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DIRECTORATE - GENERAL
FOR INDUSTRIAL AND
TECHNOLOGICAL AFFAIRS

SMALL AND MEDIUM-SIZED
ENTERPRISES, ARTISANAT DIVISION

1167/III/75 e

NATIONAL REPORTS ON THE

EQUITY FINANCING PROBLEMS OF S.M.E.

February 1976

INTRODUCTION

Financing, and in particular, equity financing is often cited as one of the key problems of small and medium-sized enterprises (S.M.E.).

For this reason the "Small and Medium-sized Enterprises, Artisanat" Working Party, which is composed of national officials, decided to examine the problem of equity financing of S.M.E. and to review the solutions which had been implemented or envisaged in the Member States.

In order to establish a basic documentation the "Small and Medium-sized Enterprises, Artisanat" Division asked the members of the Working Party to prepare a short report on the situation in each Member State on the basis of the attached plan.

Given the general interest of the subject, it has been agreed with the members of the Working Party, to circulate the national reports to all those who are interested in the subject; these reports are gathered together in this document.

For practical reasons it has only been possible to produce the document in English and in French.

SCHEMA FOR NATIONAL PAPERS ON EQUITY FINANCING PROBLEMS OF SMALL AND MEDIUM-SIZED ENTERPRISES (SME's)

1. COMPARISON OF FINANCIAL STRUCTURES OF SME's AND LARGE ENTERPRISES
   - How is typical SME financed?
   - How is typical large enterprise financed?
   - Are there any significant differences between industrial sectors? If so, what are they?

2. SOURCES OF EXTERNAL EQUITY FINANCE FOR SME's
   - What are the main external sources (i.e. other than the original owners) of equity finance?
   - What is the relative importance of private sector and governmental sector sources?
   - What are the minimum requirements for raising equity finance on the Stock Market?
   - How well do existing sources meet the needs of SME's?

3. FISCAL POLICIES
   - What effect does current fiscal policy have on selffinancing, e.g. the retention of profits?
   - Has it been modified to allow for the effect of inflation? If so, in what way?
   - Does fiscal policy have any effect on the raising of capital? If so, in what way?
   - Are there any special provisions for SME's?
   - Are there any special provisions for the different legal forms of business?

4. INITIATIVES TO RESOLVE THE PROBLEM
   - What initiatives have been taken within the past 5 to 10 years? How successful have they been?
   - What new initiatives are currently being examined either within the private or the governmental sector?

NOTE: By equity we understand share capital and retained profits.

By debt we understand bonds, bank loans (either short, medium or long term), trade creditors, bills of exchange, factoring, hire purchase and leasing of equipment, mortgage loans and sale and leaseback of property.

SOURCES

B.R. DEUTSCHLAND	:	Bundesministerium für Wirtschaft
BELGIQUE/BELGIE	:	Ministère des Classes Moyennes Ministerie van Middenstand
DANMARK	:	Handelsministeriet
FRANCE	:	Ministère de l'Industrie et de la Recherche
IRELAND	:	Department of Industry and Commerce
ITALIA	:	Ministero dell'Industria, del Commercio et dell'Artigianato
G.D. de LUXEMBOURG	:	Ministère de l'Economie Nationale
NEDERLAND	:	Ministerie van Economische Zaken
UNITED KINGDOM	:	Department of Industry

NOTE ON PROBLEMS ARISING IN THE FEDERAL REPUBLIC OF GERMANY IN CONNECTION WITH THE EQUITY FINANCING OF SMALL AND MEDIUM-SIZED ENTERPRISES (S.M.E.)

1. COMPARISION

- As a general rule, typical S.M.E. prefer the self-financing method.
- Usually, large firms are joint stock companies (Kapitalgesellschaften) and finance themselves on the capital market (shares).
- There are no significant differences in financing from one branch of the economy to another.

2. SOURCES

- Share purchase (admission of new partners) is the major source of external equity financing for S.M.E. Partners may be either active or sleeping. The latter merely contributes to the firm's capital, either through a "silent" interest or by taking over a limited partner's share. Financing through active participation in general or limited partnerships is far more usual than silent partnership.

Equity investment companies have been involved in financing S.M.E. in recent years.

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The impact of this is still rather insignificant, however, as there are serious difficulties preventing more intensive expansion (fear of loss of independence on one side, high investment risk on the other).

- Equity financing is obtained chiefly from private sources: e.g. banks, finance institutions, private individuals. On grounds of orderly management, the state pursues a policy of restraint. It does, however, promote the equity financing of S.M.E. through private companies by providing equity guarantees and counter securities, as it regards this as an effective way of assisting S.M.E. to help themselves.

