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WORKING LANGUAGE

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Subject: State aid SA. 35247 (2012/N) – The Czech Republic
The Early-Stage Capital Aid Scheme of the Czech Development, Closed-End Investment Fund

Dear Sir,

1. PROCEDURE

(1) By letter dated 7 August 2012, registered by the Commission on the same day, the Czech authorities notified, in accordance with Article 108(3) of the Treaty on the Functioning of the European Union[1] (the "TFEU") the above-mentioned measure to be assessed on the basis of the Community guidelines on state aid to promote risk capital investments in small and medium-sized enterprises[2] (the "Risk Capital Guidelines").

(2) The Commission asked for supplementary information by letter dated 3 October 2012 to which the Czech authorities replied on 14 November 2012. The Czech authorities provided additional information by letter dated 3 December 2012 and registered by the Commission on the same day.

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1 OJ C 115, 9.5.2008, p. 47.

2 OJ C 194, 18.8.2006, p. 2-22, as amended.

Vážený pan
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2. DESCRIPTION OF THE MEASURE

2.1. Objective of the measure

(3) The Czech authorities set up the public closed-end fund, i.e. the Czech Development, Closed-End Investment Fund ("*Český rozvojový, uzavřený investiční fond, a.s.*") (the "ČRUIF") to support the provision of risk capital to target enterprises.

(4) The Czech authorities informed the Commission that the ČRUIF will constitute an umbrella over two separate measures: (i) the Early-Stage Capital Aid Scheme of the Czech Development, Closed-End Investment Fund, subject to the present decision, and (ii) the Expansion Capital Non-Aid Scheme of the Czech Development, Closed-end Investment Fund, a non-aid measure notified to the Commission and subject to a separate Commission procedure[3].

(5) The Early-Stage Capital Aid Scheme of the Czech Development, Closed-End Investment Fund (the "Measure") will enable investments of ČRUIF into target enterprises together with matching private co-investments. The present decision concerns exclusively this Measure.

2.2. Granting authority, legal basis, duration, budget of the Measure

2.2.1. Granting authority

(6) The granting authority is the Ministry of Industry and Trade (*Ministerstvo průmyslu a obchodu*), Section of EU Funds, Na Františku 32, 110 15 Praha 1, Czech Republic.

2.2.2. Legal basis

(7) The legal bases of the Measure are: Act No. 218/2000 Coll., on budgetary rules; Act No. 219/2000 Coll., on property of the Czech Republic and on its acting as a legal entity and; Act No. 189/2004 Coll., on collective investment.

(8) Moreover, considering that the Measure will be partially financed from funds made available by the European Regional Development Fund (the "ERDF"), the Measure will be governed in accordance with the applicable Structural Funds Regulations[4], and in particular with the Operational Programme Enterprise and Innovation, area of intervention 1.2.

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3 State aid case S.A. 35246 (2012/N).

4 I.e.: Council Regulation (EC) No 1083/2006 of 11 July 2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1260/1999, OJ L 210, 31.7.2006, p. 25-78, as amended; Regulation (EC) No 1080/2006 of the European Parliament and of the Council of 5 July 2006 on the European Regional Development Fund and repealing Regulation (EC) No 1783/1999, OJ L 210, 31.7.2006, p. 1-11; and Commission Regulation (EC) No 1828/2006 of 8 December 2006 setting out rules for the implementation of Council Regulation (EC) No 1083/2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and of Regulation (EC) No 1080/2006 of the European Parliament and of the Council on the European Regional Development Fund, OJ L 371, 27.12.2006, p.1-163.

2.2.3. Duration

(9) The duration of the Measure is twelve years, i.e. the ČRUIF will remain operational until 31 December 2024, subject to the condition that the investment period of the ČRUIF concerning the budget stipulated in this decision will last until 31 December 2015[5]. Subsequently, until 31 December 2018, the ČRUIF will continue to invest the capital returned from the initial investments made under the Measure following the same conditions. The Measure will be put into effect on 1 December 2012 or on the date of the Commission's decision authorising it, whichever comes later.

(10) According to the Czech authorities, this timeframe will allow achieving the objective of the Measure by providing investors with a sufficiently long investment horizon to the benefit of the target enterprises. The capital shall be provided to the target enterprises for up to eight years in order to ensure enough time for the assisted projects to develop. Therefore, at the ČRUIF level, the timeframe of twelve years should enable to successfully implement the whole Measure.

2.2.4. Budget

(11) The overall budget of the ČRUIF concerning the investment period of the Measure is CZK 900 million (EUR 31.8 million[6]) out of which 85 % (i.e. EUR 27 million) shall be financed by the ERDF.

