

**How the State Aid rules
impact upon funding for
the delivery of Public
Services including
Services of General
Economic Interest (SGEI)**

Guidance notes

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GUIDANCE ON HOW THE STATE AID RULES IMPACT UPON FUNDING FOR THE DELIVERY OF PUBLIC SERVICES INCLUDING SERVICES OF GENERAL ECONOMIC INTEREST (SGEI)

Context

- One of the fundamental objectives of the EC Treaty is to create a single market in which competition is not distorted. If Member States were free to give subsidies, grants or other forms of favourable financial treatment to individual companies (or “undertakings”), there would be an inevitable risk that those “undertakings” would have an unfair advantage over competitors who do not benefit from State Aid.
- To eliminate this risk, the EC Treaty in principle prohibits subsidies which distort competition and affect trade between Member States in the EU. State aid is permitted only in limited circumstances where it can be shown to be necessary to achieve certain specified Community objectives.
- This is essential to protect competition on markets, with all the economic advantages competition brings. Subsidies can generally be seen as “something for nothing” payments, as opposed to “something for something” contractual payments for the delivery of public goods, works and services, which the market would not supply by itself. But the State aid rules will apply to payments from the public purse for public services if there is a risk of overpayment and the recipient is in a position to compete with others. In this situation there is a risk that some of the payment is a subsidy and that it might distort competition, so the State aid rules come into play. How can public authorities decide when these cases arise?

Checklist

- Is the public service activity an “economic” activity. The UK Government takes this to be a test of whether there is a competitive market for the delivery of the service. If a service is monopolised by a state body or a charity and run on a non-commercial basis as a function of the state, it is unlikely to be economic. But care must be taken to ensure that such service monopolies cannot abuse their financial position to compete in other markets. If they can, there might be cross-subsidy of such competitive activities and the State aid rules come back into play.
- If the service is economic, the next question to ask is whether the payment to the service provider is entirely commercial procurement or whether it is possible that there is an element of subsidy in the

finance. Subsidy can creep in if the procurement process is not fully competitive. There will also be a subsidy to providers, even if competitively allocated, if the activity would be supplied by the market in the absence of public sector intervention. In other words is the State supporting an activity which is inherently commercial.

- There may be good reasons for the State to offer subsidy to an inherently commercial activity, to ensure that the commercial activity meets a public interest goal, by being provided more widely, more cheaply, or by being of a higher standard. There may also be good reasons to limit access to funding for public service economic activity to a single provider or to apply conditions to a procurement process which skew the award towards a single provider or small group of potential suppliers. However, in these cases, there is a risk of distortion of competition and the State aid rules will apply.
- If the State aid rules apply, public authorities are breaking the law unless they ensure either:
 - that the spending operates within an existing UK scheme approved by the European Commission or;
 - that the spending meets the terms of a State aid “block exemption” (in particular the SGEI Decision) or;
 - that the proposed aid is notified to and approved by the European Commission before the money is spent.
- The Block Exemption route is likely to be the easiest route for compliance, except for projects which fall under the relatively narrow UK approved schemes. The Block Exemption on payments for Services of General Economic Interest (known as the “SGEI Decision”) is one potential avenue of approach for State aid payments for public service provision. The SGEI Decision offers State aid clearance for all but the largest SGEI payments below a certain threshold, subject to certain conditions. It also clears all compensation for social housing and hospitals regardless of the amount, if the conditions are met.

Why do the State aid rules apply to some cases of funding of public services?

The State aid rules form part of the original EEC Treaty, which the UK accepted as law when it joined the EEC in 1973. They form part of the Competition Policy part of the Treaty. The Treaty regulates fair competition within the common market because competitive markets are necessary for optimum economic development and therefore public welfare. The Treaty breaks down barriers to trade across all Member States, ensures that companies do not distort markets through cartels and restrictive practices

and ensures that Governments do not distort markets through subsidies, except where such subsidies are in the wider European public interest.

