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## REVISION OF THE GUIDELINES ON STATE AID TO PROMOTE FINANCIAL INVESTMENTS

16 July 2021

### I. Preliminary remarks

Undertakings play a crucial role in Member States' economies, both in terms of employment and of economic dynamism and growth, and are therefore also central to the Union's economic development as a whole.

To be able to grow and unleash their full potential, EU companies need financing. We welcome the effort by the Commission to revise Risk Financial Guidelines (the "**Proposal**" or "**RFG**"), as one of the crucial tools to support financing to small and medium enterprises.

State aid to support the provision of risk finance can be an effective means to alleviate market failures or other obstacles in access to finance and to leverage private resources.

While we welcome the effort by the Commission to provide wider flexibility to Member States in shaping measures to support financing and to clarify the rules and bring administrative simplification and more legal certainty, in our view there is still room of improvement and crucial issues to be addressed.

In the following sections, we will outline certain areas of possible intervention in order to better fulfil the objectives pursued by the Proposal to improve the access to finance for undertakings established in the EU.

### II. Broadening the definition of eligible undertakings

The scope of the General Block Exemption Regulation ("**GBER**") is restricted to SMEs <sup>(1)</sup>. In the Proposal the Commission recognizes the existence of a financing gap affecting also larger undertakings. However, the deployment of public support measures by Member States in order to facilitate the development of risk finance in their domestic markets is allowed only to small mid-caps<sup>(2)</sup> <sup>(3)</sup> and innovative mid-caps, as defined in the RFG and under the conditions set out in Section 4.2.2.1, point (a) and Section 4.2.2.1, point (b) of the Proposal.

While the inclusion within the scope of application of the RFG of small mid-caps and innovative mid-caps (according to the wider definition of "innovative mid-cap" introduced in the Proposal <sup>(4)</sup>) is to be welcomed,

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<sup>(1)</sup> SME means an undertaking fulfilling the criteria laid down in Annex I to the GBER. Namely: The category of micro, small and medium-sized enterprises ('SMEs') is made up of enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding EUR 50 million, and/or an annual balance sheet total not exceeding EUR 43 million.

<sup>(2)</sup> Small mid-cap means a mid-cap whose number of employees does not exceed 499, calculated in accordance with Articles 3, 4 and 5 of Annex I to the GBER, the annual turnover of which does not exceed EUR 100 million or the annual balance sheet of which does not exceed EUR 86 million;

<sup>(3)</sup> Mid-cap means an undertaking whose number of employees does not exceed 1 500, calculated in line with Articles 3, 4 and 5 of Annex I to the GBER, and which does not fulfill the criteria to be considered a SME.

<sup>(4)</sup> The Proposal suggests to align this definition with the GBER, by defining 'innovative mid-caps' as mid-caps that are at the same time 'innovative enterprises' within the meaning of Article 2(80) of the GBER. As a consequence, more mid-caps can be considered 'innovative mid-caps' and are therefore eligible for risk finance aid under the Risk Finance Guidelines, because the innovative character can be established, as in the GBER, either by an external expert evaluation certifying this feature or when R&D costs reach at least 10% of the total operating costs in at least one year of the three preceding the aid.



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the categories of eligible undertakings are still too narrow and no longer in line with the industry practice. In line with the proposals by the Technical Expert Stakeholder Group on SMEs established in accordance with Regulation (EU) 2019/2115, we suggest to broaden the SME definition in the financial sector in the GBER and, accordingly, in the RFG to all listed companies with a market capitalization of less than 1 billion Euro (so called Small and Medium Capitalization Companies or “SMCs”) <sup>(5)</sup>.

As noted by the TESS EU public capital markets are negatively affected by a market failure which limits considerably their ability to be a robust funding source for SMEs. EU public equity markets provide substantial social benefits, offering an effective way to share risk and allocate capital efficiently between public savings and issuers. Within this framework, initial public offerings (IPOs) enable SMEs to raise funds as they grow, and offer an exit route for early-stage investors. However, recent analyses have shown that EU public equity markets “*have fallen behind in global terms*” <sup>(6)</sup>. EU public equity markets are indeed much smaller than those in the USA, despite having a similar-sized economy, they are also smaller than Asia’s markets when measured by market capitalisation relative to GDP and much smaller than the market in the UK as percentage of GDP. Feedbacks from market participants indicate that the initial and ongoing costs of becoming a public company have risen considerably in recent decades and widened the gap between public and private equity funding. This is even more accurate with specific reference to SMEs, which have to deal with particularly burdensome regulatory costs associated with listing.

