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Europe's next leaders: the Start-up and Scale-up Initiative

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COMMUNICATION FROM THE COMMISSION

EUROPE'S NEXT LEADERS: THE START-UP AND SCALE-UP INITIATIVE

1. INTRODUCTION

High-growth firms create many more new jobs compared to other firms.¹ Start-ups scaling up into bigger firms form a large share of these businesses. They increase EU innovation and competitiveness, strengthening the economy. Such "scale-ups" can also provide social benefits, including offering more flexible and modern working arrangements.

In the Single Market Strategy, the Commission announced that it will look at how to make the Single Market more efficient for start-ups and scale-ups. Ultimately, improving the ecosystem for start-ups and scale-ups in Europe will have a direct beneficial effect on jobs and growth in the EU.

Start-ups, often tech-enabled², in general combine fast growth, high reliance on innovation of product, processes and financing, utmost attention to new technological developments and extensive use of innovative business models, and, often, collaborative platforms.

Several Member States have already put in place or are considering initiatives to create an environment conducive to innovation and entrepreneurship. As a result, there is no major difference between the EU and the US as regards the creation of new firms.³ This is particularly visible in the tech sector where EU companies are in the process of becoming world leaders in certain medium/high-tech sectors (e.g. engineering, automotive).

A number of EU initiatives contribute to job creation and growth: the European Fund for Strategic Investments (EFSI)⁴, and its extension and reinforcement, but also the Single Market Strategy⁵, the Digital Single Market⁶, and the Capital Markets Union⁷ have also provided a framework for further improvement. In addition, a stronger focus of the European Structural and Investments Funds (ESIF) on innovation and SME support, includes venture capital support to 140,000 start-ups and scale-ups⁸. EFSI agreements already target 377,000 SMEs, including start-ups.

But rather than flourishing and expanding in Europe and beyond, too few European start-ups survive beyond the critical phase of 2-3 years, with even fewer growing into larger firms.⁹

Whilst the reasons for this situation are many, it has been estimated that there could be up to 1 million new jobs created and up to €2 000 billion added to GDP in the EU over the next 20 years if the share of scale-ups would match that of the US.¹⁰ Due to the positive link between firm size and productivity, this would improve Europe's productivity growth.¹¹¹² Additionally, identifying ways to support start-ups in scaling up could also benefit traditional businesses by supporting them to operate and grow within the Single Market.

¹ According to Henrekson and Johansson, 2010, 4% of firms generate 70% of new jobs. See also: <http://www.kauffman.org/blogs/policy-dialogue/2015/august/deconstructing-job-creation-from-startups>

² Connectivity; 5G and broadband etc..

³ Although there are differences between EU Member States. OECD (2015), *Entrepreneurship at a glance*.

⁴ https://ec.europa.eu/growth/industry/innovation/funding/efsi_en

⁵ <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52015DC0550&from=EN>

⁶ <http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1447773803386&uri=CELEX:52015DC0192>

⁷ <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52015DC0468>

⁸ See <https://cohesiondata.ec.europa.eu/themes/3>

⁹ The percentage of firms that grow by less than 5 % or not at all is over 45 % in Europe compared to 37 % in the US (Bravo-Biosca, 2011, *A look at business growth and contraction in Europe*).

¹⁰ Danish SME Envoy Report, 2016, *Scale-up Companies – is a new policy agenda needed?*

<http://ec.europa.eu/transparency/regexpert/index.cfm?do=groupDetail.groupDetailDoc&id=26381&no=1>

¹¹ See Eurostat (March, 2016), *Statistics Explained: Entrepreneurship – Statistical indicators*: http://ec.europa.eu/eurostat/statistics-explained/index.php/Entrepreneurship_-_statistical_indicators#Small.2C_medium_and_large_enterprises.

¹² Productivity in companies with over 1000 employees is much higher than in other companies. Danish Business Authority.

The results of a public consultation by the Commission earlier in 2016 confirmed this picture. The key findings¹³ were that:

- start-ups looking to scale up still face **too many regulatory and administrative barriers** especially in a cross-border situation;
- for both start-ups and scale-ups, **too few opportunities exist** to find and engage with potential partners in finance, business and local authorities;
- **accessing finance** is one of the biggest barrier to scaling up.

