Broadband Delivery UK

National Broadband Scheme for the UK: Supporting the local and community roll-out of superfast broadband

State Aid Guidance: Clawback

1. What is clawback?

1.1.1 Clawback refers to the repayment of any *excess* subsidy that may have been granted to a beneficiary of State aid.

1.2 In the case of the roll out of a subsidised local broadband project, it refers to the possibility that a local body may have to recover any *excess* subsidy that the successful Framework supplier concerned has benefited from.

2. Why is it needed?

2.1 It is a requirement of the European Commission's Broadband Guidelines that the successful supplier is not over-compensated. Over-compensation could arise, for example, if demand for the wholesale broadband services is materially greater than originally expected or if the costs of delivering those services are materially less than anticipated.

2.2 While a supplier may benefit from aid provided when State aid clearance is obtained (via the Commission or, in this case, BDUK as national competence centre), that aid must be the minimum level necessary to deliver the objective of the aid (i.e. broadband roll-out in an area where the market has not and will not deliver). The minimum level necessary is arrived at on the basis of various factors which can be subject to change. It is possible that change in those factors (e.g. lower costs than originally anticipated) could mean the supplier has benefited from excess aid.

2.3 To guard against this potential risk, the Broadband Guidelines require that a clawback (or, to use Commission terminology, a reverse payment) mechanism is included in the contract with the successful supplier. The intention is that, through this mechanism, it is possible to adjust the amount of aid that the supplier has benefited from.

3. Does the European Commission have specific requirements around clawback or a particular clause or mechanism in mind?

3.1 In short, no it does not. BDUK has discussed the principles around clawback (outlined above) with the Commission but the Commission does not require a particular formula to be followed in terms of clawback mechanism.

4. **Has BDUK prepared a clawback mechanism?**

4.1 Yes, BDUK has prepared a clawback mechanism based on its discussions with the Commission and included the mechanism in the Broadband Delivery Framework Template Call-Off Contract to be used between local bodies calling off under the Framework and their selected supplier. This mechanism could potentially be duplicated on other non-framework but otherwise broadly comparable projects (although an assessment would need to be made in the particular circumstances of the project as to whether the mechanism served the required purpose).

5. **What is the structure of the BDUK clawback mechanism and how does it work?**

5.1 The claw back mechanism which BDUK has adopted for the Broadband Delivery Framework is based on the three main factors likely to drive greater than forecast profits for suppliers and therefore likely to contribute to excess subsidy (which needs to be clawed back). These three main factors are:

5.1.1 Lower actual deployment costs than forecast;

5.1.2 Higher actual take-up of broadband products than forecast (something expressly referred to in the Broadband Guidelines as a driver of excess subsidy); and

5.1.3 Higher actual revenues from 'non-broadband' products than forecast. [1]

5.2 This claw back mechanism calculates a proxy for the exact level of excess subsidy using variables that are either set at the beginning of the contract, or are able to be assured during the contract. The BDUK clawback mechanism requires the repayment of excess subsidy at the expiry of the contract. However it also includes a mechanism whereby excess subsidy identified during the life of the contract can (with the agreement of the local body concerned) be reinvested in order to extend the supplier network further into the eligible intervention area.

5.3 Further description of the BDUK clawback mechanism, including the reinvestment fund arrangement, can be found in the Annex to this guidance note (as well as being more fully set out in Schedule 5.1 of the Template Call Off Contract under the BDUK Framework).

6. **How long must the clawback mechanism be in place?**

6.1 The claw back mechanism must be in place for the life of the contract between the local body and the supplier.

7. **Do I have to use the BDUK clawback mechanism?**

7.1 Yes, if you are a local body relying on the Broadband Delivery Framework – this is a standard element of the template Call-Off Contract.

[1] The successful supplier of a local broadband project is permitted to use the subsidised broadband infrastructure to provide non-broadband products. This is allowed within certain parameters. The Commission has indicated its approval of this aspect of the BDUK Framework.

7.2 However, even outside of that Framework, BDUK recommends that local bodies acting outside of the Framework but seeking to rely on the BDUK aid scheme use the BDUK clawback mechanism (subject to undertaking an assessment of whether, in the particular circumstances of the project, the mechanism serves the required purpose).

7.3 BDUK also similarly recommends consideration of its usage by community bodies. However, BDUK accepts that this may not be appropriate in cases where the community broadband project is low value (circa £75,000 - £150,000). In such cases the exercise of a claw back mechanism would seem to be a disproportionate administrative burden. BDUK would not require a clawback mechanism in these limited circumstances. The Commission has accepted this position, which is also in line with previous Commission decisions relating to broadband projects.[2]

8. How do I demonstrate compliance with the BDUK clawback mechanism?

For a local body seeking to rely on the BDUK aid scheme a check will be undertaken by BDUK to separately assess whether the corresponding ITT and draft contract incorporate a clawback mechanism consistent with that scheme (this review will be conducted when that local body notifies the project to the National Competence Centre). In the Part 2 – State aid application a review will be undertaken by BDUK which will assess, as national competence centre, whether the proposed intervention is consistent with the terms of the aid scheme. As part of this process, local bodies will be asked to provide BDUK with a copy of the relevant contract (highlighting the clawback provision) with the successful supplier and the corresponding financial model.

8.1 The above also applies to community bodies whose projects are valued at over £150,000. However, where the value of their project is lower than that level, and the community chooses not to include a claw-back mechanism, the community body can simply confirm this in its application.

