

Subsidy Advice Unit Report on the proposed subsidy to Sports and Leisure Management Ltd

Referred by Sheffield City Council

21 November 2024

Subsidy Advice Unit

Part of the Competition and Markets Authority



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1. The Referral

- 1.1 On 7 October 2024, Sheffield City Council (the Council) requested a report from the Subsidy Advice Unit (the SAU)¹ in relation to the proposed subsidy (the Subsidy) to Sports and Leisure Management Ltd (SLM) under section 52 of the Subsidy Control Act 2022 (the Act).²
- 1.2 This report evaluates the Council's assessment of compliance (the Assessment) of the Subsidy with the requirements of Chapters 1 and 2 of Part 2 of the Act.³ It is based on the information and evidence included in the Assessment.
- 1.3 This report is provided as non-binding advice to the Council. It does not consider whether the Subsidy should be given, or directly assess whether it complies with the subsidy control requirements.

Summary

- 1.4 The Assessment uses the four-step structure described in the Statutory Guidance for the United Kingdom Subsidy Control Regime (the [Statutory Guidance](#)) and as reflected in the SAU's Guidance on the operation of the subsidy control functions of the Subsidy Advice Unit (the [SAU Guidance](#)).
- 1.5 In our view, the Council has considered in detail the compliance of the Subsidy with the subsidy control principles. In particular, the Assessment:
 - (a) clearly describes the specific policy objective and equity objective of the subsidy which it supports with appropriate reasoning and evidence (Principle A);
 - (b) clearly explains and evidences how the subsidy would change the beneficiary's economic behaviour and that the Subsidy brings about changes that would not have occurred absent it (Principle D); and
 - (c) has conducted a thorough and detailed analysis of each of the requirements of Section 29 of the Act in relation to Services of Public Economic Interest.
- 1.6 However, we identified several areas of the Assessment that could be improved by making better use of the information contained in the evidence provided to support the Council's conclusions (see paragraphs 2.22, 2.33 and

¹ The SAU is part of the Competition and Markets Authority

² [Referral of the proposed subsidy to Sports and Leisure Management Ltd by Sheffield City Council - GOV.UK](#)

³ Chapter 1 of Part 2 of the Act requires a public authority to consider the subsidy control principles and energy and environment principles before deciding to give a subsidy. The public authority must not award the subsidy unless it is of the view that it is consistent with those principles. Chapter 2 of Part 2 of the Act prohibits the giving of certain kinds of subsidies and, in relation to certain other categories of subsidy creates a number of requirements with which public authorities must comply.

2.46). As a result, the Assessment should more clearly explain and explicitly cite how the evidence submitted alongside it supports its key findings and conclusions particularly in relation to the counterfactual and proportionality of the Subsidy.

- 1.7 We discuss these areas below, along with other issues, for consideration by the Council in finalising its assessment.

The referred subsidy

- 1.8 The Council proposes to award a subsidy of up to £14.5 million to SLM towards the cost of operating 13 council owned health, leisure and wellbeing facilities in the Sheffield area (the Facilities)⁴ between 2 January 2025 and 31 March 2040.
- 1.9 SLM was selected to operate the Facilities through an open market procurement process. Bidders were required to provide a viability gap calculation (ie the shortfall in income that will be generated) spanning the delivery period for each facility. Following the evaluation of bids, SLM was chosen as having submitted the most economically advantageous tender. The Subsidy is limited to the shortfall in delivering the services over the delivery period.
- 1.10 The Council explained that the Subsidy is a Subsidy of Particular Interest because it exceeds £10 million in value. Furthermore, the Council considers the Subsidy to be a subsidy for services of public economic interest (SPEI) because health, leisure and well-being services are for the benefit of the public and that the procurement process has established these services would not be provided on an accessible basis without the Subsidy.

⁴ While the majority of the facilities are leisure centres with gym and pool facilities, they also include three golf courses, an ice rink and a tennis facility.

2. The SAU's Evaluation

- 2.1 This section sets out our evaluation of the Assessment, following the four-step structure used by the Council.