In short, the still too fragmented Single Market¹⁴ may in particular constrain start-ups and scale-ups in their growth potential. It appears that regulatory and administrative barriers often disincentivise them from innovating, valorising their intangible assets, and scaling up, EU-wide. Companies may choose to operate in non-EU jurisdictions with more growth potential, possibly resulting in EU job losses.

European public authorities, start-ups and their business partners must act collectively to avoid that the valuable efforts of start-ups are wasted. A partnership with national, regional and local authorities, and especially with the start-ups themselves, is needed. This involves authorities promoting conditions that ensure start-ups can scale up. In return those start-ups can create jobs, compete on the market and be socially responsible. The recent Scale-up Europe Manifesto¹⁵ shows that start-ups are ready to engage. The Commission welcomes this initiative from the actors in the field and its recommendations have informed the Commission's own reflections as far as these issues are concerned.

This initiative addresses three issues: **barriers**; the **shortage of partners and opportunities**; and **difficulties as regards finance**. It is based on:

- a **coordinated approach** across EU policies, building on measures in place or being developed, including sectoral approaches such as in the space sector;
- a limited and targeted set of **practical measures**; and, above all,
- **partnership**.

2. REMOVING THE BARRIERS

Many innovative young firms fear that if they grow too big they will be penalised by more burdensome rules, even without cross-border expansion. Many ongoing initiatives with the objective of lowering barriers to cross-border activities are not limited to start-ups, but can have a particularly positive impact on start-ups, e.g. the work on collaborative economy¹⁶, the ongoing initiatives to further improve service provision in the Single Market and eGovernment, or the ICT standardisation priorities¹⁷.

First of all, identifying and complying with **regulatory and administrative rules and formalities** can be time-consuming where **information** about national and EU rules is often dispersed and difficult to digest. Understanding all the tax, company, labour law and other requirements is a real challenge, especially for a start-up with limited resources or expertise. The consultation revealed that even once start-ups understand and comply with all relevant requirements, they find them overly burdensome. Nearly 40% of respondents found scaling up harder than expected.

Start-ups, in particular digital ones, also find it difficult to hire staff based in other EU countries (as tax and employment rules vary). Setting up a subsidiary is often too burdensome and does not match their needs (e.g. hiring only one person).

So public authorities at all levels – local, regional, national, European, - must act to remove unnecessary barriers and burdens and assist businesses in dealing with the unavoidable barriers.

¹³ http://ec.europa.eu/growth/tools-databases/newsroom/cf/itemdetail.cfm?item_id=8723

¹⁴ Including the Digital Single Market.

¹⁵ Scale Up Europe: A Manifesto for change and empowerment in the digital age, 2016.

¹⁶ http://ec.europa.eu/growth/single-market/strategy/collaborative-economy_en

¹⁷ http://ec.europa.eu/growth/tools-databases/newsroom/cf/itemdetail.cfm?item_id=8852

The Commission has already taken action and announced further measures in a number of these areas¹⁸. In 2017, the Commission intends to present initiatives for a Single Digital Gateway to provide easy online access to Single Market information, e-procedures, assistance, advice and problem solving services for citizens and businesses, as well as possibilities to complete cross-border procedures online¹⁹.

National authorities in the Member States Expert Group are looking into the overall regulatory framework for start-ups, supported by the Horizon 2020 Policy Support Facility, which allows individual Member States to seek recommendations on how to improve the business framework for such firms. To ensure that the Commission and Member States have detailed information and evidence on start-ups and scale-ups, under the revamped **European Observatory for Clusters and Industrial Change**²⁰, the Commission will for the first time systematically collect information on start-ups and scale-ups, conduct detailed analysis, and provide feedback and evidence to Member States to help them improve policy design and streamline implementation tools.

Second, start-ups are particularly concerned about **tax and the burden to comply with 28 different tax regimes**: 58% of respondents to the Commission's consultation reported high tax compliance costs. Small and medium-sized businesses (SMEs) spend around 30% of tax related expenditure on compliance costs, and even more if they expand cross-border²¹. Addressing this issue would make a tangible difference and could help start-ups to grow.

