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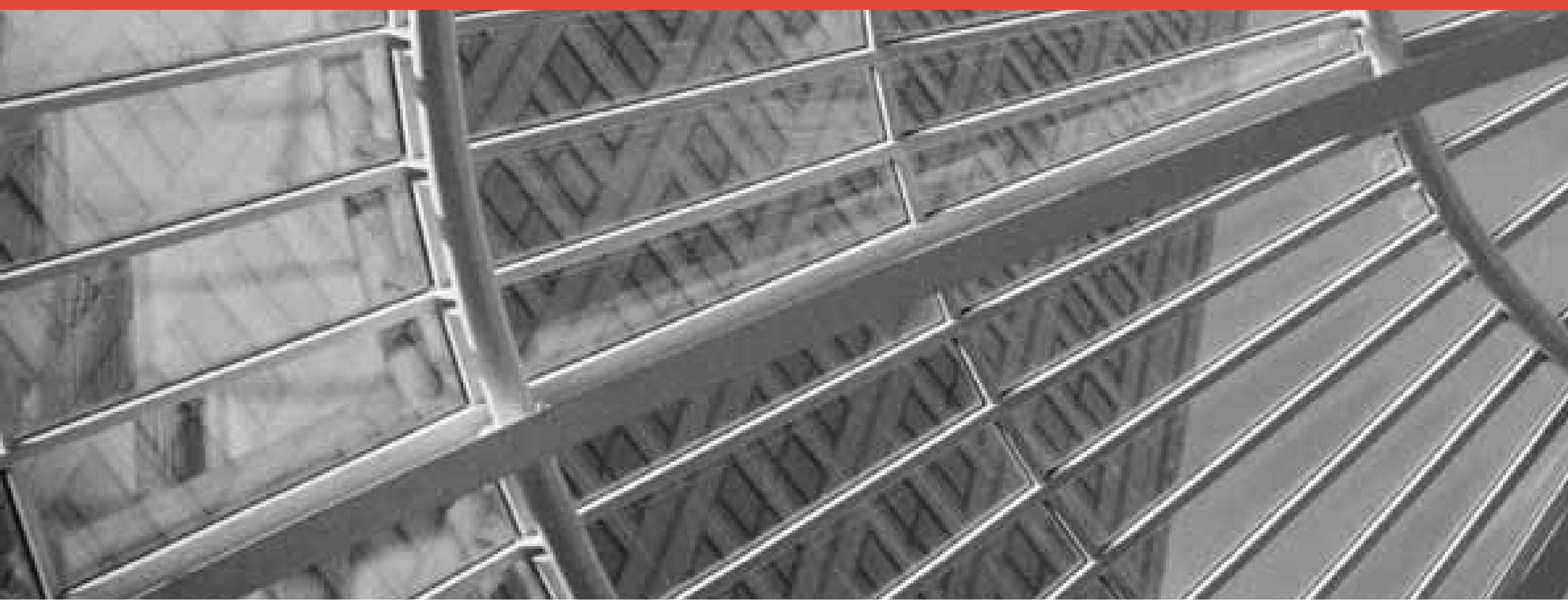
REPORT OF THE DISCUSSIONS FROM THE FEE ROUNDTABLE SERIES
'ACCESS TO FINANCE FOR SMEs'



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This document reflects the outcome of debates held in expert roundtables organised by FEE, the Federation of European Accountants. It is a collection of views, discussion points and exchange of experience and best practices, some of which are inevitably marked by the state of affairs at the time of the discussion. The main objective is to share ideas and experience and stimulate further thinking. The content of this paper should therefore not be seen as an analysis or a series of recommendations, nor does it represent the views of the speakers or any of the organisations they are affiliated with or of FEE and its Members. With this publication, FEE hopes it may provide a useful contribution to what is a critical priority for Europe's economy: Small and Medium-sized Enterprises.

1. FOREWORD OF EUROPEAN COMMISSION VICE-PRESIDENT TAJANI

Europe's economic success depends on the growth of strong, dynamic and innovative SMEs. To deliver this growth, finance is crucial. However, SMEs still often face significant difficulties in accessing the range of financing they need.

The European Commission is therefore committed to improving access to finance for small businesses. To address the diverse financing needs of SMEs a balanced mix of flexible financial instruments is provided through Structural Funds, the Competitiveness and Innovation Framework Programme (CIP) and via lending from the European Investment Bank. Two new Commission proposals presented in November 2011 - the Programme for the Competitiveness of Enterprises and SMEs (COSME) and Horizon 2020 - will reinforce the guarantee and venture capital facilities for SMEs from 2014 onwards. Furthermore, the European Commission adopted in December 2011 an Action Plan to improve access to finance for SMEs.

But improving SMEs' access to finance is not only a question of enhancing the supply side. Many of the issues relate to the interaction between companies and financial institutions. We need to overcome the communication hurdles between SMEs and finance providers, as well as increase SMEs' financial knowledge. SMEs would benefit greatly from easier access to information at local level, giving them a better chance of finding appropriate finance. Accountants and banks, thanks to their close contacts with enterprises, have a key role to play here, providing clients with information about alternative financial instruments, including relevant EU programmes.

The Commission will continue to work within the SME Finance Forum to explore new strategies to facilitate access to finance for SMEs, since mutual policy development is essential to improve the performance of the European financial system. In this context, the work of the FEE roundtable meetings on access to finance is important. I encourage the establishment of national SME Finance Fora to provide practical solutions that improve access to finance.

I believe that SMEs deserve our wholehearted support at European level and am firmly committed to helping them access the finance they need to exploit their full potential as drivers of European growth and employment.

Vice-President of the
European Commission
Antonio Tajani

2. MESSAGE FROM THE FEE PRESIDENT

SMEs are the lifeblood of the EU economy. They are key to future growth and job creation across the continent. It is therefore only logical that SMEs are a top priority for FEE as they are for European policymakers.

Professional Accountants are in the field, helping entrepreneurs finance and manage their business, enhancing their trading partners' trust, expanding their operations, seizing the opportunities of the internal market, properly applying regulation and discharging their obligations. They have to innovate and solve the daily problems of SMEs across Europe. Based on the practical experience gained in this daily involvement in all aspects of the economy and the set of values underpinning the profession's practice, FEE believes it has a contribution to make to the public policy debate. This was a key driver of this Roundtable series on Access to Finance for SMEs organised by FEE.

With this initiative we have created an opportunity to identify, discuss and share innovative solutions to benefit SMEs and the broader economy. SMEs are continuously facing challenges in raising funds and there is a need to explore further some aspects of access to finance that are novel or under-represented in policy debates.

This document is an attempt to summarise the discussions held in this Roundtable series on SMEs' Access to Finance and further share the lessons learnt. It touches on many aspects including venture capital, "green" business, credit management, on-line peer-to-peer financing, factoring, leasing... Given the importance of SMEs to the economic recovery, FEE will continue to monitor developments as they unfold and promote action as necessary, specifically in the field of improving SMEs' financial knowledge.

A majority of the Members of FEE Member Bodies are Professional Accountants servicing SMEs: often they work in Small and Medium Sized Practices (SMPs) i.e. are SMEs themselves; others are "accountants in business" and work in medium sized enterprises for instance as CEOs, CFOs or in the finance or tax departments. These Professional Accountants are a prime source of advice, support and outsourcing particularly for this category of enterprise.

In the current difficult economic circumstances, the competences and experience that Professional Accountants contribute to SMEs is even more important. It is virtually impossible to manage a business of any size without proper financial information: good captains don't navigate without compass and instruments. Finance providers need to understand and assess their risk and can't lend or fund without appropriate information and assurance. Employees are legitimately interested in the financial health of their employers. Today's strained public finance will not recover without robust trade, fair and efficient taxation and effective tax collection. Considering accounting and auditing as mere administrative burdens is like recommending driving blindfolded on a road that is bumpier than ever.

