



EUROPEAN COMMISSION

Brussels, 30.IV.2008
C(2008) 1623 final

**Subject: State aid N 14/2008 – United Kingdom
Broadband in Scotland - Extending Broadband Reach**

Sir,

I. SUMMARY

- (1) I am pleased to be able to inform you that the European Commission has assessed the measure "Broadband in Scotland - Extending Broadband Reach" (hereafter "the measure") and decided not to raise objections as the State aid contained therein is compatible with Article 87 (3) (c) of the EC Treaty.

II. PROCEDURE

- (2) By letter dated 9 January 2008, pursuant to Article 88 (3) of the EC Treaty, the United Kingdom ("UK") authorities notified a measure to the Commission for the extension of broadband access in rural areas of Scotland registered as "Broadband in Scotland - Extending Broadband Reach". By letter dated 30 January 2008, the Commission requested additional information on the proposed measure.
- (3) By letters dated on 18 January 2008 and 19 February 2008, SES Astra, a European satellite broadband operator lodged a complaint with the Commission regarding the notified measure. The complaint was forwarded to the UK authorities.
- (4) The UK authorities provided answers to the Commission's request on information and their comments on SES Astra's complaint by letter dated 6 March 2008.

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III. CONTEXT

- (5) Broadband connectivity¹ is a key component for the development of knowledge-based global, national, regional and local economies and the development, adoption and use of information and communication technologies. Broadband is of strategic importance because of its ability to accelerate the contribution of these technologies to economic growth in all sectors, to enhance social development and to facilitate innovation.
- (6) However, despite the fact that the digital communication market is rapidly growing, some regions of Scotland are characterised by a concrete risk of “digital divide”, mainly due to lack of interest of operators in bringing broadband connectivity to areas where a low population density and limited economic activity do not allow operators to offer broadband on profitable terms.
- (7) The UK authorities have already implemented a State aid scheme to overcome "digital divide" in Scotland, which was approved by the Commission under the EC State aid rules in 2004². The selected contractor (BT, the incumbent operator) by using ADSL technology, managed to upgrade and enable 378 rural and remote exchanges³ for broadband in 2005. The measure raised broadband coverage in Scotland to 99% of the households.
- (8) However, due to the technical limitations of fixed networks⁴, a small percentage of Scottish premises still cannot have broadband connectivity. This is coined as the "*Broadband Reach*" problem. These premises typically consist of far remote areas with few and geographically isolated households (with typically maximum 20 inhabitants) at the periphery of existing telecommunication infrastructure. According to the UK authorities, it is not feasible for existing operators to provide affordable broadband services for those households on commercial terms⁵. The UK authorities consider the notified broadband scheme as the final step in the telecommunication area of Scotland to fulfil the EU vision of "broadband for all"⁶ by raising broadband coverage to 100% in Scotland.

¹ Broadband services can be delivered using various combinations of communications network technologies (“platforms”). Technologies can feature either fixed or radio based transmission infrastructure, and they can substitute or complement each other according to the individual situation. Current mass-market broadband services have generally download speeds starting from 512 Kbps - 1Mbps. For business users, usually much higher speeds are needed.

² Commission decision in case N 307/2004 - *Broadband in Scotland - remote and rural areas*, adopted on 16 November 2004.

³ Exchange is defined as the geographic area within which sites are connected via the local loop (i.e. telephone cables that run to home and business).

⁴ The available bandwidth degrades with distance until eventually no broadband service can be delivered on the network.

⁵ The UK authorities argue that businesses and households on those areas have no option for broadband access apart from expensive satellite or leased line solutions.

⁶ See for instance “i2010 – A European Information Society for growth and employment”; COM(2005)229 final, 1 June 2005.