As presented in its Action Plan adopted on 6 April 2016, the Commission intends to modernise and simplify the Value Added Tax (VAT) system applying to cross border trade within the EU by creating a Single VAT Area²². It will therefore come forward in the coming months with a comprehensive package to reduce the complexity and fragmentation of the EU VAT system and thus creating an environment conducive to companies' growth and favourable to cross-border trade. In the next weeks, the Commission will propose to simplify the Mini-One Stop Shop (MOSS) and extend it to cross-border business-to-consumer supplies of goods and other services. In 2017, it will put forward a targeted VAT simplification package for SMEs, including start-ups. It will also propose a definitive VAT regime for cross-border trade within the EU that will further reduce the burden for start-ups and scale-ups.

Moreover, the recently adopted proposals to re-launch the Common Consolidated Corporate Tax Base (CCCTB) contain incentives for businesses to grow and expand cross-border within the Single Market. In particular, for innovative start-ups and scale-ups that would opt in the CCCTB, it includes a R&D super-deduction, and an allowance to ensure that equity and debt financing are treated equally from a tax point of view²³.

Thirdly, honest risk-takers are too often subject to inefficient and excessively long **insolvency procedures**. Moreover viable companies don't have the possibility to restructure. In addition, there seems to be very little room for a "second chance" for honest over-indebted entrepreneurs, although failure is often part of the path of a successful entrepreneur. Fear of failure and being penalised for that failure can discourage investing into scaling up.

¹⁸ The European Commission is continuously managing the corpus of European legislation via the Regulatory Fitness and Performance programme (REFIT) which aims to make sure that EU law remains fit for purpose and delivers the results intended by policy makers in the most efficient and effective way. It targets removing red tape and lowering costs without compromising policy objectives and EU high standards.

¹⁹ The online registration of companies will be addressed as part of the planned Commission proposal on facilitating the use of digital technologies throughout a company's lifecycle (see Commission Communication "Upgrading the Single Market: more opportunities for people and business" (COM(2015)550, p. 5; Commission Communication "EU eGovernment Action Plan 2016-2020" (COM(2016)179, p. 8; Commission Work Programme 2017 (COM(2016)710, p. 8).

²⁰ This will consult with platforms such as European Start-up Network and the Global Entrepreneurship Network

²¹ See Commission Communication: Building a fair, competitive and stable corporate tax system for the EU.

²² https://ec.europa.eu/taxation_customs/sites/taxation/files/com_2016_148_en.pdf

²³ The CCCTB could give a boost to start-ups and scale-ups to invest and expand in the Single Market. It will reward their growth-friendly activities such as investment in R&D and equity financing. To support small and innovative entrepreneurship, an enhanced deduction for R&D investments will be given to start-up companies. The CCCTB will address the preferential treatment of debt over equity which will benefit equity-financed innovative companies and start-ups in particular.

As regards **company and insolvency law**, the Commission has adopted today a legislative instrument which will (i) guarantee an early-warning mechanism and the availability of restructuring frameworks in Member States in order to restore viability and avoid insolvency, in particular for SMEs, (ii) provide for a second chance regime for individual honest over-indebted entrepreneurs through a discharge of their debts and (iii) enhance the efficiency of restructuring, insolvency and discharge procedures. The Commission also intends to present in 2017 a company law initiative to facilitate the use of digital technologies throughout a company's lifecycle, in particular in relation to their registration and to the filing of company documents and information, and on cross-border mergers and divisions, including updating the rules on cross-border mergers and complementing them with rules on cross-border divisions. As announced in Digital Single Market, and in the E-government action plan, a large scale pilot project on implementing the "once only" principle across borders in the business-to-government area will be launched in 2016 with participation of Member States.²⁴

Fourth, as regards **labour law**, the Commission will continue to facilitate compliance and respect of workers' rights by start-ups including as regards compliance with the EU rules on working time and health and safety.

Additionally, the EU will continue to use **trade** policy to open up opportunities for start-ups and scale-ups in foreign markets, in particular through trade agreements and appropriate measures to ensure predictable and clear trade rules.

