Position of the European Association of Guarantee Institutions (AECM) on the Commission's decision to prolong for two years seven sets of state aid rules, otherwise expiring in 2020, and launch an evaluation on the application of EU state aid rules adopted as part of the State Aid Modernization (SAM) process

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aecm

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Introductory remarks

On 7 January 2019, the European Commission announced its decision to prolong for 2 years seven sets of state aid rules, otherwise expiring in 2020 and launch an evaluation on state aid rules, which were adopted as part of the State Aid Modernization process. The aim of the aforementioned evaluation is to provide a basis for decisions, to be taken by the Commission in the future, about whether to further prolong or possibly update the rules.
The European Association of Guarantee Institutions (AECM) cordially welcomes the Commission's initiative and would like to provide input as to the current application of the regulations governing state aid rules.

General remarks

AECM appreciates the implementation of the State Aid Modernization reform (SAM) which has been fostering growth in a strengthened, dynamic and competitive internal market while preventing potential distortions of competition. SAM has been simplifying the procedure for aid granting authorities at national, regional and local levels allowing them to provide a range of actions boosting competitiveness and measures in favor of SMEs. Yet, our members are seeing room for improvement in the current rules.

Remarks on the *de minimis* Regulation (1407/2013)

AECM is very much in favor of the *de minimis* Regulation, which we find relatively simply. We do believe that the *de minimis* Regulation strikes the right balance between state funding and the general objective of preventing potential distortions of competition. Exemption from notification reduces the administrative burdens and complexities that managing authorities would otherwise face. AECM also finds the definition of the 'single undertakings' as envisaged in Article 2 paragraph 2, a reasonable and proportionate one. Therefore, we strongly suggest maintaining it in the future.

1) However, practice has shown that further Commission's clarifications are needed as related to:

- Aid to export-related activities
  Under the current *de minimis* Regulation it is envisaged that aid related to export activities towards third countries or Member States, namely aid directly linked to the quantities exported, to the establishment and operation of a distribution network or to other current expenditure linked to the export activity, does not fall under the provision of the *de minimis* Regulation. In this context the question arises what happens if the *de minimis* aid is used for granting working capital loans in the situation where money is used for purchase of production materials, goods etc. which after the manufacturing or without it, are sold internally and/or abroad, including goods that are sold via online shops and e-platforms (e.g. Amazon). Does the aforementioned activity represent an export-related activity or not?

The same goes for the situation where a guarantee for an investment loan is offered to a single undertaking whose business activity is related to rental equipment and purchasing equipment.

According to our opinion a clarification on the notion of aid to export-related activities within the meaning of Article 1 paragraph 1 point (d) is needed and the provision should also clarify the application of the *de minimis* Regulation on undertakings coming from small countries and located close to borders, since these SMEs are more likely to be disadvantaged by this provision.

In this regard, AECM recalls the judgement of the Court of Justice of the European Union in Case C-518/16 Sofia City Court, Bulgaria[1] where the Court referring to the Article 1 paragraph 1 point (d) of the Commission Regulation No 1998/2006[2] (currently replaced by Commission Regulation No 1407/2013, but where the provision remains exactly the same) decided (see point 55 and 56 of the aforementioned judgement) that Article 1 paragraph 1 point (d) of Regulation No 1998/2006 does not exclude all aid which may have an impact on exports, but only that which has as its direct purpose, by its very form, the promotion of sales in another State. It follows that investment aid, on condition of it not being, in one form or another, determined, in principle and in its amount, by the quantity of the goods exported, is not included within 'aid to export-related activities' within the meaning of Article 1 paragraph 1 point (d) of Regulation No 1998/2006 and therefore does not come within the scope of application of that provision, even if the investments thus supported facilitate the development of goods intended for export.

- How a public institution shall act as a public investor

  Currently, there is a lack of legal certainty and practical examples which would guide the national institutions on applying the private investor principle.
- Calculation of the gross grant equivalent (GGE)

  Article 4 paragraph 6 of the *de minimis* Regulation provides 3 options for the calculation of the GGE. Yet, practice has shown that the combination of state resources with Union resources and tranching of the risk complicates the calculation of the aid element. Therefore, in order to facilitate such calculation, AECM kindly asks the Commission for clear guidelines and practical examples on how to calculate the GGE. Moreover, referring to the transparency of the *de minimis* aid comprised in guarantees, as envisaged in Article 4, paragraph 6 point (b), we consider that the limitation of the duration of guarantee to 5 years for the amount guaranteed equal to EUR 1 500 000 and to 10 years for the amount equal to EUR 750 000, is disproportionate, since practice shows that higher credit amounts require longer duration. Consequently, AECM suggests imposing no time restriction and calculate the GGE for three years allowing longer guarantees duration.