FEE President
Philip Johnson

3. INTRODUCTION

It is recognised that Small and Medium-sized Entities (SMEs) play a vital role in the European economic recovery. Whilst economic activity remains relatively depressed in much of Europe, SMEs' demand for borrowing is also muted. This reflects the fact that most SME business owners need to place much more importance on the survival of their business and on being able to pay their staff and themselves than on business growth. However, as the economic upturn gathers pace, SMEs require access to finance of the right type and at an appropriate cost, to enable businesses to expand once again.

There is also recognition of the relevance of professional accounting services for SMEs. Even where relatively high audit thresholds have been established by national governments, there is still evidence that professional accountants serve as the main financial advisers for smaller businesses in Europe[1] as well as elsewhere in the world[2]. In smaller businesses, financial transactions are normally recorded by a book-keeper, and financial information for decision-making continues to be prepared, primarily, by the professional accountant. As the reporting information is often used by third parties, such as suppliers, tax authorities and providers of finance, including banks, the rigorous accounts compilation process adds to the reliability of the information produced.

FEE has, over the past year, organised a series of four Roundtables on Access to Finance for SMEs comprising high quality discussions between expert financiers, regulators, accountants, European Institutions and SMEs. The aim was to discuss the challenges that SMEs are facing in gaining access to external finance in many EU Member States and to identify possible solutions.

This paper summarises the discussions that have taken place. The first Roundtable considered recent developments in both the supply and demand by SMEs for various forms of external finance (including debt and equity), through the likely impact of the proposed Basel III regulations, the role of mutual or loan guarantee arrangements and an example of the practical steps that accountants can take to assist their clients where additional finance is required. The European Commission also talked about the policy options on which it was working to ensure that SMEs could continue to access the funds that they require.

The second Roundtable examined the challenges and some possible solutions in raising finance for green businesses, the importance of trade credit in ensuring that adequate liquidity is available to SMEs and the exciting and novel developments in the field of Peer to Peer finance.

The third Roundtable focussed on some of the challenges of financing at an early stage and technology businesses with presentations on the experiences of the very rapid growth new technology venture, the important role of business angels and angel networks, and revisiting the potential impact of Capital Requirements Directive (CRD IV) that implements Basel III.

The fourth Roundtable considered an Italian initiative involving professional accountants in reducing information asymmetry between small enterprises and their banks, the growing demand and provision of lease financing in Europe, the role of venture and enterprise capital in financing high growth businesses and a review of the first two years of operation of the Belgian Credit Mediator.

FEE is grateful to all of the speakers who contributed their expertise and knowledge to the events. The quality of the presentations has been excellent. The issues considered and the challenges faced are dynamic, substantive and complex. It would be over-optimistic to claim that solutions were found, but as it will be appreciated from reading the report, reservoirs of knowledge were revealed and explored. We hope that you enjoy reading this report as much as the participants benefited from the actual events!

4. REPORT: FIRST ROUNDTABLE: ACCESS TO FINANCE FOR SMEs AND THE ECONOMIC RECOVERY - CHALLENGES AND CREATIVE SOLUTIONS

As a result of the down-turn in economic activity, many SMEs have suffered losses and reductions in asset values, leading to declines in the value of guarantees that they can offer to lenders. There is also much debate on the possibility that, in seeking to promote the credit worthiness of banks, the situation for SMEs could be made even worse.

The dust has settled, but all is not well.

Two years after the collapse of Lehman Brothers, the European Central Bank's (ECB) research confirms that access to finance trails both demand and competition as a concern for Europe's SMEs.[3] Only 15% of SMEs cite it as their number one challenge, and for all their concerns small business organisations throughout Europe are no longer reporting a credit crunch.

While all of this is worth celebrating, the finance supply chain has not returned to normal. The gap between larger and smaller businesses' access to finance is widening, and SMEs' financing needs are growing faster. Smaller businesses are increasingly falling back on internal funds despite substantial loan approval rates; banks still generally see SMEs as riskier and thus require more information and collateral – in addition to levying higher fees.

Nor is this all just a matter of perceptions. The ECB's data refers also to real-life experience. On this basis, the ECB does not expect conditions to improve materially in the short term. This low-supply, low-demand equilibrium may not be as acute a problem as the disruption of late 2008, but it nonetheless posed a genuine threat to the economic recovery in Europe, which SMEs report is already running out of steam.[4]

Learning from mediation

As evidence began to emerge in the past years of a breakdown in communication between lenders and SMEs[5], different forms of mediation services became available in many European countries, including Belgium, Germany, France and Italy. The most celebrated of these, the French mediation scheme, boasts an impressive 63% success rate[6] and is credited with improving access to finance by experts both in France and abroad.[7]

Two important lessons can be drawn from the experience of formal credit mediation:

First, mediation works best in an environment of disclosure where objective evaluation is possible and universally trusted.

Second, the true contribution of mediation may lie not in its effect on supply but in its ability to improve perceptions and limit the effects of discouraged demand.

Two important lessons can be drawn from the experience of formal credit mediation:

First, mediation works best in an environment of disclosure where objective evaluation is possible and universally trusted. The French mediator's high success rates are almost certainly linked to the fact that the Banque de France maintains rigorous credit ratings for a substantial share of the company population in that country. Importantly, banks are allowed by the state to use these in determining their capital requirements.[8]

Second, the true contribution of mediation may lie not in its effect on supply but in its ability to improve perceptions and limit the effects of discouraged demand. Despite receiving such wide acclaim, the French mediation service has only assisted a very small number of rejected loan applicants in the past years.[9]

Policymakers and the accounting profession also need to take note of these lessons. Lenders around the world confirm that accountants are *de facto* mediators between banks and small businesses.[10] A clear implication is that reporting and assurance to a widely accepted standard can make a difference to SMEs' access to finance. However, standards of reporting vary substantially among the Member States, and are often driven by the demands of tax authorities rather than the information needs of creditors and other providers of finance. In light of this, the accountancy profession's role should be as much to assist owners or managers of SMEs in enhancing the value of presenting accurate financial performance data as it is to liaise with lenders.

Policymakers and the accounting profession also need to take note of these lessons.

A clear implication is that reporting and assurance to a widely accepted standard can make a difference to SMEs' access to finance.

This obligation extends not only to accountants in audit firms but also to professional accountants working in enterprises. With most of the remaining market imperfections focused on the supply of working capital, SMEs' in-house finance staff can provide insights to creditors that an external accountant cannot.

Building on guarantees

Credit guarantee schemes for small businesses were a significant and successful element of the European response to the downturn of 2008-9.[11] Countries with a robust tradition of mutual guarantees were able to avoid serious instances of market failure while those that were embracing this approach could see substantial benefits in the future as trust in the system was being established.

Acknowledging options beyond bank loans is crucial for the formulation of sound policies.

Acknowledging options beyond bank loans is crucial for the formulation of sound policies. As a permanent feature of the market for small business loans, well-designed systems of mutual guarantees are arguably superior to grants and subsidies for SMEs. They can leverage substantial funds (providing 5x to 10x leverage)[12] at a low cost while achieving modest default rates, yielding substantial additionality and limiting market distortions.[13] A significant body of evidence already exists to guide policymakers. It suggests that more centralised schemes with a small number of lenders focusing on broad coverage and high volumes can be very successful, provided that procedures and responsibilities are clearly defined and proper co-operative relations are developed between lenders, guarantors and borrowers.[14]

Warming to equity

In the aftermath of the financial crisis of 2008 and the sovereign debt turmoil of 2010, Europe's economies are moving away from debt as a source of finance at all levels. The ECB data show that SMEs have led this shift by deleveraging substantially.[15] Growing businesses need substantial amounts of finance and not all of this can be sourced internally. As a result, policymakers' attention has correctly shifted to equity finance, and how access can be improved for SMEs.