Further actions:

- *The Commission will work with the European Parliament and the Council and European Parliament to secure timely adoption and implementation of the proposal on **preventive restructuring frameworks, second chance for honest entrepreneurs and increased efficiency of restructuring, insolvency and discharge procedures**.*
- *The Commission will broaden the forthcoming guidance on best practice in Member State tax regimes for Venture Capital.*
- *To help start-ups and scale-ups to navigate the often dispersed information sources, the **Enterprise Europe Network (EEN)** will expand its advisory services with dedicated Scale-up Advisors on relevant national and European rules, funding opportunities, partnering and how to access cross-border public procurement, link up with Startup Europe and with the SME access to Digital Innovation Hubs and the manufacturing pilot lines for SMEs, under Horizon 2020.*
- *In 2017 under the High Level Group of the Competitiveness Council, the Commission will support a **major, comprehensive and detailed peer review** of all Member State rules and practices towards start-ups and scale-ups.*

3. CREATING NEW OPPORTUNITIES

The EU and Member States could further simplify the life of start-ups by supporting them in the following areas:

- connecting with the **right partners** (e.g. investors, business partners, universities, research centres);
- accessing commercial opportunities (especially **procurement** contracts);
- recruiting employees with the **right skills**, including from outside the EU.

3.1 Partners, clusters and ecosystems

²⁴ See eGovernment action plan 2016-2020 COM(2016)179, <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52016DC0179>

In recent years, the Commission and EU Member States have supported the creation of ‘**communities**’ to help start-ups connect with potential partners (e.g. investors, business partners, universities, research centres) through events, platforms, business clusters, networking and supportive local/regional ‘ecosystems’.²⁵

At EU level, the Startup Europe initiative has emerged as a recognised brand for creating links between ecosystems²⁶, focusing on connecting people, local ecosystems, international outreach and providing information through the One Stop Shop for start-ups. Whilst some progress has been achieved, activities will be reinforced, in particular matchmaking between investors, corporates and entrepreneurs as well as networking of regional decision-makers.

In addition, the European Institute of Innovation and Technology (EIT) has set up a number of Knowledge and Innovation Communities in the thematic areas of ICT, Energy, Climate Change, Health, and Raw materials with 25% of public financing, the rest being private investments. The EIT is helping on a number of fronts: entrepreneurship skills, mentoring, and start-up accelerators.

The EU has also established Thematic Smart Specialisation Platforms²⁷, linking up regions and businesses and supporting European Structural and Investment Funds (ESIF) investments for scale-ups promoted by regional networks and European Strategic Cluster Partnerships. Together with the targeted support they receive²⁸, these projects will help create opportunities for scale-ups. The Commission will encourage Member States to take part in these Thematic Smart Specialisation Platforms and to use the Horizon 2020 Policy Support Facility.

However, despite these initiatives, the public consultation showed that start-ups and scale-ups would benefit from **more coordinated support**:

- a **critical mass** of effectively interconnected EU-wide clusters and ecosystems
- better use of **accelerators and incubators**;
- an EU-wide **platform to connect** start-ups with potential partners (alongside existing public and private platforms).

Further actions:

- *In 2017, the Commission will reinforce Startup Europe which will take a wider scope beyond the ICT and web start-up sector. The Commission will coordinate EU work to **connect clusters and ecosystems across Europe, as well as bring stronger coherence between the different EU initiatives** in particular by linking up national and regional Ministries, innovation agencies and other stakeholders and ecosystems.*
- *To **connect start-ups with business partners**, in 2017, the Commission will launch a number of pilot measures on matchmaking, linking start-ups, mid-caps and larger enterprises and extend the Erasmus for Young Entrepreneurs programme to incubators and entrepreneurs in international markets.*

3.2 Procurement opportunities

Public procurement contracts can support scaling up activities, but SMEs are still under-represented²⁹ in particular for so-called ‘above-threshold’ procurement.³⁰

²⁵ The ‘entrepreneurship ecosystem approach’ explains why some cities/regions have many more start-ups/scale-ups than others, despite having the same regulatory framework. Ecosystems drive resources towards the most productive use. They make it possible to design holistic policies not achieved through traditional approaches.

²⁶ e.g. the Start-up Europe Summit, Start-up Europe Accelerators Assembly, Start-up Europe Universities network; raising awareness of the funding and networking opportunities available; linking large corporates and start-ups (Start-up Europe Partnership), and celebrating entrepreneurship.

²⁷ So far on Industrial Modernisation, Agrifood and Energy.

²⁸ e.g. on transforming regions and cities into launch-pads for digital transformation and industrial modernisation.

²⁹ Flash Eurobarometer 417 on barriers to procurement for small companies.