- The minimum requirements for setting up a joint-stock company (Aktiengesellschaft) are as follows (Companies' Law of 6 September 1965):

  - Five individuals as founders.
  - Recording and authentication of the articles of association by court or notary.
  - Registration and publication in the commercial register.
  - Shareholders' investments (minimum face value of share: DM 50) may be in cash (cash subscription) or in other assets (non-cash contribution).
  - Minimum registered capital: DM 100,000
  - Organization: Board of Management, Supervisory Board, Shareholders' General Meeting.
  - The Board of Management (one or more individuals), which is appointed for a maximum of five years by the Supervisory Board, draws up the annual statement of accounts and issues an annual report.
  - The annual statement of accounts (balance sheet) must be audited by independent auditors.
  - In joint-stock companies (Aktiengesellschaften) covered by the 1951 Iron and Steel Co-management Law there is <u>joint</u> co-management.

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Joint stock companies (Aktiengesellschaften) are allowed to trade on a stock exchange at the discretion of the governing body of the exchange in question in accordance with the exchange's regulations. (There are stock exchanges in Frankfurt am Main, Munich, Düsseldorf, Stuttgart, Hamburg and Berlin). Admission is by application only. Almost without exception, only the shares of the major public companies are negotiated on the stock exchanges in Germany.

- Basically, the sources of financing available meet the needs of S.M.E., i.e., the supply of capital is adequate to satisfy demand. Difficulties, such as there are, stem from the S.M.E's special methods of financing. There is often a spasmodic need for major, new investments which cannot be financed out of their otherwise adequate reserves. However, the capital market is generally inaccessible to S.M.E. because they are too small.

3. FISCAL POLICY

For the development of equity capital business circles are continually asking for tax concessions in the form of either a partial exemption of retained profits (investment reserve), or better tax reliefs to be granted for investments (depreciation allowances). The Government has rejected such requests so far, as it regards them as a breach of the principle of equality of fiscal treatment and subsidies, possibly leading to misinvestments not justified by the needs of the market.

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- For several years after 1948, specific fiscal measures were introduced to promote self-financing and stimulate the rebuilding of the economy, as the capital market and the supply of credit were either inadequate or non-existent. This is no longer the case (see above).

  Because of the rise in prices (monetary depreciation), low and average-income earners have moved higher up the tax scale (without enjoying a corresponding increase in real purchasing power). The chief aim of the tax reform which came into force on 1 January 1975 was to offset this.

- There are no special provisions for S.M.E. (see also paragraph 4).

- Basically, the principle of equality of fiscal treatment applies to the various legal forms of enterprises. However, mention should be made of the problem of double taxation of joint-stock companies (Kapitalgesellschaften) (corporation tax not set against the income tax which the shareholders pay on their distributed profits).

4. STEPS TAKEN TO SOLVE THE PROBLEM

   - Provision has been made in income tax legislation for profits from the sale of certain business assets not to be taxed if they are ploughed back into the business within a certain period. This is intended to mobilize idle assets and convert them into active working capital. This is not intended to increase working capital as such but to improve capital structure and make it more efficient and hence mitigate the shortage of equity capital. It can be assumed that S.M.E. have benefited from this arrangement.

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- As mentioned above, the Government has assisted private equity investment companies in an attempt to solve the problem of equity financing. For the reasons already given, this source of financing was not very successful at first, but seems to have been in greater demand recently.

- The private sector (associations of S.M.E.) is requesting the following concessions:

  • Tax-free investment reserves through which S.M.E. can save up their own capital for the purpose of investment (problem of spurts in investment by S.M.E.).

  • "Carry-back" system to supplement the "loss brought forward" system provided for in the Income Tax Law (see also paragraph 3).

REPORT BY THE BELGIAN DELEGATION ON THE FINANCING OF SMALL AND MEDIUM-SIZED ENTERPRISES (SME)

1) COMPARISON OF THE FINANCIAL STRUCTURES OF SME AND OF LARGE ENTERPRISES

Generally speaking SME have to raise their capital from among the members of the family forming the enterprise. However, the proportion of people with large fortunes prepared to take risks in the hope of eventual profits has greatly decreased, while there has been an increase in the number of those with smaller incomes seeking security and liquidity for their investments, and regular returns on their money rather than a large profit. This makes them prefer fixed-income investments, particularly in the form of savings deposits.

The share market is also unfavourably influenced by this state of affairs. But SME have virtually no access to the capital market. Owing to its operational and institutional shortcomings, this market is not very attractive for new businesses seeking to launch themselves independently of existing companies or groups; this is hardly an encouragement to the larger of the medium-sized enterprises to make the necessary effort to transform themselves into large companies which raise capital by calling on the savings of the public.

Chief among the operational shortcomings are the narrowness of the market and the existence of dominant positions, particularly where the demand for capital is concerned. The small number of Belgian securities admitted to quotation on stock exchanges in the last few years, despite the growth of a large number of companies of long standing and the setting up of many new enterprises, is symptomatic of the situation. Each stock exchange has a Quotation Committee ("Comité de la cote") which examines applications and assesses whether or not a company should be admitted to or struck from the list of quotations (Chapter II, section V of Title V of the Code de commerce).