2.3. The structure of the Measure

(12) According to the Czech authorities, the ČRUIF will be established as a joint stock company in the form of a qualified investors' fund pursuant to the national legislation on collective investment[7]. The ČRUIF shall be 100 % owned by the Czech Republic. The ownership rights shall be executed by the Ministry of Industry and Trade.

(13) The ČRUIF will serve as a special purpose vehicle for the transfer of financing to the target enterprises; it shall not pursue any other activities besides investing into target enterprises. According to information provided, the Early Stage Capital Scheme subject to the present decision and the Expansion Capital Non-Aid Scheme subject to a separate Commission procedure (see recital **(4))** will constitute two separate blocs of financing based on separate systems of accounts[8] in order to exclude any cross-subsidisation.

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5 In accordance with article 56 (1) of the Council Regulation (EC) No 1083/2006 of 11 July 2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1260/1999, OJ L 210, 31.7.2006, p. 25-78, as amended.

6 Exchange rate of 9 November 2012; 1 EUR = 25.055 CZK.

7 Act No. 189/2004 Coll., on collective investment, as amended.

8 The Czech authorities confirmed that the ČRUIF will maintain separate accounts for activities covering the early stage investments and for expansion stage investments, all costs, fees and revenues of these activities will be correctly assigned or allocated on the basis of consistently applied and objectively justifiable cost accounting principles, as well as in accordance with the requirements of the Council Regulation (EC) No 1083/2006 of 11 July 2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1260/1999, OJ L 210, 31.7.2006, p. 25-78, as amended.

(14) All business activities of the ČRUIF shall be managed by an independent professional investment company (the "ČRUIF Manager"). The role of the ČRUIF Manager will be notably the identification and due diligence of possible investment opportunities for the ČRUIF.

(15) The ČRUIF Manager will be also responsible for finding appropriate private investors which will co-invest together with the ČRUIF directly into the target enterprises. The private investors shall ensure at least 30 % capital for each individual investment. The ČRUIF Manager shall select private investors based on market principles, due to the fund's objectives, respecting sound financial management principles and with due diligence.

(16) According to information provided by the Czech authorities, due to the current stage of the development of the Czech risk capital market, direct investments at the level of target enterprises shall be considered as the most effective way to attract private capital. The Czech authorities underlined as well that due to the extent and features of the identified market failure concerning the provision of the early stage capital in the Czech Republic, it is necessary to provide the potential private co-investors with an additional incentive that would motivate them to contribute private capital into the target enterprises. This additional incentive will be provided to the private investors in the form of a call option. The call option shall not be embodied automatically in the investment contracts with the private investors, but only in case where the private investors' would not otherwise be willing to participate in the investment.

(17) The private investors will have the possibility to acquire the call option for the shares of a target enterprise owned by the ČRUIF. The private investor will be able to execute the call option between the second and the fifth year of an investment for a pre-agreed price (strike price). Moreover, upon the exit from the target company, the private investor will be obliged to pay to the ČRUIF a share on exit revenues. According to the Czech authorities, the sooner the private investor exits the target enterprise, the higher the ČRUIF's share on private investor's exit revenues will be and vice versa.

(18) According to the Czech authorities, if the given investment into the target enterprise is successful and brings revenues upon exit, it is not excluded that the private investor exercising the call option will generate a profit higher than the one which would normally be an equivalent to his/hers original share in the investment. This would constitute an additional advantage to him/her.

(19) If the given investment into the target enterprise is not successful, the private investor will not receive any preferential treatment and will bear together with the ČRUIF the full loss adequate to their respective investment share.

(20) If the call option described above is not exercised by the private investor, both the private investor and the ČRUIF will share exactly the same upside and downside risks and rewards in accordance with the *pari passu* principle.

(21) The private investors shall be completely independent from the target enterprises as well as from the ČRUIF Manager.

(22) According to information provided by the Czech authorities, in case of a lack of private investors, the ČRUIF will be allowed to provide early-stage capital (mainly seed) in accordance with the requirements of the Commission Regulation (EC) No 1998/2006 of

15 December 2006 on the application of Articles 87 and 88 of the Treaty to *de minimis* aid[9].

2.3.5. Investment structure

(23) The total maximum size of an investment tranche per target enterprise shall not exceed EUR 2.5 million over a period of twelve months.

(24) Under the Measure, at least 70 % of financing will be provided in the form of equity or quasi-equity. According to the Czech authorities, equity financing shall be provided to the target enterprises as contributions to their registered capital, by a share premium (aggio)[10] or by additional contributions to equity outside their registered capital[11], as the case might be. The share premium and additional contributions shall be provided to the target enterprise only if an investor already provided a contribution to the registered capital of the target enterprise. The share premium and additional contributions do not affect the given investor's share in the target enterprise's registered capital. Quasi-equity shall be understood as any instrument the profits of which are dependent on the success of the target enterprise and which do not have rights to secure assets in case of default. According to the Czech authorities, quasi-equity shall be provided under the Measure in the form of unsecured loans, subordinated to the other debts of the target enterprise, the repayment of which will be dependent on the economic results of the target enterprise.