The Treaty does not force Member States to run their public services according to some central, harmonised blueprint. The Treaty is silent on whether services should be contracted-out or performed in-house, for example and on how they should be funded. The competition provisions of the Treaty also do not force Member States to create competitive markets in health or social services or waste disposal, for example. A choice can still be made to monopolise some service delivery through the state. But the Treaty does insist that where there is a competitive market for services, Governments cannot distort that market with subsidies unless such subsidies have approval from the European Commission.

In order for the State aid rules to apply, there must be an element of subsidy. There is no State aid if a public authority simply pays a market price for the delivery of goods or services.

But subsidies can arise in the context of payments for public service provision if the authority does not pay a market price. This could be the case if there is no competitive procurement of an economic activity or if there is overpayment, or if public intervention in the market is superfluous for achieving the social or environmental goal and is simply designed to provide support to a local supplier of goods or services.

In these cases, if the activity is economic, there may be subsidy, giving rise to distortion of market-based competition. That is why the State aid rules can apply in these circumstances and authorities providing and purchasing public services must be aware of them.

When are activities “Economic”?

The State aid rules do not apply in principle to funding for non-economic activities. Funding for local authority planning departments or the Police, for example, is clearly not State aid because the activity is regulatory and public function in nature, rather than economic.

An economic activity is one which consists in the placing of goods or services on a given market. It is not necessary for the supplier to directly charge the consumers for the goods and services – the State could pay for the service in full, but it might still be economic. It is certainly not necessary that the goods or services are supplied at a profit for them to be “economic” activities. It is not correct either to assume that because an activity is social or in the public interest, that it is not also economic.

The activity must, however, be capable of being provided commercially and the UK view is that the concepts of “economic” and “market” must, also,

contain some element of competitive supply. If a service remains a function of the state and is, for example, provided in-house by a local Council, with no possibility of competitive supply from elsewhere, there is no market and the activity will almost certainly not be “economic” in that locality.

Example: household waste collection and disposal is conducted in-house in some localities, but is contracted out competitively in many others. No charge is made directly to customers for the service. Is it economic? Most probably it is economic in those localities which have chosen to embrace competitive supply, but not in those localities which have retained a state monopoly of in-house service provision.

Example: State education is a good example of an activity which is not deemed to be “economic”. Although State schools compete to some extent in educational terms with private schools, there is not a real “market” in state-funded education. Private schools cannot displace state schools to secure local authority funding and make a profit – at least not yet. Even Academies are overwhelmingly state funded and part of the public function activity of the state to promote public education of the young. Funding for private schools, on the other hand, would almost certainly be found to be support for an economic activity and therefore could be State aid. It would not matter whether the private schools in question were charities or fully commercial – the activity is capable of being performed on a fully commercial basis.

Example: Ambulance services would historically not be seen as economic in the UK. The services were typically run as an arm of the NHS, linked to the Accident and Emergency units of NHS hospitals. The service was provided as a public function and there was no scope for competitive supply. However, if authorities ever open up mobile emergency care and/or especially more basic patient transport services to competitive supply, a market may then develop in at least a part of this service area and the activity becomes “economic”, as is the case in some other European countries. Private companies and/or not-for-profit trusts may then compete with state providers.

Example: “Meals on Wheels” services for the elderly are, at their simplest, contracts for the preparation and transport of food. It would be hard to argue that this were not an economic activity since there are many companies who prepare and/or transport food and could easily adapt their activity to offer this service. The activity itself is not a function of the state, even if some authorities choose to perform the service in-house. If, however, it were combined with an element of social or nursing care, which required specialised training and skills, the case for arguing it to be non-economic might be stronger, is such specialised care were offered as a function of the state.

If a Service is Economic, how to avoid a State aid?

As stated above, even where the activity is economic, in order for the State aid rules to apply, there must be an element of subsidy, which distorts or threatens to distort competition and affects intra-community trade. There is no State aid if a public authority simply pays a competitive market price for the delivery of goods or services.

In practice, UK authorities will normally subject contracts for the provision of “economic activity” public services to competitive tender following the European public procurement rules. In the vast majority of these cases, there is then no need to worry further about State aid. The authorities will be paying a market price for goods or services. There will be no element of subsidy to the supplier and therefore no State aid.