2) Further, referring to Article 3 paragraph 2 of the *de minimis* Regulation, we suggest increasing the ceiling of EUR 200 000 to EUR 300 000 as the amount of *de minimis* aid,

[1] http://curia.europa.eu/juris/document/document.jsf?text=&docid=199769&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=78377

[2] https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2006:379:0005:0010:en:PDF

that a single undertaking may receive over any period of three years, should be adapted to the inflation that will have occurred by the end of the next programming period (= end of 2027).

3) As regarding Article 3 paragraph 6 point (2), AECM suggests revising the discounting requirement for the aid payable in several instalments and set a reasonable threshold for small amounts of aid that would be exempted from discounting obligation. In practice, discounting *de minimis* aid of small sums that are payable in several instalments, i.e. once a month or once a quarter, implies high administrative costs on behalf of the managing authorities. Therefore, and in line with the reasoning of the provisions laid down in Article 6 paragraph 1, AECM suggests applying no discounting obligation.

4) Lastly, AECM welcomes the fact that enterprises in difficulty are no longer excluded from the scope of the de minimis Regulation. Yet, Article 4 paragraph 6 point (a) stipulates that the "safe harbors" for the calculation of the gross grant equivalent (amount of state aid) included in guarantees and loans are only applicable to enterprises that are in a position to repay such loans in the meaning that:
   - the beneficiary is not subject to collective insolvency proceedings nor fulfils the criteria under its domestic law for being placed in collective insolvency proceedings at the request of its creditors;
   - in case of large undertakings, the beneficiary is in a situation comparable to a credit rating of at least B-.

   AECM considers that the definition of insolvency is negative for start-ups and therefore suggests reintroducing an exception for the companies up to 3 years, as set out in the former de minimis Regulation.

Remarks on the General Block Exemption Regulation (651/2014) (GBER)

1) AECM invites the European Commission to examine the possibility of including aid for financing capital under the provisions of the GBER.

2) Further, in the context of Article 14 paragraph 14 of the GBER there is a need for a definition of 'public support' in order to allow for an unambiguous application.

3) Besides, AECM suggests expanding the derogation of "firms in difficulty" included in the start-ups scheme to research, development and innovation (RDI) aid.
   The current provision on firms in difficulty seems inappropriate for innovative companies. Under the current definition of the GBER, i.e. Article 2 recital (18) (b), a company is considered in difficulty " …where more than half of its capital as shown in the company accounts has disappeared as a result of accumulated losses". AECM is of the opinion that it is inappropriate to assess the real financial capacity of a company only based on a single balance sheet criterion. Companies falling within the scope of the definition of "firms in difficulty" can nevertheless have positive cash flows and very

good market prospects. This is the case of innovative companies, which generally invest significant amounts of resources in research, development and innovation in comparison with their incomes and sometimes with long investment cycles (more than ten years for example in the biotech and microelectronics sectors). This imbalance ("losses" linked to huge expenses that reduce dramatically their own funds) is nevertheless inherent to the development model of innovative and capital-intensive companies, some of which are therefore excluded from the scope of the GBER and RDI aid eligibility.

4) Further, the GBER provides a derogation for firms under-five to make them benefit from aid on the basis of the “start-ups schemes” (Article 1, paragraph 4, point (c)). Nevertheless, since this scheme provides restricted possibilities with regard to financial instruments, this derogation has in practice a weak impact. Accordingly, it is proposed to expand this derogation to RDI aid scheme, limiting it to firms under-seven (or under-five) in order to take into account their long investment cycle (more than 10 years in some sectors such as biotechnologies and microelectronics).

   Consequently, the following writing is proposed:

   “*This regulation shall not apply to […] aid to undertakings in difficulty, with the exception of aid schemes to make good the damage caused by certain natural disasters, start-up aid schemes, **RDI aid scheme for companies under-seven** and regional operating aid schemes, provided those schemes do not treat undertakings in difficulty more favourably than other undertakings*.”

   For more information, some case studies proposed by one of our members are available in the annex to this position paper.

5) Expanding aid for start-ups to companies under-seven

   It is necessary to recognise companies under-seven as eligible in order to align all the age within the GBER, irrespective of the funding. In our opinion, it is insufficient to limit the definition of start-ups to companies under-five. In France for instance, the status of “Jeunes entreprises innovantes” covers companies under-eight, these companies still being considered as young and fragile. An innovative company needs much more than 5 years to stabilise itself and find its growth path. Six months of administrative issues followed by the design of the technical project (2 years), then the time to prepare the industrial and commercial launch of the innovation (1 year). The first turnover will finally be made within the first 3 years. During this period, the company needs support to achieve its innovative project, get finance and working capital, reinforce its treasury and prepare its fundraisings.