As regards the institutions, before 1935 mixed banks ("banques mixtes") played an important role in financing enterprises in Belgium; they made loans to viable enterprises and then took shareholdings which were put in the banks' portfolio or placed on the market with, in the latter case, implicit backing from the bank, which had closely followed the enterprise's progress. Generally, once the operation had been completed and the profitability of the business was ensured, these banks, known as merchant banks ("banques d'affaires"), placed on the market a large proportion, if not all of their shareholdings, thus freeing capital to allow them to assist others.

These mixed banks therefore acted as a link between enterprises in search of funds and savers. There was no doubt as to their usefulness in this respect. However, the particularly severe crisis of 1930 led the Belgian Government to prohibit mixed banks. In 1934 they were split up and became respectively deposit banks, which are strictly prohibited from taking out shareholdings in industry, and holding companies, which developed a tendency to establish permanent control over their subsidiaries rather than seek a real turnover of their shareholdings.

As a result, Belgium unfortunately has no bodies similar to the "investment banks" to be found in English-speaking countries.

In its reports of May 1962 and December 1967, the Government Commission on the problems of financing economic expansion ("Commission gouvernementale pour l'Etude des problèmes de Financement de l'Expansion économique"), known as the De Voghel Commission, admitted the usefulness of - and even the need for - some relxation of current banking regulations, provided, however, that one important problem was settled, namely the real independence of banks from holding companies.

In the meantime, faced with the growing need for plant and machinery generated by the intensive mechanization of industrial enterprises, and since self-financing did not provide enough equity, there was a widespread tendency for enterprises in Belgium to seek external financing. However, this appreciable expansion of long- and medium-term industrial lending which occurred at the same time as the decline in the role of equity as a means of financing fixed capital investment - continues to have an adverse effect on the solvency ratio of enterprises.

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Studies carried out in Belgium have shown that, for industry as a whole, the medium- and long-term solvency ratio curves are close to the maximum borrowing limit of 50/50. The country's financial authorities, which remain faithful to the principles of sound financial management, cannot be indifferent to this finding, particularly during periods of economic recession. The abovementioned De Voghel Commission has already stressed the point. The effects of all the credit facilities granted under the laws to encourage economic expansion would be wiped out unless equity is boosted, thus leading to stabilization of the medium- and long-term solvency ratio.

It is nevertheless true that the Belgian Government's policy on credit for the SME is entirely concentrated, as the title of the Law of 24 May 1959 itself suggests, on extending access to special credit for small business and the self-employed. This Law set up a Guarantee Fund and the Minister for Small Business and the Self-Employed ("Ministre des Classes moyennes") may, in cases which he feels are particularly worthwhile, especially from a social angle, authorize the Fund Committee to extend the Fund's guarantee beyond the limits laid down in existing rules and directives and, if necessary, cover the entire risk. Otherwise, the Fund guarantee may be granted only if the applicant provides real or personal guarantees in respect of part of the sum borrowed.

The credit institutions specially approved for this purpose have the power to decide directly on the granting of the Fund's guarantee provided a number of conditions are met, notably that the borrower's own funds are equivalent to at least 50% of the sum of his medium- and long-term borrowing and the credit requested... The limit is 25% for borrowers under 35 years of age. In any event, unless prior exemption is granted by the Minister for Small Business and the Self-Employed, the Fund guarantee to cover the risk of credit institutions may not exceed 95% of the debit balance outstanding after realization of the guarantees and exhaustion, in the Fund Committee's view, of all rights of recourse against the debtor's assets.

Moreover, pursuant to Section 9 of the Economic Expansion Law of 30 December 1970, interest rate reductions granted by the Government may be replaced, in whole or in part, by an outright capital grant of equivalent value to the extent that the scheme assisted is financed from the enterprise's own capital.

On 31 July 1975, the above provision was made applicable to the SME in Wallonia: future investments in Walloon development areas involving at least 50% of own funds will qualify for a capital grant. This system enables businesses to qualify for State aid without first having to seek a loan.

Nevertheless it should be noted that industry already finances most of its investments from its own resources and therefore, without the help of the capital market (issuing bonds, floating loans, taking up credits, receiving advances, etc.). Between 1968 and 1971 industry in Flanders and Wallonia financed almost two-thirds of its investments from its own resources. In Brussels this proportion was as high as 76%. In 1974 Bfrs 72,000 million of the additional capital invested in firms came from their own resources, as against only Bfrs 46,000 million from other sources. There are large variations in the ratio of investments financed from company resources to those financed from the long-term capital market when such long-term borrowing is analysed by sub-regions and industrial sectors[1].

2) SOURCES OF EXTERNAL EQUITY FINANCE FOR SME

In addition to self-financing, there is the capital injected through share purchases by other enterprises when the capital is increased. At the moment there are virtually no injections of capital from the family of the head of a business.

Large companies can issue additional shares with or without rights. Investment trusts (sociétés de placement) may invest in these issues as might holding companies (sociétés à portefeuille); but the latter are interested in gaining control rather than simply spreading the risks. They only look for enterprises that are already well established and have a good profit-earning record. In both cases, this desire for security and profitability of investments discourage them from promoting new ventures, which obviously present much greater risks in an economy already near saturation point.