We have identified four scenarios which could provide exceptions to this general principle:

1. Overpayment

- The most obvious case is where the State pays more than is necessary for the delivery of works, goods or services by private or not-for-profit companies. This would be hard to square with value-for-money constraints in the UK, but it may happen if authorities fail to use rigorous, competitive procurement and best procurement practice to ensure that only a market price is paid, (whether lowest price or most economically advantageous tender). And it may happen if certain types of bidder are excluded from any competition.

Example: A local authority lets a major street cleaning contract, but decides to reserve it to not-for-profit organisations as part of an effort to support social enterprise in the city. The activity has been competitively supplied for some years so it is clearly “economic”. A private company could have performed the service for less. Any potential overpayment to the not-for-profit organisation will be State aid.

2. In-house provision

- Another case is when a public service or supply is not contracted out competitively, but rather conferred on a monopoly supplier, whether within the public authority or in the form of a not-for-profit organisation or perhaps a PPP. In these cases, the State might pay more than a theoretical market price but there will often be no market and the activity may not be “economic” (see above). If the activity is not “economic”, there will normally be no State aid, even if there is doubt about over-compensation, but great care must be taken to make sure the activity is not economic. And even if the activity is not economic in

the Authority's own local area, the recipient of the subsidy may have other activities which **are** economic and competitive, so the provider of funding must also make sure no cross-subsidies are possible.

Example: A local authority has decided to retain in house the provision of doorstep waste collection and disposal services. They have never been contracted out in that authority and continue to be run by an arm of the Council, so are deemed to be "non-economic". Now the authority decides to fund a recycling centre, still within the local Council service arm, but in order to achieve efficiencies of scale, the recycling centre then bids for work from neighbouring authorities, which operate competitive supply. The recycling centre is now offering a service "on a market" and therefore performing an economic activity. A part of the funding for the recycling centre can therefore suddenly become State aid, even if its activities within its "home" authority are not economic. The home authority will have to ensure that the Recycling Centre runs its competitive, market activities on an entirely commercial and non-subsidised basis, including separate accounts and proper cost-accounting for central overheads. Otherwise a part of its direct funding for the Centre risks being State aid.

Example: An authority offers a contract to a not-for-profit organisation to organise certain cultural events and activities in its local area. The cultural events, to the extent they happened at all, were previously supplied in-house within the Council or by charities using their own resources. These particular cultural activities are most probably non-economic in nature, so the funding is not State aid. However, the recipient is also engaged in training services, some of which are supplied in competition with other providers and runs an immigration and employment service to the ethnic community it serves, again in competition with commercial suppliers of services. The authority must make sure it is not unwittingly cross-subsidising these competitive market activities.

3. Supplementing the Market

- There could also be subsidy if a public authority purchased goods, works or services which would have been supplied anyway by the market, without the need for public intervention. This scenario might arise if a public body just wanted to control how a service is supplied: e.g. ensure that a supplier invested in a local facility as opposed to supplying at a distance, or ensure lower prices for local residents, or secure a quality enhancement in service supply to certain local groups. A competitive procurement in one of these scenarios might look rather like a subsidy auction – if so, the subsidy would be minimised, but it would still be a subsidy.

Example: An authority lets a contract with a telecoms company to supply high-speed broadband connections throughout its territory. There was clear

market failure for such supply in some of the rural areas, but the market would have offered the service anyway in many of the towns and cities within the authority's territory. In addition the authority specifies minimum service quality and (in rural areas) maximum prices which the telecoms company can charge. The authority runs a fully competitive tender for the contract and argues it is simply paying the market price for the services in question. It is, however, purchasing a service which, in part, the market would supply anyway, so a part of the expenditure might be seen as compensation going beyond normal market conditions. The competitive tender will have reduced any subsidy to a minimum, but it will still probably be a subsidy and therefore a State aid.

4. Superfluous purchasing

- Finally there could also be a subsidy in the unlikely event that a public authority bought goods and services it did not need to fulfil its public functions. It might do so to support local businesses, for example. Even if it paid a market price, this would be a market distortion which might amount to State aid.

Example: An authority in Spain once bought an advance supply of a very large number of ferry tickets from the company offering services out of its main port. The purchase went far beyond the authority's internal needs and was clearly designed to promote employment in the town, rather than constitute a genuine procurement. The transaction was found to constitute State aid.

