



COMMISSION OF THE EUROPEAN COMMUNITIES

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THIRD REPORT OF THE COMMISSION

relative to the implementation of the Decision regarding
the provision of Community interest subsidies
on loans for small and medium-sized enterprises
extended by the European Investment Bank under its temporary lending facility
(the SME Facility)

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1. INTRODUCTION

The present report has been established in the framework of Council decision 94/217/EC of 19 April 1994 ⁽¹⁾, relative to the provision of Community interest subsidies on loans for small and medium-sized enterprises extended by the European Investment Bank under its temporary lending facility (the SME Facility). The report constitutes an update of the second one, which was made available by the Commission on 30 October 1995 (COM(95)485). The next report (i.e. the fourth one) will also be the final one, as the Bank expects to finalize all subsidy disbursements by the end of 1997. The Commission intends to issue this final report as soon as all the statistical information on this final phase of the life of the SME Facility has been collected, and ideally before the end of 1997.

The SME facility was established at the Copenhagen European Council (21-22 June 1993), which invited the EIB to increase the size of its temporary lending facility by 3 bn Ecu, of which 1 bn Ecu would be allocated to the strengthening of the competitiveness of European small and medium-sized enterprises. The Ecofin Council was invited to examine how the part of appropriations available for SMEs could benefit from interest rate subsidies linked to employment creation.

On 4 July 1996, the European Parliament adopted a report on the Commission's second report on the SME Facility (1484/140147/96; rapporteur: Mrs Ewing), containing a resolution on this report, as well as a number of recommendations and requests for clarification. The present report will provide further comments on the various points raised in the Ewing report, while some of the points will be dealt with more extensively in the next report, particularly the ones requiring further investigation. Parliament's suggestions will also be integrated in the preparation of the ELISE scheme ⁽²⁾, which favours investment and job creation by small firms through the extension of loan guarantees.

2. LEGAL FRAMEWORK

Following the introduction of a legislative proposal by the Commission ⁽³⁾, and the opinion of Parliament of 24 February 1994 ⁽⁴⁾, the legal base for extending Community subsidies was enacted by the Council on 19 April 1994. This Decision specifies that the interest subsidies shall be:

- linked to Ecu 1000 million of EIB loans to SMEs in the Community;
- restricted to investment projects involving the creation of employment;
- fixed at 200 basis points (2 %);
- extended for a period of 5 years to the beneficiaries of the loans.

(1) O.J. L107 of 28.04.94, p. 57. Article 3 of the Decision specifies that the Commission shall send to the European Parliament and the Council a yearly report evaluating the implementation of the Decision.

(2) O.J. C 146 of 21.05.96, p. 6.

(3) COM(93)332 of 9.07.93, subsequently amended by COM(93)577 of 16.11.93 (O.J. C10 of 14.01.94, p.13).

(4) O.J. C114 of 25.04.94.

The decision also indicates that the facility shall be administered by the EIB on behalf of the Community and that the detailed arrangements for implementing the interest subsidy mechanism shall be laid down in a cooperation agreement between the Commission and the EIB. This agreement was signed in Luxembourg on 14 June 1994. The EIB has proceeded rapidly with the operational setting up of the SME Facility, through defining detailed procedures for its network of participating global loan intermediaries and reinforcing it by nomination of national agents (cf. 3.1 and 3.2). In December 1994, the Commission and the Bank agreed the modalities for the enlargement of the SME Facility to enterprises from the three acceding Member States (Austria, Sweden, Finland) from 1 January 1995 onwards. In July 1995, the Commission and the Bank also agreed to extend the Facility to the end of 1995 and to include specific provisions regarding the re-allocation of unused shares.

3. DESCRIPTION OF THE FUNCTIONING OF THE SME FACILITY

3.1. EIB global loans

The largest part of EIB lending (75.5 % of operations within the Union in 1995) to projects takes the form of direct loans, whereby loan applications are appraised by the Bank's own staff. Direct lending is generally practiced for operations exceeding a certain size (e.g. infrastructure or larger industrial projects).

For smaller loans, and SME loans in particular, the Bank has recourse to global lending procedures, whereby framework agreements are signed with various financial intermediaries operating in the Member States. These intermediaries are then entitled to draw upon EIB resources up to certain ceilings for the purpose of extending subloans to projects which are in conformity with the rules and conditions laid down in the framework agreement. The financial intermediaries carry out the project appraisal (subject to criteria previously agreed upon with the Bank and to subsequent EIB approval) and handle all relations with the beneficiaries. The intermediaries are furthermore responsible vis-à-vis the Bank for the full and timely repayment of the global resources on-lent to the final beneficiaries. In the context of the SME Facility, the role of the financial intermediaries is largely comparable as they have assessed all individual applications and have decided whether they were eligible for subloans.

