

Isle of Wight Council
COMMISSIONING THE VOLUNTARY AND COMMUNITY SECTOR:
A DECISION SUPPORT TOOL
(Draft for discussion - Aug 2009)

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INTRODUCTION

Policy Objective

It is the objective of the IW Council's and its public sector partners to grow the proportion of local public services delivered by the Voluntary and Community Sector, often described as the 'Third Sector'.

A Decision Making Tool

You are going to commission a public service. How can you choose between open procurement or grant funding of Voluntary and Community Organisations (VCOs) to deliver your service? What do you need to do consider and do to ensure that whatever funding channel you choose, VCOs have an equal opportunity to bid for and deliver contracts and grants?

This Decision Support Tool will help you to make a decision and support your approach. It refers to other guidance on Commissioning and monitoring.

Sources

The guidance in this tool has been sourced from National Audit Office and Audit Commission guidance and case studies, and should be considered alongside the Council's Procurement and Best Value Strategies, The Voluntary Sector Strategy 2009 and the Isle of Wight Compact 2005.

This tool will be published alongside guidance on IW Council commissioning and intelligent reporting arrangements.

This tool is a guide, final decisions should be supported by expert advice.

BACKGROUND

The voluntary and community sector on the Isle of Wight has a key role to play in local delivery of public services. There is evidence, locally and nationally, that the voluntary and community sector has not been able to contribute as fully to public service delivery as it can.

This has been the result of a number of barriers to full engagement with funding opportunities ranging from competitive tendering to the making of grants. These funding channels have a number of barriers to organisations wishing to access funding. Breaking into existing funding arrangements, driving innovation and developing service delivery at the most local levels of community have become increasingly difficult.

A number of changes are needed in how services are commissioned. A focus on commissioning outcomes and regard for the needs of both private and voluntary sector providers is also required.

This tool provides outline guidance on the selection of funding channels, and how awarding and funding processes can be improved to ensure the widest possible engagement with new and existing voluntary and community sector providers.

Commissioning Principles

Effective Commissioning through third sector organisations (VCOs) means applying a number of evidence-based principles:

- Focus on outcomes, not on process;
- Mutual understanding of the funder and providers needs;
- Keep it simple; proportional to all proportional to the risk involved;
- Well-managed risk taking;
- Join up or standardise funding between partners and other funders;
- Timeliness: allow time for planning, decision making and action;
- Transparency and accountability: inclusive and open decision-making.

A 'level playing-field'

Government advice is clear. Public bodies should at all times follow public procurement policy, based on value for money, and the EU procurement rules. Procurement practices should not involve preferential treatment for third sector organisations. Equally, third sector organisations engaging in public service delivery should be made aware of procurement opportunities and how procurement rules will apply.

Ensuring successful commissioning

The key stages in ensuring that you have the widest possible range of effective providers from all sectors are:

1. Making strategic decisions.
2. Tactical considerations and decisions.
3. Implementation issues.

These stages are set out in more detail below.

STAGE 1. MAKING STRATEGIC DECISIONS.

As a starting point, Commissioning is about making arrangements to deliver public policy and your organisation's objectives and priorities.

As a Commissioner, you become a potential funder when you have been able to clarify and secure agreement from key stakeholders on these issues:

- ✓ Are you clear which policy objectives are being pursued?
- ✓ Do you have powers to commission the service?
- ✓ Is the legality of the intended commissioning clear?
- ✓ Are democratic permissions to proceed in place?
- ✓ Are your resources identified, adequate and available?
- ✓ Have you a process for identifying the intended outcomes of the commissioning?

1.1 Establish Your Commissioning objectives

Clarifying these objectives should be an inclusive process. The commissioning process should look far and wide to identify the outcomes you seek and the possible means of achieving them. See separate guidance on the inclusive commissioning process.

- ✓ **Form:** Are your objectives expressed in SMART terms.
- ✓ **Focus:** Do your objectives focus on realisable outcomes that will achieve public policy.
- ✓ **Duration:** what timescale will be needed to achieve the objectives?
- ✓ **Scope:** Will your intended outcomes represent value for money.
- ✓ **Integration:** Is there scope for internal or partner joint commissioning?
- ✓ **Reach:** Who has the skills needed to provide the services (make or buy)?