IV. DESCRIPTION OF THE MEASURE

- (9) *Objective:* The objective of this measure is to support investments necessary to ensure access to affordable broadband services in remote areas of Scotland where there is currently no broadband available and where there are no plans for coverage in the near future ("white areas"). The measure is the last step to enable full broadband coverage in Scotland.
- (10) *Legal basis:* The measure is based on Section 53 of the Scotland Act 1998.
- (11) *Target areas:* The measure targets areas where there are no affordable broadband services available. The UK authorities followed a "three-step approach" to identify those areas. The first step was to examine and identify the locations that lack broadband connectivity through market research. The second step was to examine whether those locations could be covered by the existing State aid scheme⁷. The third step was to undertake a direct consultation with the wider industry and the public affected by the problem whether any market actors would provide affordable broadband services on those areas on commercial terms, without State aid. The "three-step approach" identified approximately 3000 premises to be subject of the current State aid measure, covering approximately 1% of the households in Scotland. The UK authorities verified separately the lack of affordable broadband services on all premises (households and businesses), and collected the data (names, addresses, postcodes, etc. of citizens with no affordable broadband services) in a database.
- (12) *Beneficiaries:* The direct beneficiaries of the aid will be electronic communications operators offering broadband services. Indirect beneficiaries will be third party providers of telecommunication services and business end users in the targeted areas.
- (13) *Budget and funding instrument:* The aid takes the form of grants. The total intervention budget will be £ 3.4 million (approximately € 4.32 million). The majority of the budget [...] is planned to be spent in the first year after the adoption of the measure, afterwards [...] million per year.
- (14) *Duration of the measure:* The scheme runs from 1 April 2008 until 31 March 2013.
- (15) *Aid intensity:* The aid intensity of the project will depend on the outcome of the tender procedure, but will not exceed 60%.
- (16) *Technology:* The UK authorities do not specify the technology in the invitation to tender.

⁷ As the prior N 307/2004 broadband State aid scheme in Scotland was awarded to BT, the UK authorities examined whether it would be possible to cover those areas within the terms of the existing contract. It has to be noted that BT has no other technological offerings (such as satellite or wireless broadband offers) apart from ADSL.

* [...] this information is covered by the obligation of professional secrecy

- (17) *Procurement*: The aid will be allocated on the basis of a public tender. More specifically, the UK authorities will follow the competitive dialogue procedure in compliance with Directive 2004/18/EC⁸. The award criterion is the most economically advantageous tender in compliance with Article 29 (1) of the referred directive⁹. The contract will be awarded for a period of 3 years with a possible extension of 2 years.
- (18) *Pricing*: the retail prices of the broadband services provided by the selected supplier will be established in the course of the competitive dialogue procedure. Although the target market has a small size, the UK authorities will ensure that prices would be comparable with commercial broadband offers of urban areas to provide affordable broadband services.
- (19) *Service definition*: As a minimum, the service provider shall supply each residential and business subscriber a minimum standard broadband connection (at least 512 kbps download and 256 kbps upload speed) and a minimum contention ratio of 50:1¹⁰. Higher bandwidth offers will be available as premium services¹¹.
- (20) *Wholesale offer*: The tender will oblige the selected operator to provide wholesale access to the subsidised infrastructure to all electronic communications operators on equal and non-discriminatory conditions that enable them to replicate their own retail offers.
- (21) *Monitoring and clawback mechanism*: The aid measure includes a monitoring and clawback provision that will ensure that if compensation to the supplier is higher than initially foreseen in its investment plan, a proportional amount of the aid will be repaid¹².

V. THE VIEW OF THE COMPLAINANT

- (22) The complainant, SES Astra - a company which provides, *inter alia*, satellite broadband services in several European countries – has raised the following three main State aid related points in its submissions. It has to be noted that SES Astra did not participate directly in the tender procedure related to the

⁸ Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts. OJ L 134, 30.4.2004, p. 114–240.

⁹ Contract notice of 2007/S 193-235163.

¹⁰ The "contention ratio" is the maximum number of users sharing the connection infrastructure simultaneously.

¹¹ The UK authorities are intending to seek a future proof solution for the broadband services subject to the measure by awarding higher points in the course of the tender procedure to those operators who can offer bandwidths above the minimum required level.

¹² The monitoring and control mechanisms will be similar to the one applied in the previous State aid broadband scheme in Scotland (see footnote 7): a full reporting mechanism will require significant, regular information from the selected operator (for instance details on take-up rates, pricing as well as full details on wholesale access being provided to other suppliers). The Scottish Government, as the granting authority will monitor the compliance of the selected operator with the contract and if the selected operator fails to carry out the service in accordance with the provisions of the contract, the authority would be in the position to recover the aid.

notified measure, but indirectly as a sub-contractor of its partner organization, National Broadband Ltd¹³.