3.2. The role of national agents

In most Member States, the management of the interest subsidies has been entrusted to a single national agent per country. These agents act under the Bank's supervision and process all requests for subsidies within a single country; the final beneficiaries however have no direct contacts or links with the agent in question as the latter receive all the necessary information through the financial intermediaries. In some countries, the agent can also be an intermediary.

The agents ensure that approved applications for subsidies are registered and processed in sequence on a "first come, first served" basis. They are also responsible for the processing and verification of the evidence which the beneficiaries are invited to submit in relation to employment creation, as well as for the actual payment (and whenever needed the recovery) of the subsidy. The agents therefore play an important role in ensuring that potential and actual beneficiaries are treated in a uniform way and that all administrative procedures linked to the verification and payment of the subsidy requests are handled in a timely and consistent manner.

3.3. Agreements with intermediaries and agents

As soon as the legal framework for extending Community subsidies was in place, the Bank has started signing the necessary agreements with financial intermediaries during the second half of 1994, either by amending global lending arrangements which were already in existence or otherwise by signing new agreements.

The Bank has appointed the national agent for each Member State after consultation with national authorities. Where no agent has been appointed (as is the case in Ireland), the Bank assumes this role. The list of agents and intermediaries is provided in annex 1. Each agent has been assigned an initial share of the total facility so as to allow him to start operations; a subsequent (and final) allocation has been assigned in the course of April 1995 on the basis of the actual commitments on the first tranche. As agreed between the Commission and the EIB in July 1995, the uncommitted balance of the Facility, which only amounted to 1.65 % of its total size, was redistributed on 15 December 1995 in favour of applicants on the reserve list. The SME Facility was thus fully taken up by the end of 1995.

3.4. Characteristics of the subsidized SME loans

The subsidized subloans (SME loans) extended by the financial intermediaries to the beneficiaries are limited to 30.000 Ecu times the number of jobs created. If the loan request exceeds this maximum amount (e.g. if 200.000 Ecus of loans are applied for but only 5 new jobs are created), the loan amount additional to the ceiling imposed by the number of jobs created (50.000 Ecus) is unsubsidized.

Inversely, if the loan amount is smaller than the maximum amount (e.g. if the size of the investments is limited to 100.000 Ecu, although 5 additional jobs would allow for a loan size of up to 150.000 Ecus), the total amount of subsidies will always be limited to 10 % of the size of the loan. This explains why the average loan size per job is smaller than 30.000 Ecus in certain countries (cf. annex 3).

Subsidized loans have a maturity of at least 5 years; voluntary repayment is not allowed during the first 5 years (except upon repayment of the subsidy). The loans cannot be combined with other loans at reduced rates offered by the EIB under other agreements or with ECSC loans. No restriction is imposed on the loan currency or on the repayment characteristics (repayment schedule, grace period, ...). Loans can be either fixed or floating rate.

3.5. Characteristics of the subsidy

The Council Decision sets the subsidy rate at two percentage points. As the loans allocations to SMEs can be expressed in various currencies and as the loans can also have different repayment schedules (depending on the maturity, the length of the grace period, etc.), the actual value of the subsidy could differ between beneficiaries, even for an identical loan size. In order to ensure fair and similar treatment of all beneficiaries, the interest subsidy is therefore calculated and paid on the basis of a notional 5 year bullet loan in Ecu. For this type of loan, an interest subsidy of 2 % per annum for a total of 5 years corresponds in total to 10 % of the SME loan amount (i.e. up to 3.000 Ecus per job).

3.6. Incentives for early job creation

In view of the objectives of the SME Facility (employment creation, sustainment of growth through productive investment), special incentives are offered to applicants so as to encourage early job creation and rapid execution of investment plans. Firstly, the applications for subsidized loans from the SME Facility must be received until a certain deadline date (initially set at 31 July 1995, subsequently postponed to 15 December 1995). In addition, the total amount of interest subsidies (i.e. up to 3000 Ecus per extra job) is made available to the beneficiaries in a single payment, as soon as the following conditions relating to the investment and the creation of jobs have been met:

- the SME loan has been effectively disbursed;
- the first interest payment has come due;
- the new jobs have been in place for at least 6 continuous months;
- the evidence relative to these conditions has been presented to the national agent (through the intermediary).

