



7 November 2017

## REVISION OF THE EU DEFINITION OF SMEs

### KEY ELEMENTS FOR A SOUND APPROACH

#### 1. INTRODUCTION

In a recent inception impact assessment (8 June 2017), the Commission explained that it considers revising the EU definition of SMEs (Small and Medium Enterprises) that is embedded in the Commission's Recommendation 2003/361/EC of 6 May 2003.

This position paper presents BusinessEurope's main views on this issue, in the light of the General Court Decisions in cases T-675/2013 (K-Chimica) and T-587/14 (Crosfield).

As a reminder, in these two cases, the General Court considered that ECHA (the European Chemicals Agency in charge of implementing the REACH regulation), following the traditional practice of the Commission Services, had wrongly interpreted Article 6 in the Annex to the 2003 Recommendation and unduly denied to Crosfield and K-Chimica (a company with less than 20 employees) the benefit of the reduced REACH registration fee for small enterprises.

#### 2. REMINDER OF SOME BASIC ELEMENTS OF THE 2003 EU SME DEFINITION

The 2003 EU SME definition makes reference to the following key economic parameters:

Company category	Employees	Turnover ...	OR	...Balance sheet total
Medium-sized	< 250	≤ 50 million Euro		≤ 43 million Euro
Small	<50	≤ 10 million Euro		≤ 10 million Euro
Micro	<10	≤ 2 million Euro		≤ 2 million Euro

While the 2003 SME definition is embedded in a Commission Recommendation, about 100 EU subsequent legislative acts refer to that definition, which gives it a clear legal force in particular situations.

The spirit of the definition is to ensure that available support and special measures to reduce administrative burden are focussing on those enterprises that are most in need of it (June 2017 inception impact assessment, page 3). In order to clarify whether a particular enterprise is a "genuine SME", the Commission takes into account the economic relationships that this enterprise has with other companies. In very simplified terms, this leads to defining the following 3 categories of companies:



- a) **autonomous**: if the enterprise is either completely independent or has one or more minority partnerships (each less than 25 %) with other enterprises;
- b) **partner**: if holdings with other enterprises rise to at least 25 % but no more than 50 %, the relationship is deemed to be between partner enterprises;
- c) **linked enterprise**: if holdings with other enterprises exceed the 50 % threshold, these are considered linked enterprises.

For checking if a company **A** is an SME, the Commission Services have developed a methodology requiring (in simplified terms) to sum up:

- i. the figures of company **A**;
- ii. a proportion of the parameters of the partner companies (equal to the level of participation in the partner companies);
- iii. 100% of the parameters of the linked companies.

Some elements of that methodology (also used by ECHA) have been invalidated by recent Decisions of the General Court (see point 4 below).

### **3. REMINDER OF BUSINESSEUROPE'S BASIC POSITION REGARDING THE 2003 EU SME DEFINITION**

In 2012, BusinessEurope evaluated the 2003 EU SME definition. This led to a very broad consensus view within BusinessEurope that the 2003 SME definition was pragmatic and workable for addressing a large number of issues which interest SMEs. There was also a very broad consensus view within BusinessEurope that this basic EU SME definition should not be fundamentally modified, except possibly regarding the level of financial parameters to take account of inflation. These two points still form the core of today's BusinessEurope position, with the added consideration that the EU SME definition should continue to be fundamentally geared towards the promotion of private entrepreneurship, which is the key engine for growth in Europe. The EU SME definition should therefore not be changed regarding its provisions dealing with publicly controlled enterprises (Article 3 paragraph 4 in the annex to the 2003 Recommendation).

### **4. POLICY CONCLUSIONS TO BE DRAWN FROM THE K-CHIMICA AND CROSFIELD CASES**

The K-Chimica<sup>1</sup> and Crosfield cases have highlighted that a discriminatory treatment was wrongly being made by ECHA between "autonomous" SMEs and for SMEs integrated in particular chains of "linked" and "partner" companies, like K-Chimica and Crosfield.

The General Court Decisions led to the recognition that:

- the challenges of dealing with costly and/or complex EU regulations are basically the same for autonomous SMEs and for SMEs integrated in particular chains of "linked" and "partner" companies, like K-Chimica and Crosfield;

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<sup>1</sup> For a summarised presentation of the General Court approach (versus the ECHA approach) in the K-Chimica case, see Annexes I and II



- autonomous SMEs and SMEs integrated in chains of companies of the K-Chimica type can therefore objectively have the same need for a lighter regulatory regime than the one applicable to large companies.

The inception impact assessment of June 2017 and some recent documents of the Commission Services show that this important fact might be lost of sight when revising the EU SME definition. BusinessEurope would have liked a more sophisticated presentation of the possible policy options for revising the SME definition. The Commission documents give a disproportionate weight to one function of the EU SME definition, which is to help focusing support on those enterprises which, because of their size, face several challenges due to market failures. By contrast, the other function of the EU SME definition, which is to assist in implementing better regulation policies for SMEs, receives comparatively much less attention.