- (23) First, the complainant questions the need for State aid and in particular, the need of any aid to satellite operators, which (due to the nature of satellite technology) are able to cover all geographic areas of Scotland without State aid - in comparison with, for instance, ADSL technology.
- (24) Secondly, the complainant argues that the access to the database – which was created by the UK authorities during their market research and contains data of Scottish households and business without affordable broadband services¹⁴ - is an economic asset. According to the complainant, since this database will only be shared with the selected operator of the tender, it confers an unfair and disproportionate advantage to that undertaking. Therefore the complainant argues that access to the database should be subject to a separate State aid notification, or alternatively, the Commission should require the UK authorities to provide them access to this database which is considered as a "*vital source of market information*" which would otherwise "*unjustifiably strengthen the position of the company that wins the bid*".
- (25) Thirdly, the complainant asserts the measure and the tender is only "*formally technology neutral*": although satellite operators were selected¹⁵ to participate in the tender, those satellite operators are using different and more expensive satellite broadband solutions than SES Astra.
- (26) The complainant also raised a fourth point in its complaint, related to the tender procedure followed so far by the UK authorities to select the service provider. In this respect, the complainant argues that the tender has been flawed and has not been conducted in an open and transparent manner. The complainant argues that National Broadband Ltd./SES Astra were unreasonably excluded from the procedure: it considers that the reasons provided by the UK authorities for not selecting National Broadband Ltd./SES Astra for the tender were insufficient. Moreover, the complainant asserts that the Scottish Government only finalised the referred database¹⁶ after National Broadband Ltd./SES Astra was not selected in the tender procedure, therefore the complainant did not have access to the database and could not use that information when submitting its bid.
- (27) In light of the above, the complainant requests that the Commission does not authorize the notified aid at hand. In the alternative, the complainant requests that the Commission requires that National Broadband Ltd./SES Astra be included in the procurement process as a condition of its authorization. Finally, if the Commission refuses to issue such injunctions, the complainant requests the Commission to require that SES Astra and National Broadband Ltd. be granted access to the database of the Scottish end-users requesting broadband coverage.

¹³ National Broadband Ltd. is an Irish company offering broadband, telephone and TV satellite services.

¹⁴ See also para (11).

¹⁵ Out of eight candidates selected after the first stage of the procurement procedure, five are satellite operators. See more details about the procedure in footnote 20.

¹⁶ See also paras (11) and (24)

VI. THE VIEW OF THE UK AUTHORITIES

- (28) The UK authorities consider all point raised by the complainant unfounded.
- (29) As regards the first point raised by the complainant, the UK authorities argue that their market research¹⁷, which included a wide consultation with market operators, clearly established that there were no affordable broadband services available on market terms on the targeted areas, taking also into account the existing offers of satellite operators. As regards the broadband offers of satellite operators, according to the UK authorities, not only the monthly retail prices are significantly higher than similar broadband offers in urban areas, but they also charge high one time installation costs to the end users, therefore they are clearly not offering affordable commercial broadband services. The UK authorities explain that precisely due to the absence of any viable commercial offers, they decided to design a State aid scheme to remedy that situation, which scheme is subject to the current State aid assessment¹⁸. The UK authorities are confident that after the implementation of the current measure all end-users on the targeted areas will have access to broadband on retail prices comparable to urban areas¹⁹.
- (30) As regards the second point raised by the complainant, the UK authorities argue that the referred database was created strictly for the purpose of the Scottish Government for the measure at hand and may not be used for any other purposes or commercial gain. The UK authorities also stress that in accordance with the UK Data Protection legislation, the full database can only be provided to a contractor of the Scottish Government, as it contains personal data of individuals (such as full names, phone numbers, postal and email addresses). Furthermore, the UK authorities are claiming to use the database to reduce the amount of aid required for the measure in order to enable affordable broadband services on the targeted areas.
- (31) As regards the third point raised by the complainant about the alleged breach of technology neutrality, the UK authorities stress that the procurement is fully open and the selection criteria do not favour any technology or supplier. The aim of the UK authorities is to procure affordable broadband services irrespective of the technology or supplier. According to the UK authorities, the fact that the operators participating in the tender are planning to cover the targeted areas with a mix of different technological solutions (including wireless or satellite solutions as the complainant has also noted) also provides further evidence for the technological neutrality of the measure.
- (32) As regards the fourth point raised by the complainant related to the procurement procedure, the UK authorities provided more details on the

¹⁷ See para (11).

¹⁸ The UK authorities note that the fact that National Broadband Ltd./SES Astra also participated in the procurement procedure might provide further evidence that satellite operators were not able to provide broadband services on affordable prices at commercial terms.