While applicants have a clear incentive to go ahead as soon as possible with their planned recruitments, experience shows that the creation of new employment may take considerable time (e.g. because the jobs are linked to the implementation of an extensive investment programme). Applicants have therefore some flexibility regarding the timing for introducing their requests for the subsidy. In any event, jobs must be created no later than 31 December 1996, and requests for subsidy payment must be submitted by the beneficiaries no later than 30 June 1997.

Applicants creating less jobs than originally applied for (i.e. less than the number stated in the loan application), only receive subsidies for the jobs effectively created. In the opposite case (more jobs created than originally envisaged), the subsidies are only paid in relation to the number of jobs indicated in the application.

3.7 Improving the take-up of loans

In order to avoid that subsidies available under the present mechanism are ineffectively or only partially used, two specific provisions exist as regards the re-allocation of unused credits. Each of these redistribution mechanisms is based on the reserve lists, which national agents are allowed to constitute if strong demand exists in their country for loans from the Facility.

A first re-allocation mechanism has operated across countries and has allowed for the apportioning of any indicative shares which were still unallocated by 15 December 1995 in favour of applicants on the reserve lists (cf. section 3.3 above). This one-time redistribution has occurred on the basis and in the sequence of the dated application record maintained by the national agents.

The second type of re-allocation takes place on a continuous basis and exclusively among applicants within the same country. Applicants on the reserve list, who have satisfied all the necessary conditions regarding job creation, hereby gain the possibility to receive the subsidies which had initially been set aside for other applicants, in particular when the latter appear to

have overestimated the number of jobs which they would be able to create within the imposed time frame. This re-allocation process will be completed by the end of September 1997.

3.8. Priority for small SMEs

The EIB's customary global lending arrangements with its financial intermediaries define SMEs as enterprises with net fixed assets not exceeding 75 Mecus, less than 500 employees and not more than one third of the equity owned by a company which is not an SME. In the framework of the SME facility, the agents and intermediaries have been asked to put special emphasis on smaller enterprises, particularly the ones having not more than 250 employees, and either a turnover not exceeding 20 Mecus or total assets not exceeding 10 Mecus.

In order to favour these smaller enterprises, at least 60 % of the number of beneficiaries of subsidized loans should belong to this category of enterprises. In addition, the size of the SME loans to enterprises of this category is unrestricted, while subsidized loans to larger SMEs are limited to 810.000 Ecus (corresponding to the creation of 27 jobs).

3.9. State aid rules

The SME Facility is compatible with state aid rules applying in the Member States and complies with the Community rules for accelerated clearance ⁽¹⁾, which specify limitations on the amount of aid which can be granted, notably in relation to the total size of the investment cost, the amount of aid per job created, etc. In view of the relatively limited amounts of aid granted, administrative controls in relation to state aid can thus be kept to a strict minimum.

3.10. Control and supervision

The agents verify the entitlement of each beneficiary to its respective subsidy on the basis of the declarations made by intermediaries and beneficiaries and agreement of the EIB that its criteria are satisfied. In addition, besides the usual monitoring of its global loans, the Bank will also carry out sample checks on the documentary evidence presented in relation to the requests for subsidy payments. In the event that documents presented or statements made by a beneficiary are materially incorrect or misleading, particularly in connection with elements allowing the verification of employment creation, the payment of subsidies will be cancelled and the beneficiary will be required to repay to the intermediary institution the corresponding amounts received. The Bank has made appropriate arrangements with the agents and intermediaries to allow the Court of Auditors to exercise its mission and to verify the regularity of the interest subsidy payments.

3.11. Promotion of the SME Facility

The promotion and success of the SME Facility depends to a considerable extent on the wide availability of information about the existence and operation of the SME Facility, particularly among potential beneficiaries.

The Commission and the EIB have devoted special attention to this aspect and have prepared an information brochure, summarizing the purpose and operation of the interest subsidy mechanism, as well as the list of intermediaries to whom applications should be addressed.

(1) Communication to the Member States on the accelerated clearance of aid schemes for SMEs and of amendments of existing schemes (92/C213/03 of 02.07.92); O.J. C213 of 19.08.92, p.10.

The brochure is available in all Community languages and has been distributed through the network of financial intermediaries taking part in the mechanism. In addition, the Euro Info Centres have been invited to play an active role in disseminating information about the Facility and the modalities for taking part in it.

