



EUROPEAN COMMISSION

Brussels, 10.12.2003  
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**Subject: State Aid N 282/2003 – United Kingdom**

**“Cumbria Broadband – Project Access – Advancing Communication for Cumbria and Enabling Sustainable Services”**

Sir,

## **1. PROCEDURE**

By letter dated 26 June 2003, registered at the Commission on 3 July 2003, the UK authorities notified to the Commission, pursuant to Article 88(3) of the EC Treaty, the above mentioned measure. By letter D/54621 dated 17 July 2003, the Commission requested additional information, which was provided by the UK authorities by letter dated 22 July 2003. By letter D/55155 dated 11 August 2003 and by letter D/56108 dated 29 September 2003, the Commission requested additional information regarding the notified scheme. This information was submitted by the UK authorities by letters dated 9 September 2003 and 20 October 2003, registered at the Commission on 15 September 2003 and 22 October 2003.

On 4 September 2003, a meeting with the UK authorities took place in order to further discuss issues related to the measure.

## **2. DESCRIPTION OF THE MEASURE**

### **2.1. Objective of the measure**

The aim of the “Cumbria Broadband - Project Access (hereafter referred to as “the project”) is to ensure the provision of high-speed broadband services in Cumbria and parts of North Lancashire. By doing so, the UK authorities intend to stimulate the

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provision of affordable broadband internet access to regions characterised by extremely low population densities.

## **2.2. Rationale of the measure**

Due to their remote location, the mountainous topography and a general lack of large conurbations, Cumbria and parts of North Lancashire have little access to high speed digital services. The lack of such services is significantly impeding the socio-economic development of the region. In order to revitalise the dynamics of the region, the provision of broadband internet services is necessary. Proactive government support is hence needed as there is little financial incentive for companies to invest in providing broadband access to residential customers in such areas since costs are high relative to revenues. By pooling the demand of local public authorities as well as residential customers, the UK authorities intend to provide a time-limited integrated broadband solution for rural and remote areas where market forces may be insufficient to provide coverage. The extension of the geographical reach of broadband access is simultaneously reinforcing the Commission's goal to widen access to high-speed internet services.

## **2.3. Legal basis of the measure**

The legal basis of the measure is section 5(1) of the 'Regions Development Agency Act 1998'.

## **2.4. Duration of the project**

The duration of the project will be 3 years. An extension of a maximum period of 2 years is possible.

## **2.5. Administration of the measure**

The North West Development Agency (NWDA) will have statutory responsibility for the implementation of the project.

## **2.6. The two constituent elements of the measure**

The project combines two elements in order to generate the *critical mass of demand* to attract potential service providers:

- i. The provision of *e-government services* to public buildings including local authority buildings, museums, libraries, and fire-stations.
- ii. A service contract for the provision of technologically neutral core broadband services for residential customers.

## **2.7. The procurement process under the measure**

Under the provisions of the scheme, the future contractor will be chosen through an open tender procedure for a period of 3 years (with the possibility of extending it for up to a further two years) for the provision of broadband services throughout Cumbria and parts of North Lancashire.

An advertisement will be published in the Official Journal of the European Communities. At the same time, a general *Statement of Requirements* will be issued to potential contractors. The *Statement of Requirement* will oblige potential service providers to demonstrate a detailed financial overview of the costs of providing broadband services in the region, including detailed estimations and projections of the expected number of customers, the expected revenues, capital expenditures and fixed and variable costs of the service provision. Potential suppliers will also have to define the basis on which charges to end users and potential wholesale buyers will be made.

The final procurement of the services will be conducted in accordance with Council Directive 92/50/EC<sup>1</sup> under the negotiated procedure<sup>2</sup>. After the expression of interest by interested potential service providers, the administering authority will issue an invitation to negotiate. This invitation will incorporate a draft *Broadband Service Agreement* setting out the contractual requirements for the provision of the services. The administering authority will then invite the short-listed parties to submit their best and final offers. Finally, the contract will be awarded to the *economically most advantageous tender* (best value solution), which will not necessarily be the one offering the lowest price.

## **2.8. The provision of retail services under the measure**

The selected service provider will be contractually obliged to provide broadband services to residential customers in Cumbria and parts of North Lancashire. In doing so, the service provider will always have to provide broadband services of at least the same scope, content and quality as broadband services supplied on a national level (with British Telecom's broadband service *BT openworld* or the broadband service of any over provider that may substitute BT and provide similar services as benchmark) to end users. The selected service provider must not require an end user to acquire or maintain any particular means of communication (e.g. a telephone line or similar installations) as a prerequisite of delivering such services.

Furthermore, the service provider shall also provide a number of broadband services to public authorities in the region. It shall also provide the relevant technical infrastructure enabling such customers to connect to and use broadband services.

