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newsflash

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New financing opportunities for businesses

by Athina Siafarika

Greece, as well as Europe, requires significant volumes of new long term sustainable investment to maintain and increase competitiveness. Currently, loan-based finance dominates the market, while alternatives to traditional methods of financing are limited, contrary to the situation in the USA. This is particularly true, when it comes to European Small and Medium Sized Enterprises (SMEs), which, for example, compared with the US, receive five times less funding from capital markets.

In its new project, Capital Markets Union (CMU), part of the Juncker's Investment Plan and necessary complement to the European Banking Union, the European Commission recognizes broadly the need for promoting alternative sources of funding for businesses, especially SMEs, placing special emphasis on funds.

In this respect, the European Commission aimes at facilitating the cross border provision of services for certain categories of funds, by putting forward or/ and amending legislative texts which regulate and establish "marketing labels" for those funds, thus allowing them to "passport" their investment services across Europe. ELTIFs, EuVECA, EuSEF are indicative examples in this regard.

European Long-Term Investment Funds

The recent European Long-Term Investment Funds (ELTIFs) regulation, applicable in Member States from 9 December 2015, will allow investors to put money into companies and infrastructure projects for the long term, thus increasing the amount of non-bank finance available to companies in the EU. In particular, ELTIFs can invest in real estate, intellectual property, unlisted SMEs, as well as listed SMEs with a market capitalisation of less than EUR 500 million. Eligible assets must comprise at least 70% in eligible long-term investments. Direct holdings of over EUR 10 Million in real assets such as energy, transport, communication, education, health and so on are eligible provided that they yield a predictable return.

Importantly, the ELTIF will be available for both retail and professional investors, unless its manager decides otherwise, opting for professional investors only. ELTIFs may be marketed cross border to retail investors who have accumulated a portfolio (composed of cash deposits and financial instruments) of more than EUR 100,000, provided they invest no more than 10% of their portfolio in the new product.

It should be noted that by definition, ELTIFs are EU Alternative Investment Funds (AIFs) that are managed by Alternative Investment Fund Managers (AIFMs). However, ELTIFs have a more limited scope. Only an EU AIF is eligible to become an authorized ELTIF and only if it is managed by an EU AIFM.

European Social Entrepreneurship Funds

The European Social Entrepreneurship Funds (EuSEFs) Regulation, directly applicable since July 2013, allows EU *registered* AIFMs (sub- AIFMD threshold) to manage certain types of qualifying social entrepreneurship funds domiciled in the EU, known as EuSEFs, and to market those EuSEFs throughout the European Union.

EuSEF is actually a collective investment undertaking established in the EU which intends to invest at least 70% of its capital in "social enterprises" qualifying as eligible undertakings. For an undertaking to qualify as a portfolio undertaking for a EuSEF, it has to meet the following requirements:

a. It is not admitted to trading on a regulated market or multilateral trading facility;

b. Its primary objective, according to its articles of association etc, is to achieve social impacts (positive and measurable);

c. It provides services or goods to vulnerable, marginalized, disadgantaged or excluded persons, or employs a method of production of goods or services that embodies its social objective or provides financial support exclusively to social undertakings;

d. It uses its profits primarily to achieve its social objectives

e. It is managed in an accountable and transparent way, often involving workers, customers and stakeholders affected by its business activities.

EuSEFs may be marketed to investors are (or elected to be treated as) professional clients who are willing to invest at least €100.000 and have confirmed in writing that they are aware of the risks associated with their investment.

European Venture Capital Funds

The European Venture Capital Funds (EuVECA) Regulation establishes an "EU passporting" label for, in principle, sub-AIFMD threshold AIFs which invest at least 70% of their capital commitments in supporting young and innovative companies ("qualifying undertakings") which bear the following characteristics: they are not admitted to trading on a regulated market or multilateral trading facility (MTF), they employ fewer than 250 persons and have an annual turnover not exceeding €50 million (or annual balance sheet total not exceeding €43 million).

For further details in relation to EuVECA please refer to our November 2015 Newsletter found here:
http://www.rokas.com/en/press-articles-a-publications/capital-markets-financial-regulation

Crowdfunding

Crowdfunding is a way of raising money to finance projects and businesses. It enables fundraisers to collect money from a large number of people via online platforms. Crowdfunding is most often used by start-up companies or growing businesses as a way of accessing alternative funds. The main types of crowdfunding are the following:

- *Donation-based crowdfunding*: Individuals donate small amounts to meet the funding aim of a charitable project while receiving no financial or material return.
- *Equity crowdfunding*: Sale of a stake in a business to a number of investors in return for investment.
- *Debt-securities crowdfunding & Peer-to-peer lending:* Individuals invest in a debt security issued by the company, such as a bond & the crowd lends money to a company with the understanding that the money will be repaid with interest.

Despite the lack of a specific regulatory framework for crowdfunding in Greece, a crowdfunding platform can make use of the MiFID provisions (especially the equity model) in order to obtain authorization. Depending on the business model adopted, other legal issues may arise such as the possible application of the Prospectus Directive, the Payment Services Directive etc, as well as money laundering and investor/consumer protection considerations. Special legal advice should be sought while drawing the crowdfunding business model.

Possibilities for public funding and matched – public and private- financing

Amongst the numerous European initiatives put forward for the promotion of alternative sources of funding, "targeting" in particular SMEs, a special reference should be made to public financing channelled to businesses on the basis of development programs or through development funds, such as the Athens-based "Hellenic Fund for Entrepreneurship and Development" (E.T.E.AN. SA) and the the "Institution for Growth in Greece"(IfG). Notably, ETEAN and IfG are able to finance Greek credit institutions through loan agreements, upon condition that those credit institutions will further channel those funds to SMEs in Greece.

At the same time, the European state aid rules, especially the General Block Exemption Regulation (GBER) and the "Guidelines on State Aid to promote risk finance investments" (the Risk Finance guidelines) include certain provisions favouring SMEs, which though viable, are faced with a market failure in accessing the necessary finance. In particular, the GBER allows Member States to grant certain categories of state aid without prior notification and approval by the Commission, provided that certain conditions are met. Such categories include state aid granted to SMEs to facilitate their access to finance. On the other hand, the Risk Finance guidelines provide that financing to SMEs by the State and the entity acting on its behalf may not be granted directly to SMEs, but rather it should be provided by financial intermediaries, which carry out credit risk assessment and/or investment due diligence.

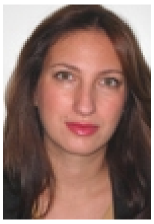
Information Asymmetry: Local intermediaries to "bridge the gap"

However, despite the possibility to offer cross-border services, funds still face an information asymmetry problem as regards the position and prospects of domestic businesses, especially SMEs. This asymmetry can be corrected by mobilizing domestic banks and other financial services providers to "intermediate" between funds and businesses.

Domestic providers should take advantage of their knowledge of the national market, their professional network and solid personal relations with their clients (corporates, SMEs etc.) and perform a "*matching*" exercise. This exercise could rely on the provision of credit information in relation to the creditworthiness of the finance-seeking company, as well as on the adoption of other criteria based on "soft law" approaches.

Greek businesses, still facing difficulties in securing sufficient and stable funding, could very much profit from initiatives such as those presented above. Thus, banks, investment firms, funds and other financial intermediaries should actively engage in the development and promotion of alternative funding solutions which will mobilize again entrepreneurship and new investments in the Greek market.

Editing author



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