(25) According to the Czech authorities, the debt component of the investments, if any, shall be provided during the advanced project stages and based on the target enterprise's needs. The target enterprise may obtain a debt (non-equity financing) in the amount not exceeding 30 % of the overall project budget. The debt instruments shall be provided under market conditions.

(26) According to the information provided by the Czech authorities, the investments made under the Measure exclude replacement capital and buy-outs.

2.3.6. Target enterprises

(27) The Measure is aimed at early stage small and medium-sized enterprises (SMEs), falling within the EU SME-definition[12] and which carry out their activities in the regions assisted by the Convergence objective of the ERDF in the Czech Republic. This covers

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9 OJ L 379, 28.12.2006, p. 5-10.

10 The share premium (or capital surplus) is the difference between the amount paid by investors for a share and its nominal value. In a balance sheet, share premium forms part of shareholder's equity. Share premium applies only for newly issued shares.

11 The additional contribution to equity outside the registered capital is another form of contributing to the shareholder's equity in the balance sheet. In accordance with Section 121 of the Czech Commercial Code, the articles of partnership may entitle the Annual General Meeting to enjoin the partners to contribute to the shareholder's equity up to 50 % of the value of the registered capital of each partner. The additional contribution to the equity outside the registered capital is an additional payment of the investor to the company which does not affect the amount of investor's ownership interest. The additional contribution may be, however, returned to the investor only in the extent in which it exceeds the loss of the company.

12 The beneficiaries are enterprises qualifying as SMEs within the meaning of the Commission Regulation (EC) No 800/2008 of 6 August 2008 declaring certain categories of aid compatible with the common market in application of Articles 87 and 88 of the Treaty (General Block Exemption Regulation); OJ L 214, 9.8.2008, p.3 and the applicable Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises; OJ L 124, 20.5.2003, p. 36-41.

all NUTS 2 regions in the Czech Republic, with the exception of Prague, i.e. the assisted areas as defined in the Czech Regional Aid Map 2007-2013[13] or in any other document which shall replace it in the future.

(28) The qualifying SMEs must be unquoted, i.e. they must not be listed on the official list of a stock exchange or on an unlisted securities market of a stock exchange.

(29) Investments in enterprises in the shipbuilding[14], coal[15] and steel industry[16] are excluded. The Czech authorities confirmed that the investments under the Measure will not support export related activities and investments will not be contingent upon the use of domestic in preference to imported goods.

(30) The investments made under the Measure will observe the sectoral restrictions stemming from the applicable Structural Funds Regulations[17].

(31) Moreover, the Czech authorities excluded from the scope of the Measure agriculture and fishery sectors, aquaculture and forestry activities, including the manufacturing, processing and marketing of products specified in Annex I to the TFEU, as well as the synthetic fibres industry.

(32) For the avoidance of any doubt, the Czech authorities confirmed that the Measure excludes financing to medium-sized companies beyond their start-up stage located in non-assisted areas. This is in any event also ensured by the fact that all beneficiaries must be located in an assisted area. The Czech authorities confirmed that the definition of seed, start-up and expansion capital for the purposes of the Measure will be in accordance with the Commission's definition, as set out in Section 2.2 (e), (f) and (h) of the Risk Capital Guidelines, namely:

- Seed stage financing is financing provided to study, assess and develop an initial concept, preceding the start-up phase.

- Start-up capital is financing for product development and initial marketing, i. e. provided to companies which have not sold their products or services commercially and are not yet generating a profit.

- Expansion capital is financing provided for the growth and expansion of a company, which may or may not break even or trade profitably, for the purposes of

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13 The areas eligible are defined in the Czech Regional Aid Map 2007-2013, approved by the Commission decision N 510/2006; OJ C 280, 18.11.2006.

14 As defined in the Framework on State aid to Shipbuilding, OJ C 317, 30.12.2003 p. 11-14.

15 High, medium and low grade category A and B within the meaning of the internal codification system for coal laid down by the UN Economic Commission for Europe.

16 As defined in Annex I in the Guidelines on National Regional Aid for 2007-2013, OJ C 54, 4.3.2006, p. 13-45.

17 For the avoidance of doubt those restrictions concern in particular: illegal economic activities (i.e. any production, trade or other activity, which is illegal under the laws or regulations of the relevant home jurisdiction for such production, trade or activity; e.g. human cloning for reproduction purposes is considered an illegal economic activity); the production of and trade in tobacco, distilled alcoholic beverages and related products; production of and trade in weapons and ammunition; casinos and equivalent enterprises; life science sector restrictions. IT sector restrictions exclude any support for research, development or technical applications relating to electronic data programs or solutions, which aim specifically at supporting any type of activity mentioned above, pornography, or which are intended to enable to illegally enter into electronic data networks or download electronic data.

increasing production capacity, market or product development or the provision of additional working capital.