## **2.9. The provision of wholesale services under the measure**

Where requested by any other potentially interested *Internet Service Provider (ISP)*, the selected service provider shall provide wholesale services to such ISPs in order to permit them to provide broadband services to those customers who wish to use a broadband provider other than the winning service provider. The service provider shall establish and maintain points of connection reasonably required - with view to sufficient capacity and sufficient number - to enable data conveyed between an ISP's telecommunications

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<sup>1</sup> Council Directive 92/50/EC of 18 June 1992 relating to the co-ordination of procedures for the award of public service contracts.

<sup>2</sup> The negotiated procedure was selected because the commercial novelty of the services required did not permit overall pricing of the services and as the service delivery is required to be on a technology neutral basis it was not possible to define the mix of technologies with sufficient precision to enable a restrictive procedure approach.

systems, its customers and the technical infrastructure to conveniently meet all reasonable demands. Such wholesale services as well as the opportunity to enter into relevant agreements shall be offered promptly without delay of any kind.

#### **2.10. The *Broadband Services Agreement* under the measure**

A *Broadband Services Agreement* will be concluded with the selected service provider. As part of this agreement, the service provider will be obliged to establish a core broadband service passing within 5 km of 90% of the citizens and businesses in the region. The *Broadband Services Agreement* will stipulate service levels and milestones to be achieved by the service provider during the agreement. The service provider shall perform services pursuant to an agreed implementation plan and in accordance with specified service levels during the term of the *Broadband Services Agreement*. The administrative authority will follow up on milestones and will monitor the performance of service levels. Delays or non-compliance will be sanctioned by liquidated damages.

The project provides for a network involving the building of technical infrastructure that will be open to all ISPs. The service provider must allow universal access to other broadband service providers delivering the “*last mile connection*” at least under the same conditions and of the same quality as it provides for its own services. The principle of technological neutrality will be respected insofar as the project will favour no particular technology nor will limit the technology choice of the region.

#### **2.11. Fees paid by residential end users under the measure**

Services to end users will be provided at a capped rate (with British Telecom’s rate as benchmark rate) specified within the *Broadband Services Agreement* regardless of whether the costs of the provision of services exceed such rate. According to the UK authorities, BT rates are the cheapest available rates for broadband services offered on a retail basis to a majority of users on a national level. Prices for wholesale services to ISPs will be derived from the service provider’s relevant costs, including a reasonable rate of return on investment. The prices for wholesale services to ISPs shall in no case exceed BT wholesale rates.

#### **2.12. Eligible costs under the measure**

Eligible costs must be directly attributable to the project and will cover only the cost of providing services for the period of the *Broadband Services Agreement*. The price payable to the service provider by the administrative authority for the provision of the services will depend on the level of demand within the region during the contract term. If demand reaches a level at which a broadband provider would reasonably be expected to provide the services without financial assistance (*e.g.* where demand reaches a level similar to that in an urban area where broadband is currently provided by the Service Provider), payments will only be made for the provision of services to the public authorities in the region.

The fees payable to the service provider will be subject to an annual internal review by the administrative authority in order to reconcile the fees with the demand levels reached. Payments will be reviewed against performance of the services in accordance with the requirements set out within the *Broadband Services Agreement*. Payments for services will only be made after satisfactory progress has been made verified against the timetable, benchmarks and milestones incorporated within the *Broadband Services Agreement*.

## **2.13. Repayment of aid under the measure**

In order to avoid over-compensation to the service provider as demand grows, a rebate mechanism will be incorporated in the *Broadband Services Agreement*. This mechanism will provide that the annual contract payments to the service provider will be abated by a percentage of the income earned in the proceeding year. If there is significant demand for the services, it is envisaged that up to the totality of the sums paid for the services may be recovered by the administrative authority.

## **3. ASSESSMENT**

### **3.1. Legality**

By notifying the measure, the UK authorities respected their obligations under Article 88(3) of the EC Treaty, although they are of the opinion that no aid is involved because a tender procedure is followed.

### **3.2. Existence of State aid**

The Commission has assessed the existence of aid within the meaning of Article 87(1) of the Treaty on two different levels, namely aid to the service provider as well as aid to residential end users.

#### *3.2.1. Aid to the service provider*

Payments for the provision of services under the project are provided by a public-funded regional development agency. The measure is therefore financed through State resources within the meaning of Article 87(1) of the EC Treaty. Moreover, the measure is selective, as the selected service provider will be a single undertaking. Furthermore, the measure has the potential to affect trade between Member States as it cannot be excluded that the selected enterprise will be engaged in activities which are subject of trade between Member States.