Step 1: Identifying the policy objective, ensuring it addresses a market failure or equity concern, and determining whether a subsidy is the right tool to use

- 2.2 Under Step 1, public authorities should consider compliance of a subsidy with:
- (a) Principle A: Subsidies should pursue a specific policy objective in order to remedy an identified market failure or address an equity rationale (such as local or regional disadvantage, social difficulties or distributional concerns); and
 - (b) Principle E: Subsidies should be an appropriate policy instrument for achieving their specific policy objective and that objective cannot be achieved through other, less distortive, means.⁵

Policy objectives

- 2.3 The Assessment states that the policy objective of the subsidy is to:
- (a) contribute to healthier lifestyles amongst the people of Sheffield by providing access to good quality health, leisure and well-being facilities at accessible prices (including concessionary pricing); and
 - (b) help improve the economy specifically in and around the facilities by increasing footfall and thereby contributing to the local economy by increasing the number of potential customers.
- 2.4 The Assessment states that improving the health of Sheffield's citizens is a priority for the Council as indicated in strategies and plans such as the Council's Sport and Leisure Strategy 2023-2033⁶ and Sheffield City Council Plan 2024-2028.⁷
- 2.5 In addition, the Council explains that the Subsidy is aimed at attracting more people into the area which will have positive knock-on effect of contributing to the local economy by increasing footfall.

⁵ See [Statutory Guidance](#), paragraphs 3.32-3.56 and the [SAU Guidance](#), paragraphs 4.7-4.11 for further detail.

⁶ [scc_sport_and_leisure_strategy_2023_to_2033.pdf \(sheffield.gov.uk\)](#)

⁷ [Sheffield City Council Plan 2024-28 | Council Plan](#)

- 2.6 In our view, the Assessment clearly describes the specific policy objective of the Subsidy which it supports with appropriate reasoning.

Equity Objective

- 2.7 Equity objectives seek to reduce unequal or unfair outcomes between different groups in society or geographic areas.⁸
- 2.8 The Assessment explains that the equity objective of the Subsidy is to contribute to healthier lifestyles and better economic outcomes through the provision of health and leisure facilities to the public on an accessible basis, including through the use of concessionary pricing to socially disadvantaged groups.
- 2.9 It states that the city of Sheffield continues to face significant economic and social challenges including the loss of traditional industries, which has caused socio-economic inequalities to emerge and deepen. It explains that this has led to lower levels of disposable income and higher levels of deprivation in Sheffield relative to other areas of the UK, with associated poor health outcomes including low levels of physical activity and higher levels of obesity.
- 2.10 The Assessment describes how areas with longstanding deprivation struggle to attract private investment to create health facilities due to lower footfall and residents with less disposable income compounding the inequality outcomes and that the Subsidy is targeted at addressing this (see paragraph 2.5).
- 2.11 The Assessment outlines targets SLM has agreed to in relation to increasing user numbers of the facilities and describes several actions SLM will take to help achieve these targets.
- 2.12 In our view, the Assessment clearly describes and evidences the equity objective that the Subsidy seeks to address. In particular, the Assessment usefully considers relevant statistics to demonstrate the existence of the inequalities targeted by the Subsidy.

Appropriateness

- 2.13 Public authorities must determine whether a subsidy is the most appropriate instrument for achieving the policy objective. As part of this, they should consider other ways of addressing the market failure or equity issue.⁹
- 2.14 The Assessment explains that the Council considered several non-subsidy means of achieving the policy objective and discusses why they were not

⁸ [Statutory Guidance](#), paragraphs 3.49-3.53.

⁹ [Statutory Guidance](#), paragraphs 3.54-3.56.

appropriate. It states for example that operating the facilities directly would be too costly and would take longer to implement, and that the Council cannot invest in the facilities at the level necessary to negate the need for a subsidy due to budget constraints. The Assessment also reasons that providing a similar level of wellbeing support without the facilities would not achieve the policy objectives at the level required. The potential for regulatory approaches is also discussed and rejected.

- 2.15 The Assessment further articulates that addressing financial shortfalls through loans or guarantees would not be viable options as the facilities are unlikely to be profitable. Finally, it discusses how selling the facilities or allowing operators to contract without subsidies would not be appropriate, as private operators might only maintain profitable facilities.
- 2.16 In our view, the Assessment demonstrates that the Council has considered other ways of achieving its policy objective and have provided an explanation as to why each alternative is unsuitable for achieving the policy objective.