2.3.7. Profit-driven investments

(33) According to the information provided by the Czech authorities, the investments in SMEs under the Measure shall be made on commercial terms and with the aim of obtaining a profit upon exit. SMEs in financial difficulties within the meaning of the Community Guidelines on State aid for Rescuing and Restructuring Firms in Difficulty[18] are not eligible for investments under the Measure.

(34) The ČRUIF Manager as well as the private investors will make investment decisions based on the assessment of the each SME's business plan including details of the product, sales and profitability development and establishing the ex-ante viability of the project, taking into account, in particular, a clear and real exit strategy for each investment.

2.3.8. Commercial management

(35) The ČRUIF Manager shall be selected in an open, transparent and non-discriminatory public tender procedure published in the Official Journal of the European Union. The tender shall be organised in line with the national public procurement rules, i.e. pursuant to the Act No. 137/2006 Col. on public procurements, as amended.

(36) The remuneration of the ČRUIF Manager shall include a performance based component and shall fully reflect the current market remuneration in comparable situations. The total remuneration of the ČRUIF Manager shall include: a flat fee (% p.a. of average value of the ČRUIF equity in the respective year), a variable fee (% p.a. of average value of capital invested in target SMEs), and a success fee (calculated as % of the total ČRUIF profit at its closure). In case the capital value of the ČRUIF decreases by 20 % or more, the ČRUIF Manager will not have a right to obtain a variable fee. The remuneration of the ČRUIF Manager will be established during the tender procedure, as it constitutes one of the main selection criteria of the tender, next to the quality of the detailed investment strategy.

(37) The management agreement signed by the ČRUIF and the ČRUIF Manager will establish, in particular, the investment objectives, structure and timeline of the Measure as well as a performance-linked remuneration of the ČRUIF Manager.

(38) The necessary management costs (i.e. a flat fee and a variable fee) shall be set according to market practice and shall not exceed, on a yearly average, 3 % of the total capital invested in the ČRUIF[19].

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18 OJ C 244, 1.10.2004, p. 2

19 The management costs should be paid in accordance with the applicable Structural Funds Regulations; in particular following article 43 (4) b) of the Commission Regulation (EC) No 1828/2006 of 8 December 2006 setting out rules for the implementation of Council Regulation (EC) No 1083/2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and of Regulation (EC) No 1080/2006 of the European Parliament and of the Council on the European Regional Development Fund, OJ L 371, 27.12.2006, p. 1–163, as amended, and pursuant to the requirements of the Revised Guidance Note on Financial Engineering Instruments adopted by the Coordination Committee

(39) The Investment Committee shall be established as an advisory body of the ČRUIF Manager. The Investment Committee shall include three external financial market experts nominated by the ČRUIF Manager and two experts nominated by the Ministry of Industry and Trade. The ČRUIF Manager shall not be bound by the Investment Committee's opinions.

(40) As private and public capital meets at the target SMEs level and the ČRUIF Manager is not allowed to invest without a business decision of the private co-investor, the actual investment therefore requires in each case negotiations between the ČRUIF Manager and the private investors. Without a business decision of the private investor and its agreement, an investment into the target SME cannot be carried out.

(41) The ČRUIF Manager shall act with professional care, respecting the provisions of the Czech Act on collective investment and other relevant financial market regulations. In particular, the Czech National Bank will supervise the compliance of both the ČRUIF and the ČRUIF Manager with the financial market regulations.

(42) Furthermore, the ČRUIF shall be managed using the Revised Guidance Note on Financial Engineering Instruments adapted by the Coordination Committee of the Funds (COCOF) of the Directorate-General for Regional Policy of the Commission[20], which determines detailed best practice rules for managing financial engineering instruments assisted by the EU Structural Funds.

(43) The ČRUIF shall operate in accordance with European Venture Capital Association (EVCA) Code of Conduct.

2.4. Cumulation with other aid[21]

(44) The Czech authorities confirmed that aid under this Measure can be cumulated with other State aid, subject to the following provisions. If the capital provided to the target SMEs under the Measure is used to finance initial investment or other costs eligible for aid under other State aid rules, the relevant aid ceilings will be reduced by 50 % in general and by 20 % for target enterprises located in assisted areas during the first three years of the first risk capital investment and up to the total amount received. The aforementioned reduction, however, will not be applied to aid intensities provided for in the Framework for State aid for Research and Development[22] or any other successor framework or block exemption regulation in this field.