Entirely Local Services

As stated above, for there to be a State aid, there must be an element of subsidy, which distorts or threatens to distort competition and affects intra-community trade. Any aid for an economic activity will normally be found to have the potential to distort competition, but in exceptional circumstances it might not affect intra-community trade.

In practice, the European courts have unfortunately set the bar extremely low for those seeking to prove that a subsidy has an impact on intra-community trade. Support for dentists in Austria was recently found to have such an impact because Austrians could go to Hungary, for example, for dental treatment if they so chose. However, support in the UK for local tradespeople, such as hairdressers or plumbers, corner shops or musicians would normally be pretty safe, as would support for local attractions run by not-for-profit bodies, such as stately homes and gardens or restored steam train lines, as such activities are unlikely to have an impact on intra-community trade. Public authorities need to be much more careful if an activity is subject to large firm competition or if a service might have the scale to attract foreign visitors (who would not otherwise have come to the UK) or where foreign

companies might choose to set up in the UK to compete in our market. Public authorities in Northern Ireland would have to be especially careful about using this exception due to trade with the Republic of Ireland.

If there is State aid, how to avoid illegality?

Not all State aid is illegal, but any State aid must be approved, directly or indirectly by the European Commission in order to be legitimate. This can happen in any one of three ways:

- By fitting the aid inside an existing UK scheme, which has been prior approved by the European Commission or;
- By fitting the aid within one of the Commission's State aid "block exemptions" or;
- By notifying the proposed aid to the European Commission and waiting for its approval before committing the expenditure.

Of these, the third option is clearly the least attractive. This is because the Commission typically takes 4-6 months to make a decision and in especially tricky cases, it can take up to 2 years. The notification process is also administratively burdensome, requiring authorities to draw up a notification and provide supporting evidence to justify its proposed action. All notifications must be submitted through BIS.

If the proposed aid is likely to seriously distort competition, it may not be approved at all. Most State aid with a genuine social or environmental or cultural focus will be approvable, on the other hand, but a delay is inevitable.

Where possible, therefore, authorities should seek to work within one of the first two options.

UK Approved Schemes

The UK has identified a number of types of State aid which commonly arise and has therefore sought prior advanced clearance for these sorts of expenditure, to save individual authorities from having to notify the Commission each time.

A full list of UK approved schemes can be found at:

http://ec.europa.eu/competition/state_aid/register/ii/by_ms_gbr.html

The main ones relevant to authorities funding public services are as follows:

Speculative and Bespoke Gap-Funding can be used to support private sector initial investment in land and property regeneration projects that would not proceed without public sector support.

http://ec.europa.eu/comm/competition/state_aid/register/ii/doc/XR-22-2007-WLAL-en.pdf

Details of this scheme can be found at:

<http://www.erd.comunities.gov.uk/Repository/WordDocuments/RegInvest2912>

Housing Gap Funding can be used to support the development of new housing for sale or private rental on the open market, or at below market value, where the costs of development are likely to exceed end use. It can also be used to reduce the sale price to purchasers in areas where individuals on low incomes are excluded from owner-occupation or the private rented sector.

Details of this scheme can be found at:

http://ec.europa.eu/community_law/state_aids/comp-2006/n293-06.pdf

Heritage Aid can be used to support the repair, restoration and rehabilitation of designated historic buildings, conservation areas, ancient monuments and historic parks and gardens where this would otherwise not happen through market forces alone. In many cases, the intention is also to ensure that the heritage interest will be maintained for the future. Lastly, the scheme will ensure public access to a greater proportion of the nation's heritage assets.

Details of this scheme can be found at:

http://ec.europa.eu/community_law/state_aids/comp-2006/n356-06.pdf

These schemes are all administered by the Department for Communities and Local Government.

There are also a number of specific schemes whose principles might usefully be drawn upon by local authorities designing their own measures. The examples below illustrate both non aid and compatible aid arguments – on a number of different legal bases.

