

# Position Paper

## UEAPME<sup>1</sup> Evaluation and Impact Assessment of Recommendation 2003/361/EC concerning the definition of micro, small and medium-sized enterprises

### Key Messages

UEAPME members feel the SME definition is still fit to achieve its strategic and specific objectives. It covers those SMEs which should be covered. The current thresholds should therefore not be changed and the staff headcount criterion should remain the major criterion. Changes would result in even more companies being considered as SMEs and in turn disadvantage micro, small and medium-sized enterprises that have less capacities and truly need support. When the underlying rationale of the SME definition is consistently applied at European level, it is sufficient to address difficulties faced by SMEs, in particular regarding the raising of finance and the participation in major EU policy programmes – e.g. the Structural Funds. An extension of the SME definition (e.g. by raising the thresholds or widening the scope) would dilute the available support for SMEs.

### Introduction

The current EU definition of Small and Medium-sized Enterprises (SMEs) is set out in Recommendation 2003/361 of the Commission adopted on 6 May 2003, which came into effect as from 1 January 2005 (“EU SME Definition”). The main factors determining whether an enterprise is an SME are: Staff headcount and turnover or balance sheet total. To qualify as an SME, the EU SME Definition requires that the number of employees must be below 250 (average headcount in full-time equivalents over a financial year) and either a net turnover of less than 50 million Euros or a balance sheet total of less than 43 million Euros. An enterprise must be autonomous or part of a group of affiliated enterprises that together fall below the ceilings.

In this category, the Recommendation makes a distinction between:

- Small enterprises: they employ less than 50 persons; the net turnover or the balance sheet total does not exceed 10 million euro;
- Micro-enterprises: they employ less than 10 persons and their net turnover or the balance sheet total does not exceed 2 million euro.

The Commission regularly monitors the implementation of the EU SME Definition. The latest evaluation carried out in 2012 concluded that there is no need for a major revision of the EU SME Definition. The final report of the study recommended clarifying the application of certain rules within the existing Recommendation by providing guidance and updating the SME Definition User Guide.

On 8 June 2017, the Commission published an Inception Impact Assessment<sup>2</sup> on the revision of the EU SME Definition. Therein, the Commission identifies the SME Definition as a structural tool to identify those enterprises which are confronted with market failures and particular challenges (e.g. access to finance) due to their size, and

<sup>1</sup> UEAPME subscribes to the European Commission’s Register of Interest Representatives and to the related code of conduct as requested by the European Transparency Initiative. Our ID number is [55820581197-35](https://ec.europa.eu/info/law/better-regulation/initiatives/ares-2017-2868537_da).

<sup>2</sup> [http://ec.europa.eu/info/law/better-regulation/initiatives/ares-2017-2868537\\_da](http://ec.europa.eu/info/law/better-regulation/initiatives/ares-2017-2868537_da)

therefore are allowed to receive preferential treatment in public support.

Through a first consultation of its member organisations that UEAPME conducted no major comments or remarks were received on the SME definition as such and/or on the transition periods. In the few cases where problems were reported, they concerned purely national issues. This means that the SME definition is satisfactory, both at European and national level. There have been also no substantial contextual changes in the EU since 2003 concerning the SME definition that need to be taken into account.

Nevertheless, UEAPME and its member organisations would like to put forward the following remarks:

## 1. Thresholds

UEAPME and its member organisations are against any increase of the headcount or financial SME thresholds. We have always considered the staff threshold of 250 persons as rather high, as it covers already 99.8% of all enterprises and two-thirds of the European economy in terms of employment. Any expansion of that threshold would make it impossible to direct financial support to those micro, small and medium-sized enterprises needing it. The current thresholds (micro, small and medium) are also part of policymaking in the Member States and the Union. It may be clear that an increase of this threshold is unacceptable, as it may lead to a "watering down" of the notion of "SME" covering nearly every enterprise.

The reasons mentioned in the 1996 Recommendation to keep the SME threshold at maximum 250 are still valid in 2017: *"Whereas the threshold of 500 employees is not truly selective, since it encompasses almost all enterprises (99,9% of the 14 million enterprises) and almost three-quarters of the European economy in terms of employment and turnover furthermore, an enterprise with 500 employees has access to human, financial and technical resources which fall well outside the framework of the medium-sized enterprise, namely ownership and management in the same hands, often family-owned, and lack of a dominant position on the market; Whereas, not only do enterprises between 250 and 500 employees often have very strong market positions but they also possess very solid management structures in the fields of production, sales, marketing, research and personnel management, which clearly distinguish them from medium-sized enterprises with up to 250 employees whereas in the latter group, such structures are far more fragile whereas the threshold of 250 persons employed is therefore a more meaningful reflection of the reality of an SME;"*

**Mid-caps:** It may be clear that this does not automatically mean that enterprises which exceed these thresholds do not deserve national/regional or EU attention. But obvious growth problems for some enterprises in single Member States must not be overcome by European programmes for SMEs. These enterprises have access to human, financial and technical resources which fall well outside the framework of the medium-sized enterprises. Also the Inception Impact Assessment (08/06/2017) states that larger enterprises are better able to take advantage of any support available. They often have very strong market positions and also possess very solid management structures in the fields of production, sales, marketing, research and personnel management, which clearly distinguish them from medium-sized enterprises. In the opinion of UEAPME, it would be more appropriate to solve this problem, if necessary, through specific measures in the framework of the relevant programmes.