Step 2: Ensuring that the subsidy is designed to create the right incentives for the beneficiary and bring about a change

- 2.17 Under Step 2, public authorities should consider compliance of a subsidy with:
- (a) Principle C: Subsidies should be designed to bring about a change of economic behaviour of the beneficiary. That change should be something that would not happen without the subsidy and be conducive to achieving its specific policy objective; and
 - (b) Principle D: Subsidies should not normally compensate for the costs the beneficiary would have funded in the absence of any subsidy.¹⁰

Counterfactual

- 2.18 In assessing the counterfactual, public authorities should consider what would likely happen in the future – over both the long and short term – if no subsidy were awarded (the ‘do nothing’ scenario).¹¹
- 2.19 The Assessment sets out its view that the ‘do nothing’ scenario in this case is that the current operator contracts will come to an end on 31 December 2024 and the facilities would close due to a lack of an operator to take on the contracts. However, it goes on to explain that the ‘do nothing’ scenario is not the appropriate counterfactual in this case, as in practice, absent the Subsidy,

¹⁰ See [Statutory Guidance](#), paragraphs 3.57-3.71 and the [SAU Guidance](#), paragraphs 4.12-4.14 for further detail.

¹¹ [Statutory Guidance](#), paragraphs 3.60-3.62.

the Council would choose to enter into an agreement with an operator for a more limited contract whereby only the profitable facilities in the portfolio would be operated.

- 2.20 The Assessment states that in this alternative counterfactual scenario, the unprofitable facilities would probably be sold and it would be unlikely for these facilities to be operated as health, leisure and well-being facilities on accessible terms. It argues that this would result in the policy objective not being achieved.
- 2.21 In our view, the Assessment clearly describes and evidences what would happen if the Subsidy was not awarded. It provides clear commentary to support its conclusion that absent the Subsidy, the non-profitable facilities would be sold and/or likely close resulting in the policy objective not being achieved.
- 2.22 However, the Assessment could more clearly explain (including by citing relevant material provided in the supporting evidence) how the non-profitable facilities that would be sold in the counterfactual, would otherwise contribute to the achievement of the policy objective.

Changes in economic behaviour of the beneficiary and additionality

- 2.23 Subsidies must bring about something that would not have occurred without the subsidy.¹² They should not be used to finance a project or activity that the beneficiary would have undertaken in a similar form, manner, and timeframe without the subsidy ('additionality').¹³
- 2.24 The Assessment explains that absent the Subsidy neither SLM nor any other operator will take on the contract if it expects it to be loss making and as such the Policy Objective would not be achieved. It supports this reasoning with evidence that the Council undertook a competitive process to appoint SLM and that no enterprise came forward offering to provide the services without a subsidy.
- 2.25 In addition, the Assessment sets out that the Subsidy will not cover direct costs and instead, it will compensate the operator for losses it will incur in delivering the contract. It goes on to explain that this should not be seen as an operating subsidy because it addresses this shortfall. The Council also state that the Subsidy will fund costs which SLM would not otherwise incur, absent them entering into the contract and therefore that these costs are additional.

¹² [Statutory Guidance](#), paragraph 3.64.

¹³ [Statutory Guidance](#), paragraphs 3.63-3.67.

- 2.26 Finally, the Assessment sets out that there is no pre-existing commitment to provide the services funded by the Subsidy and there is no reason to believe the activities would be undertaken to the same extent, either by SLM or another operator, absent the Subsidy.
- 2.27 In our view, the Assessment clearly explains and evidences how the Subsidy would change the beneficiary's economic behaviour and that the Subsidy brings about changes that would not have occurred without it.