Currently, only about 2% of SMEs use this option, despite the fact that three times as many (6%) cite it as their preferred choice. Only just over one third (37%) of Europe's SMEs would feel confident pitching to potential equity investors.[16] Moreover, equity investment is strongly cyclical and flows of funding have fallen substantially in the recession.[17]

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Although external equity finance is only relevant to a small population of fast-growing businesses – perhaps 5%-10% of Europe's SMEs[18] – small amounts astutely invested can go a very long way, financing the rapid growth of Europe's most promising businesses. Yet there is a well-documented need for intervention in this market: the combination of high levels of risk and information asymmetry, as well as steep due diligence and compliance costs, results in a shortage of equity finance for businesses trying to raise less than €2m, which is only partly addressed by business angels and syndicates.[19] This is a substantial limitation as only 3% of those SMEs that would ideally like to use equity finance need more than €1m.[20]

Additional disincentives are provided by tax, which biases entrepreneurs in favour of debt finance, and of course by regulation. The Demarigny report,[21] for instance, demonstrated that the regulatory framework is partly responsible for the fact that the European small listings market is in secular decline and provides only a trickle of liquidity to small issuers. We welcome the European Commission's Action Plan for improving access to finance for SMEs that includes proposals for reducing reporting requirements for SME listings and increasing awareness of potential for access to public markets. These are complex issues in which cause and effect are not always straightforward to understand. It is hoped that the proposed changes will lead to some positive improvement. [22]

Basel III – The devil is in the detail

Basel III has not been designed for the small, community-based banks that provide much of the flow of credit to Europe's SMEs, and the crisis that prompted its creation was not the result of lending to small businesses.[23] As a result, Basel III has the potential to cause substantial collateral damage among SMEs and the decentralised structures (such as community banking) that have helped buttress the sector, while failing to address the problem of too-big-to-fail financial institutions.

In an impact assessment, the Bank of International Settlements (BIS) estimated that higher capital requirements will have a modest effect on economic growth, but has been unable to model their effect on lending to SMEs – something which it acknowledges as a risk to its estimates. Much will depend on the details of implementation but also on the responses of lenders, who may well be provided with perverse incentives. An example of this is the use of a target leverage ratio in establishing capital requirements – there is a strong possibility that this will incentivise banks to seek out higher returns at the expense of loans to SMEs.

> **"Most importantly, the higher cost of credit in the long run will be offset by important economic and social benefits accruing not only to SMEs but a wide range of stakeholders, including corporate and individual borrowers and creditors, governments, and the EU citizens in general…" Commission Impact Assessment, Impact on SMEs, page 54**

The BIS expects that the effect of Basel III on SMEs is likely to be disproportionate[24] and it is encouraging that the European Commission, whilst arguing the SMEs will not be disproportionately impacted[25], has committed to detailed monitoring of the impacts[26]. Transparency for SMEs would also be increased if banks were to make available to SMEs information about the risk classification of their facilities and loans under the Basel regulations.

Engaging proactively with policymakers

European SMEs' access to finance will continue to be a significant issue in the recovery. However, it will revert from being a question of business survival to one of business growth. In this new environment, business organisations and the accounting profession should engage more proactively with the EU institutions. It is very positive that the European Commission is firmly committed to the Access to Finance agenda as demonstrated by the permanent status given to the SME Finance Forum, the EU Action Plan: helping SMEs access more financial resources and the provisions of Horizon 2020.

Key take-away points

Accountants

- Accountants in business and in practice need to continue to support clients through the fund raising process, not only by liaising with providers of finance but also by providing expertise to owner-managers where appropriate.
- The profession is uniquely placed to provide unbiased mediation, by preparing reliable information on SMEs' trading performance and financial situation. Accountants help business owners to provide accurate accounts (combined with added assurance where necessary) as a means of reducing information asymmetries between businesses and banks, and so reducing the total cost of capital that comprises search, credit assessment and transaction costs, plus interest charges and the risk premium.
- Accountants can work with SMEs' clients to ensure that working capital management is as effective as possible, thus helping them to avoid becoming over-reliant on external finance.

Governments, Regulators and Central Banks

- Authorities at the national level have a role to play in promoting transparency in the credit markets for SMEs. In so doing they can help reduce information asymmetries between lenders and borrowers and lower transactions costs. Increasing the availability of information that is relevant to credit decisions and ensuring that it is prepared to widely accepted standards could make a substantial difference, as would banks informing SMEs about the allocation of their loans to the Basel risk classifications (E, B, D etc).
- Moreover, national authorities need to bear in mind that SMEs' financial reporting is driven to a great extent by their own tax regimes which may not be consistent with creditors' and stakeholders' needs.

EU Institutions

- The EU institutions should aim to facilitate the production and publication of accurate historic and prospective accounting data for SMEs so that it is easy for banks, other finance providers and credit rating mechanisms to obtain reliable information that can be easily interpreted.
- They should continue to promote carefully designed and implemented mutual guarantee schemes in Member States and seek ways to improve liquidity in the secondary market for SME-issued (and often government-backed) securities. Similarly, equity funding to SMEs through the European Investment Fund and ERDF (e.g. for regional venture capital funds) should be further explored in order to provide additional realistic options to smaller businesses. This may have to include a re-evaluation of regulations that unintentionally raise the costs or constrain the availability of funding for SMEs e.g. through second tier stock markets.
- The extent to which the Basel III proposals will affect smaller banks which are not the primary target of the Bank of International Settlements, and of course lending to SMEs needs to be carefully and continuously monitored.

5. REPORT: SECOND ROUNDTABLE: ACCESS TO FINANCE FOR SMEs - MORE INNOVATIVE SOLUTIONS

Three topics which were brought by the financial crisis of 2008-9 and its aftermath: the financing of green business, trade credit and the emerging industry of Peer to Peer (P2P) finance.

Financing Green Business

Policymakers' commitment to a shift away from fossil fuels is embedded in the European Commission's targets for 2020 and is a necessity if the effects of climate change are to be mitigated.[27]

However, a great deal of path-dependence is embedded in the way people in Europe live, work and do business. Change will require persistent efforts, not a few well-aimed initiatives, and financing a sustained, EU-wide shift requires that significant amounts of money are directed at promising but unproven technologies; once supply chain investment is considered, these amounts dwarf even the European Commission's current estimates.[28] Such business models are unlikely to be profitable or cash-positive from the outset, which means that substantial amounts of venture capital will be required for them to be thoroughly tested.

It is currently impossible for renewable energy to compete with "dirty" fuels on a cost per kWh basis without extensive subsidies, not all of which will necessarily be justified by the negative externalities involved in using "dirty" fuels.[29] Withdrawing the legacy subsidies attached to fossil fuels may have an equivalent effect. But perhaps just as important as the level of subsidy, is the consistency in its application: long-term investment of the type needed from both producers and, to some extent, consumers, will be difficult to sustain unless policy is consistent across a similar time horizon.[30]

Without secure profits or cashflow, the ability of innovative small companies and young industries with unproven concepts to attract funding will depend on early-stage finance by business angels and venture capitalists, including venture capital functions within large energy firms, and also to a significant extent on equity markets large and liquid enough to provide fair valuations. As venture capitalists increasingly seek more mature firms to invest in,[31] the role of educating entrepreneurs must inevitably fall to business advisers, including professional accountants.

Change will require persistent efforts, not a few well-aimed initiatives, and financing a sustained, EU-wide shift requires that significant amounts of money are directed at promising but unproven technologies; once supply chain investment is considered, these amounts dwarf even the European Commission's current estimates. Such business models are unlikely to be profitable or cash-positive from the outset, which means that substantial amounts of venture capital will be required for them to be thoroughly tested.

SMEs, which account for a great deal of the environmental impact of industry in Europe,[32] are likely to require sustained support if they are to do their part in promoting Green growth, from state-funded business support to direct incentives and regulatory reform initiatives. Policy should explicitly consider the possibility that, without some level of subsidy, specific technologies may not break even during the lifecycle of the typical SME.