4. IMPLEMENTATION

4.1 Planned job creation

The impact of the SME Facility on the creation of additional employment has been carefully monitored. As the beneficiaries are entitled to receive 30.000 Ecus of subsidized loans for every new job created, and as the total volume of EIB loans from the Facility amounts to 1 billion Ecus, the SME Facility will thus support the creation of at least 33.333 jobs.

The statistical information on planned job creation indicates that this objective has already been largely exceeded at this stage as the total for the Union currently amounts to around 45.500 jobs (corresponding to Ecu 1 billion of loan commitments). The number of jobs which are planned to be created in each Member State are provided in annex 2, while annex 3 provides the average loan amount per additional job.

In setting the various eligibility conditions, notably the ones on employment creation, the Commission and the Bank have attempted to strike the right balance between the need to ensure genuine added value (in terms of extra jobs, investment generation, etc.) and the aspiration to avoid excessive red tape and administrative burden for the beneficiary enterprises. This implies the balancing of sometimes conflicting objectives, such as the additionality of the extra jobs, and their structural or permanent nature. In addition, excessive conditionality as regards the new jobs created has been avoided as this typically runs against broader economic policy objectives (such as the need to maintain a sufficient degree of labour market flexibility) and as the permanency of jobs cannot be fully controlled by the beneficiary enterprises (e.g. voluntary departures).

It should be kept in mind that, besides encouraging the creation of additional employment, the SME Facility has also attempted to further and accelerate productive investment, hence stimulating the competitiveness of SMEs and overall economic growth. The total volume of additional investment associated with the Facility is estimated at 4 billion Ecu.

In some countries jobs have been created with a lower average loan size than in other countries. Here it is important to note that capital intensity is not the same throughout industries and throughout the Community. Extra employment in the service industry for instance can be created with a much lower investment size than a job in a capital-intense manufacturing enterprise. As on average the loan size per job turned out to be lower than foreseen, more jobs could be created than was originally anticipated.

4.2. Take-up of loans from the Facility

The loan allocation profile in each individual Member State is provided in annex 4. The amount of allocated loans is indicated in black, while the size of the reserve lists is indicated in grey.

As the Facility has been fully used up, the total volume of allocated loans amounts to 1.000 Mecu. The cumulative reserve list exceeds 436 Mecu.

The take-up of loans from the SME Facility has been satisfactory in the large majority of Member States. Relative differences can possibly be explained by the availability in some countries of other sources of public support (from regional, national or Community levels) at more attractive terms. In addition, the structure of the banking system in each individual country could have influenced the absorption capacity, as some countries have established specialized institutions for channelling public aid to enterprises. Finally, the number and type of intermediaries in each country could also have played a role.

As far as the sectoral breakdown of loan allocation is concerned, only preliminary figures exist, the majority part of operations being in the secondary (71%) and tertiary sectors (28%) of the economies. The most prominent sector metalworking and mechanical engineering accounted for about 20 %, followed by private and public-sector services for 19%. Major other sectors (5 - 7 % each) were foodstuffs, commerce, woodworking, rubber and plastics processing, as well as paper/pulp and printing.

4.3 Priority for small SMEs

Annex 5 illustrates that financial intermediaries in each Member State have largely exceeded the requirement to allocate at least 60 % of all loans to small SMEs. The average figure for the Union amounts to about 95 %, while 80 % have been committed to enterprises with less than 50 employees.

5. BUDGETARY ASPECTS

Budgetary appropriations in relation to the payment of interest subsidies amounted to 65.5 Mecus for 1994, of which 45.5 Mecu were transferred to the Bank in mid-1994 and the remaining 20 Mecu at the end of 1994 following budgetary transfers decided by Parliament at the end of the exercise. The amount proposed by the Commission in the 1995 Preliminary Draft Budget (22.75 Mecu) was reduced correspondingly, and credits amounting to 2.75 Mecu have been approved for the 1995 budget (and paid out in early 1995). The budgetary authority approved an amount of 57.75 Mecu under budget line B5-322 "Employment and Growth" for 1996. 7.75 Mecu for interest subsidies was paid out in early 1996. It is estimated that a further 18 Mecu is needed to fully cover the cost of the Facility; this amount will most probably be paid out during the last quarter of 1996. In terms of disbursements to the beneficiaries, 31.6 Mecu has been paid out by the Bank as of the end of August 1996.

