authorisation rules and practices for Norwegian banks and insurance companies

1 Introduction

By letter dated 28 August 2017, the EFTA Surveillance Authority ("the Authority") informed the Norwegian Government that, following the judgment of the EFTA Court in Case E-08/16 (*Netfonds Holdings*),[1] the Authority had opened an own initiative case to examine whether the Norwegian authorisation rules and practices for Norwegian banks and insurance companies complied with Articles 31, 36 and 40 EEA.[2] In the letter, the Authority requested the Norwegian Government to provide information, in order for the Authority to further examine and assess the matter.

The Norwegian Government replied by letter dated 28 September 2017, where it stated that the EFTA Court had not made any decisions on whether Norwegian legislation was in line with the EEA Agreement, and that the Norwegian Government would not be able to provide further comments on the matter before the case before the national courts was concluded.[3]

The case was discussed at the package meeting which took place in Oslo on 26-27 October 2017. By letter dated 15 December 2017, the Norwegian Government replied to the Authority's letter following-up on the meeting and put forward its view that the Norwegian legislation was compliant with EEA law and that the EFTA Court had not concluded otherwise, without further explaining the Government's line of argumentation.[4]

Based on the information provided by the Norwegian Government to this date and on the information which can be drawn from the judgment of the EFTA Court in the *Netfonds Holdings* case, the Internal Market Affairs Directorate of the Authority ("the Directorate") has assessed the case and has come to the preliminary view that the Norwegian legislation is in breach of Article 31 EEA.

[1] Case E-08/16 *Netfonds Holdings ASA and others v the Norwegian Government*, not yet reported.
[2] Document No 867116.
[3] Document No 875727.
[4] Document No 889073.

2 Assessment

Section 3-3(2) of the current Norwegian Financial Undertakings Act[5] reads as follows:

> *"Three quarters of the share capital in a bank or an insurance company shall be subscribed by capital increase without any preferential rights for shareholders or others."*[6]

It should be noted that before the enactment of the Financial Undertakings Act in 2015, the Commercial Banks Act[7] and the Insurance Activity Act[8] contained materially identical provisions on this matter, which were the subject of the EFTA Court judgment in the *Netfonds Holdings* case.

Section 3-3(2) of the Financial Undertakings Act may limit promoters from owning more than 25 per cent of the shares in a bank or an insurance company. The rule thus concerns those shareholdings that enable the holder to exert a definite influence on a company's decision and to determine its activities. Therefore, the national measure at issue appears to fall within the scope of Article 31 EEA, not Article 36 or Article 40 EEA. Such a rule is by its very nature restrictive and, in the opinion of the Directorate, constitutes a restriction on the freedom of establishment under Article 31 EEA.[9]

It is established case law that a national measure which restricts the freedom of establishment laid down in Article 31 EEA can be justified on the grounds set out in Article 33 EEA or by overriding reasons in the public interest, provided that the restriction is proportionate, i.e. is appropriate to secure the attainment of the objective which it pursues and does not go beyond what it necessary in order to attain it.[10]

Norway has not provided the Authority with any explanations why it considers that the legislation is compliant with EEA law. However, in the *Netfonds Holdings* case before the EFTA Court, the Norwegian Government acknowledged that the legislation at issue appeared to constitute a restriction on the freedom of establishment, but argued that it could be justified by overriding reasons of general public interest and was proportionate.[11]

According to the established case law of the EFTA Court, the overriding reasons in the general interest capable of justifying restrictions on the fundamental freedoms in the financial sector include the protection of the functioning and good reputation of the financial service sector and the promotion of the well-functioning and efficiency of the financial markets.[12] Furthermore, in the *Netfonds Holdings* case, the EFTA Court held that the objective of "reducing excessive risk incentives of owners of banks or insurance companies," particularly in relation to the risk of misuse of power, promotes the well-functioning and efficiency of the financial markets and thus reflects overriding reasons in the general interest.[13]