For SMEs some of the opportunities presented by the shift to a Green economy might lie with the production of green energy: smart grids in particular may make this a viable proposition. However, even greater potential is presented by the management of energy consumption, from waste prevention to smart metering and behavioural cues.[33] SMEs' involvement in the Green economy will certainly be intellectual property (IP) intensive. Strengthening IP protection and, more importantly, awareness could make it easier for promising firms to attract funding, while timely and credible commitment to EU-wide standards where possible should also ensure fair valuations for such innovations.

All of this change is being attempted against the background of a substantial skills gap in occupations relevant to the cleantech and renewables industries.[34] The implication is that, unless funding to address this is explicitly tied to EU and Member State funding for infrastructure and subsidies, the return on these substantial investments is likely to be reduced.

Trade Credit and small business finance

The vast majority of business to business (B2B) transactions in Europe are made on credit, not cash.[35] This means that the most important source of short-term finance for SMEs are usually not banks but their suppliers; a finding which holds across nearly all developed and developing countries. When businesses wish or need to generate cash internally, they often end up paying their suppliers later than agreed or demanding discounts for prompt payment, especially if they have substantial bargaining power.

Some troubled businesses end up never paying at all. The resulting cascade of cashflow stress and late payments creates serious challenges for small suppliers and is responsible for a great deal of business mortality. Despite this, smaller businesses generally use credit as a marketing tool or an implicit guarantee of quality and may therefore fail to challenge late payers for fear of jeopardising valuable commercial relationships.[36]

The EU institutions are of course fully aware of how problematic late payment is for SMEs, as demonstrated in the recently enacted Late Payment Directive. However, the late payment problem is only the tip of the trade credit iceberg: this informal financial market can in some countries be twice as large as its banking equivalent. Despite the fact that trade credit was at least as acutely affected by the 2008-9 financial crisis as bank lending, and is generally vulnerable to systemic disruption, relatively little attention has been paid to trade credit as a source of finance to SMEs.

Trade credit interacts extensively with the formal banking sector. For example businesses may act as financial intermediaries by using banks' funds to extend credit to businesses that the banks themselves would not; businesses may be able to do this either because they are better informed or because they have more control over their customers than lenders do. Banks in turns take cues from trade creditors, preferring not to lend to businesses that suppliers refuse to extend credit to.[37]

This is generally prudent behaviour and suggests that the conduct of lenders cannot be judged without benchmarking it to that of trade creditors. However, it also leaves open the possibility that, when treated correctly, suppliers can help to finance credit constrained but sound and innovative businesses even in the presence of market imperfections in the banking sector.

The EU institutions are of course fully aware of how problematic late payment is for SMEs, as demonstrated in the recently enacted Late Payment Directive. However, the late payment problem is only the tip of the trade credit iceberg: this informal financial market can in some countries be twice as large as its banking equivalent. Despite the fact that trade credit was at least as acutely affected by the 2008-9 financial crisis as bank lending, and is generally vulnerable to systemic disruption, relatively little attention has been paid to trade credit as a source of finance to SMEs.

One implication of the commercial nature of trade credit is that external regulation is unlikely to have a direct effect on late payment or SMEs' working capital needs.

However, regulation can provide valuable tools (such as statutory interest) which can be used in order to build internal policies that support a sustainable flow of credit in and out of businesses. Only a comprehensive, proactive approach to credit management, coupled with easy access to credit information, can ensure that businesses, especially SMEs, provide credit to one another in a sustainable way[38]. As SMEs' advisers of choice on financial management, professional accountants have an important role to play in encouraging clients to adopt sustainable credit policies.

Peer to Peer (P2P) Finance

Since the near-failure of the banking system in 2008 and throughout its difficult recovery, the combination of low interest rates, rising risk-aversion among providers of finance, and resurgence in enterprise activity have provided a supportive environment for the incubation of a new system of financing businesses: online Peer to Peer (P2P) finance. As P2P funding typically comes directly from individuals, who provide loans to a diversified group of recipients, this type of funding promises to build a financial supply chain that is robust to the systemic risk seen in banking or elsewhere, and that could be more responsive to the non-financial values that resonate with EU citizens.

P2P business finance has been a natural extension of P2P lending for consumers, and has, in the past years, been able to duplicate many of the benefits traditionally associated with online disintermediation, by improving the economics of deposit taking and lending in favour of both investors and businesses, improving customer satisfaction and - most importantly - keeping default or failure rates low. As a result, P2P lending has achieved substantial growth despite not being covered by the formal government deposit guarantees associated with conventional bank deposits. For many Peer2Peer lenders, risk exposure is reduced through spreading loans across a large number of borrowers, a practice that is made possible by highly automated administrative systems that can allocate, document and monitor loan and repayment transactions at very low cost.

Already a wide range of financial products is available through online P2P platforms, including loans, equity investment and factoring, as well as products that blur the line between charitable or friendly giving and formal finance, such as crowdfunding.

This is important because a strong percentage of enterprise activity in Europe is driven by, and actively involves, the pursuit of social objectives – and will thus produce chiefly public benefits that do not accrue to the providers of capital.[39] For-profit credit provision still appears to be the dominant model, with non-profit funding and equity investment, in that order, slowly catching up.

Despite early successes, this industry is still in its infancy. The regulatory and policy framework surrounding it is far from harmonised across Member States, even though guidelines on microfinance exist that could potentially offer a template for common rules.[40] Crucially, the relationship between P2P finance and traditional banking, venture capital and charity sectors is still unclear, although there may be a commercial case for banks to incorporate P2P platforms in their business models. At the EU Institutions level, there is a need to take stock of best practices in encouraging and regulating this nascent industry, and Member States should consider whether there is room for tax incentives, already fairly established for informal equity financing, to be extended to P2P investing or P2P lending that does not attract a deposit guarantee.

At the EU Institutions level, there is a need to take stock of best practices in encouraging and regulating this nascent industry, and Member States should consider whether there is room for tax incentives.

The true potential of P2P finance to encourage enterprises and combat financial exclusion is still being explored. Social networks allow providers of finance to leverage an unprecedented volume and depth of personal information on entrepreneurs and company directors in order to perform due diligence. They also provide a new range of social controls similar to those implicated in the early success of microfinance initiatives which may help further reduce defaults or failure rates.[41] They even allow lenders to circumvent a bank's conventional divide between business and personal lending and thus achieve higher levels of information and security. These developments and their implications must be considered carefully by the industry, by regulators and by policymakers, so that the risks and benefits can be managed appropriately.

Key take-away points

"Financing of green business", "trade credit" and the emerging industry of "peer to peer (P2P) finance" lie at the interface between sustainable business practices and access to finance, and amongst their complexity the following themes emerge:

- Making SME finance more sustainable requires that policymakers think in the long-term. Consistent and persistently applied internal policies, external regulations, policy frameworks and subsidy schemes are therefore essential to ensure an adequate supply of sustainable finance.
- Sustainable SME finance involves a much wider range of stakeholders than the current agenda. It acknowledges positive and negative externalities and considers the importance of individual and commercial incentives and controls beyond considerations of risk and (financial) return for all involved.
- Good practice in informal SME finance cannot be mandated by regulation alone as it is a potential solution to a complex web of relationships – some collegial (e.g. P2P funding) and some commercial (trade credit within mutually satisfactory terms). Regulation should instead seek to provide tools for SMEs and other stakeholders to manage these relationships in order to smooth out imperfections in the formal and informal markets for finance and to address market failures.
- To improve the supply of SME finance, policymakers, finance providers and businesses must explore the use of types and sources of information that have so far remained underused, in order to improve due diligence and control.