All financial resources entrusted to the EIB for the payment of interest subsidies are credited on a special Community account within the Bank; interest earned on the account is credited monthly. As of the end of August 1996, the amount of accrued interest generated on the Community account within the EIB exceeded 7 Mecu. Any amount outstanding at the time of termination of the SME facility will be repaid to the Community budget.

ANNEX 1

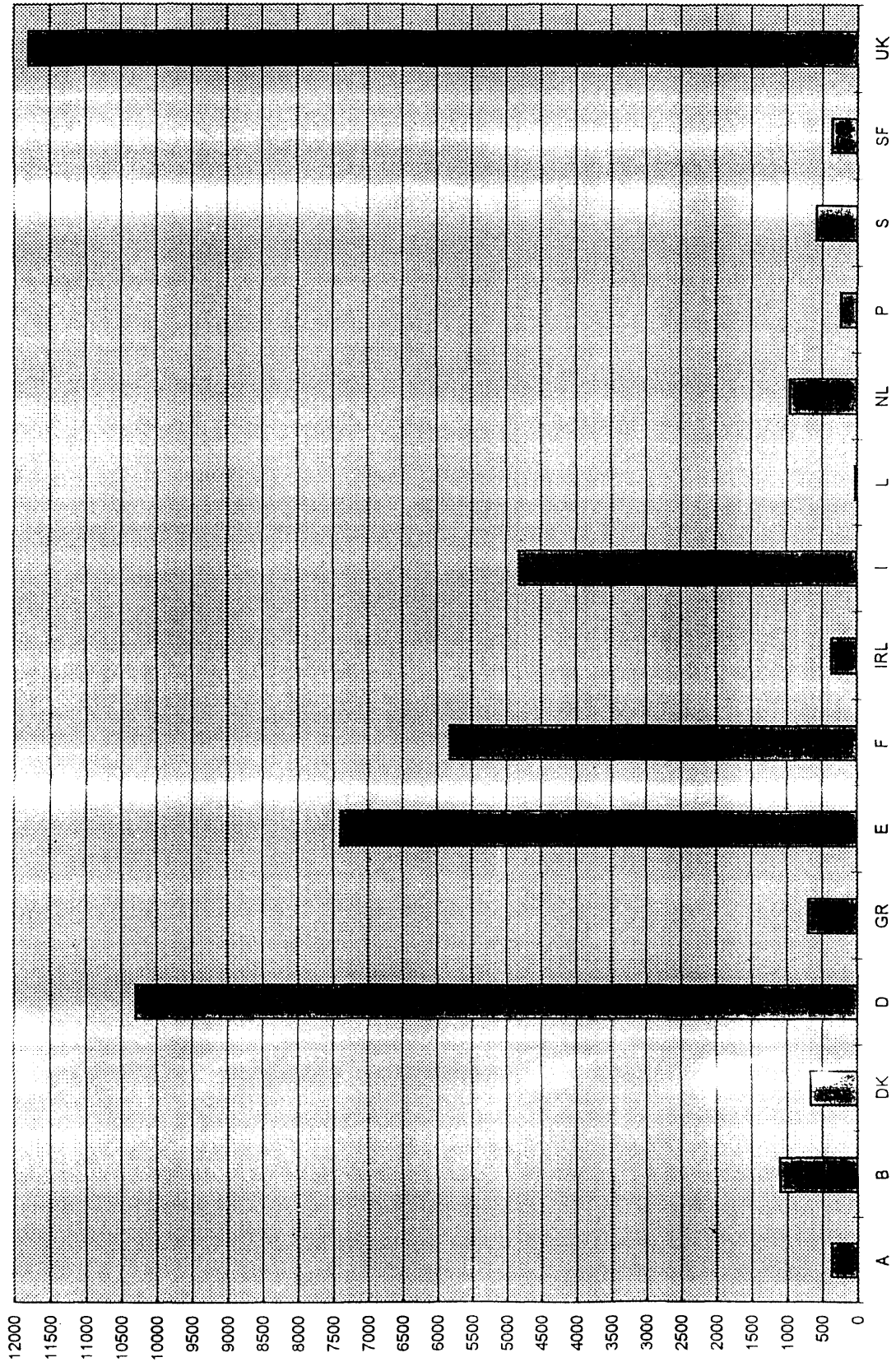
IMPLEMENTATION OF THE SME FACILITY IN EACH MEMBER STATE