[1] See table in Annex 1.

On the other hand, the Société nationale d'Investissement (SNI) and its subsidiaries, the "sociétés régionales" set up under the Law of 2 April 1962, are particularly involved in helping to finance industrial or commercial ventures by providing true risk capital without undermining the independence of the enterprises financed. The SNI is a "public interest" company in which only the Belgian Government and "public interest" financial institutions may hold shares. However it has taken the form of a limited liability company (société anonyme) for all aspects not governed by or pursuant to the Law and the articles of association approved in the latter. Generally speaking, the SNI is subject to the rules governing commercial companies as its activities are regarded as being of a commercial nature.

The task of the SNI is to promote, in the interests of the Belgian economy, the establishment, reorganization or extension of private-sector enterprises in the form of private or public limited companies or cooperative societies approved by the Conseil national de la Coopération. It also acts as a public holding company with powers to set up on its own account or help with the setting up of commercial companies, acquire holdings and interests in such companies and help to manage them........

Normally, the SNI may not acquire shares forming part of the capital of existing companies in which it does not already have an interest until it has consulted the board of the company concerned. If it is a matter of acquiring or increasing a holding as part of the functions assigned to the SNI, the latter must obtain the prior and explicit approval of the board of the company concerned. Holdings acquired by the SNI in this way are temporary unless the board has taken a decision to the contrary.

In its role as a public holding company the SNI must, in respect of certain projects, consult an Investment Committee, the members of which are appointed by the SNI Board from a dual list of candidates presented jointly by those organizations most representative of the employers' interests and by the Conseil supérieur des Classes moyennes (National Council representing small business and the self-employed). Should this Committee reject a project, it may be necessary to obtain the prior authorization of the Cabinet before going ahead with it.

It was chiefly the SNI's role as a public holding company which was affected by the changes to the basic Law of 2 April 1962 (setting up the SNI) made in the Law of 30 March 1976 relating to the organization of public sector economic initiatives. The new law gave the SNI authority to increase its capital to Bfrs 9,000 million with Government guarantees. The private sector, which had previously held some 10% of the share capital, no longer has a holding so that the SNI has ceased to be a part publicly, part privately owned company.

The turnover of investments made by the SNI has proved to be fairly slow. Experience has shown that, as a rule, heads of enterprises which have received assistance from the SNI, far from being in a position to buy back the holding must in many cases seek additional capital either to maintain expansion or to finance takeovers. Shares held by the SNI can be offered to the public and admitted to quotation on a stock exchange with the approval of the parties concerned only in the case of fairly large enterprises which have achieved a fairly high and steady level of profitability and provided market conditions are favourable.

From its formation until 30 September 1975, the SNI decided to engage in 275 operations involving 176 different companies at a total cost of Bfrs 8,540.8 million. 261 of these operations were implemented, involving a total of Bfrs 6,921.8 million invested in 166 different enterprises. During the same period, the SNI relinquished, in full or in part, holdings in 64 different enterprises. The total amount involved was Bfrs 847.1 million, with capital gains over the book value totalling Bfrs 179.6 million.

These results were achieved despite the fact that 57% of all the investments made were in new or recently-formed enterprises, i.e., in schemes under which it takes quite sometime until holdings can be relinquished on normal financial terms.

In addition, because of its "public interest" role the SNI has invested large sums in SME in spite of the risks attached and the particularly high cost of this policy. In 1974, it was estimated that 50% of the enterprises financed by the SNI employed fewer than 75 workers, although this percentage has tended to decrease more recently. During the accounting year 1973/74, 45% of the total workforce of firms financed by the SNI were employed in enterprises with a labour force of less than 100 and 75% in enterprises employing fewer than 300. In 1974/75, the first figure had fallen to 43% while the second remained unchanged.

	1973/74	1974/75
Enterprises employing[1]	Percentage of total workforce	Percentage of total workforce
Fewer than 50	27.5%	25.6%
Between 50 and 100	17.5%	17.1%
Between 100 and 200	18.8%	19.5%
Between 200 and 300	11.2%	13.4%
Between 300 and 400	7.6%	8.5%
Between 400 and 500	6.2%	4.9%
More than 500 persons	11.2%	11.0%
	100.-%	100.-%

Looking at the SNI's investments from the point of view of the turnover of the firms assisted, the proportion of enterprises with a turnover of more than Bfrs 500 million has increased by over 10% in recent years while there has been a drop of the same size in the proportion of firms with a turnover of less than Bfrs 50 million. This trend towards enterprises with a higher turnover is due to a number of factors: an expansion of sales made possible largely by SNI assistance,

[1] The table does not include newly launched enterprises not yet able to offer marketable goods or services nor enterprises in which the SNI holds less than 2% of the capital.