6. REPORT: THIRD ROUNDTABLE: ACCESS TO FINANCE FOR SMEs - EARLY STAGE AND TECHNOLOGY BUSINESSES

In Europe and indeed around the world, a small minority of the businesses born each year tend to account for a disproportionately large share of job creation and value added – the top 4-5% fastest-growing firms in a given cohort may be responsible for as much as 40%-50% of jobs created.[42] Hence, given the limited resources available to policymakers, it is very compelling to prioritise support for high-growth firms in order to maximise return on investment. On the other hand, given their impressive performance, one might think that high-growth firms should have no problems accessing finance; this, however, is not always the case.

Funding high-growth firms: Whose job is it?

Growth firms take greater risks, are more likely to have a majority of their value tied up in intangible assets and their most profitable projects can remain cash-negative for some time before they start paying off. This generally means that debt will not always be a suitable means of financing their growth. In fact, Europe's high-growth SMEs are significantly (ca. 23%) *less* likely to obtain all of the bank lending that they apply for than other growing or even steady-state businesses. Yet more than 75% of high-growth SMEs still report that their preferred source of finance would be bank lending,[43] and EU SMEs in general use more bank finance than their counterparts in the US[44].

Apart from this strong preference for bank lending, high-growth firms finance themselves opportunistically, including through public funding or subsidies. In fact, one in nine high-growth SMEs (11.2%) use grants or subsidised loans, and there is evidence that young high-growth firms benefit significantly from such funding, especially if it is given selectively.[45] Unfortunately, other potentially suitable types of finance meet with much greater aversion.

Business angels: delivering on the promise of networks

Only a small minority of fast-growing EU SMEs (ca. 4%) use external equity finance, and only about 7% cite it as their preferred source of financing.[46] While raising external equity is neither an appropriate nor an efficient solution to most businesses' financing needs, it is potentially much better suited to high growth firms. In fact a good deal of the financing of high-growth SMEs already takes place through quasi-equity instruments such as directors' loans[47] which may, to some extent, be compensating for the incompleteness of the venture capital market. This is corroborated by the fact that high-growth firms are more likely than other SMEs in Europe to report that the types of funding they need are not available at any price.[48] Although high-growth and innovative firms are generally likely to need more funds than other SMEs, for amounts between €100,000 and €1m the difference in demand between high growth and other SMEs is greatest.[49]

Business angels are crucially important to filling the lower end of this gap, and yet Europe's business angel sector is still only one quarter of the size of its US counterpart – even though Europe's SME output is larger.[50] Still, the financial crisis has pushed more dealflow towards Europe's business angel networks not only through the retrenchment of other venture capitalists but also by raising awareness of non-bank sources of finance. Applications have doubled throughout Europe and angel network numbers are growing, although this is almost entirely due to significant progress in Eastern Europe.[51]

Business angels increasingly co-invest with other angels and with early stage funds in an effort to fill the equity gap in Europe.

EBAN Position Paper – June 2010

In such times it is very important to manage the expectations of entrepreneurs and policymakers. Although the targeted investment of business angels can go a very long way, angel networks only channel funds to about 1%-4% of all the businesses whose business plans they receive.[52] This ratio can only be improved in a sustainable way by either improving the calibre of applicants and plans submitted or investing in the skills of investors themselves. Even among Europe's high-growth SMEs, the majority of owners and managers say they would not be comfortable talking to equity investors,[53] Changing this will require that networks further engage the rest of the business support industry, both public and private.

One factor hampering such efforts is that there is currently no such thing as ”good practice” among angel networks. A shake-out appears to be very likely in this sector over the coming years, as many of the multitude of business angel networks are currently operating models that are simply unsustainable. Regardless of which network models survive this, it is already clear that angel networks generally have the potential to deliver value to angel investors and companies seeking investment alike[54] and thus supporting network growth and increasing professionalism should be a major agenda for policymakers, networks and the business support community. Other objectives of this shared agenda should be to ensure a steady flow of new investors (including more women), to avoid the need for external regulation, and to firmly establish angel investment as an asset class in its own right.

While investment by business angels makes an important contribution to Europe's economic dynamism, it is important to note that their strong bias towards the ICT (Information and Communication Technologies) sector[55] does not reflect the actual sector distribution of high-growth firms – which are not over-represented in ICT and are, if anything, over-represented in services.[56] Rather, it most likely reflects the interests and career paths of high-net-worth individuals, many of whom will have made a significant share of their fortunes in the days leading up to the dot-com bubble. Seen in this context, the gradual shift of angel funding towards the creative industries is worth both celebrating and supporting.

Investment readiness, coaching and mentoring

It is tempting to infer that the lack of easily accessible alternatives to bank lending could be forcing high-growth SMEs in Europe to make sub-optimal financing decisions. However, lack of awareness and investment-readiness may be even more significant barriers.[57]

Typically, equity investors respond to high quality business plans with significant personal input from the entrepreneurs, documented market Unique Selling Points (USPs), high growth potential, appropriate Intellectual Property Protection, realistic pre-money valuations and viable exit plans for investors. While some of these lie within the scope of traditional business support, significant investment in mentoring and capacity building among entrepreneurs and potential investors is necessary as well. Projects such as *Ready for Equity!*[58] have the potential to address such needs but they will need to work with professional advisers to expand their scope and reach.

Investment readiness schemes, however, are neither a quick fix nor a cheap one.[59] Building up the required expertise, reputation and administrative capacity is time consuming and expensive, and the costs cannot be borne by the end-user. The most successful programmes are those that engage in the (more costly) critical diagnostic and business support components and which provide connections to other business support programmes. It is these functions in particular that would benefit substantially from the input of professional advisers such as accountants.[60]

It is tempting to infer that the lack of easily accessible alternatives to bank lending could be forcing high-growth SMEs in Europe to make sub-optimal financing decisions. However, lack of awareness of alternative sources of funds (such as Business Angels) and lack of investment-readiness may be even more significant barriers.

Investing in Exit Routes

Both entrepreneurs and investors in high-growth firms are motivated by the prospect of successful exits. Since the publication of the Demarigny report[61] in early 2010, the EU institutions have considered quite rigorously how Europe's regulatory environment can become less daunting for would-be small issuers. That said, it is still the case that trade sales are a much more common exit route than Initial Public Offerings (IPOs), which are generally reserved only for the best performers. Trade sales also tend to be more common but also less successful in Europe than in the US.[62]

Therefore, improving support for business transfers needs to be at least as high a priority for both the public and private sectors as the more glamorous subject of small business IPOs. The accounting profession, in particular, has a role to play in advising SMEs on such transactions, including on the protection and valuation of intangible assets. It will also need to broaden its offering to include elements of stakeholder management as well as the ability to provide unbiased feedback to the entrepreneur.

Improving support for business transfers needs to be at least as high a priority for both the public and private sectors as the more glamorous subject of small business IPOs. The accounting profession, in particular, has a role to play in advising SMEs.

CRD IV: What price will fast-growth SMEs have to pay for stability?

International efforts to strengthen bank capital and liquidity requirements are a welcome response to the financial crisis of 2008-9 and the Capital Requirements Directive (CRD) IV package, Europe's contribution to this important initiative, is to be welcomed. However, in the impact assessment presented alongside the European Commission's proposals for the associated regulation,[63] it is said that the provisions of CRD IV will not hit SMEs disproportionately.

