EUROPEAN COMMISSION

Brussels,

C (....) ….

**Subject: N 26/2007 - Poland**
**Aid to capital funds investing in micro, small and medium enterprises**

## 1. PROCEDURE

1. By letter dated 11 January 2007, registered by the Commission on the same day, the Polish authorities, having regard to Article 88 (3) EC, notified to the Commission the above-mentioned scheme.

2. By letter of 22 January 2007, the Commission requested additional information on the aid scheme. By letter dated 19 February 2007 the Polish authorities provided the information.

## 2. DESCRIPTION OF THE SCHEME

3. The aid granting scheme involves four major participants:

- private investors, who create risk capital funds - such funds are legal persons or organisational units without legal personality, whose exclusive aim is to make investments in SMEs,
- managers or management companies of such funds,
- National Capital Fund, and
- potential investees (SMEs).

4. The sole objective of the National Capital Fund is to administer the provision of financial support to risk capital funds which invest in undertakings established in Poland, and especially in innovative or research and development enterprises. The establishment of the National Capital Fund is subject to approval of the competent Minster for Economy. The state resources will be channelled through this Fund to private risk capital funds which will be chosen in open tender procedure. In this way the Fund will co-invest with private risk capital funds in selected SMEs.

### *2.1. Objective of the scheme*

5. The aim of the scheme is to reduce the equity gap present in Poland. This measure intends to facilitate the establishment and development of venture capital funds providing funding to innovative and growth-oriented small and medium-sized enterprises ('SMEs')[1] in their all stages of development up to expansion stage.

### *2.2. Legal basis of the scheme*

6. The following were presented by the Polish authorities:
   - Draft Regulation of the Minister of Economy on financial support granted by the National Capital Fund;
   - Act of 4 March 2005 on the National Capital Fund, Journal of Laws from 6 April 2005- text available on http://isip.sejm.gov.pl/prawo/index.html);

### *2.3. Background of the scheme*

7. According to the Polish authorities private investors are not encouraged to make investments in the SMEs up to their expansion stage. There is no real market for venture capital investments. Neither banks nor pension funds are interested in this type of investments. Despite the lack of capital supply the Polish authorities claim that there is an unsatisfied demand for venture capital investments from many small and medium enterprises in their early stages of development.

8. According to the Polish authorities the equity gap in Poland reaches the level between PLN (Polish zlotys) 0,1-2 million (EUR 0,02-0,5 million) and PLN 8-10 million (EUR 2 - 4.5 million) respectively, depending on the project's features and the sector in which the investees are active. In particular, at present private investors are not interested in carrying out investments of a relatively low value and at the same time of relatively high investment risk. The programme should help to reduce the risk capital funds management costs, create the atmosphere of credibility by engagement of public resources as well as to promote the development of a venture capital market.

9. Currently the Polish authorities are running the seed capital support programme approved by the Commission (N 599/2005). However, taking into account that the latter programme focuses only on seed capital and the total amount of state support is limited (EUR 18 Million,) the Polish authorities do not consider it sufficient to stimulate the proper development of a risk capital market.

[1] As defined in Commission Regulation 70/2001 EC on the application of Articles 87 and 88 of the EC Treaty to state aid to small and medium-sized enterprises (OJ L 10 of 13.11.2001, p. 33) and Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises (notified under document number C(2003) 1422; OJ L 124, 20.05.2003, p.36).

*2.4. Beneficiaries of the scheme*

*2.4.1. SMEs*

10. The principle beneficiaries are SMEs up to their expansion stage. Undertakings in difficulty, as defined by the ‘Community guidelines on State aid for rescuing and restructuring firms in difficulty’[2], are excluded from the scope of eligibility.

11. The risk capital funds shall not invest in SMEs active in the following sectors: iron and steel production, coalmining, shipbuilding, financial services including factoring and leasing, tenancy or lease of assets, legal services, accounting services, real estate brokerage and wholesale or retail commerce. SMEs cannot engage in production or trade in weapons, tobacco products, alcoholic beverages or narcotic substances.

12. Financial aid cannot be provided to risk capital funds which will condition their investments on the export activities of the targeted SMEs or their use of domestic in preference to imported goods.