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inflationary price rises, greater SNI involvement in major capital-intensive projects of public and regional value

Annual turnover in Bfrs million[1]	1972/73 Percentage of number of enterprises	1972/73 Percentage of capital invested by SNI	1973/74 Percentage of number of enterprises	1973/74 Percentage of capital invested by SNI	1974/75 Percentage of number of enterprises	1974/75 Percentage of capital invested by SNI
Less than 50	32.9	23.8	20.5	22.4	22.1	11.9
Between 50 and 100	9.2	2.5	14.1	8.9	11.6	8.7
Between 100 and 200	23.7	13.3	29.5	14.7	20.9	11.2
Between 200 and 300	13.2	7.3	10.2	7.5	14.0	16.6
Between 300 and 400	6.6	21.4	9.0	9.1	5.8	4.4
Between 400 and 500	2.6	1.1	3.9	4.9	5.8	3.3
More than 500	11.8	30.6	12.8	32.5	19.8	43.9
	100.-	100.-	100.-	100.-	100.-	100.-

It would appear, however, that the recent changes to the institution made in 1976 are unlikely to affect the SNI's policy towards SME. They should be seen rather as a consequence of the end of the boom. However, in order to extend its operations even further, to spread the risks and make its operations more effective, the SNI has established links with various types of organizations. Under this policy, which it has been following for a number of years, the SNI has assisted in the setting up of specialized investment and financing undertakings. For example, together with the Compagnie Bruxelles-Lambert as an equal partner it set up a company specializing in the financing of firms and in particular SME. Similarly, it has participated in establishing specialist leasing companies such as Fininvest (for leasing industrial and commercial premises and machinery) and Infibel (for leasing industrial installations and computers). Still with the same objectives in mind, the SNI acquired

[1] The table does not include newly launched enterprises not yet able to offer marketable goods or services nor enterprises in which the SNI holds less than 2% of the capital.

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an interest in S.A. IBEL, which was engaged mainly in sea, road and river transport and in port activities, and also acquired, through N.V. VIBEM (an associated company), an indirect stake in Gevaert Photo-Producten N.V. and MERCATOR S.A., an insurance company.

3) FISCAL POLICY

As fiscal policy is the responsibility of the Department of Finance this report makes only a few comments on points within its specific scope.

(i) First it should be stressed that there are no taxation provisions granting SME special treatment to help them compete on the market.

(ii) Following the Law of 25 June 1973 which, amongst other things, reformed the corporation tax system, there is no longer any distinction between rates of taxation for distributed and undistributed profits. (The rate is lower when taxable profits amount to less than Bfrs 3 million).

However, distributed profits are again taxed with a few adjustments (practically at half rate) in the hands of recipients.

Where the profits of an industrial, commercial or agricultural undertaking are taxed under personal income tax arrangements, there is no speecial tax system for undistributed profits. Only the capital gains resulting from the realization of assets may qualify for a lower rate of tax.

(iii) Asset revaluation, particularly during a period of inflation, does not benefit from tax exemption except in the case of capital gains obtained or recorded when one or more new activities were brought into an existing company or into a company to be established in Belgium, subject to this contribution being remunerated solely in shares or "parts" representing corporate rights.

(iv) Finally, the pressure exercised on incomes from industrial and commercial activities, particularly the increase in corporation tax, has a very discouraging effect on portfolio investment and other risk investments in industry.

On the other hand, under the economic expansion laws, temporary exemption from the property tax (précompte immobilier) may be granted not only in the case of investment financed from own funds, but also in the case of investment financed from borrowed funds. This exemption applies even to investments in immovable property made by enterprises employing fewer than 100 workers and receiving aid under the Law of 24 May 1959. It should be noted that the period of exemption is extended from two to four years if 5% of the investment is self-financed although the two-year limit still applies if the investment is located outside development areas in which case there would normally be no exemption.

The Economic Expansion Law of 30 December 1970 also exempts any contributions of assets to companies having legal personality from the proportional registration tax if these contributions (at least Bfrs 3 million) are for investments which help to create new activities and new jobs (at least 10) in development areas.

Furthermore, following the adoption of the Law of 29 June 1975, the profits of any enterprise (except financial and similar establishments) are exempted from taxes in respect of 15% of additional funds invested in immovable property and business equipment in Belgium between 1 July 1975 and 31 December 1975 and, pursuant to Section 56 of the Law of 30 March 1976 concerning economic recovery measures, the tax exemption provided for in the Law of 29 June 1975 is extended to profits for the 1976 taxation year or, for taxpayers whose accounts do not coincide with the civil year, for the first accounting year ending after 30 June 1976, when these profits have been used to make additional investments in Belgium between 1 January and 30 June 1976 inclusive.

The same Economic Recovery Law of 30 March 1976 also set up a Solidarity Fund financed in part by an exceptional and a temporary levy on companies, associations, establishments or bodies subject to corporation tax or the tax on non-residents. However, if the taxpayer can prove that he has made investments in tangible or intangible assets in his enterprise in Belgium during 1976 of more than 110% of the average of his profits over the period 1972 to 1974 inclusive, the rate of the temporary special solidarity levy is automatically reduced by the margin by which investment exceeds the abovementioned figure.