This view directly contradicts the findings of every other international organisation to examine the issue, including the Financial Stability Board's (FSB) Macroeconomic Assessment Group (MAG) itself.[64]

The European Commission's argument is that the effect on SMEs will not be disproportionate because:

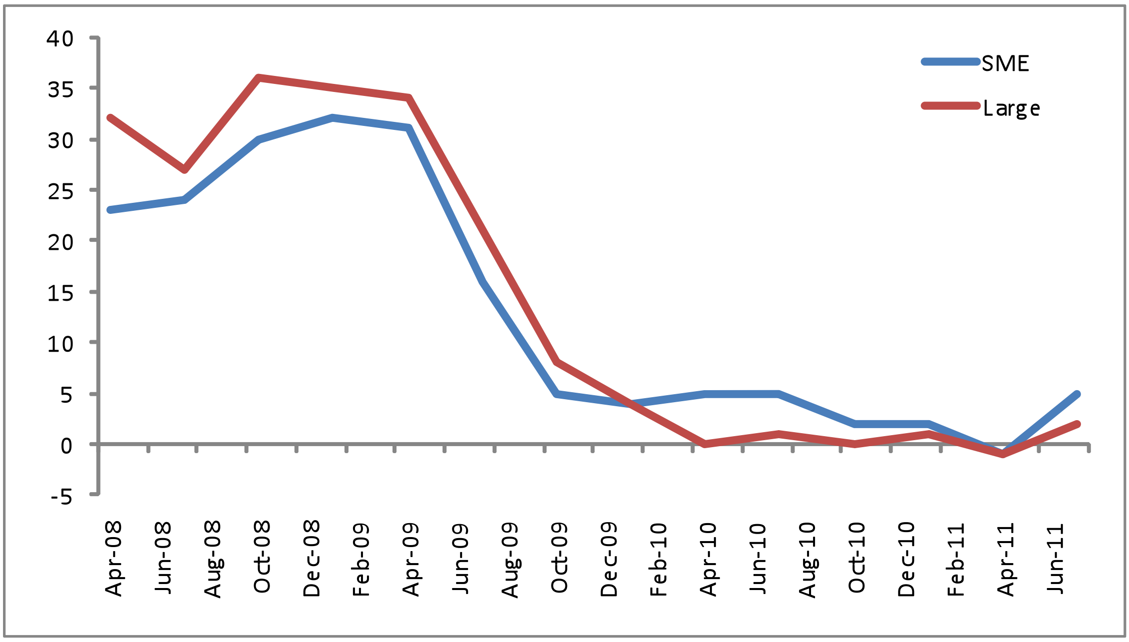
a) Evidence from the adjustment to higher capital requirements already underway among European banks suggests that large businesses have been affected to a greater extent than small ones.

b) SMEs transact mostly with smaller banks, which are better capitalised.

c) The benefits of financial stability are greater for SMEs than for large businesses.

Overall, it is best not to treat the brief period from Q4 2010 to Q1 2011 as indicative of future trends of small business lending. This period has been atypical in many ways and follows unprecedented levels of support from governments to both banks and SMEs, accompanied with significant political pressure on banks to increase lending. Nor does this period represent the amount of time during which banks have known about (and begun to prepare for) the likely provisions of Basel III – December 2009 would be a more appropriate benchmark.[65] Since that time but not before, and always according to the same data cited by the European Commission, European banks' margins on loans to SMEs not characterised as "risky" have consistently widened faster than those for large businesses (see Fig. 1).

Figure 1: Changes to European Banks' margins on less risky loans to enterprises, by size (diffusion index)[66]



It is important to note that low-growth, steady-state businesses, which form the majority of the SMEs population, especially after a recession, rarely face difficulties sourcing finance; it is faster-growing firms with strong financing needs that face more difficulties.[67] In the UK, for instance, 1% of the SMEs population (established, high growth, consistently profitable and cash-positive businesses) accounted for 13.4% of the demand for finance in 2007, but failed to obtain about 19% of the finance they sought.[68]

Another 10% of the population that had the same profile but exhibited steadier growth accounted for 44% of all demand and only failed to obtain 0.2% of the finance they sought.

While it is true that smaller banks tend to carry more SME loans as a percentage of their assets than large ones, it is not necessarily true that most SMEs, especially faster-growing ones, do business with small banks.[69] If anything, the behaviour of loan margins suggests that the bulk of the reaction to capital and liquidity requirements is so far coming from banks with significant bargaining power.

Moreover, smaller banks with less centralised decision making in less concentrated sectors are more likely to use rationing (including discouraged demand) as opposed to pricing strategies to manage their exposure to SME loans, so the effect of their more modest recapitalisation on overall lending volumes could be significant.[70]

In light of the evidence on the likely impact of CRD IV on lending to SMEs, we welcome the European Commission's decision to introduce a review clause on the preferential risk weight for exposures to SMEs under €1 million. However, what is needed is not an ad-hoc fix but a proper appreciation of the risk posed by small business loans. The implicit assumption in proposed capital ratios remains that loans to SMEs are about sixteen times as risky as government bonds – when a glance at any economic website or broadcast would tell otherwise.

Key take-away points

While regulators have a crucial role to play in mitigating the effects of CRD IV on lending to SMEs, there is also a significant role for the banking industry to play, or indeed both sides working together. Lenders can help lending to SMEs, especially fast-growing ones, recover much sooner by doing the following:[71]

- Improving risk and loan-loss provision models, data quality and internal reporting systems.
- Ensuring that demands for security are reasonable and take intangible assets properly into account; considering covenants as a complement or alternative to security where appropriate.
- Shifting more assets from trading into lending to the real economy.
- Making a point of attracting SME deposits as a more stable source of funding.
- Reviving the market for securitisation of state-guaranteed SME loans; even in 2006, it was estimated that only about 1%-2% of SME lending that could benefit from such a treatment was actually being securitised.[72] Even worse, about three quarters of all SME loan securitisation pre-crisis was taking place in Spain and Germany alone.[73]

7. REPORT: FOURTH ROUNDTABLE: ACCESS TO FINANCE FOR SMEs - FINANCING GROWTH, EQUIPMENT AND TRADE

This time, in contrast to the previous Roundtables when optimism about future prospects had been gradually improving, Autumn 2011 has seen a deterioration in economic prospects, making Access to Bank Finance for SMEs even more difficult.

Synergies between SMEs, Accountants and Banks

As trusted advisers accountants do much more for their SMEs clients than auditing or preparing accounts, they are frequently involved in advising smaller enterprises on the best ways to finance their businesses. As an example, the Italian accountancy profession has taken steps to formalise this relationship to the advantage of SMEs and also banks.

In Italy there are more than 4,5 million enterprises; of which 99.8% are SMEs that employ 81.7% of the workforce in the country and create 72.5% of GDP. The largest group of these are micro entities (less than 10 employees) representing 94.8% of all SMEs. It is well known that micro entities face particular difficulties in raising finance. In many cases, this may be because it is difficult to identify their business assets or distinguish them from personal assets; their annual accounts are not detailed, financial management is informal and unsophisticated, and for these reasons amongst others there is significant asymmetry of information between the enterprise and its stakeholders such as a bank.

In response, CNDCEC (the Italian Institute of Professional Accountants) has established formal agreements with Unioncamere (the Union of Business Registers) and ABI (the Italian Bankers Association). The objective of these agreements is to reduce the asymmetry of information between banks and enterprises; and to improve the quality of financial information both for enterprises and for their stakeholders. As a result, it is expected that the amount of finance available to SMEs will increase in response to greater completeness and transparency of the information produced. The potential for such improvements extends beyond Italy. In the UK, for example, lenders claim that all of the success to date of the newly-introduced loan appeals process is due to the increased supply of financial information.

In order to achieve these goals a list of approved accountants that are “expert” in financial analysis is prepared by the Chamber of Commerce. When requested, these expert accountants analyse the accounts and balance sheet of the enterprises and, when satisfied, provide a certificate of accuracy about the financial data. On receiving this certificate, banks have agreed to accelerate the process of making finance available to these businesses, thus saving time and reducing costs.

Expert accountants preparing a certificate must be independent of both the enterprise and the bank. This is a novel initiative designed to reduce the high levels of information asymmetry that are known to be a major cause of difficulty in relationships between banks and small, especially young enterprises. It will be very interesting to monitor the Italian experience.

Asset Finance

Leasing is the most popular form of asset finance for SMEs[74] and Leaseurope, the trade association representing the European leasing and automotive rental industries, has released a report on the use of leasing amongst European SMEs. The research was undertaken by Oxford Economics and is based on a survey of just under 3,000 SMEs across 9 industrial sectors in 8 countries (Germany, France, UK, Italy, Spain, Netherlands, Poland and Sweden). The research was conducted in July 2011.

