NEFI Network of European Financial Institutions for Small and Medium Sized Enterprises

**NEFI comments on the DRAFT COMMISSION REGULATION (EU) No …/..**

**of 17.7.2013**

**on the application of Articles 107 and 108 of the Treaty on the Functioning of the European Union to *de minimis* aid**

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The Network of European Financial Institutions for Small and Medium Sized Enterprises (NEFI) welcomes the initiative of the European Commission to launch a consultation on the second draft of the new de minimis regulation and appreciates the opportunity to provide comments on the proposed draft.

NEFI consists of 17 financial institutions from 17 different EU member states. All NEFI members share a public mission to facilitate the access to finance for SMEs by offering them financial services and expertise. All NEFI members act complementarily to and in cooperation with the national banking system through co-financing, risk-sharing, expertise and advisory services in order to address shortcomings in the SME financial markets.

## I. General remarks

As compared to the present regulations the Commission proposals introduce limitations on *de minimis* aid, provide additional bureaucratic burden and generate legal risk related to vague definitions.

Examples of such solutions are linked with:

- modified and limited duration of de minimis aid;
- modified definition of Undertakings in Difficulty;
- definition of single undertaking.

In our opinion, adverse changes in the *de minimis* regulations will restrict the support to SMEs suffering from economic crises and difficult access to banking loans. The limitations of *de minimis* aid will jeopardize the use of financial instruments in the next EU financial prospective. The proposed changes are contradictory to the objectives of the general EU policy pointing out the significance of small and medium sized enterprises.

- The implementation of the new regulation will be more demanding and costly than the current one because of requirements on additional data, on up-dating of software supporting the processes within state authorities and entities providing the assistance to final beneficiaries.

- More precise wording and supplementary clarifications are still necessary to avoid confusions and wrong implementation. The draft Regulation still contains many ambiguous rules that may generate legal risks of questioning their proper interpretation. It applies in particular to the exclusion of “other current expenditure linked to the export activity”, the admissibility of ad hoc



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*de minimis* aid and the methodology of calculation of gross grant equivalent for guarantees in the context of introducing into the methodology the reference to the guarantee period.

- Maximum state aid threshold: A common postulate during the first round of the consultation was to increase the maximum level of *de minimis* aid that is currently at EUR 200 000 or EUR 100 000. It was proposed to at least revalue that limit by the inflation rate due to the real depreciation of allowed *de minimis* aid level. The argument given for maintaining the current limit is the "EC experience", however there is no explanation on what kind of experience it is and the Commission does not refer anyhow to the arguments in favour of increasing the limit.

- Cumulating aid: If *de minimis* aid is deemed not to disrupt the market competition due to its low value, then the obligation to verify the cumulation of it with other state aid types, is inconsequent. The bureaucratic procedure (analyzing the aid intensity), to verify if the decisions comply with the cumulation rule, generates the most significant burden of applying the *de minimis* aid. In the point 12 of the preamble it has been said that "It should also provide for clear rules on cumulation that are easy to apply", but no such rules are provided in the regulation.

## II. Comments on individual items

### 1. Preamble, points 18-19. Methodology of gross grant equivalent calculation

The example of how to calculate the gross grant equivalent has been given for a loan of the amount of 500.000 EUR and duration of 2,5 years. It is still unclear, however, what parameters should be used for calculating gross grant equivalent for guarantees not exceeding 750.000 EUR, but exceeding the period of 5 years (ex. given for period of 8 years). The example given in point 19 of the preamble can be interpreted in different ways and does not constitute a clear and unambiguous answer.

### 1.1. Applicability of the methodology to guarantees for other debt instruments

We propose to enable to use the clear easy applicable rule also to other types of debt instruments than loans, for example:

> In order to simplify the treatment of guarantees of short duration securing up to 80 % of a relatively small loan, this Regulation should provide for a clear rule that is easy to apply and takes into account both the amount of the underlying loan and the duration of the guarantee. ***This rule may be applied only to the guarantees for the basic transactions covering financial instruments like loans, credits and leasing.*** This rule should not apply to guarantees on underlying transactions not constituting a ***debt***, such as guarantees on equity transactions.

The proxy value as the percentage of guaranteed loan should be maintained as the preferred solution (see comment on para 4 2a)

### 2. Article 1, paragraph 1, point d) the term "other current expenditure linked to the export activity"

This term is ambiguous. Such expenses can concern e.g. buying materials for the production of export goods as well as subsidizing the amount of export goods and establishing and running the



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distribution network. Although from the context, one may understand that the aid towards the latter two should not be allowed, a literal interpretation gives the opportunity of broad understanding under which any current expenses for export activity could be covered. It is implicitly crucial to clarify abovementioned rule in an unambiguous way.