³⁰ Procurement with a value equal to or higher than the thresholds set in EU legislation.

Public procurement, a €2 trillion market, represents a great potential for start-ups/scale-ups to grow. Today, this potential is not yet sufficiently used. Compared to their weight in the economy, start-ups/scale-ups do not get a proportionate share of public contracts³¹. Better support to contracting authorities on using the market opportunities and the modernised procurement tools is necessary to improve the uptake of innovative start-ups/scale-ups. In particular, preliminary market consultations and innovation partnerships can be powerful ways for start-ups/scale-ups to pitch their innovative products to public buyers. Start-ups/scale-ups will thus more easily achieve success in public procurement. Rolling out e-procurement is essential in that regard.

A well designed public procurement of innovation has already helped bring untested ideas to market thus creating cross-border growth opportunities.

In the first FP7 innovation procurement actions SMEs won 2.5 times more contracts than in standard exercises (73% versus 29%) and 15 times more contracts were awarded cross-border than the average in public procurement in Europe (29% versus 2%).³²

In 2014, the EU adopted a new public procurement framework providing opportunities for start-ups to access public procurement. However, it appears that national or regional/local tendering authorities are not yet sufficiently aware of these possibilities.

Further actions:

- *In 2017, the Commission will introduce measures on **EU procurement** to: (i) establish innovation brokers to build networks of buyers interested in public innovation procurement, link them with innovative businesses and help the businesses access risk funding³³; (ii) encourage all Member States to set ambitious innovation buying targets; (iii) provide guidance on innovative procurement³⁴, drawing on the Innovation Partnership.*

3.3 Skills

Growing companies need to recruit employees with the right **skills**, in particular **technical**, **financial** and **digital** skills. Entrepreneurial mindset, **management** and **leadership** skills for scaling up are also crucial.

Based on the ‘**New Skills Agenda for Europe**’ (June 2016), the Commission is working to improve **skills quality** and their **relevance to the job market**.

Three initiatives will address these challenges:

- The forthcoming ‘**Digital Skills and Jobs Coalition**’ – supports cooperation between education, employment, industry.
- The ‘**Blueprint for Sectoral Cooperation on Skills**’ – improves skills intelligence, addresses skills shortages.
- The forthcoming “**big data tool**” on skills intelligence and forecasting as part of the “Skills Panorama”.

The Commission has also set up two frameworks to improve the teaching and assessment of skills:

- European Entrepreneurship Framework (EntrComp);
- Digital Competence Framework (DigComp).

³¹ This is particularly true for procurement with a value equal to or higher than the thresholds set in EU legislation.

³² <https://ec.europa.eu/digital-single-market/en/news/updated-results-ongoing-pre-commercial-procurements-pcp-projects>

³³ These brokers would identify and aggregate the needs of public buyers, identify potential suppliers, funnel ideas and fund the most promising ones in particular sectors.

³⁴ Based on the modernised public procurement directives.

It will work with Member States to promote these frameworks nationally. At the same time, the EIT will pursue and increase its work in training Master students with combined technical and entrepreneurship skills.

The Commission is also promoting ICT professionalism – the European e-Competence Framework³⁵ for ICT professionals is now a standard. Finally, the ability to attract the best talent, including from outside the EU - is another important driver of its success. In June 2016, the Commission proposed to reform the **EU Blue Card** to better attract highly-qualified third-country national workers.³⁶ As talent from abroad can also make an important contribution in founding start-ups, more work needs to be done within the EU to attract and support them.

Further actions:

- *In 2017, the Commission will build on the New Skills Agenda by looking into scaling up the activities of the **EIT** to promote entrepreneurship, management and innovation skills.*
- *The Commission will encourage Member States to make more use of Erasmus+ Knowledge Alliances, and the HEInnovate self-assessment tool.*

3.4 Enhancing EU innovation opportunities for start-ups and scale-ups

The Commission has provided increased support to SMEs through the Horizon 2020 research and innovation framework programme, either as partners in collaborative projects with research organisations and other firms, or as single beneficiaries. It has also boosted support for innovation including through more demonstration projects, facilitated access to experimentation and pilot facilities, actions on innovative procurement and reinforced financial instruments. As a consequence, SME participation has increased and is currently above the 20% target level.