¹⁹ Although the retail prices of the measure are to be established in the course of the tender procedure, the UK authorities aiming to achieve a monthly cost of approximately £ 20 with negligible installation costs for the bandwidth of 512kbps/256kbps. In comparison, the UK authorities argue that similar satellite offers - based on the information provided on their websites and including the one-time installation fees - requires approximately € 400 - € 600 expenditure from the end-users in the first month and the monthly retails prices afterwards would still be well above the targeted £ 20.

conduct of the procedure: in compliance with the competitive dialogue procedure, the procedure takes place in several stages to reduce the number of solutions during the dialogue stage by applying objective and pre-defined award criteria. First, the UK authorities have sent pre-qualification questionnaires ("PQQ") to all interested service providers. The authorities have selected the suitable candidates after evaluating the answers of the PQQs based on pre-defined objective criteria (such as background information, service quality and operation, corporate governance and financial review). Following this stage, the suitable candidates received a request for proposal ("RFP") document outlining the commercial arrangement that are envisaged and requesting outline technical information on the solution. The example areas were chosen to allow the potential suppliers to demonstrate how they would address the wide range of issues to be found in serving these remote areas. After the assessment of the answers of the RFPs the next stage is to send request for tender ("RFT") for the remaining suitable candidates²⁰.

- (33) As regards the alleged flaw and non-transparency of the procurement procedure, the UK authorities reiterate that the competitive dialogue procedure is used for awarding the aid; and the sole basis on which the contract shall be awarded to a service provider is the award criterion for the most economically advantageous tender. The UK authorities argue that the tender is being conducted in full compliance with the requirements of the relevant national legislation and the EU public procurement directives in a fully open and transparent manner²¹. According to the UK authorities, National Broadband Ltd./SES Astra were not selected in the tender procedure on the basis of an objective evaluation of the information they submitted to the PQQ. The UK authorities also consider that they have sent sufficient reasoning for not selecting National Broadband Ltd./SES Astra to proceed into the next stage of the tender procedure by email of 18 January 2008²². In particular, the bid of the complainant was rejected by the UK authorities on the basis that it did not provide sufficient evidence on the capability of their proposed solution to address the market problem, no evidence was presented to demonstrate the necessary resources or project management skills required, there was a lack of satisfactory references and no evidence was provided regarding the financial status of the company or its ability to service a multi-million pound project²³.

²⁰ According to the UK authorities, the Scottish Government received 21 requests for PQQs, 20 responses were submitted and scored. Following this stage, 8 suppliers were sent request for proposal document. 6 suppliers responded with proposals, one of which was non-compliant in the service offering. The remaining 5 were scored in detail and it was decided that it was worth continuing the competitive dialogue process with all the remaining potential suppliers. Currently, the UK authorities are at the stage of assessing the bids for the RFPs.

²¹ For instance, the UK authorities mention that they provided clear procedural guidance in the PQQs, an open Suppliers' workshop was organized, detailed Q&A document were sent to candidates summarizing the issues of the Suppliers' workshop; regular updates were provided on the dedicated website of the project, etc.

²² The UK authorities have sent the reasons for not selecting National Broadband Ltd./SES Astra to proceed into the next stage of the tender procedure by email of 18 January 2008, as required by Article 41 of the referred Directive 2004/18/EC. According to the complainant, when compiling the PQQ, they believed that the submission was merely a preliminary questionnaire and a more rigorous examination process would follow.

²³ Furthermore, the UK authorities also note that National Broadband Ltd./SES Astra do not seem to provide broadband service in Scotland and their relevant satellite broadband offer in Ireland is also well above the average UK broadband prices and is not in the affordable range. Furthermore, according to the UK authorities, National Broadband Ltd. does not have a commercial offer of min 512kbps/256 kbps

- (34) As regards the alleged denial of access to the database²⁴ raised by the complainant, the UK authorities assert that equality of treatment was ensured among all tenderers through the whole tender procedure, considering also the access to the database: the same, limited access rights were provided to all the potential tenderers without discrimination. As the UK authorities explain, all potential suppliers received with the PQQ a sample of 11 areas to illustrate the issues that the notified measure aims to address²⁵. The RFPs gave details of 5 sample areas to the candidates that they could use to demonstrate the practical applications of the technologies proposed. The UK authorities also claim that a partial database will be shared only with those suppliers that are to be asked to respond for the RFT, sufficient to enable accurate pricing for their offers to supply broadband services on the targeted areas²⁶. The UK authorities also note that the complainant did not question the need for State aid on any of the sample areas it had access to.