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STATISTIQUE ANNUELLE DES INVESTISSEMENTS INDUSTRIELS
Etablissements en activité occupant 20 personnes ou plus
ANNEE 1974 - Valeur (en 1 000 F) - Chiffres provisoires

INDUSTRIES	I. Augmentation du capital investi (T.V.A. déductible exclue)						
	Machines, installations et véhicules, neufs et usagés		Construction de bâtiments et d'autres ouvrages	Achats d'immeubles, de bâtiments existants et de terrains bâtis et non bâtis		Total	Investissements sociaux (1)
	Total	dont véhicules pour les transports à l'extérieur		Total	dont terrains non bâtis		
Industries extractives							
Houillères et leurs centrales électriques, cokeries indépendantes et minières, fabriques d'agglomérés de houille	229 870	4 620	84 230 (3)		..	314 100	..
Minières, carrières, industries connexes et exploitation de terrils	1 054 943	105 499	200 182	123 664	107 387	1 378 789	6 845
Total							
Industries alimentaires et des boissons							
Fabriques de conserves de légumes, confitureries et siroperies	277 681	16 522	83 609 (3)		..	361 290	..
Industrie laitière	839 563	118 934	446 156	21 695	6 398	1 307 414	7 217
Industrie du travail des grains	359 366	18 745	27 683	22 781 (3)	..	409 836	..
Boulangeries, boulangeries-pâtisseries, pâtisseries	89 986	27 105	25 562	7 816 (3)	-	123 364	..
Industrie des biscuits, biscottes et pains d'épice	204 896	15 037	35 015	4 778 (3)	..	244 689	..
Sucreries, raffineries de sucre et fabriques de sucre inverti	1 216 979	15 355	244 914	13 078	6 672	1 474 971	6 456
Industrie du chocolat et de la confiserie	257 343	34 747	28 678	23 022 (3)	..	309 043	..
Fabrication d'aliments composés pour animaux	557 309	83 122	267 172	16 224	3 014	840 705	4 117
Brasseries, brasseries-malteries, malteries	2 112 583	150 549	741 837	289 720	719	3 144 140	7 177
Autres industries des boissons	443 565	38 344	90 053	39 398	15 906	573 016	2 710
Autres industries alimentaires	1 322 500	175 313	365 971	66 792	15 812	1 755 263	11 555
Total							
Industrie du tabac	***396 669***	***19 378***	***177 646***		..	***574 315***	***7 883***
Industries chimiques							
Industrie chimique proprement dite	8 471 079	155 778	1 307 630	436 518	208 039	10 215 227	70 649
Industrie du savon, des détergents de synthèse, des produits d'entretien, des parfums et produits de beauté	579 007	19 980	552 984	192 141 (3)	..	1 324 132	..
Industrie des produits pharmaceutiques	565 037	31 084	371 282	83 259	15 625	1 019 578	36 961
Total							
Industrie du caoutchouc	***420 667***	***18 555***	***60 908***	***12 120 (3)***	..	***493 695***	..
Industrie du bois et du liège	***1 847 163***	***307 618***	***607 394***	***170 085***	***57 308***	***2 624 642***	***38 484***
Industrie du papier							
Production du papier et du carton	1 450 064	22 110	221 354	103 966	..	1 775 384	4 727
Transformation du papier et du carton	677 078	39 843	199 240	71 332	10 854	947 650	7 633
Total							
Industrie de l'impression	***1 222 098***	***53 750***	***544 047***	***58 046***	***16 083***	***1 825 190***	***42 390***
Industrie des cuirs et peaux	***64 029***	***5 656***	***42 568 (3)***		..	***106 597***	..

(1) Les investissements sociaux ne constituent qu'une indication étant donné qu'il n'est pas toujours possible de tracer une limite exacte entre ces investissements et les investissements productifs.
(2) Valeur des ventes, des démolitions, des destructions et des désaffectations.
(3) Y compris les investissements sociaux.