The new SME instrument has already supported innovation projects in 1,924³⁷ SMEs. However, evidence and stakeholder views³⁸ demonstrate that Horizon 2020 is better at supporting existing technologies and companies, than start-ups that are innovating in new markets or at the intersection between digital and physical technologies. Current support is seen as too complex, inflexible and slow for their needs.

In light of the above, the Commission intends to make changes to Horizon 2020 for the period (2018-2020). These include:

- adopting a fully **‘bottom-up’ approach** — so innovative projects that cut across sectors/technologies become eligible for support;
- making it easier for start-ups to **access financial and technical support**;
- targeting market-creating, breakthrough innovations with **scale-up potential**.

Building on this, and based on the results of the mid-term evaluation of Horizon 2020, the European Commission will consider creating a **European Innovation Council**³⁹ for future programmes to contribute to generating breakthrough innovations that can capture and create new markets.

In addition to consideration of specific SME needs, such as open and facilitated access to experimentation and pilot facilities, and in cooperation with regions on innovation hubs, the **Innovation Radar** initiative makes it easier to spot Horizon 2020-funded innovations with market potential early on and the teams behind them (e.g. SMEs, start-ups, spin-offs, universities).

³⁵ <http://www.ecompetences.eu/>.

³⁶ Also in 2016, the reform of the immigration rules for third-country national students and researchers was adopted, giving them the right to stay in the EU to look for a job or set up a business for at least 9 months following graduation or finalization of research (Directive (EU) 2016/801).

³⁷ Drawing on the Innovation Partnership and taking into account social and green aspects.

³⁸ https://ec.europa.eu/research/eic/pdf/eic_call_for_ideas-overview.pdf#view=fit&pagemode=none.

³⁹ Working name

The **European Institute of Innovation and Technology** (EIT) has established pan-European accelerators for innovative companies. In addition, the EIT will explore the setting up of schemes to invest directly in the scaling up of existing innovative companies by attracting additional investment from public and private sector sources and existing instruments.

Moreover, it is too difficult for start-ups and scale-ups (and SMEs more widely) willing to do so, to secure and valorise intellectual property rights (**IPR**) because of a lack of precise information and expertise on how to use IPRs strategically as investment/growth vehicles; relatively high system costs; difficulty in getting IPRs valued;⁴⁰ and high enforcement costs.

Only 9% of EU small companies use registered intellectual property and even less use rights with an EU-wide coverage (3% register EU trade marks)⁴¹. This often prevents them from reaping the large potential benefits of their innovation efforts. Compared to their peers, SMEs actively using IP generate 32% higher revenue per employee allowing them to offer more attractive wages and increase their workforce faster. IP is therefore key for the scaling-up process of innovation small firms.

Finally, innovators, and particularly start-ups, often face regulatory barriers or uncertainties in introducing their innovations to market. As part of its Better Regulation agenda, the Commission is taking into account the potential impact on innovation of current and new regulation⁴², in line with the “innovation principle”⁴³ as requested by the Council.

Further actions:

- *To **improve innovation support**, the Commission intends to make changes for the remaining period of Horizon 2020 to provide bottom-up support targeting breakthrough innovation projects with the potential for scaling up, and will consider reinforcing this approach in future through a **European Innovation Council**⁴⁴.*
- *The Commission will use the **Innovation Radar** to connect potential business partners and investors with Horizon 2020-funded innovators to support them to scale up.*
- *The Commission will carry out an evaluation of the **Innovation Deals** scheme allowing innovators to work with public authorities and other stakeholders to find ways to address perceived regulatory barriers, and if successful, expand it to other relevant areas. In this context, the Commission will also explore an enabling framework for **regulatory sandboxes**.*
- *In 2017-18, the Commission intends to adopt a set of measures to **support the use of IPR by SMEs**⁴⁵ namely (i) streamlining awareness on existing IP Support schemes for SMEs; (ii) developing an EU IP mediation and arbitration network for SMEs; (iii) encouraging the creation of European-level insurance schemes for litigation and IP theft; (iv) improving coordination of IP support funding schemes, including by means of a possible guidance to Member States⁴⁶.*

3.5 Social economy and social enterprises

Globally, there is increasing interest in social innovation as a way to sustainable growth, e.g. fair trade, distance learning, mobile money transfer, integrating migrants, and zero-carbon housing.