Step 3: Considering the distortive impacts that the subsidy may have and keeping them as low as possible

- 2.28 Under Step 3, public authorities should consider compliance of a subsidy with:
- (a) Principle B: Subsidies should be proportionate to their specific policy objective and limited to what is necessary to achieve it; and
 - (b) Principle F: Subsidies should be designed to achieve their specific policy objective while minimising any negative effects on competition or investment within the United Kingdom.¹⁴

Proportionality

- 2.29 The Assessment sets out how the Subsidy has been designed to ensure proportionality. It explains that a 30-year financial model was developed to assess the long-term financial implications and affordability of a range of investment options, including in house and external provision, for providing health and leisure facilities.
- 2.30 It concluded that the procurement of an external commercial operating partner on a contract of 15.25 years was the most appropriate option, within the financial constraints under which the Council operated.
- 2.31 The Assessment sets out that the Subsidy is intended to be limited to the shortfall in delivering the services. It explains that an external partner was selected via an open and competitive selection process where information from the bidders was used to provide a viability gap calculation for the operation of the facilities based upon the Council's financial model.
- 2.32 The final size of the Subsidy was set through the competitive bidding process which determined the choice of external partner. The Subsidy will be paid in monthly instalments reflecting the financial operating deficit of the Facilities. It is capped at £14.5 million over the contract term, with the potential for annual

¹⁴ See [Statutory Guidance](#) paragraphs 3.72-3.108 and the [SAU Guidance](#), paragraphs 4.15-4.19 for further detail.

adjustment of payments against actuals to allow for repayment (clawback) in the event of excess profit. The performance of the services will be monitored as part of the contract process. The Assessment also states that no other subsidies are being offered for the same purpose and that regular reviews will be carried out to ensure the services delivered and to ensure the Subsidy is not excessive.

- 2.33 In our view, the Assessment demonstrates and evidences that the Subsidy is proportionate and limited to the minimum necessary to operate the Facilities. However, it could more clearly explain the level of services which need to be provided by the Council in order to achieve the stated policy objective, drawing on material provided in the supporting evidence.

Design of subsidy to minimise negative effects on competition and investment

- 2.34 The Assessment considers a number of features relevant to how the Subsidy design would minimise negative effects on competition and investment within the UK.¹⁵ The Assessment also notes that the Subsidy is unlikely to be distortive as it represents only around 4% of the total operating costs of the Facilities.
- 2.35 In our view, the Assessment clearly demonstrates and evidences how design features of the Subsidy contribute to minimising any negative effects on competition and investment within the UK. It could however have provided some more detail on the how the review, monitoring and clawback mechanisms set out in paragraph 2.32 will operate in practice.

Assessment of effects on competition or investment

- 2.36 The Assessment states the relevant market is the delivery of health, well-being and leisure services to the public. In particular, the provision of facilities which people in Sheffield use to exercise. It considers that the direct competitors are other operators of health, well-being and leisure services to the public in Sheffield who would be most likely to benefit should the Subsidy not go ahead.
- 2.37 The Assessment explains that the Subsidy is unlikely to be distortive given its relative size and because the facilities are already in operation. It also argues that the impact on the market is regarded to be limited as the Facilities already exist and that they will only potentially compete with a subsegment of privately owned health, leisure and wellbeing facilities, as the Council's Facilities are not designed to compete with 'higher end' services.¹⁶ Moreover, it also notes

¹⁵ Discussed in paragraph 2.32 above.

¹⁶ CMA investigation into the gym market in 2016 outlined that there are different types of health centres on offer including budget, midrange and higher end offerings: See: Evaluation of the OFT's enforcement action on health and fitness contracts.

that, in the longer term, the impact on competitors may be positive as many of the people who sign up at privately owned facilities begin at accessible facilities, such as those provided by the Council.

- 2.38 The Assessment provides some competitive analysis of the various activities offered by the Facilities (Swimming, Gyms, Sport Halls, Health and Fitness studios). This analysis includes modelling of the balance between supply and demand for these activities in Sheffield, drawing on a Sport England facilities planning model.¹⁷
- 2.39 The Assessment states that, for swimming, the supply/demand modelling indicates that the continued operation of these Facilities would achieve the best overall balance in continuing to meet demand for swimming pools across Sheffield up to 2034 and beyond. It also noted that a survey conducted by ukactive¹⁸ showed that the increasing cost of heating pools was placing pressures on the supply of swimming facilities.
- 2.40 In our view, the Assessment appropriately considers and evidences the effect of the Subsidy on competition and investment. However, the reasoning is not always clear. For example, even where a subsidy is only funding facilities which already exist, it still has the potential to distort competition. The Assessment therefore could consider the impact of the Subsidy on SLM's overall competitive position in the wider leisure service market, even if this is expected to be modest.