(Situation as of September 1995)

Member State	Agent	Intermediaries
Austria	BÜRGES	INVESTKREDIT
Belgium	SNCI/NMKN	SNCI plus other EIB global loan intermediaries through SNCI
Denmark	FIH	FIH
Germany	KfW	Whole banking system through KfW
Greece	Ministry for the National Economy	All global loan intermediaries
Spain	ICO	Whole banking system through ICO
France	CDC	BFCM, CCCC, CCBP, CFD, CNCA, CNCM, CMB, CBG-PARIBAS, CCF
Ireland	EIB	ICC and AIB
Italy	MCC	All global loan intermediaries
Luxembourg	SNCI	SNCI
Netherlands	NIB	NIB, ING, ABN AMRO
Portugal	IAPMEI	All global loan intermediaries
Sweden	SEK	SEK
Finland	KERA	KERA
United Kingdom	Barclays	Barclays, Barclays MBF, Midland, Royscot Trust, The Royal Bank of Scotland, Bank Scotland, Clydesdale, Northern Bank

ANNEX 2

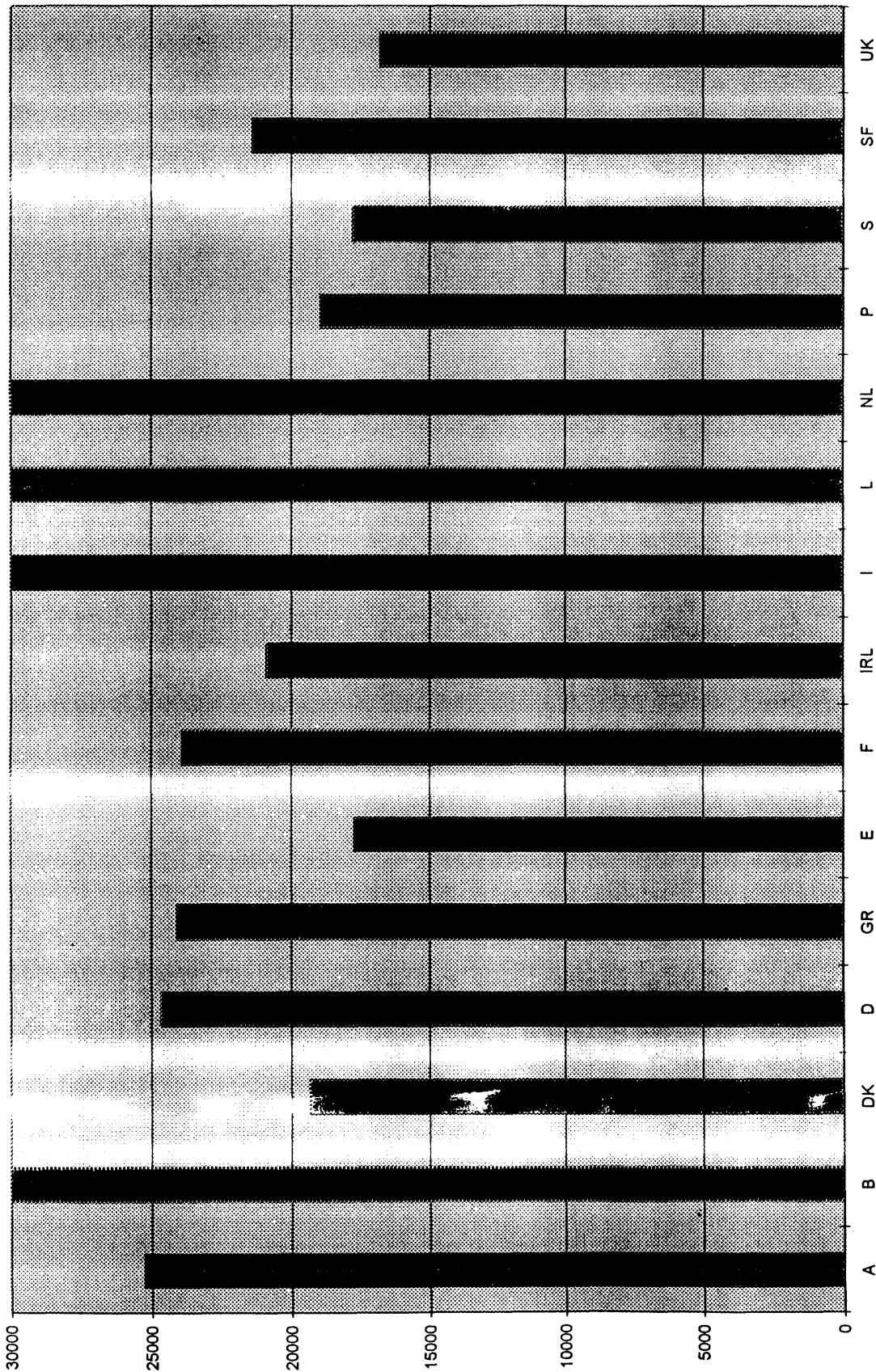
PLANNED JOB CREATION
(Situation as of 31 July 1996; in units)