You should not proceed until these issues are clarified and agreed.

1.2 What are the available funding channels?

Once objectives, outcomes and possible means of delivering or providing outcomes have been clarified and have support, you are in a position to choose one of the following funding channels for delivering your programme:

1. Procurement: used to acquire goods, works or services in the pursuit of value for money; – *“the optimum combination of whole-life cost and quality (or fitness for purpose) to meet the user's requirement”* – normally achieved through competition.

2. Grant: used to fund an activity where the provider is in broad alignment with your objectives. At one end of a continuum, you may wish to give money to a VCO because you want to give support for

specified aspects of the VCO's work. At the other, you may wish to give a grant in return for services. Grants given to support the provision of specific services, may need to be treated as a 'restricted fund' in the VCO's accounts; i.e. only used for defined purposes.

3. Grant-in-aid: you can fund all or part of the costs of the body as grant in aid, where you have decided that the VCO should provide a arm's length activities that are in close alignment with the funder's objectives. This relationship is characterised by a high level of trust, often over the long term. Funding will be an unrestricted fund for the organisation, because it is not for any specific project. The VCO may commit to deliver certain outcomes or improved services to qualify for the funding, but with grant-in-aid there are no restrictions on how funds can be spent. The decision whether to pay a grant or to provide grant in aid depends primarily on the level of detailed control which a funder requires, or wishes, to exercise over the funding.

In practice, there is some overlap between these first three funding channels.

4. Direct public sector service provision: This tool does not develop guidance on this channel. It is increasingly the case the commissioners are guided away from direct delivery of local public services. This is based on the need to evidence value for money. It is also the case that commercial or social return on investment is needed and there is increasing emphasis on developing locally based service provision often by local communities themselves. Before deciding that direct provision is the best approach, you should seek advice on intended and un-intended outcomes.

NOTE: EU restrictions on state aid

Commissioners need to identify at an early stage, and periodically review, if their commissioning might represent state aid. EU law on state aid aims to prevent member states from unfairly distorting competition within the EU. State aid is where all of these issues are present:

- Funding is granted by the state or through state resources (including LAs);
- It favours certain undertakings or the production of certain goods;
- It distorts or threatens to distort competition;
- It has the potential to affect trade within the EU.

If in any doubt, you should consult an expert adviser.

1.3 Procurement or grant/grant-in-aid?

The first choice you need to make is between on the one hand procurement and on the other grant or grant-in-aid.

Is there an existing market of potential providers?

Generally, the more competitive the existing market, the more likely it is you should use procurement. An existing highly competitive market with known capacity to deliver gives you a choice of provider; likely to lead to greater effectiveness, economy and efficiency in your programme.

While competition can deliver value for money, you may want to take an approach that will encourage a broader range of better or new providers to enter the market. There may also be no real market – perhaps a single organisation with limited capacity, or even no (known) potential provider. This could suggest a grant or grant-in-aid to one or more organisations to develop their capacity and hence begin to build the market ('market making') or deliver something likely to create a market.

What kind of commission is it?

Which of the following three 'modes' is to be funded, based on the objectives of the commissioning programme?

- **Service financing:** funding a particular service (ongoing) or project (time limited) that will contribute to commissioning objectives. Procurement will most often be appropriate in this mode.
- **Development funding:** developing new capacity or innovation, or the capacity of an existing organisation that will contribute to commissioning objectives. This mode is appropriate for the use of grant or grant-in-aid.
- **Strategic funding:** supporting organisations that are of strategic importance in that they facilitate the achievement of specific commissioning objectives. This mode would be appropriate for the use of grant or grant-in-aid.

Sometimes, commissioning objectives cover more than one mode. For example:

- **Development funding:** for instance, to enable organisations to build and equip day care facilities to help disabled live independently, and
- **Service/project financing:** to pay the same organisations to provide those disabled people with training.

In deciding how to commission in this circumstance, funders must take account of proportionality: establishing two separate programmes, you will impose additional administrative burdens on funder and provider. It is also important to bear in mind that supplying capacity-building funding and procuring services from the same organisation may give rise to conflict with EU state aid rules and/or procurement rules against discrimination in favour of particular suppliers. You should seek advice.