VII. ASSESSMENT OF THE MEASURE: PRESENCE OF AID

- (35) According to Article 87 (1) of the EC Treaty, “*any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market*”. It follows that in order to be qualified as State aid, the following cumulative conditions have to be met: 1) the measure has to be granted out of State resources, 2) it has to confer an economic advantage to undertakings, 3) the advantage has to be selective and distort or threaten to distort competition, 4) the measure has to affect intra-Community trade.

State resources

- (36) The notified measure is financed by resources of the Scottish Government. Hence, state resources are involved.

Economic advantage

- (37) *Selected operators*: Through the tender process, the selected operators will receive financial support which will enable them to enter the market and provide broadband services on conditions not otherwise available on the market. Although a competitive tender procedure tends to reduce the amount

(download/upload speeds) in Ireland that the measure at hand is aiming to procure – their closest service offer is 1024 kbps/128 kbps.

²⁴ See also para (11).

²⁵ The UK authorities note that had National Broadband Ltd. (which also received the referred PQQ) considered any of those sample areas commercially viable without the notified State aid scheme, they could have used this information to market to consumers in these areas. According to the UK authorities, they have seen no evidence of any activity from any supplier in these areas to indicate that there is a commercial case for the provision of affordable basic broadband without the project.

²⁶ See also para (11).

of financial support required and to avoid excessive profits, the aid will also allow the operators to offer end-to-end services *prima facie* at lower prices than if they had had to bear all costs themselves and thus attract more customers than under normal market conditions. The selected operators will also acquire ownership of the networks as well as other tangible and intangible assets with State funds (e.g. equipment, customer relations) even after the lifetime of the projects. In view of the above, it is clear that an economic advantage will be granted to the selected operators.

As regards the point raised by the complainant on the access to the database created by the UK authorities²⁷, the Commission notes that the UK authorities followed a "three-step approach"²⁸ to identify the areas where state intervention is necessary to provide affordable broadband services to all Scottish citizens. This extensive market research activity materialized in a database which identified the customer premises where no affordable broadband offers are currently available on market terms. The Commission also notes that the said database was created only for the sole purpose of the measure at hand. The Commission considers that the results of the market research (including the database in question) have to be considered as an important and integral part of the notified measure and should not be subject to a separate State aid assessment. Indeed, access to the database by the selected tenderer is part of the measure at hand, which enables the latter to more precisely assess the targeted areas needed to be covered by the broadband services, thus at the same time potentially reduces the aid amount necessary for the measure. Contrary to the allegations of the complainant, the Commission sees no evidence that access to database will "*unjustifiably strengthen*" the position of the selected operator: the latter will be able to use it only for the purpose of providing broadband in an area where there are currently no affordable broadband offers available. Therefore, access to database in question is not liable to confer to the selected service provider an advantage over and above the advantage conferred by the measure itself.

- (38) *Third party providers*: In the areas covered by the project, there is no broadband connection and therefore no broadband wholesale offer, preventing market entry of third parties such as service providers which do not have their own infrastructure. Therefore, third party providers of broadband services using wholesale access provided under the measure might also benefit from the state resources, as they will be customers of the selected operators.
- (39) *End users*: The measure aims at facilitating the provision of broadband services to residential and business users which are currently available in the target areas. Whereas residential users are not subject to State aid rules, it is not excluded that businesses in the targeted geography might indirectly benefit from service coverage. However, it is not evident at this stage that the measure confers a sufficiently identifiable advantage on such businesses.

Distortion of competition

²⁷ See para (24).

²⁸ See also para (11)

- (40) The intervention of the State alters the existing market conditions by allowing the provision of broadband services by the selected operators and, potentially, third party providers. A number of firms are likely to subscribe to the services provided by the selected suppliers instead of more expensive market-based solutions (for instance satellite or leased lines). Therefore, the fact that a new broadband service becomes available at a lower price than existing has the effect of distorting competition.
- (41) In addition, while the UK authorities decided to intervene precisely in view of the lack of private initiatives in the targeted areas, it cannot be excluded that market initiatives could become viable in some areas in the longer term. By securing this project, the chosen operators will be capable of establishing their business and developing their customer base, enjoying a first mover advantage over prospective competitors.
- (42) The scheme is also selective in that it is addressed to undertakings active only in certain regions or in certain markets for electronic communications services. These selectivity elements also induce a potential distortion of competition²⁹.