⁴⁰ Report on access to finance for the Cultural and Creative Sectors (European Commission, 2015).

⁴¹ Intellectual property rights and firm performance in Europe: an economic analysis (EUIPO, 2015).

⁴² In the forthcoming revision to the research and innovation tool under the Impact Assessment guidelines.

⁴³ https://ec.europa.eu/epsc/sites/epsc/files/strategic_note_issue_14.pdf

⁴⁴ Working name

⁴⁵ Additional details on these measures are provided in the accompanying Staff Working Document. These measures will be developed in close cooperation with the EUIPO (EU Intellectual Property Office).

⁴⁶ SWD(2016) 373 of 22.11.2016, "Putting intellectual property at the service of SMEs to foster innovation and growth".

Social start-ups⁴⁷ therefore have high potential for innovation and positive impact in economy and society at large.⁴⁸ Their business model — combining economic efficiency with societal-centred objectives⁴⁹ — has proven very resilient.⁵⁰

And there are good prospects for such start-ups, due to increasing demand for social innovation and the rise of new technologies and collaborative platforms. In addition, many have potential for scaling proven business models which could be replicated in other territories. However, these companies still find it hard to secure funding and support, especially due to the following factors:

- lack of recognition and understanding of their economic potential;
- insufficient exploitation of modern technologies.

Moreover, the Commission has launched with the European Investment Fund new financial instruments to boost lending to social enterprises, as well as new social impact equity instruments under the European Fund for Strategic Investments.

Further actions:

- *Building on the Social Business Initiative, the Commission will encourage social start-ups to **scale up**, including through measures focussing on better access to finance, improved access to markets, and strengthening regulatory frameworks by advising Member States on policy design.*
- *The Commission will also explore measures to facilitate uptake of new technologies, use of new business models⁵¹ and to support impact financing of the social economy and social enterprises through EU development/neighbourhood policies and international fora (e.g. G20 Inclusive Business platform)⁵².*

4. ACCESS TO FINANCE

Removing and simplifying regulation, and increasing opportunities for matchmaking, public contracts and effective recruitment will help start-ups to scale up and create sustainable jobs. **Access to finance** is a key barrier to address.

Although the problems that EU firms face in the start-up phase are not larger than those faced in the US, academic evidence and the public consultation confirm that there are substantial differences during the scaling-up phase. This is partly due to the amount of funding available for venture capital investment: it is estimated that in 2014 only around €5 billion was available in the EU, compared to more than €26 billion in the US⁵³.

Additionally, **European venture capital funds** are smaller on average⁵⁴ and cannot sufficiently help companies grow from start-ups to mid-caps to global players. In 2007-2012, the average size of European venture capital funds (at final closing) was €61 million and 50% were smaller than €27 million; the average US venture capital fund in 2014 was \$135 million in size.⁵⁵ This is a particular problem for scale-ups, as funding tends to dry up with time.

⁴⁷ A social start-up is a start-up that produces societal impact.

⁴⁸ http://eureka.sbs.ox.ac.uk/761/1/Social_Innovation.pdf, Oxford Said Business School, Social Innovation.

⁴⁹ <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2013:347:0238:0252:EN:PDF..>

⁵⁰ http://europa.eu/rapid/press-release_CES-12-60_en.htm?locale=en

⁵¹ In 2017, the Commission will launch a Social Innovation Challenge Platform to incentivise social enterprises to team up with other types of enterprises to co-develop solutions to societal challenges. It will also launch a call to analyse and collect best practice on how social enterprises can better use the digital economy.

⁵² <http://www.un.org/sustainabledevelopment/sustainable-development-goals/>

⁵³ Thomson ONE in BSG Perspectives 'The State of European Venture Capital'.

⁵³ Thomson ONE in BSG Perspectives 'The State of European Venture Capital'.

⁵⁴ NVCA report for US figures, data EU report for EU figures.

⁵⁵ 'Assessing the Potential for EU Investment in Venture Capital and Other Risk Capital Fund of Funds' study.

Being able to choose from a range of **exit strategies** is key for investors. They have to know that they will be able to redeem their investments, be it through an IPO, a trade sale to another company, a sale to a later stage venture capital or private equity fund, or to resell to the founder(s) of the company. Yet the current lack of information on financing possibilities leads to uncertainty and less investment. Equally, the more later-stage financing is available, the more likely first- and second round investors are to invest.

