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**Subject:** State aid SA.32820 (2011/NN) – United Kingdom  
Aid to Forensic Science Service

Sir,

## **1 PROCEDURE**

- (1) On 5 April 2011, the UK authorities notified an aid amounting to £20 million in favour of Forensic Science Service Ltd ("FSS"). The aid had already been paid in February. In addition, on 31 March 2011, the UK Government had entered into an additional grant agreement with FSS for £8.7 million to fund a voluntary redundancy scheme.
- (2) As the aid had already been paid to the company in February and March 2011 in breach of the stand-still obligation, the case has been considered not as an aid notification but as a non-notified aid. The British authorities were duly informed about this change on 27 May 2011.

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- (3) An information request was sent to the UK authorities on 26 April and 14 October 2011. The UK authorities replied on 4 July and 14 October 2011. A conference call took place on 16 June 2011.
- (4) Following a meeting with the British authorities on 26 July 2011, a liquidation plan was submitted on 17 August and updated on 30 September 2011. A last meeting with the British authorities took place on 20 September 2011.

## **2 DESCRIPTION OF THE MEASURE**

### **2.1 The beneficiary**

- (5) FSS was established in 2005 and is 100% owned by the UK Government. It provides a full range of forensic science services in England and Wales, mainly to police forces and criminal justice agencies such as the Serious Organised Crime Agency and the UK Border Agency. It employs scientists to analyse materials and traces found at crime scenes and to report on those findings in the course of criminal proceedings in the courts. FSS provides essential services to the Criminal Justice System (CJS) and to the public at large by supporting the fair prosecution of criminal behaviour.
- (6) In addition to the services provided to the CJS, FSS also provides consulting services. FSS' main customer in consulting is the United Arab Emirates.
- (7) FSS employed 1300 staff in January 2011. FSS' turnover in 2009/2010 was £113 million, and for this period it generated operating losses of £12.7 million before "exceptional items"<sup>1</sup> (operating losses of £50.6 million post "exceptional items"). Based on management's accounts, FSS' turnover in 2010/2011 was £87.3 million, and for this period it generated operating losses of £12.3 million before "exceptional items" (operating losses of £98 million post "exceptional items").

### **2.2 The forensic market**

- (8) Unlike in the rest of the EU Member States where the provision of forensic analysis for criminal justice systems is dealt with through in-house or centralised state provision, the market for the provision of forensic science services in England and Wales has been gradually opened to competition since the mid-1990s.
- (9) A recent review of the England and Wales forensic science services market by PricewaterhouseCoopers LLP ("PwC") (commissioned by the UK Government to provide expert evidence) indicates that the size of the contestable (externally spent) forensics market in the UK in 2009 - 2010 was around £165 million<sup>2</sup>. PwC has further estimated that the size of the market has shrunk to circa £117 million in 2010/2011 due to the following factors:

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<sup>1</sup> Additional costs that include the expected costs which will be incurred to support managed closure of business (impairment loss, staff exit costs, lease surrender costs and pensions)

<sup>2</sup> Written Evidence submitted by the National Policing Improvement Agency (NPIA) to the Science and Technology Committee of the House of Commons.

- falling prices as a result of greater competition introduced by procurement processes;
- reduction of forensic submission volumes by police forces and;
- falling crime levels in certain areas.

- (10) At present, FSS is the largest provider with circa 60-65% market share in England and Wales. In addition, there are three other main suppliers that provide these services namely, LGC Forensic Ltd, Orchid Cellmark (Europe) Ltd and Key Forensic Services Ltd with about 23% market share between them – the rest of the market being made up of small companies providing niche services.

### **2.3 The measure**

- (11) The total amount of state aid involved in the liquidation of the company is currently estimated at a maximum of £109 million. The measure at stake consisted in direct grants amounting to £20 million and £8.7 million in favour of FSS. The remaining part of the aid will be granted also in the form of direct grants. The British authorities have informed the Commission that this amount could be reduced as a result of on-going negotiations with the company's creditors.
- (12) The total estimated liquidation costs are divided as follows:
1. Operating support until closure: £30 million. The money will be used to pay loan interest, pension deficit and trade creditors who would otherwise not provide the necessary goods/services for the company to continue operating during the liquidation period.
  2. Support at closing down: £55 million for staff exit costs.
  3. Support to settle liabilities: £32 million (...).
- (13) The total costs therefore are estimated at £117 million and an additional £1 million will be needed for FSS' project costs. As mentioned above, the total state participation amounts to £109 million, the remainder, i.e. £ 9 million will be covered by anticipated asset sales (£6 million) and a £3 million surplus generated by sales of sites that were closed during previous restructuring efforts.