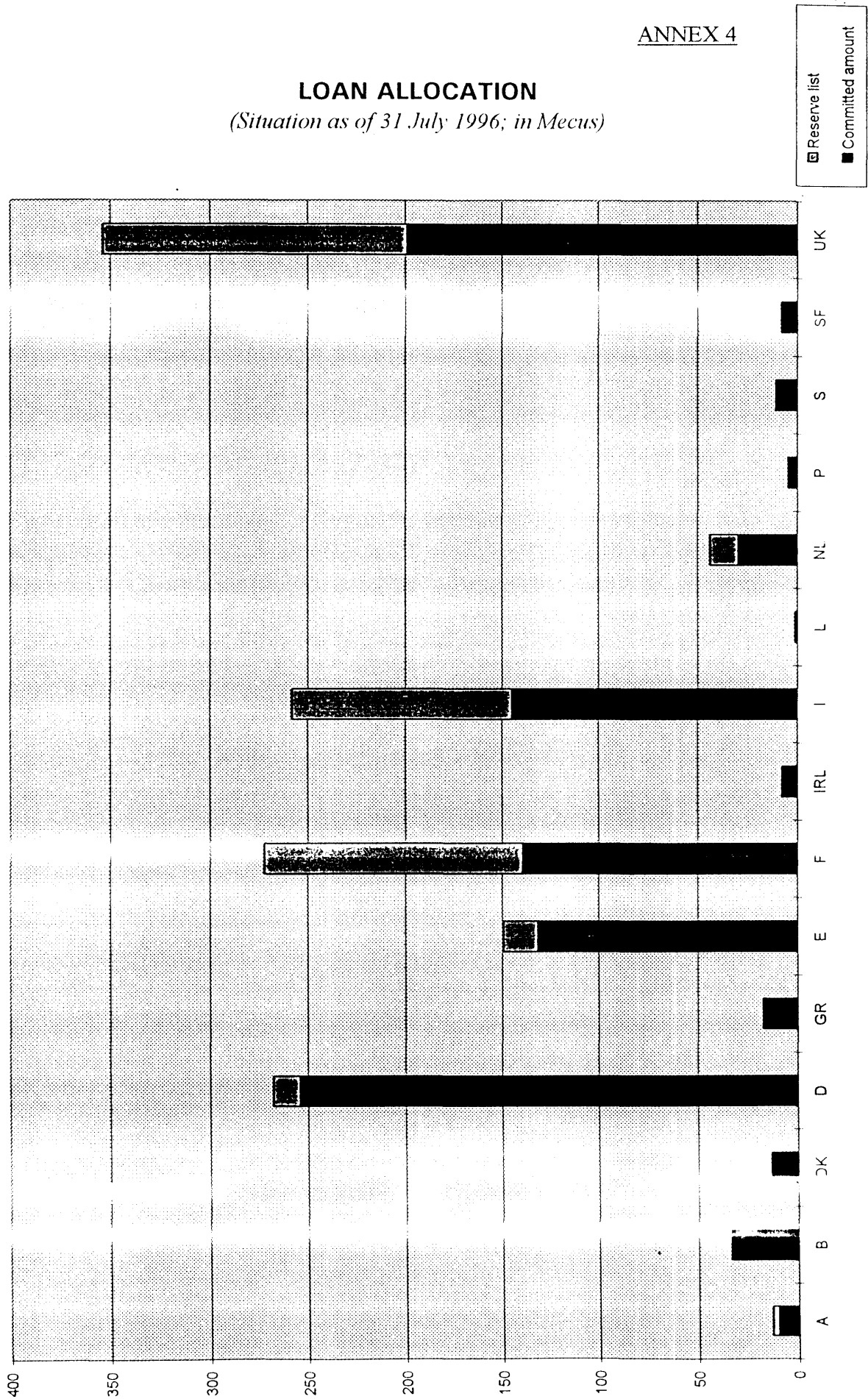
ANNEX 3

AVERAGE LOAN SIZE PER JOB CREATED

(Situation as of 31 July 1996; in Ecus)