When accessing **public funding**, 85% of respondents to the public consultation called for better coherence and transparency of funding initiatives, and better targeting of companies who could be tomorrow's leaders.

The Commission is addressing these issues across several policies. In the mid-term budget review, it proposed to increase the budget for EFSI⁵⁶, and COSME, reinforcing existing financial instruments and mobilising additional financing for SMEs in the start-up and scale-up phases.

Since 2010, the EU Programme for Employment and Social Innovation (EaSI) and its predecessor have opened up €1 billion in microcredits for setting up or developing a small business, providing support to over 100,000 micro-entrepreneurs across Europe.

The **Capital Markets Union** launched in 2015 will also help. The Commission is taking forward a comprehensive package of measures to support venture capital and risk capital financing in the EU. In conjunction with the Single Market Strategy, it proposes to create a pan-European Venture Capital Fund of Funds to tackle the small size and fragmentation of European venture capital funds, attract more private capital back to venture capital, enable more SMEs to be financed for longer periods of time, and diversify funding for start-ups, innovation and non-listed companies⁵⁷. In addition, in July 2016, the Commission adopted a proposal to amend the Regulations on European Venture Capital Funds (EuVECA) and, as mentioned above, on European Social Entrepreneurship Funds (EuSEF) to facilitate further cross-border financing for SMEs. Complementing the pan European Venture Capital Fund of Funds and EFSI, the Commission will look into the potential added value of additional **incentives to venture capital** through for instance schemes allowing privately owned and managed investment funds to benefit from public guarantee when raising debt financing in order to make equity and debt investments in start-ups and scale-ups.

The Commission will also continue to monitor **tax schemes/incentives** for investments into start-ups/scale-ups, and building on successful approaches implemented by Member States and the results of the on-going study on the effectiveness of tax incentives for Venture Capital and business angels to attract more patient capital, it will consider further ways to support Member States' policy design.

To strengthen exit strategies for early investors in start-ups and scale-ups, and complementing the upcoming pilot project for a Pan European match-making platform as well as Start-up Europe initiatives, in 2017-2018 the Commission will monitor the creation of SME growth markets, a new category of multilateral trading facilities that will be given legal form by the Markets in Financial Instruments Directive II (MiFID II)⁵⁸. This will make it easier to raise capital for medium-sized firms, and to share best practice. The Commission will identify market-led and public initiatives that foster the admission of SME shares to trading and explore workable solutions to regulatory issues and market failures.

Further actions:

- *The Commission and the European Investment Fund will make the cornerstone investments in 2017 in the new, independently managed **Pan European Venture Capital Fund of Funds** alongside major private investors to increase the size of Venture Capital Funds in Europe and overcome current fragmentation. The EU cornerstone investments of up to €400m will be*

⁵⁶ <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52016DC0581&from=EN>

⁵⁷ A call for expression of interest to select pan-European Fund of Fund promoters has been launched in November 2016.

⁵⁸ Directive 2014/65/EU.

capped at 25% of the total capital in the Funds of Funds, bringing a potential of at least €1.6bn additional investments to Venture Capital in Europe.

- *In 2017, the Commission will coordinate a pan-European platform where Member States' best practice on crowdfunding can be shared, together with an assessment of financing gaps in **alternative sources of finance**, to understand whether further public financing or other measures are needed.*

5. CONCLUSION

Despite its many young and innovative entrepreneurs, Europe is not yet fully tapping the potential of its entrepreneurial capacity and talent.

Although action has been taken at national as well as EU level to encourage the creation of start-ups, more needs to be done.

Starting and scaling a company across Europe has to become simpler. The goal is for Europe to become the first choice for ambitious entrepreneurs to set up and grow their breakthrough business ideas into successful companies in well-performing ecosystems. In return, they will create new jobs, foster social responsibility and some will become global leaders.

The present Communication proposes a coordinated approach across EU policies to be delivered through a set of pragmatic measures. Working in partnership with all levels of government, in Member States, regions and cities and all stakeholders - including start-ups and scale-ups themselves - will also be necessary for its efficient and successful implementation.

The Commission invites the European Parliament and the Council to endorse this Communication and to actively engage in its implementation, in close cooperation with all relevant stakeholders.