13. The SMEs will operate in the regions eligible for assistance under Article 87 (3) (a) or (c) EC.

*2.4.2. Private investors*

14. Private investors establish risk capital funds in an appropriate legal form (with or without legal personality). Through risk capital funds they participate in the distribution of proceeds from exiting investments on more favourable terms than the National Capital Fund. In case the investment does not provide the agreed level of return, private investors will have a higher chance to regain the contributed capital as well as to obtain the agreed rate of return in comparison with the National Capital Fund.

*2.5. Administration of the scheme*

15. National Capital Fund and the Ministry of Economy.

*2.6. Funding of the scheme*

16. The estimation of the total amount of funding equals EUR 180 million, out of which EUR 153 million will be covered from the resources of the European Regional Development Fund (ERDF) and EUR 27 million from the national budget. This does not include the necessary private contribution.

*2.7. Duration of the scheme*

[2] OJ C 244, 01.10.2004, p.2.

17. The duration of the scheme is from 1 March 2007 until 31 December 2013.

18. The investments and exits from them should be done within 10 years from the investment of National Capital Fund into a risk capital fund. More precisely the period of 10 years starts running from the date of signing the agreement between the National Capital Fund and a risk capital fund concerned. Two extra years can be granted if economic reasons justify it, including, in particular, those related to ensuring the possibility of profitable conclusion of the investment. It has to be stressed at this point that the feasibility of investment strategy presented by a risk capital fund will be one of the crucial points assessed during the selection process.

19. The Polish authorities have confirmed that no state aid can be granted before the decision approving the measure is taken by the European Commission.

### *2.8. The role of the National Capital Fund under the scheme*

20. The National Capital Fund represents the public investor in the scheme. Its revenues constitute state resources, including European funds from the EU budget. The Polish government appoints its representatives in the supervisory board. There are restrictions in place guaranteeing that the persons taking investment decisions on behalf of National Capital Fund are not in any way related to the chosen risk capital funds.

21. The National Capital Fund announces public tenders. The outcome of the tender is published in a nationwide daily and in the Public Information Bulletin.

22. The National Capital Fund grants financial support to private risk capital funds by way of:

- taking up and acquiring their shares or stock;
- participating in risk capital funds operating in the form of limited partnerships, partnerships limited by shares or other organizational units without legal personality;
- acquiring their investment certificates or units of participation;
- acquiring bonds, bonds convertible into shares, privileged bonds or subscription warrants issued by such risk capital funds;
- making non-repayable payments to finance some of the expenses incurred by a risk capital fund to prepare investments and to monitor a portfolio of such investments.

### *2.9. Selection of private risk capital funds*

23. The National Capital fund will choose the best applicant among risk capital funds in a public tender. The offer should contain information concerning, inter alia:

- the organization and legal status of the risk capital fund;
- the date the risk capital fund was created and its expected duration;
- the investment objective and the investment policies of the risk capital fund and a risk analysis;
- the geographic scope and sectors of investment activities pursued by the risk capital fund;
- the size of investment projects and their expected duration and the minimum expected rate of return;
- the expected forms and the expected amounts of financial support, together with the forecast cost of investment preparation and monitoring of the investments portfolio;
- personal data of the persons who have a decisive influence on investment decisions of the risk capital fund, including in particular members of its managing authority or persons handling fund's affairs, together with a description of their qualifications and professional experience;
- the assumed total amount as well as dates and terms of making payments to the risk capital fund by the entities investing in that fund;
- the rights of risk capital fund investors, with a particular focus on their rights to share in the fund's income;
- a marketing plan and intended investments of the risk capital fund;
- previous experience of the risk capital fund managers with regard to investments of innovative as well as research and development enterprises.

24. The National Capital Fund and the risk capital fund selected in the tender enter into an agreement on financial support. The National Capital Fund cannot invest more in a given risk capital fund than the amount of contributions of private investors.

25. The agreement on granting financial support should specify in particular:
    - the effects of non-performance or improper performance of the agreement;
    - the requirements concerning annual reporting on the investments made by the capital fund, as stipulated in the agreement, together with an evaluation of the investments portfolio;
    - the terms of access granted to auditors appointed by the National Capital Fund to the capital fund's books and records;
    - a clear and realistic exit strategy for each investment

### *2.10. Investment decisions*

26. The investment decisions will be taken by the risk capital fund management which has the obligation to use economic criteria with regard to the selection of investment projects, after conducting profitability and investment risk analysis, including, especially, an environmental impact assessment. This all should be done on the basis of a business plan reliably drawn up which will include a detailed product or service analysis and sales and profits prognoses. The managers will observe the principles of limiting investment risk, acting according to best knowledge and best practices in the management of a capital fund. They will be supervised by the National Capital Fund in accordance with the terms of the agreement between the latter and a respective risk capital fund.