Step 4: Carrying out the balancing exercise

- 2.41 Public authorities should establish that the benefits of the subsidy (in relation to the specific policy objective) outweigh its negative effects, in particular negative effects on competition or investment within the UK, and on international trade or investment.
- 2.42 The Assessment lists expected benefits of achieving the policy objective which relate to the overall health and wellbeing of the local community resulting from improved access to public sport and other well-being activities.
- 2.43 It states that these will lead to increased physical activity among those who are inactive and could therefore reduce the prevalence of illnesses such as obesity, heart disease, and type 2 diabetes. The Assessment also explains that the improved access to these activities is expected to have a positive

¹⁷ [Facilities Planning Model | Sport England](#), a computer model that helps to assess the strategic provision of community sports facilities across a defined geographic area, intended for use by local authority partners (or other strategic planning bodies) to help inform strategic planning and assessments of need for community sports facilities across their areas.

¹⁸ [Who We Are | ukactive](#).

impact on mental health, workplace productivity and fostering community pride.

- 2.44 The Council acknowledges that the Subsidy may have a negative competitive impact on privately owned facilities as their customers may choose to move to the Council facilities. However, it states that this impact will likely be minimal as the services offered by the Council (i) differ from those offered at the more exclusive end of the leisure market, (ii) are generally not located in the same areas and (iii) offer services not always supplied by private gyms. The Assessment then concludes that the positive impacts of the Subsidy outweigh the negatives.
- 2.45 In our view, the Assessment clearly sets out the positive effects of the Subsidy in relation to the policy objectives, as well as potential negative impacts, and conducts a balancing exercise between them in line with the Statutory Guidance.
- 2.46 To strengthen the Assessment, the Council could draw on relevant material cited elsewhere to consider how the benefits that will be realised from the Subsidy represent an increase in comparison to the counterfactual 'status quo' scenario, where only unprofitable leisure facilities would close. The Assessment could also consider benefits related to achieving the second element of the policy objective in paragraph 2.3(b) above) regarding improving the local economy in and around the Facilities.

Other Requirements of the Act

- 2.47 The Council has identified that the Subsidy would engage Section 29 of the Act because it involves the delivery of a SPEI. The Assessment sets out a thorough and detailed analysis of each of the requirements of Section 29. These include that:
- (a) the subsidy is limited to what is necessary to deliver the SPEI services having regard to costs of delivery and reasonable profits;
 - (b) the subsidy is given in a transparent manner, meaning that the subsidy is given in accordance with a written contract (or other legally enforceable arrangement in writing), which sets out the terms of the subsidy and contains certain prescribed information; and
 - (c) arrangements are in place to regularly review the subsidy to ensure it remains limited to the minimum amount necessary and that any excess funds can be recovered.
- 2.48 The Council has set out in a detailed table that:

- (a) In relation to Section 29 (2), the Subsidy meets the requirements because it is limited to the amount necessary to deliver the services and for SLM to generate a reasonable profit. This is supported by the fact that an open market procurement process was used to select the operator and there are provisions in place to secure reductions to the Subsidy paid should the viability gap be less than anticipated.
- (b) In relation to Section 29 (3), the Subsidy will be given in a transparent manner. The contract with SLM will set out the terms of the Subsidy and include all the information required by the Act (sections 29 (4) and (5)).
- (c) In relation to Section 29 (6) and (7), the contract will contain provisions which enable the Council to review the use of the Subsidy to ensure compliance with the terms of the contract and the requirements of the Act and for the recovery of the Subsidy in the event of misuse. In addition, there will be checks carried out as to the use of the Subsidy at least once every 3 years in line with the requirements of the Act.

2.49 In our view, the Assessment has clearly considered the application of each of the section 29 requirements which it supports with significant reasoning and evidence.

21 November 2024