Effect on trade

- (43) Insofar as the intervention is liable to affect providers of electronic communications services from other Member States, the measure has an effect on trade. The markets for electronic communications services are open to competition between operators and service providers, which generally engage in activities that are subject to trade between Member States.

Conclusion

- (44) In view of the above, the Commission considers that the notified measure grants an economic advantage to the selected operators, third party operators and final users that exercise an economic activity. The project is publicly funded, distorts competition and has an effect on trade between Member States. Therefore the Commission regards the notified measure as constituting State aid within the meaning of Article 87 (1) of the EC Treaty.
- (45) Having established that the project involves aid within the meaning of Article 87(1) of the EC Treaty to the selected service providers, third party providers and businesses, it is necessary to consider whether the measure can be found to be compatible with the common market.

VIII. ASSESSMENT OF THE MEASURE: COMPATIBILITY

- (46) The Commission notes that the project aims to ensure the widespread availability and use of broadband services in currently unconnected rural and remote areas with no prospect for coverage on commercial terms in the near

²⁹ Judgement of the Court in case C-143/99, *Adria Wien Pipeline*, Slg. 2001, I-8365.

and medium term and, as such, does not fall under one of the existing frameworks and guidelines.

- (47) It should be noted that although some of the areas covered by the measure are eligible to receive regional investment aid under the derogation of Article 87(3)(a), not all of the targeted locations are assisted areas within the meaning of the Regional Aid Guidelines³⁰.
- (48) 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 Treaty³¹ which 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.

- (49) In order to be compatible under article 87(3)(c), an aid must pursue an objective of common interest in a necessary and proportionate way. In particular, the measure shall be assessed with respect to the following questions:
- (1) Is the aid measure aimed at a well-defined objective of common interest (i.e. does the proposed aid address a market failure or other objective)?
 - (2) Is the aid well designed to deliver the objective of common interest? In particular:
 - (a) Is the aid measure an appropriate instrument?
 - (b) Is there an incentive effect, i.e. does the aid change the behaviour of firms?
 - (c) Is the aid measure proportional, i.e. could the same change in behaviour be obtained with less aid?
 - (3) Are the distortions of competition and the effect on trade limited, so that the overall balance is positive?

VIII.1. The support of broadband rollout is in line with the common interest

Community policy

- (50) As outlined in its Communication “i2010 – A European Information Society for growth and employment”³² and the eEurope Action Plan 2005³³, the

³⁰ See Guidelines on national regional aid for 2007-2013, OJ C 54, 4.3.2006 and N 673 / 2006 – “UK - Regional aid map 2007-2013”, United Kingdom of 20.12.2006.

³¹ This approach was also followed by the Commission in other cases, see for instance: State aid decisions for cases N 307/2004 “Broadband in Scotland – remote and rural areas”, United Kingdom of 16.11.2004, N 442/2007 “Aid in favour of broadband in remote areas of Veneto”, Italy of 23.10.2007 or N 570/2007 “Broadband in rural areas of Baden-Württemberg”, Germany of 23.10.2007. The decisions are available at the following website: http://ec.europa.eu/comm/competition/state_aid/register/ii/.

Commission actively supports the widespread availability of broadband services. There is clear evidence of regional economic development benefits resulting from greater broadband deployment, including job creation and retention as well as improved health and education services³⁴. In order to achieve better broadband coverage, the Commission encourages Member States to put comprehensive national broadband strategies in place.³⁵ By improving broadband access for citizens and businesses in areas of Scotland where these services are not satisfactorily available, the measure helps achieving greater cohesion and is therefore in line with the common interest.

Market failure and cohesion considerations

- (51) Lack of broadband coverage is due, among other factors, to some of the typical economic problems associated with networks industries. Due to economics of density, broadband networks are generally more profitable to roll-out where potential demand is higher and concentrated, i.e. in densely populated areas. Because of high fixed costs, unit costs escalate dramatically as population densities drop. Remoteness also plays a role, requiring bridging longer distances in the backhaul and in the last mile. In addition, although equipment costs have fallen as volumes increase, they remain a significant cost and major barrier to roll-out. In areas where demand is not very developed and coverage of cost is uncertain, private operators might find it difficult to find a source of funding for broadband infrastructure, which has a long life and amortisation period.
- (52) Hence, by providing financial support for the establishment of infrastructure to provide basic wholesale and retail broadband services in such areas of Scotland, the authorities pursue genuine cohesion and economic development objectives.
- (53) Contrary to the argument of the complainant on the absence of a justification for providing State aid³⁶, the Commission notes that the provision of widespread and affordable broadband services is a mean to prevent the exclusion of European citizens from social and economic development, which is a clear policy aim of the Community³⁷. Therefore the objective of the measure in question is fully in line with the common objectives of the EU. Furthermore, according to the findings of the UK authorities, satellite operators are currently not providing affordable broadband services on the targeted areas on commercial terms (as evidenced by the above mentioned market research and the wide industry consultation conducted by the UK authorities³⁸). Thus the argument of the complainant that no aid is necessary

³² COM(2005)229 final, 1 June 2005.