Newquay Cornwall Airport Development – infrastructure aid to regional airports:

http://ec.europa.eu/community_law/state_aids/transports-2007/n303-07.pdf

North Yorkshire NYNET Project – provision of rural broadband:

http://ec.europa.eu/community_law/state_aids/comp-2006/n746-06.pdf

Aid of a Social Character for Air Services in the Highlands and Islands of Scotland:

http://ec.europa.eu/community_law/state_aids/transports-2008/n027-08.pdf

Screen East Content Investment Fund – no aid decision on regional film fund:

http://ec.europa.eu/community_law/state_aids/comp-2006/n194-06.pdf

Great Yarmouth Outer Harbour – no aid decision for funding of open access port infrastructure:

http://ec.europa.eu/community_law/state_aids/transports-2005/n503-05.pdf

Commission Block Exemptions

Three Block Exemptions are relevant in a public service context. The best option is to use the General Block Exemption, where possible, as it gives legal clarity. De Minimis is an option where authorities are offering small scale support, but there is always a slight worry about cumulation where volumes of aid start approaching the limit.

The “SGEI” Block Exemption explained below is also an option. It is particularly adapted to support for public service delivery, but its scope is not fully clear and the conditions must be adhered to. It may be the only option for some types of expenditure, but where possible, it is better to design out the State aid by using competitive procurement, for example, or consider the scope to use an existing scheme or other block exemption than to rely on this instrument.

De Minimis:

<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2006:379:0005:0010:EN:PDF>

The De Minimis Regulation allows for aid of up to €200k to be provided to any undertaking regardless of size, so long as the enterprise has not received de minimis aid from any other source in the last three years which would result in the total de minimis aid to that company exceeding the threshold. De minimis aid cannot be given to road hauliers or farmers or for directly export-related activities. While we do not need to report on the granting of De Minimis aid to the Commission, records must be kept for a minimum of ten years.

The requirement to limit De Minimis aid for any individual recipient to €200k over three years applies to all De Minimis aid from all public funds for that company. Given that it is very difficult to identify how much De Minimis aid a company has received from all public funds, there is an element of risk in offering aid on this basis especially when an authority is offering amounts close to the threshold. The risk can be mitigated by asking the recipient to declare any previous De Minimis Aid received, but this doesn't offer total security. BIS recommends that authorities exercise care in using De Minimis, if it looks possible that the aid would materially distort competition and cause other businesses to complain.

General Block Exemption (GBER):

<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:32008R0800:EN:NOT>

This new Regulation is broad in scope and authorises aid, within specified limits, in favour of small to medium sized businesses (SMEs), research, innovation, regional development, training, employment, risk capital, environmental protection and measures promoting entrepreneurship including aid for young innovative businesses, newly created small businesses in assisted regions and measures to help female entrepreneurs. There are provisions that are specific relating to the kind of aid that is being granted and there are also common provisions covering issues such as transparency and reporting to the Commission.

Aid schemes that use this Regulation as legal cover must be registered with the Commission within 20 days of implementation.

The GBER is mostly designed to allow public authorities to provide business support, especially for SMEs, to encourage economic development. Most of its provisions are of limited relevance for authorities concerned solely with public service delivery. However, some of the regional development and environmental aid provisions, in particular, may be useful in offering state aid cover when authorities seek to engage businesses and commercially active social enterprises in public service delivery, especially when critical infrastructure needs to be developed to enable the public service offering.

SGEI Decision (Block Exemption):

<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2005:312:0067:0073:EN:PDF>

This block exemption is specifically designed to allow support for undertakings, where such support is necessary for the delivery of public services. It is however difficult to interpret, depending, as it does, on the

concept of a SGEI, a concept not generally familiar to UK lawyers. Conditions also apply, which might prove onerous for some authorities.

BIS advises that the block exemption should only be used if necessary and that public authorities must, if they rely on this instrument, take the trouble to understand it, including its limitations.

a) What is an SGEI¹?

Defining an SGEI is the responsibility of each EU Member State, but the Commission has stated that it is up to them, when called upon, to assess the economic nature of the activity in question and to check that the Member State has not committed a manifest error of assessment by classifying it as a task of general interest.

This means that the UK has a wide discretion to define SGEI, but this is subject to review and correction by the Commission and the European Courts if our definition is so wide as to be beyond a reasonable margin of discretion.