Funding: the role of trust

The main difference between grant and grant-in-aid is the scale and duration of funding, plus the level of trust between you and the potential providers. You may already have strategic partnerships with a small number of suppliers. For VCOs in this position, there is often a high degree of longstanding trust, which could favour the use of grant-in-aid.

Grants are funds entrusted to the trustees or board members of the VCO – it is a relationship of trust and agreement rather than a contract. The difference is simply between entrusting the TSO with funding for a specific project (grant) or towards its overall work (grant-in-aid). You would need to be sure this was not state aid.

Define the scale and scope of funding

Large scale procurement or grants can bring benefits through reduced procurement and management costs, but they don't always offer best value for money and may, in the long term, reduce supplier diversity.

You should consider whether the funding should be divided into smaller lots; for example, to ensure that local community needs and/or capacity are fully recognised and enabled. This will encourage good cost and quality bids from smaller VCOs and providers that have strong community links and experience.

Joint commissions or shared delivery processes will change the scale of funding. This can be much more efficient than existing funding schemes or inadvertently developing new, overlapping schemes with other commissioners. Local services are often funded by several local public bodies, outcomes can be pooled or jointly commissioned; small local providers can collaborate to jointly deliver outcomes.

Getting the scale right can involve answering these questions?

- Can you divide the funding into smaller, more local lots?
- Are you looking to sub-contract the funding?
- If using a prime contractor, are you aware what management fees will be charged and what they will do for you?
- Can your programme's objectives be met through an existing programme, including anything provided or planned by colleagues or other public bodies?
- Can you ring-fence your funding within an existing programme.
- Have you considered un-intended outcomes?

If, having considered joined-up options, you decide to establish a separate financial stream for your programme, you should ensure that your funding model is aligned with other relevant funding streams. For example, different funders and commissioners should rely on evidence collected by each other, rather than duplicating or complicating funding, monitoring or inspection requirements.

1.4 Strategic summary

You have considered:

- ✓ Commissioning Objectives;
- ✓ The most appropriate funding channels;
- ✓ The state of the likely provider market;
- ✓ What kind of commissioning you are considering;
- ✓ The degree of trust you have with potential providers;
- ✓ The scale of funding.

You now have the information you need to identify or prioritise the most appropriate funding channel for delivering your commissioning objectives and outcomes.

In the next stage, the decision making process will to be further developed by considering the practical issues involved in actioning your selection and ensuring that you can engage VCOs with your chosen funding process in the most effective way.

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STAGE 2. TACTICAL CONSIDERATIONS AND DECISIONS.

At this stage, you will make a series of detailed tactical decisions about the design of the funding model. The choices and guidance in this section must be considered *before* the award process begins.

Many considerations and decisions in this stage apply equally to all three channels (procurement, grant and grant-in-aid).

2.1 Determine the degree of competition for funding

Under Procurement

Under the procurement model, above a certain financial threshold, there will usually be a competition between potential providers. Some form of advertising or open competition is often regarded as best practice and helps achieve value for money.

Procurement should involve no preferential treatment for VCOs or any other organisation. You should seek advice on the procurement process.

However, you should take action to ensure that VCOs are not disadvantaged:

- ✓ Make sure that all potential providers are aware of the procurement opportunity and how to bid;
- ✓ Encourage VCOs to seek expert help in bidding;
- ✓ The procurement process must focus on desired outcomes;
- ✓ Ensure that requirements for local, social or environmental conditions are clear from the start;
- ✓ Standard terms and conditions should not discriminate against VCOs;
- ✓ The procurement process must be proportionate to the scale of the funding;
- ✓ Make sure that all involved understand 'value for money' as the optimum combination of whole-life costs and quality that meet the user's requirement;
- ✓ Remove any minor terms and conditions in the proposed contract between you and the provider that might disadvantage VCOs, or explain at the start that these can be part of post-tender discussion;

Under grant or grant-in-aid

If the grant or grant-in-aid channels are used, the funder has more discretion about the degree of competition. However, you must still act fairly. For example:

- If there is no competition between potential providers, there must be a good reason for this;
- Where there is a competition, such as in the Prospectus grant-making approach, this must give all potential providers fair access.