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of the Funds (COCOF). Therefore the management costs shall be financed by the ERDF only until 31 December 2015, proportionally to its contribution to the budget of the ČRUIF.

20 Adopted in accordance with article 44 of Council Regulation (EC) No 1083/2006 of 11 July 2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1260/1999, OJ L 210, 31.7.2006, p. 25-78, as amended.

21 Without prejudice to article 54 (5) of Council Regulation (EC) No 1083/2006 of 11 July 2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1260/1999, OJ L 210, 31.7.2006, p. 25-78, as amended.

22 OJ C 323, 30.12.2006, p. 1

2.5. Monitoring and reporting

(45) The Czech authorities have committed to comply with the monitoring and reporting provisions in section 7.1 of the Risk Capital Guidelines. Annual reports shall be submitted to the Commission containing information on the investments effected under the Measure, including a list of all the beneficiary enterprises, as well as a brief description of the activities.

(46) The Measure will not be applied before its full text has been published on the following websites: www.mpo.cz and www.mpo-oppi.cz. The Czech authorities undertook to maintain detailed records regarding the granting of aid under the Measure for at least 10 years.

3. ASSESSMENT

(47) The Commission has assessed the Measure in the light of Article 107(1) and (3) of the TFEU and, in particular, on the basis of the Risk Capital Guidelines, which clarify the application of the State aid rules of the TFEU in the field of risk capital measures targeting SMEs.

3.1. Existence of State aid

(48) According to Article 107(1) of the TFEU, any aid granted by a Member State or through state resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market. Thus, for a measure to constitute State aid within the meaning of that provision, the following four criteria must be present.

(49) Thus, in order for a risk capital measure to fall within the scope of Article 107(1) of the TFEU, four cumulative criteria must be met:

- the measure must involve the use of State resources;
- the measure must confer an advantage on an undertaking;
- this advantage must be selective in that it is limited to certain undertakings;
- the measure must be capable of distorting competition and affecting trade between Member States.

(50) In line with Section 3.2 of the Risk Capital Guidelines, the assessment of whether State aid is present in a risk capital measure is carried out on three different levels:

- at the level of the investors;
- at the level of the investment fund, investment vehicle and/or its manager;
- at the level of the enterprises in which the investment is made.

3.1.1. State aid to investors

(51) In accordance with point 3.2 of the Risk Capital Guidelines, where private investors make investments on terms more favourable than public investors, or than if they had undertaken such investments in the absence of the measure, then those private investors will be considered to receive an advantage. By contrast, the Commission will consider the investment to be effected *pari passu* between public and private investors, and thus not to constitute State aid, where public and private investors share exactly the same upside and downside risks and rewards and hold the same level of subordination, and normally where private independent investors provide at least 50 % of the funding.

(52) In the present case, the ČRUIF, a fund owned 100 % by the Czech Republic, shall made investments into the target SMEs using the public resources imputable to the State, see recital (**12**). The investments of the ČRUIF shall be made together with the private investors. The private investors shall provide at least 30 % of capital invested into target SMEs, see recital (**15**). Moreover, in case of private investors exercising their call options, it is not excluded that the private investor will actually generate a higher profit than that equivalent to their original share of the investment, see recital (**18**). Considering the above the private investors who invest into the target SMEs will receive an advantage. The private investors will not therefore be treated *pari passu* with the public investor (i.e. the ČRUIF). The Measure therefore provides for a selective advantage to certain investors through the State resources. Moreover it cannot be excluded that the private investors are engaged in activities which may affect trade between Member States.

(53) The Commission therefore considers that there is State aid within the meaning of Article 107(1) of the TFEU at the level of investors.

3.1.2. State aid to the Fund and /or the Fund Manager

(54) Pursuant to Section 3.2 of the Risk Capital Guidelines, the Commission tends to take the view that a fund is a vehicle for the transfer of aid to investors and/or enterprises in which the investment is made, rather than being an aid beneficiary itself. However, measures such as fiscal measures or other measures involving direct transfers in favour of an investment vehicle or an existing fund with numerous and diverse investors with the character of an independent enterprise may constitute aid, unless the investment is made on terms which would be acceptable to a normal economic operator in a market economy and therefore provides no advantage to the beneficiary.

(55) Furthermore, as stipulated in Section 3.2. of the Risk Capital Guidelines, aid to the fund's managers or the management company will be considered to be present if their remuneration does not fully reflect the current market remuneration in comparable situations. On the other hand, there is a presumption of no aid if the managers or management company are chosen through an open and transparent public tender procedure or if they do not receive any other advantage granted by the State.

(56) In the present case, the ČRUIF will exclusively make risk capital investments into target SMEs and for a limited period of time. It constitutes an intermediary vehicle managed by the ČRUIF Manager which shall be chosen on the basis of an open, transparent and non-discriminatory public tender procedure, i.e. through a competitive selection procedure. Finally, the remuneration of the ČRUIF Manager will include a performance based component; see recitals **(9), (13), (35), (36)** and **(37)**.