There are a number of things that can be said about SGEIs' characteristics that will help to avoid misclassification.

Economic: What is clear is that the term only covers services which are "economic". If an activity is not "economic", the State aid rules do not apply and there is no need to worry about Block Exemptions or whether the activity is an SGEI.

General Interest: The services must also be provided in the interests of the general populace. There must be an element of public good for the population as a whole, whether environmental, social, cultural or other, non-economic welfare. The fact that a service contributes to the economic development of the region or increases employment will almost certainly not be enough, by itself, to qualify the service as an SGEI.

A service which the market would supply anyway, to the standard required by the state, would almost certainly not be an SGEI. If there is no market failure it will be difficult to justify the existence of an SGEI.

A service for the benefit of a small sub-section of the community only would also probably not qualify, unless the service targeted special needs.

¹ In this context, you may have heard of the Altmark case. This however does not provide guidance on whether an activity is an SGEI. Instead the case sets out conditions which if met mean that funding for the provision of an SGEI is not aid. It is the view of the UK that these conditions are difficult to meet and we are not aware of any instances in the UK where all the conditions have been met. More recent case law might lead one to infer a softer approach, but the position is rather unclear. At present, we would therefore not rely on Altmark or subsequent cases to determine the presence of aid in SGEI funding; rather we would recommend that you follow the principles articulated in the first part of this guidance.

Services provided to assist businesses only, such as business incubation services, or finance for small businesses, would probably not be SGEIs.

The UK also takes the view that a pure localised, spatial market failure would not be sufficient to give rise to an SGEI if the service in question can be sourced elsewhere by the general public.

Example: It might be difficult to claim that the establishment and operation of a new recycling facility in one location would constitute the provision of an SGEI where there is a facility with adequate capacity nearby.

Example: It might be difficult to claim that support for undertakings building or operating airports or port infrastructure constituted compensation for provision of an SGEI in areas that are already served by functionally adequate transport facilities.

Example: An authority wants to support healthier eating, especially higher consumption of fruit and vegetables. The strategy has three prongs:

- Provision of information leaflets by the state through a general mailing and hand-outs in doctors' surgeries and schools. This would be unlikely to raise State aid problems. The economic bits of the activity (printing and bulk mail) would probably be contracted out competitively and the non-economic bits (content and distribution through doctors and schools) would probably not be "economic".
- Subsidies to independent local grocers for delivery of reduced-price fruit and vegetables to certain people living in poor-health neighbourhoods. This would clearly be subsidy of an economic activity and it would have the capacity to distort competition in the groceries market. It would probably not be justifiable as an SGEI, because people in the poor-health neighbourhoods would have been able to access fruit and vegetables in supermarkets anyway and the subsidised doorstep deliveries from independent grocers may end up costing them as much as it would have cost them to shop at a large supermarket. The policy in that case would be mainly a subsidy to independent local grocers and it would need to be squared with the wider State aid rules.
- Payments to the companies with long-term contracts providing food in state schools, NHS hospitals and prisons to encourage them to supply healthier meals with more fruit and vegetables. This would be support for an economic activity, but supporting it in this way probably would be state aid for an SGEI as the measure would have a clear public health benefit and would benefit such a sizeable minority of people that it would be in the "general interest". It would have the potential to be State aid because the support would not initially be subject to competitive pricing. Of course, as the contracts came up for renewal

the healthy eating specification could then be built into the tender conditions such that the State aid could then be removed.

Example: A community website is set up to assist citizens in accessing locally available goods and services. It contains a number of features:

- Details of Council services which are supplied for free and guidance on how to interact with service providers, plus public service announcements. This feature would most likely be mainly public function and support for non-economic activities so there would be no State aid issues. The website would only have to take care when promoting any Council services which are offered in competition with other service providers. These services would probably be economic.
- Promotion of local business services requiring local presence and local tourism facilities on a non-discriminatory basis with user generated content. This would be support of economic activity but it might well be an SGEI as it would help citizens to access locally supplied services (which is in the public interest). In practice, the local authority might prefer to rely on the De Minimis Block Exemption here as the advantage to each business would be very small.
- Promotion of services which do not require local presence (e.g. insurance services or savings products) but with access only for locally established companies. This would be support for an economic activity and would not be an SGEI. The support would not meet a general interest objective (the needs of the citizens could equally be met by companies located outside the local area), rather it would be support for local employment in the financial services companies concerned.