2.2 Determine the duration of the award

The duration of the award is an important issue for both VCOs and funding bodies.

A short-term award (one year or less) may be appropriate in certain circumstances, for example where the source funding has a limited duration.

However, the Isle of Wight Local Compact 2005 seeks to ensure longer term funding of at least three years or longer for VCOs.

Long-term funding reduces risk and uncertainty for providers and is more cost effective for funders. Longer-term financial arrangements will be especially appropriate where funding is to be used either for capital projects or long-term services.

Whatever duration is selected, it must represent demonstrable value for money to the funder as well as recognise the needs of the provider.

2.3 Build in full cost recovery

Full cost recovery

The Isle of Wight Local Compact 2005 and the government recognises that providers will incur costs over and above the direct provision of a service. You have an interest in meeting a fair share of these costs because it helps to ensure that the provider can deliver its activities in a sustainable way.

This means that your programme must finance its 'fair share' of all providers' administrative costs. This principle is known as 'full cost recovery'. In addition, if the provider is a charity, you must not expect it to subsidise the cost of your programme from donations that it receives.

Under procurement

Under procurement, it is up to:

- ✓ The provider to bid at a price that it considers to be appropriate, taking account of all its costs;
- ✓ You to accept (or not) that bid. In deciding this, you must consider whether the potential provider's proposed price is sustainable. You cannot give preferential treatment to TSOs. However, as part of good risk management, you must consider the sustainability of any bid.

Under grant

If you give money to a VCO to contribute its purpose, you must check that the proportion of the grant that will go towards administrative costs is reasonable and provides value for money. The grant-making process will ask for this information.

If you give a grant to a VCO for provision of a service. You and the provider must transparently agree the full cost of the activities that the provider will carry out on your behalf and the proportion of those that will go towards administrative costs. This is based on transparent costing, rather than pricing.

Under grant-in-aid

Under grant-in-aid, your funding is not restricted to specific activities, so it can be harder to establish the correct amounts of funding needed, including full cost recovery. However, where the funding is intended, for example, to allow the TSO to develop its services in a way that requires taking on additional staff, you and the provider must ensure that the funding will be sufficient to cover at the very least the full costs of those staff and an appropriate share of administrative costs. This is also based on transparent costing, rather than pricing.

2.4 VAT

The VAT treatment of funding agreements with third sector organisations may vary from case to case and will depend upon the individual circumstances. Activities may either be outside the scope of VAT, exempt from VAT or taxable at the standard, reduced or zero rate of VAT.

There may be a considerable gain from awarding grants over a procurement, with no or reduced provider exposure to VAT. You should seek advice as any misunderstanding about VAT may impact upon funding decisions and mechanisms.

2.5 Determine the payment formula

Basis of payment

'Basis of payment' can include payment:

- 'Up front' to finance set-up costs
- On completion of milestones towards an output or outcome
- On the achievement of outputs or outcomes
- At fixed intervals
- At the end of the period of the agreement.

Payments can:

- Vary to reflect the cost of each stage, period or achievement
- Be spread out over a longer period.

The basis of payment can also include:

- The arrangements for the funder or commissioner to recover or reconcile any underspent grant. (Not applicable through the procurement channel).
- Arrangements for the provider to compensate you – over and above any clawback – for the consequential loss associated with any failure to deliver. This generally only applies to an award made through

procurement. You cannot sue a provider for loss if the award was a grant or grant-in-aid.

Timing of payment to the provider

This can be in arrears or in advance. Payment in advance can be made to VCOs where there is a clear operational requirement.

Agreeing the basis and timing

A funding model must include the appropriate mix of bases and timings. The payment formula must flow from:

- ✓ The objectives and outcomes of the programme;
- ✓ The agreed approach to risk management.

In addition, you must:

- ✓ • Agree with the provider and record the payment formula in the Funding Agreement or contract;
- ✓ • Ensure the payment formula meets the needs of the programme;
- ✓ • Make the payment formula must be wholly necessary and proportionate (for example, large VCO with substantial liquid reserves may not need advance payment).
- ✓ • Ensure arrangements for making the payments are clear – for example, if you will need the the VCO or provider to invoice you, make clear the dates on which invoices should be raised, and give them a realistic indication of how long it will take from them raising an invoice until they can expect to receive payment.