> **Leasing provides the possibility to finance a significant proportion of the purchase price of an asset.**
>
> **Leasing also enables SMEs to use equipment without having to worry about considerations linked to ownership.**

Of the SMEs surveyed, 40% used leasing in 2010 and this figure was expected to increase to 43% in 2011. In 2010, 16.7% of total SME investment was financed by leasing, a figure which was expected to grow to 18.6% in 2011.

As might be expected, SMEs using lease finance had a greater need to acquire physical assets than those firms that did not use leasing. According to the report, European lessees invested 57% more in their businesses on average than non-users of leasing. Interestingly the popularity of leasing as a source of finance grows overtime, with a 25% take-up rate for SMEs less than 2 years old and a 50% for firms between 2 and 5 years old. This is probably because very young firms prefer to use their own resources,[75] if possible.

Amongst the reasons that leasing is popular with European SMEs is the fact that leasing provides the possibility to finance a significant proportion of the purchase price of an asset, often without having to offer supplementary guarantees or collateral. Lessees can also better manage their finances by spreading payments over the life of the asset. Leasing also enables SMEs to use equipment without having to worry about considerations linked to ownership, such as what will the second hand value of the asset be when it is no longer required?

> **Leasing is the most popular form of asset finance for SMEs.**

Interestingly, European SMEs access leasing through a range of distribution channels. The research shows that most SMEs use more than one channel. Vendor leasing is the most popular, with businesses facilitating the sale of its products by enabling potential buyers to obtain a leasing package covering much of the purchase cost. In 2010, 67% of SMEs used vendor leasing packages compared to 58% that accessed leasing through bank branches and 36% arranged their leases directly with leasing companies.

In future, under Basel III, financing SMEs through lease contracts is likely to be even more attractive to financial institutions. As a consequence obtaining assets through lease financing is likely to remain popular with European SMEs for the foreseeable future.

Venture and Enterprise Capital

The European Venture Capital Association (EVCA) estimates that there are 1,700 private equity firms active in the EU. These firms employ around 29,000 people who manage 4,200 active funds. In 2011 capital under management is estimated to be €524bn.

These funds provide two main types of finance to European SMEs: Venture capital, which is invested into young, entrepreneur-led, high-potential companies that are often driven by technological innovation; Enterprise capital, which is private equity investment[76] into more established businesses that want to internationalise, professionalise or further develop their products and services.

In total about 26,000 European companies have received venture and enterprise capital investment, and more than 22,000 of these are SMEs. Three quarters of the money invested is in early stage ventures and about one quarter are more established SMEs in receipt of “enterprise capital”. Early stage ventures typically receive smaller investments, on average €140,000. More established enterprise investments average €650,000 per investment.

The European Commission is adopting a regulation on Venture Capital Funds that should enable a true integration of the venture capital market in Europe and strengthen the supply of venture capital.

EU Action Plan: helping SMEs access more financial Resources, December 2011

Most venture capital houses funds raise investments from pension funds, insurance companies, family offices, private endowments and public sector agencies, such as the European Investment Fund. These sources can invest in businesses ventures through a variety of routes. The most common is to place their capital (usually through a limited partnership arrangement for a 10 year period) in the hands of a Venture Capital (VC) fund. However, alternative routes are to invest through a ”fund of funds” or to co-invest directly into companies, alongside a VC fund.

Under the limited partnership model, funds are committed for a fixed time usually through a ten-year limited partnership. The exact details of the investment agreement are negotiated between the VC fund proprietors (called General Partners) and the arms length providers of investment funds (called Limited Partners). The contractual arrangements associated with investments are designed to provide strong alignment of interest between the General Partners, the VC fund managers, the Limited Partners and, post investment, the management teams of investee businesses. Thus the VC General Partner and the VC Fund Investment staff receive a basic income plus a much more attractive performance based compensation package (called “carried interest”) that is strongly linked to achieving performance targets.

An alternative to investing directly into a Limited Partnership managed by a VC fund is for investors to place their money in “funds of funds”. This can be appropriate in some circumstances and offers the following advantages. Many pension funds need to allocate more capital in single investments than individual venture capital funds can cope with. Investing in funds of funds enables large pension funds to indirectly make investments into much smaller venture and enterprise capital funds. Investing through a fund of funds also provides diversification across a number of venture capital funds, thereby reducing exposure to risk. Funds of funds also provide “instant access” to venture capital funds without the provider of capital needing to have direct knowledge of the VC market.

Venture Capital investments in private businesses have to be sold in order to realise a capital gain that is eventually returned to the investors. These sales are known as “exits”. Typical exit routes can be listed through “IPOs” on the stock market if regulatory requirements and market conditions allow;[77] more commonly in recent times many growth companies are bought by larger corporations in transactions known as “trade sales”. More recently because of depressed stock market values and uncertain economic prospects the “secondary market” for VC investments has grown. In these circumstances companies are sold to other venture capital and enterprise capital funds. This can be attractive because venture and enterprise capital funds often specialise in certain stages of business development (e.g. early stage investments) and certain sizes of investment because no single investment should represent more than (say) 15% of their total funds under management. However, it remains to be seen just how successful “secondary” investment transactions will prove to be for both the private equity buyers and sellers of the businesses.

In Europe there are some significant barriers to growth in the amount of venture and enterprise capital available to ambitious businesses. There are relatively few long-term investors with skills and interest in innovation & entrepreneurship (e.g. university endowments, foundations and family offices). For example there are only 2, 500 family offices in the EU, and 11, 000 in the US. There is a similar ratio in respect to pension funds and university endowments.

In their efforts to minimise systemic risk, European regulators are working on a range of proposals including Capital Adequacy Requirements (Solvency II) for insurance companies; the Institutions for Occupational Retirement Provision (IORP) Directive Review – the potential reproduction of Solvency II for IORPs; CRD IV for Banks (BASEL III); and the Alternative Investment Fund Managers Directive (AIFMD). All of these could influence the flow of funds into venture and enterprise capital in either a positive or negative way. It is to be hoped that the outcome of these developments will, like Horizon 2020,[78] be beneficial for the industry and will not further reduce the supply of funding or adversely affect the investment processes associated with uncovering and investing in European SMEs with significant growth potential.

Evidence to date is that the European Commission and the European Securities Market Association (ESMA) are making significant progress, but coping with regulatory uncertainty remains a challenge. The bigger picture is that in order to smooth out economic cycles Venture and Enterprise Capital must be enabled to act as a counter-cyclical force, investing most when human capital is relatively readily available and physical asset prices are comparatively low, thereby stimulating additional economic activity. However, even in the absence of regulatory constraints, the reality is that in the next few years Europe is most likely to experience a reduced supply of available venture capital. This will lead to overall lower levels of economic activity but, perversely, higher investment returns to the holders of scarce equity capital resources!

Credit mediation

Many small companies are unable to access bank credit and this is actually in their interest, as well as their banks! The role of the credit mediator is, therefore to intervene when asked but only when there is a high quality loan application either from a new business or in respect of renewal of an existing facility.

Two years of experience have led to the conclusion that communication (or lack of it!) is at the heart of many of the situations in which credit worthy SMEs have been unsuccessful in obtaining or renewing their bank facility. Challenges for the banks have centred around whether all the possible types of funding that might be made available have been fully considered. Has adequate time been made available to consider the financing request and to allow proper communication between the SME and the bank manager? Finally, how considerate has the bank's response been to the SME, for example has enough information been provided to fully explain the bank's decision in the case of a credit refusal? Where businesses do not understand the reason for the bank's decision they cannot respond constructively to the situation.