(57) The Commission therefore considers the ČRUIF as a vehicle for the transfer of aid to private investors and/or SMEs in which the investment is made and not a separate aid beneficiary. Since the ČRUIF Manager is selected through an open and transparent public tender procedure and his remuneration includes a performance based component and reflects the current market remuneration in comparable situations, the ČRUIF Manager does not receive any advantage granted by the State.

(58) The Commission therefore concludes that there is no State aid within the meaning of Article 107(1) TFEU at the level of the ČRUIF and/or the ČRUIF Manager.

3.1.3. State aid to enterprises in which investment is made

(59) Finally, according to Section 3.2 of the Risk Capital Guidelines, where aid is present at the level of the investors or the investment fund, the Commission will normally consider that it is at least partially passed on to the target enterprises and thus that it is also present at their level. This is the case even where investment decisions are being taken by the managers of the fund with a purely commercial logic.

(60) As stated above in recital (**52**), the Measure involves State resources. At the same time, the Measure facilitates the provision of risk capital to SMEs, which may otherwise not be available, or at least not to the same extent, in the absence of the Measure, see recital (**23**). The Measure therefore confers an advantage to the target SMEs. The Measure is selective as only certain qualifying SMEs are eligible for investments, see recital (**27**). The Measure therefore confers a selective advantage to the target SMEs which might distort or threaten to distort competition. Since it cannot be excluded that the target SMEs are active in intra-EU trade, an impact on competition and trade cannot be excluded either.

(61) The Commission therefore considers that there is State aid within the meaning of Article 107(1) of the TFEU at the level of SMEs in which investment is made.

3.1.4. Conclusion

(62) Under the Measure, the publicly owned fund, i.e. the ČRUIF, will make investments into the target SMEs using the public resources imputable to the State. Thus the Measure involves the State resources. Furthermore, the selective advantages granted through the State resources will be conferred to the private investors and the target SMEs respectively; see recitals (**53**) and (**61**). Finally, since it cannot be excluded that both the private investors and the target SMEs are active in intra-EU trade and compete with undertakings in other Member States, an impact on competition and trade cannot be excluded either.

(63) The Commission therefore considers that the Measure involves State aid within the meaning of Article 107(1) of the TFEU at the level of the private investors and the SMEs in which the investment is made.

3.2. *De minimis* aid

(64) Under the Measure, in case of a lack of private investors, the ČRUIF will be allowed to provide early-stage capital (mainly seed) in accordance with the requirements of the

Commission Regulation (EC) No 1998/2006 of 15 December 2006 on the application of Articles 87 and 88 of the Treaty to *de minimis* aid, see recital (**22**).

(65) The Commission concludes that *de minimis* financing under the Measure does not meet the criteria of Article 107(1) of the TFEU.

3.3. Lawfulness of the aid

(66) By notifying the measure before its implementation, the Czech authorities respected the obligations under Article 108(3) of the TFEU.

4. COMPATIBILITY ASSESSMENT

4.1. Criteria for assessing the compatibility of the Measure

(67) Since the Measure constitutes State aid at the level of the investors and the target SMEs, the Commission shall examine whether this aid is compatible with the internal market under Article 107(3) TFEU. The Risk Capital Guidelines are applicable to the case at hand, since the measure concerns the provision of risk capital to SMEs.

(68) State aid for the provision of risk capital must result in a net increase in the availability of risk capital to SMEs, in particular by leveraging investments by private investors. The risk of a lack of incentive effect means that some enterprises funded through publicly supported measures would have obtained finance on the same terms even in the absence of State aid. The need to provide incentives depends on the size of the market failure related to the different types of measures, beneficiaries and development stage of the SMEs. A risk capital measure is well designed if the aid is necessary in all its elements to create the incentives to provide equity to SMEs in their seed, start-up and early stages. State aid will be inefficient if it goes beyond what is needed to induce more risk capital provision.

(69) The Commission considers that the incentive effect, the necessity and proportionality of an aid measure required for compatibility under Article 107(3) of the TFEU have been substantiated where the conditions set out in Section 4.3 of the Risk Capital Guidelines are met.

4.1.1. Preliminary criteria for assessing the compatibility of the Measure

(70) Section 2 lays out the scope of application of the Risk Capital Guidelines. Section 2.1 requires the exclusion of aid to enterprises in the shipbuilding, coal and steel industry, and to enterprises in difficulty. Furthermore, the Risk Capital Guidelines do not apply to aid to export-related activities, namely aid directly linked to the quantities exported, to the establishment and operation of a distribution network or to other current expenditure linked to the export activity, as well as aid contingent upon the use of domestic in preference to imported goods.