### **2.4 The Liquidation Plan**

- (14) The Liquidation Plan envisages that FSS' work will be transferred to other suppliers, followed by the winding-down of the company. There will be three main routes for transitioning of FSS' work:
- re-procurement or transfer under existing contractual arrangements of forensic contracts by police forces to FSS' competitors (62% of FSS' business);
  - in-sourcing : 17% of FSS' business will be removed from the market through in-sourcing of forensic services by the Metropolitan Police Service (MPS) of Greater London;
  - business sale: the remaining 21% of FSS will move to a new or existing supplier as part of a competitive sales process for a single FSS site in Wetherby.

- (15) The company, according to the information submitted by the British authorities (...) will cease operations by 31 March 2012. Some residual functions will be maintained, namely FSS pension's scheme guarantee and FSS archive material<sup>3</sup>.

#### *2.4.1 Re-procurement*

- (16) Initially, competition for the provision of forensic science services was introduced by police forces acting either in an individual capacity or in collaboration with other police forces. The majority of contracts were awarded through the West Coast Consortium multi-supplier contract or the National Forensics Framework Agreement (NFFA). 14 police forces in the North West, South West and Wales regions have been able to use clauses within their existing contract to migrate their work currently carried out by FSS to other forensic service providers. The transition was completed by the end of July 2011 (11% of FSS business).
- (17) In April 2011, an "invitation to tender" (ITT) was issued under NFFA (for those forces that were not party to the West Coast Consortium contract) to all approved forensic suppliers inviting them to compete for all of the work currently provided by FSS. MPS has run its own tender on similar lines to NFFA for analytical services (14% of FSS business). All other contracts under the ITT were awarded by 16 August 2011 and will take effect from October 2011 (29% of FSS business).
- (18) The remaining 8% of FSS business consists of work for Her Majesty's Revenues and Customs, the Crown Prosecution Service and other customers. These smaller areas are also being transferred to new suppliers by re-procurement.

#### *2.4.2 In-sourcing by the Metropolitan Police Service (MPS)*

- (19) The in-sourcing of FSS' business, i.e. the recovery, interpretation and reporting of forensic science examinations, aims to meet the own operational requirements of the MPS in order to mitigate the risk of service failure. MPS will not compete in the forensics markets that remain open to competition. The new operating model involves MPS employing forensic scientists who would ensure the most effective and cost efficient contribution of forensic science. The services selected for purchase from commercial providers (the out-sourcing of DNA and analytical services) are those that MPS judges to be available from multiple providers and will allow MPS to achieve a better value for money through price competition.

#### *2.4.3 Business sale*

- (20) The remaining assets (core assets and non-core assets) of FSS are offered for sale. The sales process will be conducted through a transparent and non-discriminatory process open to all potentially interested buyers provided they fulfil the conditions required by the

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<sup>3</sup> FSS pension scheme will be supported by the Government guarantee to protect the historical benefits of scheme members. Concerning FSS archive material, this is an ongoing liability for the UK Government in order to support the CJS (investigation of cold cases)

North-East forces. All bidders will have received the same information and time to evaluate the asset. The UK Government and FSS will choose the highest bidder.

- (21) Unlike other police authorities in England and Wales, the seven individual police authorities in the North East region have expressed a preference for the transfer of related FSS activities to a new or existing supplier through a sales process. For that reason, these activities and the related assets, notably a laboratory in Wetherby, will be sold to the private sector through a competitive sales process.

### **3 ASSESSMENT OF THE AID**

#### **3.1 Existence of aid**

- (22) The Commission has to assess whether the measure notified by the UK authorities constitutes state aid within the meaning of Article 107(1) of TFEU, according to which *"Save as otherwise provided in the treaties, 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 internal market."*
- (23) Based on the information given by the British authorities, the Commission has proceeded with an assessment of the measures under Article 107(1) of TFEU. In this context, the Commission notes that the liquidation plan is financed from the general budget and hence involves state resources. Then, as FSS is the only beneficiary of the measure, it is considered as a selective advantage granted to the company. And finally even though the forensic market is a very specific market linked to an essential state function, competition may be distorted and such a distortion can have an impact on intra-community trade, as operators from other Member States may offer their services in the UK or may decide to purchase operators active in the UK.