2.6 A proportionate application and appraisal process

The application and appraisal process for funding, whether via grant, grant-in-aid or procurement, is an important tool in providing a 'level playing-field' for VCOs. Small VCOs in particular may be deterred by lengthy or excessively complex processes. Bearing in mind the need for proportionality, you should consider:

- ✓ the best means of making VCOs aware of the funding opportunity;
- ✓ the clarity of information provided, particularly the eligibility criteria;
- ✓ the amount of supporting information required (e.g. trustees' reports and financial information);
- ✓ A realistic timetable that will be adhered to;
- ✓ the scope for supporting VCOs in making their applications;
- ✓ the inclusiveness (stakeholder involvement) and transparency of your decision making process;
- ✓ Constructive feedback or debriefing, particularly to unsuccessful applicants.

2.7 Intelligent monitoring and reporting

Monitoring and reporting enables successful management of your commissioning programme. It also enables accountability and is a development opportunity for you and the provider, regardless of which funding channel is used.

VCOs require intelligent and proportionate monitoring arrangements, but relationships with commercial providers benefit from the same approach. Properly arranged monitoring that is embedded into contracts and funding agreements is based on:

Understanding that disproportionate reporting and monitoring creates a cost burden for funder and provider;

- ✓ Early discussions on reporting with stakeholders and potential providers;
- ✓ Explaining the scale and nature of reporting requirements at the application or tender stage;
- ✓ The need to justify reporting and monitoring; establishing the level needed through risk assessment;
- ✓ Clear communication: Using simple language and forms.
- ✓ Feedback: Help VCOs understand how you use their information.
- ✓ Use of existing or standard reports and sources, particularly where there is joint funding.

Please see separate guidance on ensuring intelligent and proportionate monitoring and reporting.

2.8 Fraud and counter-fraud

Funding relationships with any outside organisation are potentially open to abuse by fraudsters. You should consider the potential impact of fraud on your funding programme and ensure that there is general awareness of your organisations anti-fraud policies, and any risks involved in making awards.

STAGE 3. IMPLEMENTATION

You have now designed the key features of a funding model that is appropriate to your programme. Your next steps to implement the model will depend on the features of the model, in particular the selected channel. For example, you may need to initiate a competitive grant process through a grant-making Prospectus or to undertake a procurement process.

3.1 Guidelines on implementation.

Ensure that the person or body who will be implementing your funding model understands its 'letter and spirit' and acts accordingly. Involve them in the design stages so they are familiar with the reasons why you have designed the financial model the way you have.

If the implementation is through an intermediary such as a procurement team or grant making group, ensure that they also understand your motives and the "letter and spirit" that you wish to implement.

Annexe A

Risk management and funding VCOs.

Risk is uncertainty of outcome. It can arise in two ways:

- Threats: damaging events that can lead to failure to achieve objectives
- Opportunities: constructive events that can, if exploited, help with the achievement of objectives but that are also surrounded by threats.

There are two aspects of risk:

- The probability that a risk will materialise
- The impact that the risk would have on the effectiveness, economy or efficiency of the programme if it did arise.

It is impossible to eliminate risk from any financial arrangement. It would, in any case, be undesirable to do so: the desire on your or the provider's part to avoid a risk can create an incentive on you or the provider (respectively) to deliver the programme's objectives. This correctly implies mutuality. When you allocate the risks in a commissioning programme between a public body and the organisation in receipt of finance, you must not offload as much risk as possible onto the recipient.