(71) As indicated in recitals **(29)** and **(33)**, the Measure excludes aid to enterprises in the shipbuilding, coal and steel industry as well as to enterprises in difficulty and the requirements for eligible investments do not include any provision that the aid would be conditioned upon export activities of the targeted SMEs or their use of domestic in

preference to imported goods. Therefore, the Measure complies with Section 2.1 of the Risk Capital Guidelines.

(72) As indicated in recital **(26)**, investments made under the Measure exclude replacement capital and buy-outs. Given that replacement capital and buy-outs are excluded, the Measure complies with the definition of venture capital under point 2.2(i) of the RCG and private equity under point 2.2(b) of the Risk Capital Guidelines.

(73) As indicated in recital **(28)**, the Measure will provide risk capital to unquoted SMEs in their seed, start-up and expansion phase which complies with Section 2.1 of the Risk Capital Guidelines.

(74) The Commission will consider that the incentive effect, the necessity and proportionality of aid are present in a risk capital measure and that the overall balance is positive where all the conditions in section 4.3 of the Risk Capital Guidelines are met.

4.1.2. Maximum level of investment tranches

(75) According to Section 4.3.1 of the Risk Capital Guidelines, the risk capital measure must provide for tranches of finance, whether wholly or partly financed through State aid, not exceeding EUR 2.5 million per target SME over each period of twelve months.

(76) As indicated in recital **(23)**, the investment tranche per target SME under the Measure will not exceed EUR 2.5 million over a period of twelve months.

(77) The Measure therefore complies with Section 4.3.1 of the Risk Capital Guidelines.

4.1.3. Restriction to seed, start-up and expansion financing

(78) In line with Section 4.3.2 of the Risk Capital Guidelines, the risk capital measure must be restricted to provide financing up to the expansion stage for small enterprises, or for medium-sized enterprises located in assisted areas.

(79) As indicated in recitals **(27)** and **(32)**, the Measure is restricted to provide financing up to the expansion stage for small enterprises, or for medium-sized enterprises located in assisted areas. Seed, start-up and expansion capital are defined in line with the definition set forth in point 2.2 (e), (f) and (h) of the Risk Capital Guidelines, see recital **(32)**.

(80) The Measure therefore complies with Section 4.3.2 of the Risk Capital Guidelines.

4.1.4. Prevalence of equity and quasi-equity investment instruments

(81) Section 4.3.3 of the Risk Capital Guidelines requires that the risk capital measure must provide at least 70 % of its total budget in the form of equity and quasi-equity investment instruments into target SMEs. As regards the qualification of quasi-equity instruments, according to Section 4.3.3 of the Risk Capital Guidelines, the Commission will take into account the degree of risk in the target enterprise's venture borne by the investor, the potential losses borne by the investor, the predominance of profit-dependent remuneration versus fixed remuneration, and the level of subordination of the investor in the event of the enterprise's bankruptcy.

(82) The Czech authorities confirmed that at least 70 % of the investments made under the Measure will be in the form of equity and quasi-equity which shall mean any financing instrument the profits of which are dependent on the success of the enterprise invested into and which do not have rights to secure assets attached to such instrument in case of default, see recital **(24)**.

(83) The Measure therefore complies with Section 4.3.3 of the Risk Capital Guidelines.

4.1.5. Participation by private investors

(84) Section 4.3.4 of the Risk Capital Guidelines requires at least 50 % of the funding of the investments made under the risk capital measure to be provided by private investors, or for at least 30 % in the case of measures targeting SMEs located in assisted areas.

(85) The Czech authorities confirmed that the Measure targets SMEs located in assisted areas and at least 30 % of capital of each of the measure will be provided by the private investors; see recitals **(15)** and **(27)**.

(86) The Measure therefore complies with Section 4.3.4 of the Risk Capital Guidelines.

4.1.6. Profit-driven character of investment decision

(87) The profit-driven criterion is considered to be met if the cumulative conditions under Section 4.3.5 of the Risk Capital Guidelines are fulfilled.

(88) Firstly, according to Section 4.3.5 (a) of the Risk Capital Guidelines, a significant involvement of private investors (as described in Section 4.3.4 of the Risk Capital Guidelines), providing investments on a commercial basis directly or indirectly into the equity of the target enterprises, must be present. As indicated in recital **(15)**, the Measure involves at least 30 % of private investors investing on a commercial basis directly at the level of target SME. Therefore the condition of Section 4.3.5 (a) of the Risk Capital Guidelines is complied with.

(89) Secondly, pursuant to Section 4.3.5 (b) of the Risk Capital Guidelines, a detailed business plan for each investment, establishing a project's *ex ante* viability, must exist. Under the provisions of the Measure, each investment will be made on the basis of a business plan to ensure the *ex ante* viability of the project, see recital **(34)**. Therefore, the condition of Section 4.3.5 (b) of the Risk Capital Guidelines is complied with.