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[5] Lov om finansforetak og finanskonsern (finansforetaksloven) av 10. april 2015 No 17.
[6] Unofficial translation by the Directorate [Original wording*: "Tre firedeler av aksjekapitalen i bank eller forsikringsforetak skal være tegnet ved kapitalforhøyelse uten fortrinnsrett for aksjeeiere eller andre."*]
[7] Lov om forretningsbanker av 24. mai 1961 No 2.
[8] Lov om forsikringsvirksomhet av 10. juni 1988 No 39 and subsequently Lov om forsikringsvirksomhet av 10. juni 2005 No 44.
[9] See Case E-08/16 *Netfonds Holdings*, cited above, para. 111.
[10] See e.g. Case E-9/11 *ESA v Norway* [2012] EFTA Ct. Rep. 442, para. 83, and Case E-08/16 *Netfonds Holdings*, cited above, para. 112.
[11] Case E-08/16 *Netfonds Holdings*, cited above, paras. 75-82.
[12] Case E-08/04 *ESA v Liechtenstein* [2005] EFTA Ct. Rep. 46, para. 24, Case E-09/11 *ESA v Norway*, cited above, paras. 84-86, and case law cited.
[13] Case E-08/16 *Netfonds Holdings*, cited above, para. 114.

The Directorate thus acknowledges that the objectives of the Norwegian legislation may in principle reflect overriding reasons in the general interest (e.g. reducing risk incentives by ensuring a sufficiently dispersed ownership, which seems to be the aim of the legislation), but the legislation must still comply with the principle of proportionality, i.e. be suitable and necessary.

The Directorate notes that in the *Netfonds Holdings* case, the EFTA Court dealt with two alternative interpretations of the Norwegian legislation, as the exact nature of the measures appeared disputed. Irrespective however of which interpretation is to be applied, the Directorate is of the opinion that the result is a disproportionate restriction on the freedom of establishment under Article 31 EEA.

The Directorate is of the opinion that the Norwegian legislation, if understood as a requirement that *three quarters of the shares in new banks and insurance companies must be subscribed without preferential rights*, is not suitable for attaining risk reduction through dispersed ownership. As no preferential rights can be imposed in relation to 75 per cent of the shares, the ownership of these shares will be determined entirely by market interest in the public issue. If there is no broader public interest in the issue, there is nothing to prevent e.g. the promotors of the bank/insurance company, who obtain 25 per cent of the shares on authorisation, from obtaining the remaining 75 per cent. Or, for example, to prevent one outside investor from obtaining the remaining 75 per cent of the issue. The national measure does not therefore appear to prevent, in a systematic way, the promotors or any other investor from obtaining more than 25 per cent of the ownership of the bank/insurance company at the time of authorisation.[14] If, on the other hand, the legislation is understood as a requirement that *persons other than the promoters must subscribe three quarters of the shares in new banks and insurance companies*, this would still not prevent other investors from acquiring shares beyond 25 per cent.[15] The issue rule contained in Section 3-3(2) of the Financial Undertaking Act therefore does not seem suitable to achieve the objective which the Directorate understands the legislation pursues.

Even if the legislation at issue were considered suitable, the Directorate is of the opinion that it goes beyond what is necessary to attain any risk-reduction objective. It is for the Norwegian Government, in addition to raising the ground(s) for justification, to demonstrate that the measure is necessary.[16] However, as pointed out by the EFTA Court, there appear to be alternative means of obtaining the objective pursued, which are less restrictive while equally effective, such as to subject the granting of an authorisation to banks and insurance companies to special conditions aimed at preventing the risk of misuse of power.[17]

Therefore, as its information currently stands, the Directorate is of the opinion that the Norwegian legislation at issue is in breach of Article 31 EEA.

With regard to the alleged administrative practice dealt with by the EFTA Court in the *Netfonds Holdings* case, entailing that individuals and legal entities are not authorised to own more than 20 to 25 per cent of the shares in banks and insurance companies, it should be noted that the Directorate is still assessing this aspect of this case.

[14] See Case E-08/16 *Netfonds Holdings*, cited above, para. 120.
[15] Ibid, para. 121.
[16] Case E-08/16 *Netfonds Holdings*, cited above, para. 127, and Case E-09/11 *ESA v Norway*, cited above, paras. 87-88.
[17] See Case E-08/16 *Netfonds Holdings*, cited above, paras. 133-134.

3 Conclusion

In light of the above, the Norwegian Government is invited to submit its observations on the content of this letter by 20 March 2018. After that date, the Authority will consider, in light of any observations received from the Norwegian Government, whether to initiate infringement proceedings in accordance with Article 31 of the Agreement between the EFTA States on the Establishment of a Surveillance Authority and Court of Justice.

Yours faithfully,

Gunnar Thor Petursson
Director
Internal Market Affairs Directorate

This document has been electronically authenticated by Gunnar Thor Petursson.