**3. Article 2 point d) a single undertaking**

The main issue of the "single undertaking" approach is its feasibility because of changes of links among entities in question. It could be assumed that the national *de minimis* register will not be able to absorb and record the changes in links among the entities. In this regard, it is very questionable whether national *de minimis* registers will be able to become reliable instruments where an on-line check is needed or whether there is a free capacity for a particular single undertaking.

This would be a crucial problem in comparison with the current situation. A key advantage of the national *de minimis* register, in countries where available, will be lost and a lot of "manual" work will be necessary to calculate a total amount of *de minimis* aid for a particular undertaking, mining data related to all linked enterprises stored in the database. An operation lasting usually a few minutes could last hours. Furthermore, it is unclear whether it is mandatory to analyse and to take into account the linked entities outside of the particular Member State. In latter case it is even more complicated to develop a national electronic register which leads to a non-usable *de minimis* regulation.

Independently on the above comment, following two key questions remain with regard to the wording of the letter d):

a) At what moment the links among enterprises in question have to be assessed? Is it at the moment the application for an aid was submitted or at the moment an aid is provided (a contract is signed)?

b) What links have to be analysed? Is there the same approach as within the SME definition, i.e. the full chain of the linked enterprises in both directions (up and down) have to be identified?

We have serious doubts that these new administrative requirements which should eliminate a part of the *de minimis* aid which otherwise could be provided, will not have any substantial and positive impact on the fair market competition but it will make the implementation of measures under *de minimis* more complicated, costly and less user friendly.

**4. Article 2 letter e*l* (iv) and (v) undertaking in difficulty**

In our opinion is the *de minimis* regulation not the right document for defining "undertaking in difficulty". Hence, the Community guidelines on State aid for rescuing and restructuring firms in difficulty should be used and the *de minimis* regulation should be linked to that guideline.

It is important that the definition is specified once, as otherwise contradictions might occur due to different durations of regulations and guidelines. Further regulations and guidelines should be linked by a dynamic link, as to ensure the correct usage of definitions at any point of time.

Nevertheless, few detailed considerations are stated below:

Article 2(e) of the draft provides a more specific definition of 'undertaking in difficulty' so that, in addition to partial changes made to previous criteria, three new independent conditions



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(subparagraphs iv-vi) have been added for a company to state that it is in difficulty. We feel that the scope of the proposed criteria (iv) and (v) for the definition of an undertaking in difficulty is unnecessarily expansive. Both criteria are disproportionately restrictive compared to previous criteria for the definition of an undertaking in difficulty, considering that each subparagraph of Article 2(e) alone is a sufficient interpretation of being in difficulty.

With regard to the applicability of both of the above mentioned criteria, it should be noted that they are also disproportionate to the new, proposed criteria (vi). In the subparagraph in question, the status of being in difficulty is linked to the CCC rating issued by a credit rating agency to that undertaking. However, in real terms, it is fairly obvious that no credit rating agency would issue an undertaking a CCC rating based solely on fulfilling either of the preceding criteria ((iv) and (v)). Instead, the criterion concerning a CCC rating in (vi), in and of itself, effectively meets the general definition of an undertaking in difficulty.

The proposed **criterion (iv)** for Article 2(e) is that the book debt to equity ratio must be greater than -7.5 for an undertaking to be declared in difficulty. The book debt to equity ratio is the proportion of interest bearing debt to an undertaking's equity. Book debt to equity ratio indicators cannot, however, be considered as being very descriptive, as the ratio can vary widely from field to field and cannot, therefore, provide a precise threshold value for what would constitute being 'in difficulty'. Moreover, the indicator definition might be unclear as to what debt amounts should be included and, on the other hand, what equity amounts can be considered equity.

The proposed **criterion (v)** for Article 2(e) is that the undertaking's earnings before interest and taxes (EBIT) to interest coverage ratio has been below 1.0 for the past two years. The proposed requirement means that if the earnings before interest and taxes (operating profit on the financial statement) are not sufficient enough to pay interest, the undertaking would be threatened with bankruptcy or a liquidity crisis. However, it should be kept in mind that, because depreciation is not a cash-based amount, the result after depreciation will not necessarily indicate any problems for the review period. In some situations, when an undertaking is making a strategic change, it is even normal that the result after depreciation will not be sufficient enough to pay interest for a number of years. Consequently, such a strict criterion would significantly increase the number of undertakings in difficulty, as defined here, even if they were actually viable. Meeting the criterion alone is therefore in no way an indication of an undertaking's equity or liquidity position.