(90) Lastly, as set out in Section 4.3.5 (c) of the Risk Capital Guidelines, a clear and realistic exit strategy must exist for each investment. As stated in recital **(34)**, there is a clear and realistic exit strategy for each investment. Therefore, the condition of Section 4.3.5 (c) of the Risk Capital Guidelines is complied with.

(91) The Measure therefore complies with Section 4.3.5 of the Risk Capital Guidelines and investment decisions of the ČRUIF can be considered to be profit-driven.

4.1.7. Commercial management

(92) According to Section 4.3.6 of the Risk Capital Guidelines, the management of a risk capital measure or fund must be effected on a commercial basis. This criterion is considered to be fulfilled where the manager behaves as managers in the private sector

seeking to optimise the return for investors. Section 4.3.6 of the Risk Capital Guidelines lays down three conditions in this respect.

(93) Firstly, according to Section 4.3.6 (a) of the Risk Capital Guidelines, there should be an agreement between a professional fund manager and the fund's participants, providing that the manager's remuneration is linked to performance and setting out the objectives of the fund and proposed timing of investments. As indicated in recitals **(36)** and **(37)**, the management agreement will set out the ČRUIF investment objectives, structure and timeline as well as a performance-linked remuneration of the ČRUIF Manager. Therefore, this condition is complied with.

(94) Secondly, pursuant to Section 4.3.6 (b) of the Risk Capital Guidelines, private market investors must be represented in decision-making, such as through an investors' or advisory committee. As indicated in recital **(40)**, private investors shall invest directly at the level of the target SMEs. Without a business decision of the private investor and its agreement, an investment into the target SME cannot be carried out. Therefore, it could be concluded that private co-investors are represented in the investment decision-making process. Therefore, the condition of point 4.3.6 (b) of the Risk Capital Guidelines is also complied with.

(95) Thirdly, Section 4.3.6 (c) of the Risk Capital Guidelines stipulates that best practices and regulatory supervision apply to the fund. As indicated in recitals **(41), (42)** and **(43)**, the ČRUIF will operate in accordance with the best available practices concerning fund management and functioning and, in particular, in accordance with EVCA policies and guidelines. Therefore, this condition is also complied with.

(96) The Measure therefore complies with all conditions laid out in Section 4.3.6 of the Risk Capital Guidelines so that the ČRUIF may be considered to be managed on a commercial basis.

4.2. Cumulation

(97) According to Section 6 of the Risk Capital Guidelines, where capital provided to a target enterprise under these measures is used to finance initial investment or other costs eligible for aid under the block exemption regulations, guidelines, frameworks, or other State aid documents, the relevant aid ceilings or maximum eligible amounts will be reduced by 50 % in general and by 20 % for target enterprises located in assisted areas during the first three years of the first risk capital investment and up to the total amount received. This reduction does not apply to aid intensities provided for in the Community framework for State aid for Research and Development or any successor framework or block exemption regulation in this field.

(98) The Czech authorities confirmed that they would apply the above cumulation rules, see recital **(44)** above. The Measure thus complies with Section 6 of the Risk Capital Guidelines.

4.3. Reporting and monitoring

(99) Section 7.1 of the Risk Capital Guidelines lays out conditions for the provision of annual reports on risk capital measures and for publication and recording obligations of the Member States.

(100) The Czech authorities undertook to comply with these reporting and monitoring obligations, see recitals **(45)** and **(46)**. The Measure therefore complies with section 7.1 of the Risk Capital Guidelines.

4.4. Conclusion

(101) In light of the above, the Commission considers the Early-Stage Capital Aid Scheme of the Czech Development, Closed-End Investment Fund to fulfil the conditions as set out in the Community Guidelines on State aid to promote risk capital investment in small and medium-sized enterprises. It therefore considers the Measure to be compatible with the internal market pursuant to Article 107(3)(c) of the TFEU.

5. CONCLUSION

(102) The Commission has accordingly decided to consider the aid to be compatible with the Treaty on the Functioning of the European Union.

(103) The Commission reminds the Czech Government that, in accordance with Article 108 (3) of the TFEU, all plans to refinance, alter or change this aid scheme have to be notified to the Commission.

(104) The Commission further reminds the Czech Government to provide an annual report on the implementation of the Measure.

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http://ec.europa.eu/competition/elojade/isef/index.cfm

Your request should be sent by registered letter or fax to:

European Commission
Directorate-General for Competition
Directorate for State Aid
State Aid Greffe
B – 1049 Brussels
Fax No.: +32 2 296 12 42

Yours faithfully,
For the Commission

Joaquín ALMUNIA
Vice-President