You must allocate risk in a balance that is effective, economical, efficient and fair. You must consider:

- **The objectives of the programme.** Some programmes, such as experimental pilot programmes, are inherently more risky than others. All programmes will carry some risk. It would be unfair to deal with this by allocating all the risks to the potential provider. Doing so would also undermine the achievement of the programme's objectives; by deterring some potentially good providers from taking part in the programme
- **The extent to which each party has control of the risk.** You must not expect the provider to bear all the demand risk (that is, the risk that the estimated demand for the service does not materialise) if you have much of the control over the demand. At the same time, it is appropriate for the provider of the service to bear the output risk: that is, the risk that the provider does not deliver the required outputs, leading to a loss of desired outcomes. But this must be on the basis that these outputs have been fully agreed between the funder and provider at the award stage.
- **The capacity of the potential provider.** For example, an organisation with large reserves will be in a better position to manage cash flow than a small organisation with small reserves. If your programme is large or complex, you should hold a risk meeting (or series of meetings) to apportion risks. In a risk meeting, you can share your concerns about the risks in the programme with others and reach a balanced view. It may be appropriate at times for the risk meeting to include public sector partners and representatives of the third sector. The allocation of risk should also be embodied in the written funding agreement between funder and provider.

Annexe B:

Note on State Aid (National Audit Office, 2009)

EU restrictions on state aid

EU law on state aid derives from the Treaty of Rome and aims to prevent member states from unfairly distorting competition within the EU, except in certain permitted circumstances. Where a state intervention distorts competition, this will usually constitute a state aid. The Treaty expressly prohibits the granting of state aid except in certain circumstances where the European Commission has discretion to approve state aid that does not unacceptably distort the internal market.

A state aid exists if all of the following four criteria apply to the proposed funding:

- It is granted by the state or through state resources
- It favours certain undertakings or the production of certain goods
- It distorts or threatens to distort competition
- It has the potential to affect trade within the EU.

These are discussed below.

State resources

The use of government/public spending which constitutes a state aid is allowed in certain circumstances. There are a range of instruments through which approval of a state aid may be achieved. These include existing approved schemes, the 'block exemption regulations', the 'de minimis regulation' and seeking approval for a particular aid or aid scheme directly from the European Commission.

State aid policy evolves over time. So, for each public programme involving funding, there is a need to test compatibility with current state aid policy.

Favouring an undertaking

An 'undertaking' is an entity that undertakes 'economic activity'. An economic activity is an activity that could be carried out for profit. As such, many VCOs carry out activities that qualify them as 'undertakings'. Whether or not a VCO will be an 'undertaking' will be related solely to the nature of the activities it carries out. Legal form or constitution (such as charitable or not-for-profit status) does not have a bearing on whether or not an entity is an 'undertaking'.

Economic activity is activity for which there is a market in comparable goods or services. It can include voluntary and non-profit-making public or private bodies, such as charities or universities, when they engage in activities that have commercial competitors. It can include activity by the self-employed/sole traders, but generally not employees as long as the aid does not benefit the employers, private individuals or households.

So you need to determine whether or not your proposed programme is an economic activity. There is case law to help interpretation here: for example, air traffic control is not determined as an economic activity.

To count as favouring an undertaking, the aid must:

- Be available to certain undertakings but not others in the member state. It must select individual businesses, sectors, areas, sizes of business, or production of certain goods. A benefit available to all businesses is not state aid but a general measure;
- favour undertakings by conferring an advantage on them. An advantage may be direct (eg grants) or indirect (eg favourable loan terms or services provided at less than market cost, or relief from charges a business would normally bear).

Distortion of competition

This test will be met, if state resources potentially or actually strengthen the position of the recipient in relation to competitors. Almost all selective aid will have potential to distort competition – regardless of the scale of potential distortion or market share of the aid recipient.

If a policy objective is to make a market, funding plans will have to be assessed on a case-by-case basis. In some cases, moving from a monopoly to a market would suggest a noneconomic activity that is intended to become an economic activity. However, market making in itself is likely to represent a state aid.

Intra-EU trade

Any programme proposed by a funder should not inhibit trade between members of the EU. This includes potential effects. Most products and services are traded between member states. Aid for almost any selected business or economic activity is capable, therefore, of affecting trade between states, even if the aid recipient itself does not directly trade with member states. The only likely exceptions are single businesses, such as hairdressers or dry cleaners, with a purely local market not close to a member state border. The case law also shows that even very small amounts of aid can affect trade.