9. Is there anything else I should know about clawback?

9.1 State aid approval will require a project to regularly report on the use of the clawback mechanism. Therefore suitable reporting and monitoring obligations should be built into the local body's contract with the supplier to support the local body’s own obligations. This is reflected in the template set of reports provided in Schedule 6.4 to the Template Call Off Contract.

BDUK/ July 2014

[2] A similar approach was accepted in the case of a previous German scheme – State aid N 368/2009.

Annex

Further detail on the BDUK clawback mechanism and reinvestment fund

1. How and when the claw back assessment will be undertaken

1.1 The three main factors described in Q5 above will be assessed as follows:

1.1.1 **Deployment:** actual deployment costs (relating to eligible expenditure) will be compared to forecast deployment costs and, if they are lower, the full difference shall be treated as excess subsidy. In general, this assessment will be undertaken once only, following implementation of the final part of the network when the last of the deployment costs have been incurred. If, however, the local body decides to exercise the reinvestment option, a similar deployment assessment will take place at the end of any such further deployment.

1.1.2 **Take up:** actual take-up of broadband products on the network will be compared to the forecast take-up at agreed points in time set out in the contract between the local body and the supplier. The net surplus/deficit of take-up during each relevant period will be multiplied by a proxy figure for the net margin (as specified in the contract[3]). The aggregate of this calculation over all previous periods up to that point shall be treated as excess subsidy. The agreed points in time when this assessment of take-up (actual v forecast) will take place are: at the third anniversary of the contract (subject to there being later implementation stages – where the first assessment may be linked to completion of implementation where appropriate); at every subsequent second anniversary; and at the end of the contract.

1.1.2 **Non-broadband products:** actual revenues for non-broadband products sold on the network will be compared to the forecast revenues for non-broadband products during each relevant period and multiplied by a proxy figure for the net margin (as specified in the contract) multiplied by a specified percentage figure.[4] The aggregate of this calculation over all previous periods up to that point shall be treated as excess subsidy. The agreed points in time when this assessment of revenues (actual v forecast) will take place are the same as noted above for take-up of broadband projects.

2. Investment ratio

2.1 By applying an investment ratio related adjustment to the clawback calculation with respect to broadband revenues means that the clawback will accrue slower where it has invested a higher proportion in relation to the public subsidy. The purpose of this approach is to further incentivise the supplier to commit to a higher leverage from public subsidy, and to strive for additional take-up throughout the contract life. The excess subsidy to be returned must not exceed the subsidy to the supplier.

3. Reinvestment fund

3.1 Local bodies are able to use a mechanism whereby excess subsidy identified during the life of the contract can, at the local body's discretion, be reinvested in order to extend the supplier network further into the eligible intervention area.

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[3] Refer to paragraph 10 of Schedule 5.1 of the Template Call Off Contract under the BDUK Framework for detail.
[4] Refer to paragraph 11 of Schedule 5.1 of the Template Call Off Contract under the BDUK Framework for detail.

3.2 The reinvestment fund will be created using the excess subsidy as follows:

3.2.1 The entire excess subsidy under the deployment assessment, both the original deployment assessment and any subsequent deployment assessment following the exercise of the reinvestment option;

3.2.2 50% of the aggregate calculation under each of the take-up assessments, less the funds already transferred under previous such assessments (so long as that figure is a positive number);[5]

3.2.3 50% of the aggregate calculation in relation to the non-broadband product assessments, less the funds already transferred under previous such assessments (so long as that figure is a positive number).[6]

3.3 The purpose of the reinvestment fund will be to invest in extending the new State subsidised broadband network but only subject to strict controls:

3.3.1 The reinvestment will only take place if the local body considers it appropriate and if the local body is able to agree a mutually acceptable project with the supplier.

3.3.2 The reinvestment will take place in areas that were the subject of the original mapping exercise and public consultation by the local/community body, which were subsequently designated as white basic or white NGA areas and which went on to form the geographic basis of the local/community broadband projects put out to tender. In short, reinvestment would take place in areas where complete coverage could not be achieved using the planned subsidy for that particular project.

3.3.3 In the event that other areas are identified as possible reinvestment targets, such reinvestment will only be permitted if:

(a) The local body first undertakes a mapping exercise and new public consultation in accordance with the guidance in the Broadband Guidelines (e.g. published online, open for at least one month). For further guidance in this area, please see **State Aid Guidance: Mapping and State Aid Guidance: Public Consultation**;

(b) The mapping/public consultation confirms the other areas are basic white areas in the case of basic broadband investment or white NGA areas in the case of NGA broadband intervention;

(c) Reinvestment in the other areas is compatible with the public procurement rules and does not undermine the open tender process run at the outset or the identification of the successful supplier as presenting the most economically advantageous offer (both requirements under the Broadband Guidelines). Public procurement case law at an EU level recognises that some change can happen during the life of a public contract and sets parameters within which change may be accommodated. Insofar as BDUK has signposted this possibility to all bidders in the competition for the BDUK Framework,

[5] The other 50% at each take-up assessment will remain with the supplier. At the end of the contract any remaining balance will be clawed back by the local body

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any network extension is relatively small compared to the overall project, and the basis for agreeing that extension have been set out in the Framework, BDUK considers this approach can be compatible with the public procurement rules.

3.3.4 In the event that reinvestment takes place, the reinvestment fund will be reduced by the amount corresponding to the cost of the network extension.

3.3.5 Any unspent balance of the reinvestment fund will accrue compound interest during the life of the contract, and at the end of the contract life the unspent balance (plus compound interest) will become part of the clawed back amount.

BDUK/ July 2014