Moreover, there is no evidence of market failure in relation to Mid-caps and hence there is no need for public intervention to improve financing conditions for these enterprises.

**Sector approach:** This may lead to a more complex definition and more administrative burden. In addition the differences between many sectors are disappearing, especially in the services sector. Sector specificities are best addressed in sectoral legislation and/or by eligibility criteria of funds.

Conclusion: increasing the staff headcount stated in the Recommendation would not be reasonable. In addition also the financial thresholds (balance sheet total and turnover) relating to the definition should, according to UEAPME, not be adapted in line with the cumulative inflation rate. The effect of inflation varies significantly from one country to another with some southern EU economies experiencing static prices or even deflation in the past few years. While the current financial threshold are well known and easy to remember, an adaptation to inflation would lead to a loss of this advantage. In addition, any changes to the definition would create difficulties and administrative burdens for existing SMEs due to practical issues associated with the application of a new definition.

Finally, the Member State option to use lower thresholds has to be kept. (Article 2 of the Recommendation)

## 2. Start-up and scale-up – Lock-in effect

In the Inception Impact Assessment the Commission, when mentioning the “problem” the initiative of the review aims to tackle, states that *“In this context it should also be considered that the thresholds set by the Recommendation could lead to certain lock-in effects that would discourage SMEs to scale-up by fear of losing the support that the SME status provides. European SME associations claim that approximately 70% of SMEs prefer to maintain the SME status rather than growing fast and thus creating growth and jobs.”*

The document further states under Option 2, sub-option c) that: *“Introduce additional considerations to the benefit of start-ups and scale-ups could also be envisaged. These could, inter alia, concern enhanced participation of venture capital or extension of the 2-year period during which scale-ups would still maintain the SME status.”*

First of all UEAPME wants to highlight that it has never claimed *“that approximately 70% of SMEs prefer to maintain the SME status rather than growing fast and thus creating growth and jobs”*. Indeed this reference is taken out of its context. We stated<sup>3</sup> that *“Public authorities and especially the European Commission gave and give almost exclusive focus on “start-ups” and “growth enterprises” (which are now called “scale-ups”). In UEAPMEs view, attention has to be given to “traditional” SMEs as well, as 70% of SMEs would like to stay in their current situation.”* It was also explained why they want to stay in their current situation, which has nothing to do with their SME status in the sense of the definition: *“... “small giants”: small enterprises which are not visible, but who want to guarantee the quality of their products and their services. They cannot guarantee the quality of their products or their services if they become too big. This is the economic reality. Most of the owner-managers perceive some “ideal size” for their enterprise. This often means that they wish to grow but that this growth is limited by concerns about maintaining control of day to day operations and step- in- costs from expansion of the enterprise. For example, owner-managers may wish to avoid delegating responsibility to others, which might be the result of growth.”*

According to the Recommendation (Article 4 (2) of the Annex) a company only loses its SME status two years after exceeding the headcount or financial ceilings. Our members did not encounter any problem with this rule and also the Commission does not put forward any arguments to prolong this period.

Rapid growth companies are among those most susceptible to failure and one might argue that the increased scrutiny that comes once a company crosses a threshold is a small regulatory incentive for internal controls, reporting requirements and they like to grow as the business grows. The policy debate on high growth firms is more centred on providing a supportive ecosystem than the provision of direct support (as you would for more vulnerable firms). This is partly because these firms are generally more capable of accessing investment through the private sector. Therefore granting greater leeway to high growth firms through a legal definition – whose primary purpose is to address market risk or failures such as difficulties accessing external finance – may be seen

<sup>3</sup> See UEAPMEs Position Paper on the Start-up Initiative, 20<sup>th</sup> July 2016, [http://www.ueapme.com/IMG/pdf/UEAPME\\_position\\_on\\_the\\_Start\\_Up\\_Initiative.pdf](http://www.ueapme.com/IMG/pdf/UEAPME_position_on_the_Start_Up_Initiative.pdf)

as unnecessary. Allowing exemptions to a rule introduces regulatory complexity where in this case it may not be needed or desirable.

The Commission points out that the thresholds set by the Recommendation could lead to certain lock-in effects that would discourage SMEs to scale-up by fear of losing the support that the SME status provides. It seems to us that the issue of scale-ups (of which no definition is given or exist) is brought up for political reasons. Indeed as the Commission mentions scale-ups represent a very small portion of EU SMEs. Scale ups that lose their SMEs status will be even rarer.