Example: Support for music festivals. The activities of hosting and marketing concerts and supplying music services may or may not be fundamentally economic and competitive. A festival of early church music, for example, hosted in churches, would probably be non-economic, whereas support for a guitar festival hosted through pubs and clubs may well be support for an SGEI. The aim of bringing music to the people and highlighting talent which would otherwise not be commercially exploited would probably be justifiable as in the general interest, but the activities would be fundamentally economic. (Note, however that support for local musicians might be an entirely local service and therefore not a State aid at all because there would be no impact on intra-community trade (see above). The aid to pubs and clubs, on the other hand, might not escape on this basis, if there were large pub chains involved).

Over time the festival might develop its own commercial momentum and might even attract acts or audiences from other EU countries. At that point continuing public support might stop being support for an SGEI and become simply State aid, unless it was focused on enriching the musical experience in ways that could not be achieved on a purely commercial basis.

b) Legal protection for State Aid for SGEIs

The Block Exemption covers the following cases of aid:

- Annual aid for a service of general economic interest (SGEI) of less than €30m given to undertakings whose annual turnover in the last two financial years was less than €100m.
- Aid of any amount for hospitals and social housing – provided that providers are carrying out SGEIs.
- Compensation for air or maritime links to islands with annual traffic in the last two financial years of less than 300,000 passengers.
- SGEI compensation for ports and airports where annual average traffic in the last two financial years does not exceed 1 million passengers in the case of airports and 300 000 passengers in the case of ports.

Aid for SGEIs in the fields of broadcasting and land transport is not covered by the Block Exemption. Only support for operational service delivery is covered by the Block Exemption. It would not directly cover investment aid for a company to set up a new factory or warehouse, for example.

c) What are my responsibilities if I am giving aid under the Block Exemption?

You must define the Service of General Economic Interest that you want to have provided. The Commission recommends that you consult on the terms of the SGEI and in particular seek the views of consumers – this is only a recommendation and not an absolute requirement. The definition should be as precise as possible.

You must entrust the SGEI to the recipient undertaking properly. Entrustment may be made by means of primary legislation, a contract or a Ministerial letter. However it is done it must set out the following:

- The nature and the duration of the public service obligations, and what is to be supplied and the quality required
- The undertakings and the territory concerned
- The nature of any exclusive or special rights assigned to the undertaking
- The parameters for calculating, controlling and reviewing the compensation
- The arrangements for avoiding and repaying any overcompensation.

This entrustment document should be made publicly available, for example on a website. Competitors should be able to see exactly who you are funding, where, why and how much you are giving. If competitors are

unaware of the terms of your entrustment they may complain to the Commission that you have given unnotified aid.

You must ensure that there is no over compensation – i.e. you must pay only the amount needed to discharge the service but allowing the undertaking to make a reasonable profit based on a rate of return on capital adjusted to the level of risk to which the undertaking is exposed in carrying out the service. This should not exceed the normal profit levels of companies in the sector. SGEI funding is only supposed to ensure that the entrusted company is no worse off because it carried out the service – it should not be significantly better off.

You must make regular checks to ensure that there is no over compensation. This is not fire and forget aid. However if there is over compensation and it is less than 10% of the annual compensation this can be carried over to reduce payments the next year.

You must keep detailed records of the aid given. The UK will have to provide reports every three years on the working of the block exemption. These records are the only way of proving that you have complied with the block exemption and have not given illegal aid. They must be kept for ten years and the Commission can ask to see them at any time.

d) Separate Accounting:

If an undertaking is performing SGEIs alongside other, fully commercial activities, there must be separate accounts for both activities according to the State aid Transparency Directive BIS will be issuing separate guidance on this subject in the near future. It is the responsibility of the aid grantor to ensure both that aid recipients are aware of this legal obligation and that aid can be recovered from recipients who fail to comply.

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