The Commission also considers that the measure distorts competition by conferring an advantage on the appointed service provider. In order to provide the required services within the region covered by the *Broadband Services Agreement*, the UK authorities have stated that there will be a need for significant investment in technical infrastructure (e.g. for the deployment of new infrastructure and/or the upgrade of existing infrastructure) by the successful service provider. The service provider will, *via* the fees charged to the public and to the residential private customers, be compensated for the costs of the initial investment in the technical infrastructure. This infrastructure will, however, remain in the ownership of the service provider upon termination of the *Broadband Services Agreement* and the service provider will hence be able to exploit it commercially. Moreover, by being selected to provide broadband services to a broad range of local public authorities and institutions over the whole duration of the *Broadband Services Agreement*, a certain aggregated level of demand for broadband services will be confined to the service provider and will hence not be available to potential competitors. Accordingly, the Commission considers that the project can confer an advantage to the service provider.

This conclusion is, in the light of the conditions set out by the Court of Justice in its *Altmark*<sup>3</sup> judgment, not altered by the fact that the service provider will be selected through a tendering procedure. First, it should be noted that the UK authorities intend to use a negotiated procedure, so that the terms of the eventual agreement with the service provider are not clear yet. Therefore, the second condition of the *Altmark* judgment, according to which the parameters on the basis of which the eventual compensation is calculated have to be established beforehand in an objective and transparent manner, is not fulfilled in the present case, since these terms will be set out in the *Broadband Services Agreement*, to be finalised in the negotiations with the candidate service providers. Second, given that the infrastructure will be in the ownership of the service provider after termination of the agreement, it cannot be excluded that the compensation awarded eventually exceeds what is necessary to cover all or part of the costs that the service provider will incur in discharging itself of its obligations.

In view of the above, the Commission cannot exclude the existence of aid at the level of the service provider.

### 3.2.2. *Aid to residential end users*

The project involves the provision of broadband services to individuals and enterprises in Cumbria and parts of North Lancashire. The Commission considers that private individuals are not undertakings within the meaning of Article 87(1) of the EC Treaty and thus cannot be considered to be recipients of aid.

As far as enterprises situated in the region are concerned, the Commission has come to the following conclusion. The project involves the use of state resources, as public funding is made available for the provision of broadband services to enterprises. The measure is selective, as it is limited to undertakings established in the region and has the potential to affect trade between Member States as it cannot be excluded that the enterprises benefiting from the measure will be engaged in activities which are subject of trade between Member States.

Moreover, the measure distorts competition by conferring an advantage on the enterprises. The enterprises will enjoy access to broadband services more rapidly and to conditions that they would not have enjoyed under normal market conditions. This is demonstrated by the fact that under the *Broadband Services Agreement*, the service provider will always charge prices not exceeding those in “wired-up” urban areas, like London and Manchester. As demand for broadband services in such “wired-up” urban areas will regularly exceed the demand in rural and remote areas like Cumbria and parts of North Lancashire, it follows that the price for such services would have to be significantly higher in the remote areas. Enterprises under the present scheme are thus only charged prices of highly populated urban areas. Consequently, the difference between these two prices is borne by the public and hence constitutes an advantage for the user enterprises of Cumbria and North Lancashire, in particular with respect to enterprises located in other remote areas that do not benefit from a similar scheme.

The Commission therefore considers that there is state aid at the level of the enterprises.

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<sup>3</sup> Judgement of the Court of 24.07.2003 in case C-280/00, *Altmark*.

### 3.3. Compatibility of the aid

Having established that the project involves aid within the meaning of Article 87(1) of the EC Treaty to the service provider and to the enterprises, it is necessary to consider whether the measure can be found to be compatible with the common market.

The Commission notes that the project intends to ensure the widespread availability and use of high-speed broadband services in rural and remote areas. The Commission acknowledges that the existing frameworks and guidelines cannot be applied to assess aid measures that specifically target this objective. The Commission therefore considers that the assessment of the compatibility of the measure with the common market needs to be based directly on Article 87(3)(c) of the EC Treaty. Article 87(3)(c) of the EC Treaty states that “aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest” may be considered to be compatible with the common market.

#### 3.3.1. Necessity of the measure

The need to make broadband infrastructure widely available to businesses and citizens at affordable prices throughout Europe was underlined in the *e-Europe 2005 Action Plan*<sup>4</sup>. e-Europe is part of the Lisbon strategy to make the European Union the most competitive and dynamic knowledge-based economy. The Commission recognised that the information society plays a crucial role in the economic and social development of Europe and concluded that the widest access to high-speed broadband services is a fundamental aspect of this strategy. The Commission furthermore underlined the fact that action is needed to stimulate the development of broadband services and infrastructure. The Commission Communication "*Road to the knowledge economy*"<sup>5</sup> identifies the need for Member States to have national broadband strategies in place by the end of 2003 and sets clear targets. The Commission notes that the project under question intends to meet the three main objectives set out within the Lisbon strategy, *i.e.* provision of a faster, cheaper and secure internet access, investment in people and technology based skills and stimulation of the use of the internet both in relation to e-commerce and e-government.