The TESS recommendation to the Commission is to review in the RFG the definition of an SME listed on alternative venues (MTFs or SGMs) to allow a higher number of smaller companies to benefit from tax incentives which would be deemed compatible with State aid rules. Furthermore, the TESS recommended to broaden the current exemption for “scouting costs” to costs of research which was conducted for SMEs listed on alternative venues (such as MTFs or SGMs).

In a report published few days ago by the OECD <sup>(7)</sup> it is noted that stock markets play a key role in providing companies with equity capital that gives them the financial resilience to overcome temporary downturns, while meeting their obligations to employees, creditors and suppliers. At the same time, since 2005 more than 30,000 companies have delisted from stock markets globally, notably in the United States and EU. These delistings have not been matched by new listings, which has resulted in a considerable net loss of publicly listed companies. This means that compared to the 2008 financial crisis, many thousand fewer companies have so far been able to access this important source of market-based finance. In particular, the structural decline of SMEs IPOs means that a larger portion of smaller growth companies have been distanced from immediate access to public equity financing. OECD holds that it should be an overarching policy objective to facilitate access to public equity markets for sound businesses. This will help strengthen the balance sheets of viable corporations and the emergence of new business models that are essential for a sustainable recovery and long-term resilience in the case of future shocks and from the perspective of inclusiveness, a well-functioning public equity market would also provide ordinary households with the opportunity to directly or indirectly share in the return on capital, giving them additional options for managing savings and planning for retirement.

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<sup>(5)</sup> *Empowering EU capital markets for SMEs - Making listing cool again*. Final report of the Technical Expert Stakeholder Group (TESS) on SMEs, May 2021.

<sup>(6)</sup> Oxera Consulting LLP, *Primary and secondary equity markets in the EU*. Final Report, November 2020, available in <https://www.oxera.com/wp-content/uploads/2020/11/Oxera-study-Primary-and-Secondary-Markets-in-the-EU-Final-Report-EN-1.pdf>.

<sup>(7)</sup> OECD, *The Future of Corporate Governance in Capital Markets Following the COVID-19 Crisis*, 30 June 2021.



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OECD recommendation is to take the necessary actions to address any structural weaknesses in the stock market ecosystem that discourage smaller growth companies from going public where policy makers and regulators should take a proactive approach to address the cost of listings.

The introduction of a new category of SMCs would allow to extend tax incentives and other supporting measures to a wider number of companies so to end the continuous decline of EU financial markets for SMEs as clearly proved by TEGS. While the spectrum of possible beneficiaries would significantly increase, the Commission will continue to be bound to the conditions set out in the Guidelines (and in the Treaty) when assessing the measures notified by Member States: this, in our opinion, would significantly limit the risk of moral hazard and other negative effects in terms of distortions of competition and impact on trade between Member States.

The Commission confirms its view in the Proposal that companies listed on the official list of a regulated market cannot be supported through risk finance aid under the RFG, since the fact that they are listed on a regulated market demonstrates their ability to attract private financing (see also recital 76 of the GBER).

In our view, para 23 of the RFG reflects a simplistic position, which does not mirror the position taken by the Court of Justice in this field. Not only there may be circumstances of public measures addressed to listed companies not fulfilling the conditions laid down in Article 107(1) TFEU (e.g. selectivity, advantage or impact on trade), but also exceptional cases where the compatibility criteria under 107(3) TFEU are indeed met. This may be the case of purely general measures, applied on a no discrimination basis or of aid granted to address specific obstacles that capital markets and listed companies (on regulated markets or MTFs) are facing, which may be compatible with the internal market under Article 107(3), lett. c) TFEU. Thus, we respectfully propose to delete the express prohibition laid down in the GBER and in the RFG relating to aid to listed companies on regulated markets or, as recommended by the TEGS, to further explore by the Commission whether SMCs listed on regulated markets should be supported by tax incentives compatible with the RFG.