Options where your programme may constitute state aid

To deal with the problem you can:

- Consider developing or adapting proposals to omit or minimise the element of state aid
- Design or adapt the proposed aid to fit within the terms of one of the state aid schemes which the European Commission has approved for the UK
- Design or adapt the proposal to fit existing 'block exemption' regulations
- Seek formal approval for the aid from the Commission. (This may be on the basis of the Commission's various state aid frameworks or guidelines or on the basis of the relevant articles of the Treaty of Rome.)

Block exemption regulations

There are three 'block exemption regulations' that allow certain, limited types of aid to be granted without prior Commission approval provided they comply

with the criteria set out in the regulations. The three regulations relate to aid for:

- Investment in SMEs and research and development aid to SMEs
- Training
- Employment.

For state aid measures that satisfy all the conditions of the SME, training or employment regulation, the member state is required to send to the Commission standard summary information about the aid measure within 20 working days of the implementation of the measure. This should be sent to DTI's state aid branch for onward transmission to the Commission.

De minimis

The 'de minimis' regulation in state-aid rules allows undertakings in all sectors (other than agriculture) to receive up to a maximum of 100,000 Euros 'de minimis' aid from all public sources over a rolling three-year period. Again, this is subject to compliance with the terms set out in the regulation; these include a requirement for the keeping of records of all 'de minimis' aid granted for ten years.

Separate rules exist regarding 'de minimis' aid in the agriculture sector.

Seeking approval for state aid from the Commission

Where it is not possible to redesign a measure to avoid state aid or to fit it under an existing scheme or the block exemptions, it may be possible to seek approval from the Commission. Where this is necessary, aid cannot be granted to potential recipients until Commission approval has been received.

Seeking approval can be a complicated and lengthy process. A straightforward notification to the Commission can take on average five to six months to achieve approval. Where a case is more complex or does not fit easily within the Commission's state aid guidelines, the approval process can take considerably longer. You will need to ensure that you allow sufficient time to obtain Commission approval within your policy timetable.

If you think your programme may require state aid approval from the Commission, you should consult with an expert adviser.

Annexe C:

Note on funding channels (National Audit Office, 2009)

Principles

Public bodies' use of the three channels (procurement, grant, grant-in-aid) available for funding the activities of VCOs has been highly inconsistent.

There are a number of reasons for this:

- Commissions do not always fit neatly into any one of the three channels;
- Until recently, there has been little good guidance to funders and commissioners on the appropriate circumstances in which to use a particular channel;
- In recent years, for good policy reasons, government has extended the concept of grant to include grant with conditions about levels of service and grants awarded following competition between potential recipients. This has constructively blurred the distinction between grant and procurement.

Change

The situation continues to develop: for example, the National Audit Office's recent report on government's financial relationships with VCOs suggested that, as more TSOs established strategic funding with government, grant-in-aid might become more widespread for funding.

Differences

In principle, the distinction between financial channels is technical: all the money in question is public funding. However, there are practical consequences. In particular:

- When you choose the procurement channel, your decisions are governed by a large and detailed body of EU and UK law.
- Grant and grant-in-aid can allow more flexibility and discretion to the funder to vary the required outputs;
- The choice of channel affects what recipients are able to do with any surpluses (i.e. whether or not the funder will seek to 'claw back' surpluses);
- The VAT position may differ: sometimes the amount of irrecoverable VAT incurred by the VCO may be less under the procurement channel.

There is no hard-and-fast rule as to which funding channel is appropriate for a particular situation. However, some factors tend to make procurement more suitable while others favour grant or grant-in-aid. **Procurement is often favoured where:**

- Funding is being provided primarily for specific service or project objectives, rather than for 'development' or 'strategic' purposes;
- The market of potential suppliers is well-developed – there are several potential suppliers to choose from, who have the capability to meet your objectives, can respond easily to new demands and where there is little risk of market failure during the period of your programme. A well-developed market should also mean that price benchmarks for the service will be available;

Conversely, **grant or grant-in-aid is often more suitable** where development or strategic funding is emphasised. Other factors which tend to favour grant or grant-in-aid are:

- A desire for innovative or experimental products or services;
- Outcomes (the desired end results) rather than outputs (the measurable or numerical results of a given input) are to be specified.

Grant-in-aid is particularly favoured where the funding situation is 'non-contestable', i.e. where there is a unique supplier.

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