6) Expanding the eligible costs to innovation aid for SMEs

   AECM proposes to update the Article 28 paragraph 2 of the GBER by expanding the eligible costs to innovation aid for SMEs as following:

   ”*The eligible costs shall be the following:*

a) costs for obtaining, validating and defending patents and other intangible assets;

b) costs for secondment of highly qualified personnel from a research and knowledge-dissemination organization or a large enterprise, working on research, development and innovation activities in a newly created function within the beneficiary and not replacing other personnel;

c) costs for innovation advisory and support services;

***d) costs for prototyping, miniaturization, scaling-up, design, performance verification, testing, demonstration, development of pilot lines, validation for market replication, including other activities aimed at bringing innovation to investment readiness and maturity for market take-up**.*"

This change would enhance the legal certainty and give more flexibility, acting in favour of the innovation funding for SMEs, by making clear that advanced innovative projects led by SMEs could be financed through this article, in particular technology demonstration.

7) Revising the SME definition

In order to determine the real economic capacity of an SME, the current EU SME Definition takes into account all (direct and indirect) partners and linked enterprises.
Recent rulings of the European Union Court of Justice suggest that only some relationships should be taken into account. According to the ruling of the ECJ, ownership data calculation should be dismissed when it is below 50%. This constitutes a burden for financial intermediaries and has no economic justification since the external shareholding is a minority one. Above 50%, an exemption should be foreseen for business angels' and private equity funds' ownership. Indeed, they are key to support the scaling-up of SMEs and their ownership is temporary (average holding period is 5 to 7 years).

8) In addition, the GBER lists a large number of different levels of aid intensity for SMEs, which makes it operationally difficult with different calculations for different articles/schemes using GBER. Hence, more streamlined and harmonized provisions are required.
Moreover, according to Article 17 paragraph 6, the aid intensity shall not exceed 10 % of the eligible costs in the case of medium-sized enterprises. AECM is of the opinion that a higher threshold would facilitate a wider reach of loan size. Thus, we suggest increasing it as this threshold is too restrictive.

9) Besides, we are of the opinion that the level of additional information required from SMEs should be kept at minimum given the added requirements placed on banks regarding declarations in documentation which adds to the complexity of loan products and to the time of the lending process i.e. eligible costs, incentive effect, etc.

10) Finally, the requirements for evidence of counter-factual in certain instances are burdensome and act as an impediment to using the GBER.

11) Last but not least, AECM strongly suggests ensuring a seamless combination of national resources with Union funding centrally managed by the Commission i.e. ensuring that COSME programme aligns with Article 7 of the GBER.

About AECM's members

The 48 members of the European Association of Guarantee Institutions (AECM) are operating in 29 countries in Europe. They are either private sector guarantee schemes or public promotional institutions or banks. Their mission is to support SMEs in getting access to finance. They provide guarantees to SMEs that have an economically sound project but do not dispose of sufficient bankable collateral. AECM's members operate with counter-guarantees from regional, national and European level.

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Annex: Case studies

1) The *company EE*, involved in the biotechnologies sector and established 7 years ago, is specialised in the development of innovative diagnosis solutions. Its balance sheet is severely impacted by the losses caused by its intense RD activities. In 2018, the company applied for a national financial mechanism (a contest). Its project was deemed highly promising but was not taken on because of its "firms in difficulty" status: it made the funding of the project impossible.

2) The *company FF,* established in 2011 is specialised in the development of digital solution to dematerialise documents. The company has experienced an extremely fast growth but could not get access to RDI funding because of the losses impacting its balance sheet. It has impeded the expansion of this company which has nowadays more than 70 workers.

3) Among companies over-three and deemed "in difficulty", there are a non-negligible number of companies from the digital sector with a SaaS business model (Software-as-a-Service). By implementing such business model, it is common that during several years companies grow at a fast rhythm and face at the same time heavy losses primarily because of the acquisition cost of new clients. During this period, companies are often considered as "in difficulty" according to some ratios whereas their economic foundation is strong and solid (growth in the number of clients, long commitments, few subscription cancellations).
   The access to finance of these companies is cut or restricted and they cannot pursue their RDI activities. Same happens for their access to public guarantee schemes. It is for instance the case of the *company II* which is considered "in difficulty" during the fiscal year 2017. The company had to continue its development with public support to RDI, which could limit its development. Yet, it seems to be on a "hypergrowth" trajectory and it has just achieved a € 50m fundraising in 2018.