As a result of this, implementation of criteria (iv) and (v) in accordance with the proposal would significantly restrict the granting of aid/funding in situations where public intervention and the addressing of market failure would be most justified. If the draft is realised in its proposed form, it will have considerable negative impacts on the availability of funding for small and medium sized enterprises and, in turn, on the general financial market situation. This would surely lead to an increase in otherwise avoidable bankruptcies in Europe's already difficult economic situation. Combined with low growth throughout Europe and the recession preceding it, this change is as unfavourable a measure as possible due to the fact that efforts are being made to use enterprises as a driver to restore growth in European economies.

The proposed measures are therefore in conflict with common economic goals throughout Europe.

Adjusting the proposed criteria with different threshold values can be considered an insufficient measure, as these proposed criteria are, in and of themselves, the types of requirements that do not adequately indicate the actual viability of an undertaking. Using longer review periods in the analysis of these criteria also fails to produce adequate value added for application of set requirements. As a



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result, we recommend that proposed criteria (iv) and (v) be omitted from the definition of 'undertaking in difficulty'. Instead of these separate and independent criteria, we want to emphasize the importance of a comprehensive examination of an undertaking's economic situation. This must be made by using at least two or three different criteria that all must deliver until the undertaking can be classified as an undertaking in difficulty.

**5. Article 4 para 2/a**

The proxy value as the percentage of guaranteed loan (13,33%) should be maintained as the preferred solution, the simplest method of the calculation of the state aid equivalent (with other options: safe harbour rates and notification).

We propose not to limit duration of loans guaranteed under *de minimis* rules – as it is in actual regulation.

Proposed methodology of aid equivalent calculation is still unclear. The question remains if for the guarantee amounting to 750.000 EUR, covering 80% of the loan and given for the period of 10 years, the aid equivalent is:

- 200.000 EUR (because the maximum guarantee level for period of 10 years is 750.00 EUR);
- 100.000 EUR (because the maximum guarantee level for de minimis aid is 1.500.000 EUR).

We suggest illustrating the typical combinations with the examples and clear methodology.

The requirement "the loan is secured by collateral covering at least 50 % of the loan" should be deleted. The value of collateral will be a permanent subject of disputes because different methodologies can be used to calculate it. There should be the same approach applied as in para 5 (guarantees) where no requirements on collateral exists.

It is not clear whether the methodology of gross grant equivalent calculation can be used for loans and guarantees with longer maturity than 10 years or higher loan and guarantee amount. We support to use the same methodology of gross grant equivalent for longer maturity and/or higher amount of loans/guarantees up to the maximum level of *de minimis* aid (EUR 200 000/100 000). The wording of the Article 4 should be more precise regarding this issue.

**6. Article 6 para 5**

The draft of the regulation states: "Member States shall record and compile all the information regarding the application of this Regulation. Such records shall contain all information necessary to demonstrate that the conditions of this Regulation have been complied with."

The wording is vague. For the reasons of the legal certainty an exhaustive overview, related to the types of information which should be stored, should be added.

**7. Minimum *de minimis* aid threshold**

We propose to consider the opportunity to set a minimum threshold of the *de minimis* aid which should be granted and recorded. If reference rate in case of loans and safe-harbour premiums and in case of guarantees are used to calculate the gross grant equivalent, the *de minimis* aid may be as low as 1 euro or less. Therefore, we propose to set a minimum threshold (for example EUR 1000 – 0,5%



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of maximum *de minimis* aid ceiling) where lower gross grant equivalent doesn't have to be granted and recorded.

**8. "Ad hoc" *de minimis* aid**

Another issue that still remains unresolved is admissibility of the "ad hoc *de minimis* aid" i.e. given outside of the guarantee program. The binding (until 06.2014) version of the regulation in article 2, paragraph 4, letter d, includes the following rule: "Individual aid provided under a guarantee scheme (…) shall be treated as transparent de minimis aid when the guaranteed part of the underlying loan provided under such scheme does not exceed EUR 1 500 000 per undertaking."

In the current draft version the requirement of state aid being granted under the guarantee program is removed. Does it mean that it will be allowed to grant the guarantee not under a programme and still use the abovementioned methodology of calculation of the grant equivalent? We ask you to clarify this in the text.



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