#### **3.2 Lawfulness of the Aid**

- (24) The UK authorities have implemented the aid prior to an approval by the European Commission. Therefore they have violated their obligation according to Art. 108(3) of the TFEU.

#### **3.3 Assessment of the compatibility of the aid**

- (25) The Commission may declare State aid compatible with the internal market pursuant to Article 107(3) of the TFEU. According to the case-law of the Court, the burden of proof for demonstrating that a measure is compatible lies on the Member State.<sup>4</sup>

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<sup>4</sup> Judgement of 28 April 1993, Italy / Commission (C-364/90, Rec.\_p.\_I-2097) (cf. point 20); judgement of 15.12.1999, Freistaat Sachsen e.a. / Commission (T-132/96 et T-143/96, Rec.\_p.\_II-3663) (cf. point 140); judgement of 29.04.2004, Italy / Commission (C-372/97, Rec.\_p.\_I-3679) (cf. point 81).

- (26) The Commission has wide discretion in matters falling under Article 107(3) of the TFEU.<sup>5</sup> Exercising this discretion, it has issued guidelines and notices setting forth criteria for declaring certain types of aid compatible with the internal market based on Article 107(3) TFEU. It is constant jurisprudence that the Commission is bound by the guidelines and notices that it issues in the area of supervision of State aid inasmuch as they do not depart from the rules in the Treaty and are accepted by the Member States.<sup>6</sup>
- (27) The notified aid falls into the scope of application of the Rescue and Restructuring guidelines,<sup>7</sup> but the UK authorities agree with the Commission that the aid does not meet the conditions set out in these guidelines.
- (28) According to point 20 of the Rescue and Restructuring guidelines, a firm in difficulty cannot be considered an appropriate vehicle for promoting other public policy objectives until such time as its viability is assured. The application of this principle would normally lead the Commission to finding that the notified aid cannot be declared compatible with the internal market.
- (29) When applying its powers under Article 107(3) of the TFEU, the Commission is, however, also bound by the other provisions of the Treaties. For the present case, Article 4(2) of the TEU is of relevance, which states: "*The Union shall respect [...] their essential State functions, including [...] maintaining law and order.*"
- (30) The forensic services provided by FSS to the CJS are essential for enabling law enforcement in the UK, as without them, the investigation of crimes and the prosecution and condemnation of offenders would be seriously slowed down.
- (31) The Commission therefore considers that in this exceptional situation, it is appropriate to assess the compatibility of the notified measure directly under Article 107(3) letter c of the TFEU.
- (32) Art. 107(3)(c) TFEU 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 internal market. According to the Court's case law the Commission may declare state aid compatible with the internal market if the state aid pursues an objective of common interest,<sup>8</sup> is necessary to reach this objective,<sup>9</sup> and does not adversely affect trading conditions to an extent contrary to the common interest.

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<sup>5</sup> Case C142/87 *Belgium v Commission*, 1990, ECR I959, paragraph 56, and Case C39/94 *SFEI and Others* [1996] ECR I3547, paragraph 36

<sup>6</sup> Case C-313/90 *CIRFS and Others v Commission* [1993] ECR I-1125, paragraph 36; Case C311/94 *IJssel-Vliet* [1996] ECR I-5023, paragraph 43; and Case C351/98 *Spain v Commission* [2002] ECR I8031, paragraph 53.

<sup>7</sup> JO C 244 du 1.10.2004, p. 2.

<sup>8</sup> Judgement of the Court of 14 January 2009, *Kronoply v. Commission* (T-162/06, Rec. p. II-1; especially points 65, 66, 74, 75)

<sup>9</sup> Judgement of the Court of 7 June 2001, *Agrana Zucker und Stärke / Commission* (T-187/99, Rec.\_p.\_II-1587) (cf. point 74); Judgement of the Court of 14 May 2002, *Graphischer Maschinenbau / Commission* (T-126/99, Rec.\_p.\_II-2427) (cf. points 41-43); Judgement of the Court of 15 April 2008, *Nuova Agricast* (C-390/06, Rec.\_p.\_I-2577) (cf. points 68-69).