From the SMEs' perspective, the important challenges have typically been firstly, and mirroring the position of the bank, whether all appropriate financial instruments have been considered. For example if, as noted above, a supplier of lightweight trucks sells these with an associated financing package that will reflect the cost of finance and risks associated with exactly this type of asset, it is probably inappropriate to seek to finance this purchase through the local branch of a bank unless it too has a specialist product targeted at this type of transaction. Secondly, the question of how much effort has the business invested in convincing the bank that the funding requested is for a sound business proposition that will lead to full repayment. Much harsher economic prospects mean that SMEs need to really convince the banks about their plans.

For business plans to be successful good opportunities must be married with highly competent and motivated owner-managers pursuing appropriate business strategies.

Finally, not all business owners display the level of commitment to their business ideas that will be necessary to be successful in the current challenging economic environment. In such circumstances, raising additional finance is probably not a wise course of action. For business plans to be successful, good opportunities must be married with highly competent and motivated owner-managers pursuing appropriate business strategies.

In markets characterised by asymmetric information, there may be an important role for an independent mediation between banks and SMEs. Mediation is needed to resolve situations in which a potentially credit worthy business does not receive the bank support that is needed. The major challenges identified are indeed “information asymmetries” where one or more parties to the transaction do not have information that the other party has. Often this has been exacerbated by poor communication from either or both parties, i.e. a failure to pass the necessary information across. One even greater communication barrier exists. Very few SMEs are aware of the services of the Credit Mediator and it is likely, therefore, that the observations made above represent only the tip of the iceberg.

Key take-away points

- The Italian initiative, taken by the accountancy profession (CNDCEC) and the Italian Bankers Association supported by the Union of Business Registers is a novel approach to reducing information asymmetries between banks and SMEs.
- Leasing is an important and flexible source of asset finance for SMEs. The ownership rights of lessors provide advantages in the provision of finance through leasing that arms lengths lenders and investors do not enjoy. Consequently, lease finance can be made available more often and at lower overall cost than many other sources of finance. In addition, initiatives such as vendor financing where an asset can be obtained by an SME alongside the necessary lease finance package, make this a very attractive source of funds for SMEs. Leasing is already a popular source of finance for many businesses and the new Basel III regulations are likely to result in a continued increase in the supply of lease financing made available to SMEs over the next few years.
- In markets characterised by asymmetric information, there may be an important role for an independent mediation between banks and SMEs. The major challenges identified are indeed “information asymmetries” where one or more parties to the transaction do not have information that the other party has. Accountants have an important role to play by providing advice on the range of financial instruments available to their SMEs clients (the number one source of difficulty in the cases reviewed by the Credit Mediator) and in presenting the SME’s requests for funding in a complete and professional manner (the second most common source of difficulty). However, one even greater communication barrier exists. Very few SMEs are aware of the services of the Credit Mediator. In countries where independent credit mediators exist, accountants may also have a role in disseminating this information to their clients.

Improving access to a wider range of SME finance requires substantial re-education for entrepreneurs and business owners, and a robust advice and business support offering. While governments and the EU institutions have their role to play, trusted advisers such as accountants need to live up to their responsibilities too.

8. THANK YOU NOTE FROM THE FEE CEO

SMEs and SMPs have long been a strategic priority for FEE that has performed significant work specifically aimed at benefiting this essential part of its constituency for instance, on matters such as SMEs accounting and financial reporting, on audit, alternative assurance and the implementation and proportionality of International Standards on Auditing (ISAs), sustainability, professional ethics or taxation.

To enhance even more our contribution in this field, we have decided to integrate the SME-SMP dimension into all areas of our activities so that the specificities and concerns of what is in reality the vast majority of Europe's economy lies at the heart of everything we do. To this end, FEE has created a task force that ensures such integration is effective and monitors that SMPs issues are duly considered and addressed.

In addition, in the midst of the crisis, this task force felt the need to launch a specific initiative to inform and stimulate the policy debate on SMEs' access to finance. This has produced a series of most fruitful discussions thanks to the genuine approach developed by the task force enabling a select group of stakeholders to exchange views, share best practices and brainstorm on innovative solutions.

Thanks to the energy and commitment of the task force's chair, Prof. Francis Chittenden, and the support he received from all the members of the task force and from Mr. Emmanouil Schizas, the benefits of this project can now be shared amongst a broader community.

This paper is unfortunately only a partial reflection of what has been discussed. It should also be seen as a report of debates that took place at a particular point in time in a period where developments in the economic, social, technological and regulatory environments are extremely rapid. The views in this paper were expressed by various stakeholders during group discussions and they should not be seen as the position of any organisation the different participants were identified with or a position of FEE or any of its Member Bodies. This paper has simply the same objective of the series of roundtables: stimulating the debate. We hope it may be of help to SMEs, SMPs and policymakers.

FEE would like to express its keen gratitude to all the speakers and stakeholders who have participated to these roundtables and engaged wholeheartedly in debating with us.

FEE CEO
Olivier Boutellis-Taft

9. SPEAKERS LIST

- **Dr Judith Ay**, Senior Adviser for Economic Affairs, European Savings Banks Group (ESBG)
- **Erik Berggren**, Senior Adviser, BUSINESSEUROPE
- **Dr Giorgia Butturi**, Professional accountant and auditor, Studio Butturi, Italy (member FEE SMP Task Force)
- **Jean-Christophe Capelli**, CEO, FriendsClear, France
- **George Cocu**, CFO, SC Gaz Sud SA, Romania
- **Chris Dauw**, The Belgian Credit Mediator
- **Veronique Genre**, Senior Economist, European Central Bank
- **Edit Herczog**, Member of the European Parliament
- **Dörte Höppner**, Secretary General, European Private Equity and Venture Capital Association (EVCA)
- **Gerhard Huemer**, Director Economic Policy, European Association of Craft, Small and Medium-Sized Enterprises (UEAPME)
- **Jacqueline Mills**, Senior Adviser, Leaseurope
- **Claire Munck**, Managing Director, European Trade Association for Business Angels, Seed Funds, and other Early Stage Market Players (EBAN)
- **Dr Salima Paul**, Senior Lecturer, University of West of England, Bristol, UK
- **Andrew Petry**, Partner, City law firm Addleshaw Goddard LLP and Head of Energy & Infrastructure Finance, UK
- **Monica Stefan**, FCCA, Audit Partner, SOTER & PARTNERS, Romania
- **Bart Van Coppenolle**, Founder & CEO, Right Brain Interface, Belgium
- **Dr Vesa Vanhanen**, Deputy Head of Unit, European Commission, DG Enterprise and Industry

10. END NOTES

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FURTHER INFORMATION

About the FEE SMP Task Force

Many accountants are active in Small or Medium-sized Practices (SMPs) and/or are servicing Small and Medium-sized Enterprises (SMEs) as their prime source of advice and outsourcing. A lot of accountancy firms are SMEs themselves.

The FEE SMP Task Force ensures that the views and interests of SMPs are integrated across all activities and working streams of FEE. It also actively takes up burning SME policy issues, e.g. by organising the series of FEE SME Access to Finance Round Tables.

Links

For the work of the FEE SMP Task Force, view.

For more information on the FEE Roundtables Series on Access to Finance for SMEs (including presentations and other documents), view.

FEE First Roundtable (video), view.

To learn more about FEE and about the accountancy profession in Europe, read the latest FEE Review downloadable from our website (www.fee.be).

About FEE

FEE (Fédération des Experts-comptables Européens – Federation of European Accountants) is an international non-profit organisation based in Brussels that represents 45 institutes of professional accountants and auditors from 33 European countries, including all of the 27 EU Member States.

FEE has a combined membership of more than 700.000 professional accountants, working in different capacities in public practice, small and big accountancy firms, businesses of all sizes, government and education, who all contribute to a more efficient, transparent and sustainable European economy.

Contact: Leyre Fuertes, FEE Project Manager

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ACCA 29 Lincoln's Inn Fields London WC2A 3EE United Kingdom / +44 (0)20 7059 5000 / www.accaglobal.com