EUROPEAN COMMISSION
IMPACT ASSESSMENT BOARD

Brussels,
D(2011)

Opinion

Title **DG MARKT - Impact Assessment on a Proposal for a European Venture Capital Framework**

(draft version of 27 September 2011)

(A) Context

Access to venture capital in the EU is characterised by the fragmentation of the market along national lines. Due to different legal rules applicable to the raising of venture capital, operators of venture capital funds sometimes face barriers when fundraising or investing outside their domestic markets. The Commission considers that this fragmentation limits the overall supply of capital for SMEs with the potential to carry out innovation and grow rapidly. Venture capital funds face problems reaching the critical mass they need in order to spread their portfolio risk, develop sectoral specialization and cover their costs. A new impetus for resolving market fragmentation came with the adoption of the Europe 2020 Strategy and Innovation Union in 2010. Supported by the European Council of February 2011 that called for removing the remaining regulatory obstacles to cross border venture capital, the Commission committed in the Single Market Act (SMA) to ensure that by 2012 venture capital funds established in any Member State can raise capital and invest freely throughout the EU. In addition, Member States were invited to ensure that differences in tax treatment would not lead to double taxation, which would hamper cross-border venture capital investments.

(B) Overall assessment

The report should be strengthened significantly in several important respects. First, it should provide a much more concise, focussed and evidence-based description of the wider context and of the core problems, clearly highlighting the linkages with other related initiatives. In particular, it should much better demonstrate why fragmentation of rules on venture capital represents an impediment to fund raising and SME financing. This should include a description of past trends for capital allocation across funds, before and during the economic crisis. Second, the report should consider a broader range of options and should provide more information on the range of stakeholders' views on the pros and cons of potential options. Third, the report should include a much more in-depth assessment and comparison of the overall effectiveness, coherence and efficiency of the proposed measures, distinguishing the effects of these measures on a stand-alone basis and explain the extent to which other complimentary measures, for instance in the field of taxation, may be necessary to realise the full benefits. Finally the report should better present differences in stakeholder views throughout the report and should explain how compliance will be ensured and progress monitored.

Given the nature of these recommendations, the Board asks DG MARKT to submit a revised version of the report, on which it will issue a new opinion.

(C) Main recommendations for improvements

(1) Clarify the context and strengthen the analysis of the problems. The report should better explain the context for this initiative by clarifying how it links with other SME related initiatives including any linkages on taxation issues for venture capital funds. The report should define the core problem in a more concise manner in particular by clearly explaining that the central issue being addressed is the ability of venture capital funds to access funding on a cross-border basis in the EU. This should include a brief description of the process involved when a venture capital fund wants to operate in another Member State as well as available evidence on investment trends in the EU and the US before 2007. In light of the range of factors influencing cross-border venture capital funding, the report should also better demonstrate the extent to which the core problem can be attributed to fragmentation of rules in the EU and/or to other issues such as the ongoing financial crisis or other "natural factors" (linguistic barriers, geographical distances, etc). The report should better present the evidence for fragmentation of rules across Member States, clearly showing how such fragmentation is an impediment to raising funds and consequently to funding for SMEs. It should also show why previous measures aimed at improving access to funding by venture capital funds, such as encouraging mutual recognition, have not been effective. In light of the identified need to raise additional funds, the report should clarify the extent to which this will be met by a rebalancing of investments between venture capital funds and other funds, notably private equity funds.

(2) Consider a broader range of options. The report should consider a broader range of potential options for addressing the problems identified (e.g. improved mutual recognition or the amendment of the Directive on Alternative Investment Fund Managers). It should clearly explain why some options may be discarded and strengthen the intervention logic by establishing stronger links between the options, problems and objectives. It should also better describe the content of the current options and should explain the reasoning underlying the selection of the current range of options for the levels of qualifying investments in a venture capital fund.

(3) Better assessment of impacts. The report should provide a more in-depth assessment of the overall effectiveness, coherence and efficiency of the preferred option making greater use of quantification of estimates. In particular it should much better demonstrate the impact of reducing the fragmentation of rules in the EU on the allocation of capital across different funds and the ability of venture capital funds to raise additional investment on a cross-border basis and consequently on improving the access to venture capital funds by SMEs. It should distinguish the effects of the proposed measures on a stand-alone basis and should also illustrate the extent to which other complimentary measures, such as the avoidance of double taxation, may be necessary to realise the full effects of the measures proposed. The report should better explain the impact of the measures on Member States individually and collectively distinguishing between those where national rules are already in place and others. The report should discuss the effects, if any, on private equity funding or other forms of funding that might be available to SMEs.

(4) Better present stakeholders' views and improve monitoring and compliance issues. The main text of the report should illustrate more extensively stakeholders' views both in favour of and against the report's analysis of problems, selection and assessment of the preferred options. The report should better develop the monitoring mechanism and clarify what indicators and what sources will be used to measure success of the proposed measures, and how and when the future evaluations will be organised. The report should provide more information on how the proposed regulation will be enforced in the Member States in order to ensure that the proposals are not circumvented.

Some more technical comments have been transmitted directly to the author DG and are expected to be incorporated in the final version of the impact assessment report.

(D) Procedure and presentation.

The introductory section including background on the venture capital industry should be shortened considerably. A summary table comparing the impacts of the options should be added. The structure of the report should be improved considerably by clearly separating the description of the policy options from its analysis and by describing the impacts of all options, not only the preferred ones.

(E) IAB scrutiny process	
Reference number	2011/MARKT/050
External expertise used	No
Date of Board Meeting	19 October 2011