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Total général	II. Réduction du capital investi (T.V.A. exclue) (2)	III. Amortissements pour l'ensemble du capital investi — Matériel et outillage	III. — Bâtiments et autres constructions	III. — Total	IV. Financement des investissements — Par les ressources propres des entreprises	IV. — Par des ressources autres que celles des entreprises	INDUSTRIES
							Industries extractives
[illegible] 100	139 203	1 155 481	285 940	1 441 421	169 788	144 312	Houillères et leurs centrales électriques, cokeries indépendantes et minières, fabriques d'agglomérés de houille
1 [illegible] 634	173 524	849 056	226 817	1 075 873	1 045 919	339 715	Minières, carrières, industries connexes et exploitation de terrils
[illegible]	*312 727*	*2 004 537*	*512 757*	*2 517 294*			*Total*
							Industries alimentaires et des boissons
[illegible] 200	24 533	204 495	30 591	235 086	183 872	177 418	Fabriques de conserves de légumes, confitureries et siroperies
[illegible] 631	80 841	562 604	104 114	666 718	931 519	383 112	Industrie laitière
[illegible] 836	27 462	303 078	39 860	342 938	..	..	Industrie du travail des grains
[illegible] 364	18 399	77 773	15 766	93 539	85 751	37 613	Boulangeries, boulangeries-pâtisseries, pâtisseries
[illegible] 689	7 944	102 838	15 972	118 810	109 879	134 810	Industrie des biscuits, biscottes et pains d'épice
1 [illegible] 427	76 127	671 795	118 841	790 636	..	..	Sucreries, raffineries de sucre et fabriques de sucre inverti
[illegible] 043	54 120	165 164	69 609	234 773	204 746	104 297	Industrie du chocolat et de la confiserie
[illegible] 822	53 792	375 149	126 468	501 617	510 520	334 302	Fabrication d'aliments composés pour animaux
1 [illegible] 317	252 327	1 351 077	379 825	1 730 902	2 087 553	1 063 764	Brasseries, brasseries-malteries, malteries
[illegible] 726	95 345	366 766	52 001	418 767	483 053	92 673	Autres industries des boissons
1 [illegible] 818	163 736	807 590	188 845	996 435	1 154 036	812 782	Autres industries alimentaires
[illegible] 263	*854 626*	*4 988 329*	*1 141 892*	*6 130 221*			*Total*
[illegible] 098	*86 847*	*190 706*	*94 683*	*285 329*	*459 378*	*132 720*	*Industrie du tabac*
							Industries chimiques
[illegible] 876	1 021 109	10 582 556	1 299 087	11 881 643	7 643 063	2 642 813	Industrie chimique proprement dite
[illegible] 132	27 481	220 438	100 955	321 393	525 541	798 591	Industrie du savon, des détergents de synthèse, des produits d'entretien, des parfums et produits de beauté
[illegible] 539	35 716	366 014	173 285	539 299	715 584	840 955	Industrie des produits pharmaceutiques
[illegible] 547	*1 084 306*	*11 169 008*	*1 573 327*	*12 742 335*			*Total*
[illegible] 696	*40 281*	*300 009*	*64 158*	*364 167*	..	..	*Industrie du caoutchouc*
[illegible] 128	*134 768*	*1 285 323*	*280 398*	*1 565 721*	*1 569 848*	*1 087 278*	*Industrie du bois et du liège*
							Industrie du papier
1 [illegible] 106	183 231	1 357 781	177 366	1 535 147	1 061 082	719 024	Production du papier et du carton
[illegible] 290	160 920	653 544	149 356	802 900	619 880	335 410	Transformation du papier et du carton
[illegible]	*344 151*	*2 011 325*	*326 722*	*2 338 047*			*Total*
[illegible] 880	*147 202*	*881 219*	*210 262*	*1 091 478*	*774 673*	*1 092 907*	*Industrie de l'impression*
[illegible] 507	*10 631*	*62 395*	*18 831*	*81 226*	*64 310*	*22 387*	*Industrie des cuirs et peaux*

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INDUSTRIES	I. Augmentation du capital investi (T.V.A. déductible exclue)						
	Machines, installations et véhicules, neufs et usagés		Construction de bâtiments et d'autres ouvrages	Achats d'immeubles, de bâtiments existants et de terrains bâtis et non bâtis		Total	Investissements sociaux (1)
	Total	dont véhicules pour les transports à l'extérieur		Total	dont terrains non bâtis		
Industrie textile (4)							
Préparation des matières textiles	184 612	22 356	45 499 (3)		..	230 111	..
Filatures (5)	1 076 072	13 614	189 322	46 383	4 527	1 311 777	7 5[illegible]
Tissage	2 395 933	57 327	721 760	52 236	12 140	3 169 92[illegible]	25 0[illegible]
Achèvement à façon de produits textiles	395 472	9 521	65 013	71 804	53 568	532 289	2 40[illegible]
Fabrication de matières textiles diverses	205 901	8 411	80 598 (3)		..	286 49[illegible]	..
Industrie de la bonneterie	240 747	11 625	33 579	5 675	-	280 001	73[illegible]
Total							
Industrie de l'habillement							
Industrie du vêtement et de la confection	485 661	67 056	184 346	98 754	18 960	768 761	7 69[illegible]
Industrie de la chaussure et de la pantoufle	56 594	4 127	6 867		-	63 461	[illegible]
Total							
Industrie du raffinage du pétrole	*1 174 294*	*11 989*	*4 356 271 (3)*	-	-	*5 520 665*	..
Industrie des minéraux non métalliques							
Industrie de la terre cuite	407 166	43 293	148 964	37 080	33 590	591 710	1 [illegible]
Industries céramiques	459 360	3 729	101 620	19 584	2 897	580 564	2 30[illegible]
Verre (production, transformation et façonnage)	1 993.439	17 856	690 523	14 280	..	2 698 242	3 [illegible]
Industrie du ciment	1 460 579	7 029	192 107 (3)		9 189	1 652 696	..
Industries des agglomérés de ciment et des produits en asbeste-ciment	657 313	95 976	165 567	63 766	7 333	886 646	6 [illegible]
Total							
Industries métallurgiques							
Sidérurgie	13 221 842	112 914	2 456 026	129 156	66 688	15 807 024	85 [illegible]
Industrie des métaux non ferreux (établissements producteurs et transformateurs)	2 684 776	20 770	679 575		..	3 364 351	32 [illegible]
Industrie des fabrications métalliques	13 483 054	837 494	5 086 641	883 471	202 026	19 453 166	309 [illegible]
Total							
Industrie de la transformation des matières plastiques	*1 334 224*	*38 805*	*437 029*	*64 666*	*33 463*	*1 835 919*	*15 [illegible]*
Industries manufacturières n.d.a.	*1 178 387*	*259 889*	*96 667*	*41 082*	*10 951*	*1 316 136*	*[illegible]*
Industrie de la construction (6)	*5 058 816*	*1 323 861*	*756 377*	*231 395*	*90 117*	*6 043 687*	*14 [illegible]*
Electricité, gaz, eau							
Electricité (sauf autoproduction) (7)	6 681 704	81 644	9 366 261	111 409 (3)	44 660	16 159 374	..
Industrie du transport et de la distribution publique du gaz	667 905	16 230	2 705 467	27 839 (3)	..	3 401 211	..
Production et distribution de chaleur et de vapeur	54 570	420	698	-	-	55 2[illegible]	-
Industrie de l'eau	158 261	33 380	3 004 446	52 083 (3)	..	3 212 79[illegible]	..
Total							
Total général	*80 371 156*	*4 275 856*	*38 018 334 (8)*	*3 868 324 (8)*	*1 303 981 (8)*	*122 257 814 (8)*	*[illegible] (8)*