Furthermore, the Commission recognised the need to encourage the deployment of broadband infrastructure in less favoured areas, where geographical isolation and low density of population can make the cost of upgrading the existing infrastructure unsustainable<sup>6</sup>. In rural areas, the unavailability of adequate infrastructure is an important obstacle for the development of certain economic activities, as well as a source of social disparities. The investment costs to meet present and future requirements for the development of the Information Society are often difficult to justify on purely commercial grounds in these areas. The Commission stressed the need to enable less favoured areas to come to the forefront of information society development by

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<sup>4</sup> Communication from the Commission, e-Europe 2005: An information society for all, 28.5.2002 COM(2002) 263 final.

<sup>5</sup> 11.2.2003 COM(2003) 65 final.

<sup>6</sup> Commission staff working paper, Guidelines on criteria and modalities of implementation of structural funds in support of electronic communications, 28.7.2003, SEC(2003) 895.

accelerating broadband deployment. The present project concerns a rural and mountainous area with low population that acts as significant disincentive to the private sector development of infrastructure necessary for the provision of broadband, given that the cost of rollout per potential customer increases as population density decreases.

### 3.3.2. *Proportionality of the measure*

In order for an aid measure to be compatible with Article 87(3)(c) of the EC Treaty, it must be proportionate to the objective and must not distort competition to an extent contrary to the common interest.

In this respect, the Commission notes the following elements:

- An open, transparent and competitive tender procedure will be used to select the service provider. The invitation of expression of interest and the use of the negotiated procedure for the selection of the service provider should allow to limit the amount of the state intervention.

- The fees payable to the service provider by the administrative authority will be directly linked to the level of demand for broadband within the region. In order to avoid over-compensation to the service provider, a rebate mechanism will be incorporated in the service agreement. According to this mechanism, as demand grows, a percentage of income received by the service provider for the provision of services to end users will be off-set against public support for the project.

- The UK authorities have committed themselves to include in the *Broadband Services Agreement* a specific obligation on the part of the service provider to keep separate accounts for commercial and non-commercial activities, in line with the Transparency Directive. Such a system will allow to calculate and to justify the compensation of the service provider and will ensure that there will be no over-compensation.

- The service provider must guarantee universal access to other operators at non-discriminatory conditions. Local exchange points and/or points of presence must be made available to any interested service provider to provide the “last mile connection”.

- A post termination obligation with respect to maintaining open access to the network will be included in the *Broadband Services Agreement*. Accordingly, the service provider must ensure that the infrastructure remains fully accessible to third party operators on non-discriminatory terms after the end of the *Broadband Services Agreement*

- The project is technologically neutral, *i.e.* it does not favour any particular technology.

- The project is limited in time (3-years contract with a possibility of extending it up to 2 years).

- Moreover, as regards the state aid in favour of the commercial end users of the broadband services, the Commission notes that the services shall be provided at a capped rate with British Telecom's rate, which according to the UK authorities will be the cheapest available rate for broadband services offered on a retail basis to a majority of users on a national level, serving as the benchmark (see above point 2.11). Therefore, the commercial end users will not be put in a position more favourable than that of their competitors in “wired-up” urban areas.



In view of the above, the Commission considers that public investment to the project will only be provided to the extent necessary to attain the objective of stimulating the use of broadband within a rural and remote area of the UK. Therefore, the Commission considers that the measure is proportionate to the objective and does not distort competition to an extent contrary to the common interest.

**Conclusion:**

In the light of the above, the Commission has come to the conclusion that “Cumbria Broadband – Project Access” is compatible with Article 87(3)(c) of the EC Treaty.

**4. DECISION**

On the basis of the foregoing assessment, the Commission concludes that the aid involved in “Cumbria Broadband – Project Access” is compatible with the EC Treaty.

The Commission reminds the UK authorities to submit an annual report on the implementation of the project. The report shall provide enough details for the Commission to monitor whether the Project distorts competition to an extent contrary to the common interest.

The Commission further reminds the UK authorities that all plans to modify this aid scheme have to be notified to the Commission.

If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site: [http://europa.eu.int/comm/secretariat\\_general/sgb/state\\_aids/](http://europa.eu.int/comm/secretariat_general/sgb/state_aids/). Your request should be sent by registered letter or fax to:

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Yours faithfully,

For the Commission

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