By looking too much at the EU SME definition as a tool for optimising SME access to EU finance, there is a danger of artificially excluding a significant population of companies from the benefit of EU measures aimed at reducing administrative and regulatory costs for SMEs. The EU SME definition must be fit for defining which company population can, in some specific circumstances, benefit of a lighter EU regulatory regime or of regulatory exemptions. It would not be appropriate to define this company population with criteria aimed at assessing whether companies are part of a larger group. Such an approach might lead companies like K-Chimica and Crosfield to be again requested to pay the full REACH registration fee. More generally, it would lead to exclude many companies from the benefit of any EU SME-g geared lighter regulatory regimes. BusinessEurope would be totally opposed to a revision of the EU SME definition leading to such an outcome.

For BusinessEurope, the revision of the EU SME definition must on the contrary be aligned with the conclusions of the General Court Decisions in the K-Chimica and Crosfield cases, and address the problems rightly identified in the wording of the 2003 Recommendation.

The General Court Decisions have shown that the 2003 SME definition is not up to standards regarding clarity of the wording (in particular when it describes the methodology to be applied to assess if an enterprise can have the SME status – cfr Article 6 in the Annex to the 2003 Recommendation).

The Decisions also highlighted that part of that methodology is based on too theoretical considerations, which can lead to impose unrealistic administrative tasks and costs on enterprises that wish to check their SME status. The Decisions showed for example that the traditional interpretation of Article 6 by ECHA and by the Commission Services could lead, in certain cases, to there being no limit as to the data that must be obtained and considered regarding the enterprises situated either upstream or downstream the company that wishes to know if the legislator classifies it as SME or not.

BusinessEurope therefore very much welcomes the clarification brought in by the General Court Decisions about how article 6 should be interpreted and implemented. With a view to ensuring legal certainty regarding Article 6 and reducing administrative burdens for companies, BusinessEurope recommends a targeted intervention aimed at rewriting Article 6 in a way that reflects the approach of the General Court Decisions in the K-Chimica and Crosfield cases.



## **5. ASSESSING THE SME-STATUS OF A COMPANY: THE NEED FOR A USER-FRIENDLY APPROACH**

Any calculation methods set up in a revised definition should be simple and straightforward to apply for SMEs, which should always be able to do the calculations by themselves. Introducing new complex models would impose new burdens on SMEs which would need to spend time on advanced calculation methods or even to pay for counselling in order to determine whether they are an SME or not. The current “SME definition user guide” has an easy-to-use format. The same simplicity must characterize a revised definition in order to avoid that SMEs depend on accountants or other counsellors in order to know whether they are to be regarded as an SME or not.

Any adjustment of the SME definition should however remain strictly aligned with and closely linked to practices in accountancy. The current SME definition is aligned with accountancy practices in the sense that it also distinguishes between ownership of 25-50% (which does not require consolidating the accounts of the associated companies) and ownership of 50% and above (which requires consolidation). Within accountancy, simple rules thus define whether or not to consolidate the balance sheets. Simple methodologies, that are well aligned with accountancy rules, should also be used in the context of the revised SME definition.

A simple way of dealing with the recent Court rulings could be to state in the “SME definition user manual” that an SME which is part of a consolidated balance sheet is an SME only if the group balance sheets stay within the thresholds set in the SME definition.

## **6. SUPPRESSING CONSTRAINTS FOR COMPANIES FINANCED BY VENTURE CAPITAL**

BusinessEurope observes that Article 3 in the Annex to the 2003 Recommendation often has a negative impact on access by SMEs to venture capital and/or on growth prospects once venture capital has been obtained. The current provisions in Article 3.3 ultimately lead to situations where all companies in which a venture capital manager has invested are treated as “linked enterprises”. As a result, all these companies can only fail to qualify as SMEs. In other cases, due to the uncertainty caused by the current definition, companies backed by private equity which could claim the SME status are not able to do so. We therefore call for amending the 2003 EC Recommendation in a way that stipulates that a company is autonomous when a venture capital fund invests in it, whether or not this fund holds 50% or less of the capital or voting rights.