Regarding possible lock-in effects for start-ups/scale-ups, there is no evidence at all that some enterprises deliberately refrain from growing due to the SME definition. The Commission does not give any evidence and also our member organisations have no information indicating that potentially crossing one of the thresholds would represent a barrier to the scaling up of the enterprise. Lock-in effects exist but they relate rather to taxation and labour market provisions or other rules having nothing to do with the EU SME Definition and in categories below 250 employees. This is even confirmed in the Commission report “Evaluation of the application of the Think Small First Principle in EU legislation and programmes”<sup>4</sup> which mentions that there are possible risks of threshold effects due to size related exemptions in the following directives:

- Directive 98/59 regarding collective redundancies: consultation procedures are only to be carried out if at least 10 dismissals are planned in companies with 20-100 employees;
- Directive 72/221 regarding annual surveys of industrial activity: annual surveys are only to be carried out in enterprises employing more than 20 persons. Smaller firms only participate every five years.

The possible lock-in effects have - as shown - nothing to do with the EU SME Definition but with specific thresholds in the respective policy fields.

Therefore UEAPME rejects option 2c. A two-year transition period is in our view sufficient for start-ups to grow and there is no so called lock-in effect for companies that are hindered growing into big companies because of the definition.\*<sup>5</sup>

### 3. Public entities – autonomous enterprises – partner enterprises

It is unclear why organisations run by public authorities require special treatment. Member States may already bring those entities within the scope of company law using a Member State option. It is unclear why this needs action at EU level. Small autonomous local authorities, as well as companies with investments by venture capital companies can already benefit from the advantages of the SME definition. It would be unhealthy if a public authority was able to conduct all its operations through a matrix of shell “SMEs” to the point where transparency and the ability to hold the authority accountable is lost or impaired.<sup>6</sup>

### 4. Legal issues

The consequences of the two judgments of the Court of Justice of the European Union of 15 September 2016, in cases T-675/13 (Chimica) and T-587/14 (Crosfield), should be examined to ensure that they do not result in a considerable increase in the overall number of SMEs, possibly by making use of specific corporate structures. So far any information on the practical relevance of these judgements and the number of enterprises concerned is missing. Of course it has to be ensured that the definition of linked enterprises and partner enterprises is

<sup>4</sup> Evaluation of the application of the Think Small First Principle in EU legislation and programmes” Specific Contract Reference: ENTR/E4/04/93/1/08/17; Framework Contract on Evaluations ENTR / 04 / 093, Lot 1,DG ENTERPRISE AND INDUSTRY, Draft Final Report Submitted by GHK, 16 September 2008, p.52.

<sup>5</sup> With the exception of CPME.

<sup>6</sup> See article 3 Annex of the Recommendation

sufficiently clear. However, corporate structures of SMEs are normally not complex. From UEAPME's perspective the consequences of the two judgements should therefore be examined in detail to clearly identify the concrete need for regulatory clarifications. Ultimately, it should not result in more companies being covered by the SME definition in general or because they intentionally make use of specific corporate structures in order to fall under the SME definition.

## 5. A better control of the application of the definition in all EU programmes

In the past years the Commission has taken measures to adapt programmes and policies to the new SME definition.

Nevertheless a better control of the application of the SME definition in all EU programmes remains a priority, without imposing additional red-tape to the "real" SMEs, in order to avoid that funding is going to "fake" SMEs. As the aim of the new definition was to ensure that support measures are granted only to those enterprises which genuinely need them, UEAPME also reiterates its demand to the Commission to publish verified data on SME participation in all EU programmes.

A widening of the SME definition would be in contradiction with the principles of the European Small Business Act. Instead of widening the definition it would be better to work on more targeted programs at the Union level for the small and micro enterprises, as they need it the most and urgently (access to finance, awareness, capacity building ...). In addition, all data available indicate that SMEs are underrepresented in European support programmes.

## 6. Lack of attention for small and micro-enterprises

The existing category of micro-enterprises is not able to reflect labour market changes towards more self-employment (one-person-enterprises), which constitute according to the SME Observatory more than 55% of all enterprises.

This leads to the suggestion to even sub-divide the sector of micro enterprises for certain programmes and other purposes of economic policy in order to better focus programmes and policies towards these enterprises. But this has to be decided on a case by case basis.

In general, we can only regret that despite the clearer definition of small and micro enterprises, which has been introduced by the Recommendation, this has not been followed by more targeted programmes at Community level for these enterprises. It has been neither followed at European level by a statistical and economic analysis of the different categories of SMEs (especially the smallest ones), as also requested by the European Parliament, nor an analysis has been conducted about the benefits the different categories of SMEs gain from European programmes.

**Conclusion:** for UEAPME there is no need for changes in the EU SME definition, in particular the headcount and financial thresholds. The two-year transition period should be maintained\*<sup>7</sup> and the consequences of the two Court of Justice judgements should be further examined. UEAPME insists on a close co-operation and involvement in the coming months.

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<sup>7</sup>\* With the exception of CPME.