(33) It is established Commission practice<sup>10</sup> that measures may be declared compatible directly under Art. 107(3)(c) TFEU, if they are necessary and proportionate and if the positive effects for the common objective outbalance the negative effects on competition and trade. In this regard, the Commission considers it appropriate to assess the following questions:

- (1) Is the aid measure aimed at a well-defined objective of common interest?
- (2) Is the aid well designed to deliver the objective of common interest? In particular:
  - (a) Is the aid measure an appropriate and necessary instrument, i.e. are there other, better-placed instruments?
  - (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?

#### *3.3.1 Objective of common interest*

(34) The measure has the objective of ensuring, in the period of the orderly liquidation of FSS, the continued functioning of the CJS in the UK. It thereby contributes to safeguarding an essential State function protected by Article 4(2) TFEU.

#### *3.3.2 Conditions to achieve the objective of common interest*

##### Appropriateness:

(35) In normal cases, the liquidation of a company should be accomplished through an insolvency procedure without any need for state aid. The Commission considers, however, that in the present case, the aid is granted in order to ensure the managed wind-down of FSS with a view to avoid disruption in the CJS. The Commission considers that the British authorities have sufficiently justified that a bankruptcy of FSS would jeopardise the functioning of the CJS and ultimately public order. Therefore, in the light of Article 4 (2) TFEU, the Commission considers that the aid is the appropriate tool. As the company is to be liquidated, the Commission considers that direct grant is the most appropriate aid measure.

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<sup>10</sup> Community framework for state aid for research and development and innovation OJ C 323, 30.12.2006, p. 1., point 1.3; Community guidelines on State aid for environmental protection, OJ C 82, 1.4.2008, p. 1., point 1.3.

### Necessity:

- (36) As FFS has a large market share, and over 40 contracts with police forces, a liquidation of FFS would have involved that all of their forensic work would have stopped. Hundreds of cases being investigated would have been suspended, and potentially evidence could have been lost. This would have had a knock-on effect on the court and prison systems, with suspects on bail having to remain in prison for far longer than would normally be the case. Ultimately, it could have given rise to Court challenges on human rights grounds.
- (37) In addition, the police forces emphasised the risk that the former FFS staff could not be available to give evidence in future trials, once they leave FFS. When the investigating scientist is unavailable for court appearances, specialists who take on fresh cases must review the material independently, a process that can cause severe delays when complex evidence is involved. Therefore, without the controlled transfer of experienced staff there would be significant backlogs with the risk of discontinued court cases. The British authorities therefore considered the risks to be unacceptable and decided it was necessary to support a managed wind-down of FFS.
- (38) The Commission agrees that additional support was necessary to achieve that objective, given the financial situation of FFS which would have entered into insolvency in January 2011 without financial support. The liquidation support is limited to the minimum necessary in time and in its amount.
- (39) As regards the time, FFS (...) will be closed in March 2012. The liquidation phase is indeed limited to the period strictly necessary for the orderly winding-down.
- (40) As regards its amount, i.e. the liquidation costs, the aid element of the envisaged operational funding needed until the closure of the company amounts to £30 million. The money will be used to pay staff salaries, loan interest, pension deficits and trade creditors, who would otherwise not provide the necessary services/goods for the company to continue operating during this period (e.g. electricity suppliers, facility management services, rent payments).
- (41) In addition, the UK envisages support covering non-operational costs that would be incurred upon closure of the company such as redundancy payments and settlements of rents under outstanding leases. The support is granted only to creditors that could jeopardise the managed wind-down of the company and could therefore pose a threat to the CJS.
- (42) The British authorities argue that some of these payments may be required in advance of closure in order to reduce the overall closure costs for the Government. This would be the case for early redundancy schemes where, given the decision to undertake a solvent closure, the Government would save salary costs and minimise disruptions in industrial relations by making payments prior to closure.

### *Staff exit costs*

- (43) Government funding to support staff exits is expected to be £55 million. This amount has been calculated based on the FFS workforce redundancy costs following their contractual terms. They are to receive six weeks of pay per year of service, with a maximum



accruable entitlement of 42 months pay. These terms are the same whatever the category of staff and reflect the public sector origins of FSS.