³³ COM(2002)263 final, "eEurope 2005: An information society for all".

³⁴ For an overview, see: Lehr, Osorio, Gillet and Sirbu (2005): "Measuring Broadband's Economic Impact", and Orazem, Peter, University of Kansas Business School (2005), "The Impact of High-Speed Internet Access on Local Economic Growth".

³⁵ Commission Communication COM(2004) 369 of 12.05.2004, "Connecting Europe at High Speed – National Broadband Strategies".

³⁶ See para (23).

³⁷ See also para (50).

³⁸ See also para (11)

because broadband satellite providers can geographically cover the area targeted by the measure does not negate the existence of a market failure as far as the provision of affordable broadband services is concerned. In this respect, the Commission sees no reason why satellite operators should not participate in the tender procedure. The fact that several satellite broadband operators (including National Broadband Ltd./SES Astra) are indeed participating in the tender procedure related to the measure may be seen as further evidence that satellite broadband operators are not providing affordable broadband services to citizens on the targeted areas in the absence of public support.

VIII.2. Well-designed aid

(a) Aid is the appropriate instrument

- (54) The measure at hand is part of several instruments that support the development of broadband connection in the United Kingdom, and more specifically in Scotland. Whereas *ex ante* regulation, for example, has facilitated broadband deployment in urban and more densely populated areas, it is unlikely to lead to sufficient investments for the provision of broadband services to underserved areas as it presupposes the existence of broadband access infrastructure. Hence, in situations such as those under examination, there is no alternative to granting public funding to overcome the lack of broadband connectivity.
- (55) In view of these considerations, the Commission concludes that, in the case at hand, public funding for the provision of broadband services is an appropriate instrument to achieve the set objectives.

(b) The aid provides the right incentives to operators

- (56) As explained above, the recipients of the aid will be selected by public tender. Tenderers will submit investment plans indicating the amount of aid that they consider to be necessary to carry out the investment given the anticipated investment and operating costs and revenues. Therefore, the aid should provide a direct and appropriate investment incentive for the selected operators. The UK authorities are confident that these financial incentives will ensure that the provision of broadband services will continue in the areas covered by the notified scheme after the end of the contract period³⁹.

(c) Proportionality

- (57) The UK authorities have designed the measure in such a way as to minimise the State aid involved and potential distortions of competition arising from the measure. In this respect, the Commission notes, *inter alia*, the following positive elements in the design of the measure:

³⁹ The UK authorities are aiming to select a supplier that will generate sufficient revenue to maintain its ongoing provision after the duration of the State aid scheme to provide affordable and sustainable broadband service to Scottish citizens.

- (a) *Market analysis and consultation of operators*: The "three step approach" chosen by the UK authorities clearly identifies which geographic areas should be covered by the measure at hand. By consulting with all stakeholders in a transparent manner, including the contractor of the existing State aid broadband scheme⁴⁰, the authorities also minimize distortions of competition with existing providers and enable these operators to plan their activities.

In relation to the allegation by the complainant regarding the access to the database⁴¹, the Commission notes a thorough market research is an important element for the assessment of a State aid measure. In particular, market research or "mapping" provides evidence for the *necessity* of the measure, and supports the *proportionality* of the state intervention by limiting any potential distortion of competition *vis-à-vis* existing operators and reducing the amount of State aid required for the measure. As the Commission has also noted in the past⁴², this "mapping exercise" is generally required in order to clearly identify the targeted areas requiring public support.

- (b) *Open tender*: the recipients of the aid will be selected by a tender procedure. These procedures will have the effect of maximising the effect of the aid provided while minimizing any potential advantage granted for the selected operator. The subsidy will be awarded to the economically most advantageous tender.