27. The remuneration of fund managers consists of two parts. First part is paid on the basis of an agreement between the investor and the fund manager from the administrative expenses of the fund. This remuneration will be dependent on the investment results of the fund. Moreover, there is an additional part of remuneration which is only paid out after payments to private investors and the National Capital Fund are made during the final distribution of proceeds of any investments. Therefore, the fund manager’s remuneration will be linked to the disbursement of the fund resources and the performance of the fund.

28. The fund will be legally prevented from investing in SMEs, the shareholders or stakeholders of which were persons connected with the investor prior to the first investment by family ties, employment or management relationships. The same applies to the relationship between the fund management and a potential investee.

29. Private investors will have influence on decision-making with regard to investments of the risk capital fund. The management of the fund will have to ask for the opinion of the investor's committee. Private investors will be also represented in the supervisory committee of the risk capital fund.

### *2.11. Participation of public and private investors under the scheme*

30. The investments in the SMEs will be at least in 50% financed from the private funds.

31. The public funding cannot exceed 65% of the administrative costs of risk capital funds, including legal advice and management costs.

32. The total value of capital fund management costs, including the value of costs of investment preparation and investment portfolio monitoring, may not exceed 5% of private annual average contributions into the risk capital fund.

### *2.12. Size of investment in target companies under the scheme*

33. The scheme envisages a global limit of investment in a target SME by one or more risk capital funds which receive support from the National Capital Fund. The

investment cannot exceed in total EUR 1.5 million expressed in PLN during the whole existence of the scheme. At the same time each investment in an investee cannot exceed 20% of the total declared value of the risk capital fund.

### *2.13. Profit and losses distribution under the scheme*

34. The resources originating from the sale of investments or other way of withdrawal from the investment by the fund manager, including the repayment or the interest on the debt instruments will be divided as follows:

    - in the first turn, to the investors of the capital fund until the moment of receiving amounts equal to the contributions made;
    - in the second turn, to the National Capital Fund until the moment of receiving an amount equal to the granted financial support;
    - in the third turn, to the investors of the capital fund until the moment of receiving the return rate in an amount specified in the agreement on granting financial support;
    - in the fourth turn, to the National Capital Fund until the moment of receiving the return rate specified in the agreement on granting financial support.

35. The remaining resources will be divided among persons or an entity managing the fund, investors of the fund and the National Capital Fund in accordance with the agreement on granting aid. Therefore, the risk capital fund cannot reinvest the public money without going through new application procedure.

### *2.14. Aid instruments under the scheme*

36. The basic form of investing is the made-for-profit acquisition of newly issued shares of the SMEs. The risk capital fund can also acquire participations in partnerships or other entities having no legal personality, as well as subscribe for debt instruments. The latter can only concern the same undertakings for which shares or participations were acquired.

37. The interest charged on the undertaking's debt instruments subscribed for by the risk capital fund or on loans granted by the capital fund to the undertaking may not be less than the reference rate determined by the European Commission, published in the European Union Official Journal, in force at the date the debt instruments are subscribed for or the loan agreement is concluded. In the case of unsecured debt instruments or unsecured loans, interest may not be less than the reference rate[3] increased by 400 basis points or more, if the Lombard interest rate calculated by the National Bank of Poland, published in the Official Journal of the National Bank of

[3] Commission Notice on the method for setting of the reference and discount rates (97/C 273/03).

Poland, increased by 100 basis points, in force at the date the debt instruments are subscribed for or the loan agreement**, is higher than reference rate**.

38. The debt instruments cannot exceed 30% of the investment in a target SME.

### *2.15. Cumulation of aid under the scheme*

39. Every SME – beneficiary of risk capital aid is obliged to limit by 20% the relevant aid ceilings or maximum eligible amounts of state aid to which it is entitled to during a period of three years from the date when it has received resources from the risk capital fund for the first time. This obligation does not apply to public aid granted on the basis of Community framework concerning state aids for research and development[2)] or any successor framework or block exemption regulation in this field.