- (44) Under compulsory redundancy arrangements, employees are entitled to their contractual notice period. The contractual notice period for the majority of FSS staff is 6 months. These terms would have forced FSS into committing to departure dates typically 6 months into the future, with harmful consequences such as service disruption to the CJS at a time when the major transition was in progress and when FSS capacity was essential. As a result some employees would have left too soon and the company would not have been able to deal with the workload or, on the contrary, other employees would have completed their work far in advance of their departure date and FSS then would have been obliged to provide Pay in Lieu of Notice for the remainder of the contractual period.
- (45) The British authorities sought to rationalise the staff exit costs as much as possible. Therefore, an agreement was reached in February 2011 to support the company in offering voluntary terms to all staff. By reducing the notice periods to one month under the terms of the Voluntary Redundancy Scheme (“VRS”), the company can achieve an effective transition. The VRS gives the British authorities the flexibility to make employees redundant step-by-step when they are no longer necessary for the on-going activity before the closure of the FSS.
- (46) The company anticipates that it will save £6.6 million against standard contractual terms through the VRS. The scheme has been in place since March 2011. The only means by which redundancy costs could have been further decreased would be allowing for an insolvent closure resulting in staff becoming creditors in the administration process. As previously described, an immediate insolvent closure posed unacceptable risks to the CJS.

#### *Benefit to landlords*

- (47) The principal reason for honouring its lease obligations is that if the UK Government decided not to pay the rent settlements, the landlords could present a petition to the court on the grounds that the FSS could not pay its debts. The court could then make an order for the company to be placed into compulsory liquidation. FSS administration or compulsory liquidation would have had presented a significant and unacceptable risk to the CJS.
- (48) The UK Government intends to cancel the leases currently held by FSS. It should however be noted that FSS together with the UK Government negotiate with each landlord the extent of any rent settlements and therefore payments could be lower than expected at this stage. A reduction of £10 million in the overall amount of rent settlements has already been achieved in between August and September 2011.

#### *Conclusion on necessity*

- (49) For these reasons, the Commission considers that the UK authorities have demonstrated that the aid is necessary to achieve the objective of common interest defined above.

Proportionality:

- (50) Due to the closure of FSS activities (through transfer, sale or actual closure) the support given to FSS will not result in distortions of competition where FSS assets are sold on market terms. Given FSS' serious financial difficulties, liquidation support to maintain FSS' operations for a limited time as part of a managed closure would not result in distortions of competition. The need to continue the activity during this period is justified by the necessity to safeguard the Criminal Justice System whilst its work is transitioned to other forensic suppliers. This support will not benefit FSS and instead would be beneficial to its competitors as they have confirmed that closure over too short a timescale would put them under great pressure. The aim of the British authorities is to liquidate FSS at the lowest costs possible which is achieved by negotiations with landlords and the VRS. The relatively long period needed for the exit of FSS from the forensic market would allow the competitors to prepare for the take over of work, necessary facilities and staff. Moreover, the re-tendering of contracts by police forces and sale of parts of FSS will potentially increase competition as there would be a scope for new entrants to the market through the purchase of FSS' assets.

*3.3.3 The balance between the objective of common interest and the distortions of competition and the effect on trade*

- (51) As already mentioned above, a state aid is compatible with the internal market if it is necessary to reach the objective of common interest and if it does not adversely affect trading conditions to an extent contrary to the common interest.
- (52) As far as the forensic market is concerned, the liquidation aid is likely to involve distortions of competition and have an impact on intra-community trade, as absent the aid, FSS would have ceased business immediately and the on-going contracts would have been re-tendered.
- (53) However, the Commission insists on the fact that FSS will cease operations by 31 March 2012. Since October 2011, the company has stopped taking new cases and has no longer been competing in the forensic market. The liquidation aid is not used by FSS to win new contracts. On the contrary, FSS' business is being sold to competitors. Therefore, the distortions of competition remain limited.
- (54) On balance, the Commission considers therefore that the objective of common interest, i.e. ensuring the continued functioning of the CJS in the UK, outbalances the negative impact on competition.

#### 4 CONCLUSION

The Commission regrets that the United Kingdom put the aid to Forensic Science Service Ltd. into effect, in breach of Article 108(3) of the Treaty on the Functioning of the European Union.

However, it has decided, on the basis of the foregoing assessment, to consider the aid compatible with the Treaty on the Functioning of the European Union.

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/eu\\_law/state\\_aids/state\\_aids\\_texts\\_en.htm](http://ec.europa.eu/eu_law/state_aids/state_aids_texts_en.htm).

Your request should be sent by registered letter or fax to:

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Yours faithfully,

For the Commission

Joaquin ALMUNIA  
Vice-President