Another key point to address, and one of the main problems of the previous framework was that it targeted only SMEs in their early growth development stages; however, also undertakings in later growth stages may face market failures. Thus, we strongly support the proposal by the Commission, in Section 3 of the Proposal, to modify the current point 47(c) so that measures that allow companies to receive risk finance aid more than ten years after registration can be assessed under the RFG.

Another area that deserves careful scrutiny is the possibility to grant risk finance aid to undertakings in difficulty.

The enduring effects of the pandemic crisis and its impact on EU undertakings (still heavily reliant on debt and with banks loans accounting for an important part of their financing sources) should be factored in the Proposal, which should not be considered in a vacuum, but should instead complement other pieces of legislation in the State aid area, including the State aid Temporary framework.

Accordingly, we suggest to revise point 27 of the Proposal in order to prevent access to finance only to undertakings subject to insolvency proceedings according to the relevant domestic rules, while other undertakings in difficulty should remain eligible to receive aid.



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### III. Extending the applicability of the RFG to individual (ad hoc) measures

The Commission confirms in the Proposal that will only apply the principles set out in the RFG to risk finance schemes. The provisions will not be applied in respect of *ad hoc* measures providing risk finance aid to individual undertakings, except in the case of measures aimed at supporting a specific alternative trading platform.

We respectfully submit that individual aid and aid schemes are subjected to the same rules and frameworks and there is no reason to prevent Member States from notifying *ad hoc* measures to individual undertakings. Again, if the Commission finds a notified measure incompatible with the internal market, authorization will not be granted under the RFG and the measure will not deploy its effects. However, we suggest to remove the general prohibition for Member States to notify individual measures to the Commission under the RFG.

In this regard, it is important to underline that risk finance aid measures are already subject to a number of limitations, since they must be deployed only through financial intermediaries or alternative trading platforms, except for fiscal incentives on direct investments in eligible undertakings.

### IV. On the evidence needed to demonstrate a specific market failure and quantification thereof

In the Proposal, the Commission emphasizes that State aid can only be justified if it can bring about a material development that the market cannot deliver itself and that that there is no general market failure as regards access to finance for SMEs or mid-caps, but only a failure related to certain groups of SMEs and some types of mid-caps, depending in particular on the specific economic context of the Member State concerned (para 53).

Member States face great difficulties in demonstrating the existence of specific market failures and in quantifying the gap. In this regard, the Report “Evaluation support study on the EU rules on State aid for access to finance for SMEs” acknowledges that “it is almost impossible to measure market failure directly”<sup>(8)</sup>.

The Commission has made certain changes in the Proposal aimed at making the requirement to quantify the funding gap more proportionate, *i.e.* the requirement will only remain in place for schemes with the largest amounts of aid for individual beneficiaries (above the 15 million thresholds).

Our proposal is to remove the quantification requirement also for larger amounts and to add a legal presumption whereby, once an *ex ante* assessment demonstrates the existence of a specific market failure (or another relevant obstacle in access to finance), quantification is not required.

### V. Focus on tax incentives. Widening the scope of possible benefits

We appreciate the idea by the Commission to allow fiscal instruments risk finance investments above the 15 million Euro threshold, provided that can be justified on the basis of the *ex ante* assessment (see para 149 of the Proposal).

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<sup>(8)</sup> Final report, published in 2020, p. 52.



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Indeed, tax incentives, both at the investor and at the undertaking level, are the most effective instruments to pursue the objectives of the RFG and to boost

While the GBER covers fiscal incentives granted to independent private investors who are natural persons providing risk finance directly or indirectly to eligible SMEs, the RFG allows measures applying similar incentives to corporate investors.

Moreover, we suggest also to raise the 30% threshold currently provided for tax relief for invested amount in eligible undertakings (see para 151 of the Proposal).

#### **VI. Coordination with the existing State aid rules**

Section 4.2.4.4. of the Proposal provides a laconic section devoted to cumulation of risk finance aid with other instruments. However, given the complexity of the existing rules, the Section does not provide a helpful guidance to either Member States or prospective beneficiaries.

It is therefore suggested to include a specific section of the Proposal with practical examples and explanations on how and on what conditions finance aid can be granted to investors and undertakings, in light of the existing rules and framework, including the GBER and the State aid Temporary Framework.

This, in our opinion, will contribute to increase transparency and predictability of the application of the existing rules, to the benefit of both public and private stakeholders.