Contrary to what the complainant has argued in this respect⁴³, the Commission notes that the UK authorities have committed to award the contract to the service provider selected on the basis of an open, transparent and non-discriminatory tender procedure, following publication of a contract notice in the Official Journal of the European Union. Based on the information provided by the complainant and the UK authorities, the Commission sees no evidence that the tender procedure related to the measure at hand was flawed, or the equality of treatment among the tenderers through the whole tender procedure was breached. Therefore the conduct of the tender procedure by the UK authorities is not such as to question the Commission's conclusion that the aid involved in the measure at hand is compatible⁴⁴.

- (c) *Wholesale access*: The selected operator will have to provide access to the subsidised networks to other operators on equal and non-discriminatory terms that will enable the latter to compete on the retail level.

- (d) *Minimising effects on existing infrastructure providers and operators*: The freedom for the service providers to choose the most efficient way of procuring the necessary infrastructure, either by building, buying or leasing it from third parties minimises duplication and enhances economic efficiency.

⁴⁰ See also paras (7) and (8).

⁴¹ See paras (24) and (37).

⁴² For reference of other State aid broadband measures approved by the Commission see footnote 31.

⁴³ See para (26).

⁴⁴ In any event, the allegations regarding the tender procedure would normally fall under a separate investigation under the applicable procurement rules, and the present decision is without prejudice to a separate infringement procedure.

Bidders have the possibility to contribute their infrastructure to the project, or acquire or rent infrastructure from another operator, which limits the economic impact of the project for operators that may already have basic electronic communications infrastructure in place.

- (e) *Minimisation of price distortion*: The UK authorities confirmed that the selected operators will have to offer retail services at prices that are comparable to the average prices in areas where the service already exists.
- (f) *Technological neutrality*: The project is technologically neutral, i.e. it does not favour a priori any given technology.

As regards the point raised by the complainant on the lack of technological neutrality⁴⁵, the complainant has not put forward any sufficient evidence to support its allegation that the tender process was technologically biased. The fact, that as the UK authorities have also noted, the tenderers are planning to cover the targeted areas with a mix of different technological solutions (including wireless or satellite solutions as the complainant has also noted) provides sufficient evidence for the technological neutrality of the measure.

- (g) *Clawback provision*: The monitoring and clawback provision will ensure that if the beneficiaries make profits that are higher than initially foreseen in its investment plan, a proportional amount of the aid will be repaid.
- (h) *Limited duration*: The UK authorities anticipate awarding contracts for a limited duration of maximum five years. A minimum contract duration of three years is considered necessary to enable the selected operators to establish a solid business case for their investments that will also allow them to continue delivering services beyond the contract duration.

VIII.3. The distortions of competition and the effect on trade are limited, so that the overall impact of the measure is positive

- (58) The Commission concludes that the notified measure will offset a geographical and commercial handicap and is objectively justified to address the lack of availability of broadband services due to the insufficient density of potential and actual subscribers to make delivering broadband services economically viable on a purely market-driven basis. The target group of the scheme includes both local businesses and citizens who will benefit from the availability of broadband services in both their day-to-day business activity and in the quality of life benefits that broadband access affords to citizens.
- (59) In view of the characteristics of the project and of the safeguards applied by the UK authorities, the overall impact on competition is deemed to be positive. On the effect on trade, the Commission does not identify negative spill-overs for other Member States.
- (60) On balance, the Commission concludes that the overall effect of the measure is deemed to be positive. The measure is clearly in line with the objectives of Article 87 (3) (c) EC Treaty as it facilitates the development of certain

⁴⁵ See para (25).

economic activities (retail and, indirectly, wholesale broadband services) in certain remote and rural areas. The intervention is designed in a way that does not distort competition or affect trading conditions to an extent contrary to the common interest.

VIII.4. Conclusion

- (61) In the light of the above, the Commission has come to the conclusion that the aid involved in the notified measure is compatible with Article 87 (3) (c) of the EC Treaty.

IX. DECISION

On the basis of the foregoing assessment, the Commission has accordingly decided that the aid measure "Broadband in Scotland – Extending Broadband Reach" is compatible with Article 87(3)(c) of the EC Treaty.

The UK authorities are reminded that, pursuant to Article 88(3) of the EC Treaty, they are obliged to inform the Commission of any plan to extend or amend the measure.

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://ec.europa.eu/community_law/state_aids/index.htm

Your request should be sent by encrypted e-mail to stateaidgreffe@ec.europa.eu or, alternatively, by registered letter or fax to:

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Yours faithfully,

For the Commission

Neelie KROES

Member of the Commission