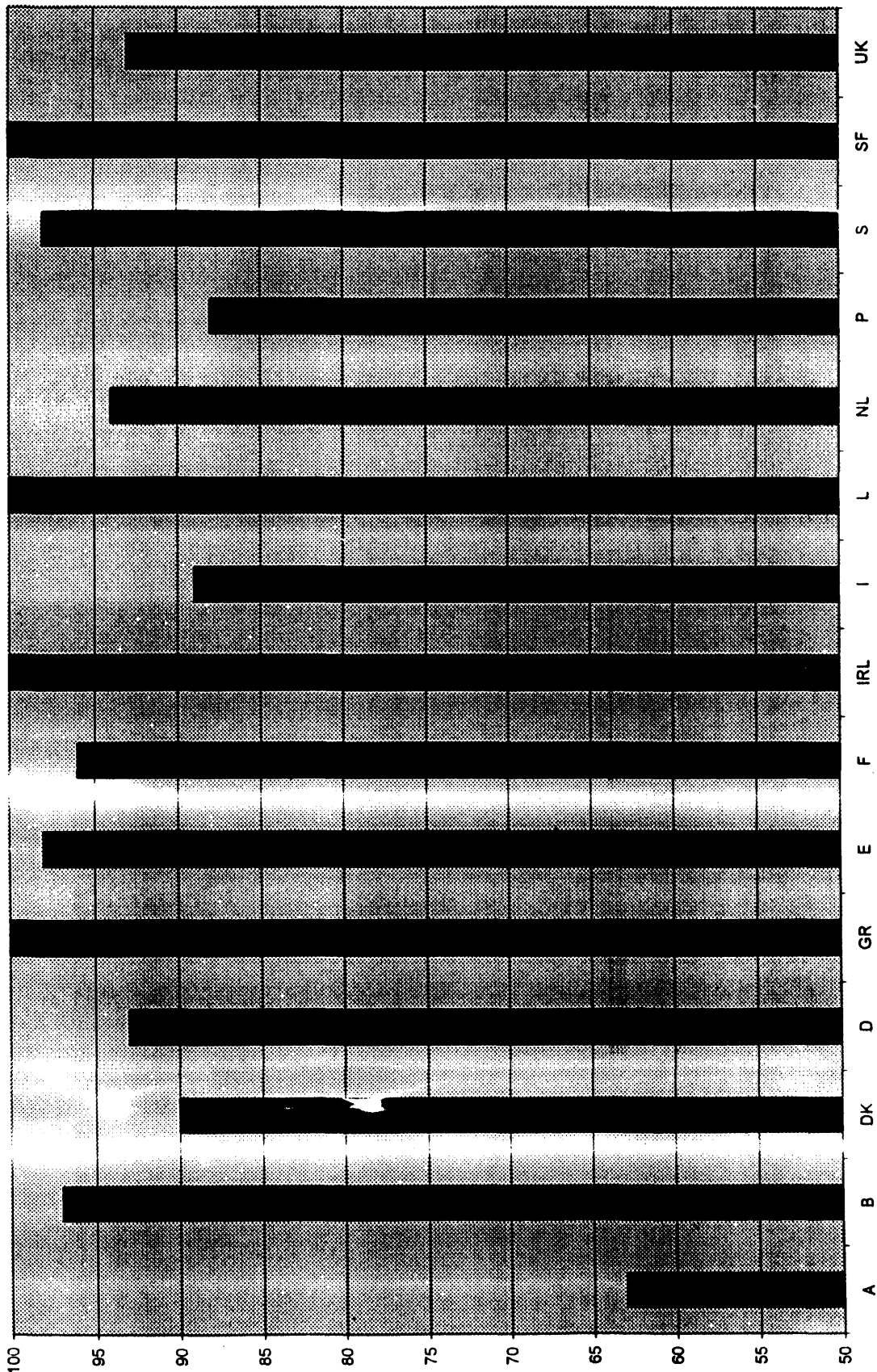


LOAN ALLOCATION
(Situation as of 31 July 1996; in Mecus)



ANNEX 5

PERCENTAGE OF SMALL SMEs
(Situation as of 31 July 1996; in percent)



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DOCUMENTS

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