## **7. CONCLUSIONS**

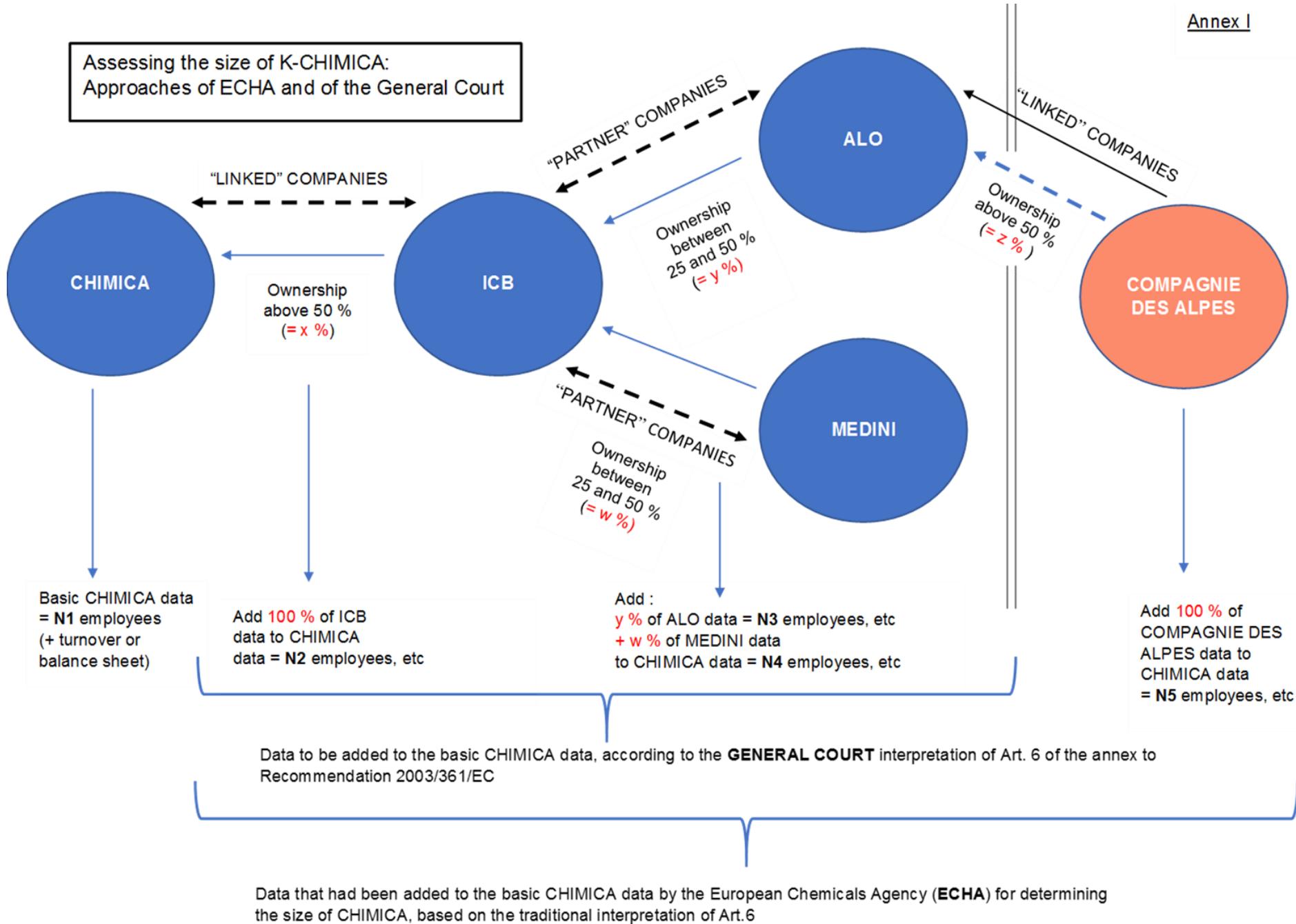
In conclusion, BusinessEurope recommends that the basic EU SME definition should not be fundamentally modified, except to take into account the recent jurisprudence from the K-Chemica and Crosfield cases, to facilitate equity financing by financial intermediaries and to possibly adjust the level of financial parameters, to take account of inflation. This inflation adjustment should be done with due care, and not result in including, in the scope of the EU SME definition, a new segment of bigger players compared with what was foreseen in the 2003 definition.



As a final thought, BusinessEurope notes that the role played by mid-caps in the economy is recognized in a number of scattered EU initiatives (Horizon 2020, EFSI,...). Following the assessment of the EU SME definition, it could be useful that the Commission holds a strategic discussion on the topic of mid-caps.

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Assessing the size of K-CHIMICA:  
Approaches of ECHA and of the General Court



RECOMMENDATION 361/2003: DATA TO USE TO GRANT THE "SME STATUS,, TO A COMPANY "A,, HAVING RELATIONSHIPS WITH OTHER COMPANIES	
(1) Practice of the Commission before the 2016 General Court (G.C.) Decision in the Chimica case	(2) Changes required by the 2016 General Court (G.C.) Decision in the Chimica case
Chain of companies with <b>L</b> -> <b>P</b> elements	Chain of companies with <b>L</b> -> <b>P</b> elements
<p><b>L</b>: Linked enterprise; <b>P</b>: Partner enterprise</p>	
	The data of this company need to be taken into account
	The data of this company must not be taken into account