(1) Les investissements sociaux ne constituent qu'une indication étant donné qu'il n'est pas toujours possible de tracer une limite exacte entre ces investissements et les investissements productifs.
(2) Valeur des ventes, des démolitions, des destructions et des désaffectations.
(3) Y compris les investissements sociaux.
(4) A l'exclusion de la fabrication de fils et fibres artificiels et synthétiques reprise dans les industries manufacturières n.d.a.

Total général	II. Réduction du capital investi (T.V.A. exclue) (2)	III. Amortissements pour l'ensemble du capital investi — Matériel et outillage	III. — Bâtiments et autres constructions	III. — Total	IV. Financement des investissements — Par les ressources propres des entreprises	IV. — Par des ressources autres que celles des entreprises	INDUSTRIES
							Industrie textile (4)
230 111	25 250	97 161	9 212	106 373	183 862	46 249	Préparation des matières textiles
1 319 342	269 671	806 678	162 088	968 766	923 203	396 139	Filatures (5)
1 194 964	435 056	1 528 928	270 039	1 798 967	2 202 727	992 237	Tissage
534 692	22 765	329 044	43 893	372 937	347 469	187 223	Achèvement à façon de produits textiles
286 499	49 795	130 120	37 375	167 495	204 584	81 915	Fabrication de matières textiles diverses
280 739	25 768	272 088	32 759	304 847	175 100	105 839	Industrie de la bonneterie
[illegible] 446 347	*828 305*	*3 164 019*	*556 366*	*3 719 385*			*Total*
							Industrie de l'habillement
[illegible]76 460	88 401	445 798	162 091	607 889	517 369	259 091	Industrie du vêtement et de la confection
[illegible]4 147	12 882	45 378	6 772	52 150	53 601	10 546	Industrie de la chaussure et de la pantoufle
[illegible] 607	*101 [illegible]*	*491 176*	*168 843*	*660 039*			*Total*
[illegible] 439 565	*347 455*	*1 452 174*	*1 592 523*	*3 044 697*	..	..	*Industrie du raffinage du pétrole*
							Industrie des minéraux non métalliques
592 850	74 789	335 298	100 925	436 223	436 995	155 855	Industrie de la terre cuite
583 067	19 932	191 463	50 720	242 183	270 368	312 699	Industries céramiques
[illegible] 792 113	167 395	887 692	218 963	1 106 655	853 735	1 848 378	Verre (production, transformation et façonnage)
[illegible] 452 686	32 308	768 904	79 659	848 563	965 120	687 566	Industrie du ciment
[illegible]93 465	65 800	638 593	109 626	748 219	651 452	242 013	Industries des agglomérés de ciment et des produits en asbeste-ciment
[illegible] 424 181	*360 324*	*2 821 950*	*559 893*	*3 381 843*			*Total*
							Industries métallurgiques
[illegible] 132 680	544 907	15 622 848	1 971 061	17 593 909	14 011 083	1 881 597	Sidérurgie
[illegible] 337 703	244 657	1 538 362	244 824	1 783 186	1 923 535	1 473 668	Industrie des métaux non ferreux (établissements producteurs et transformateurs)
[illegible] 752 538	1 264 873	9 467 582	3 134 619	12 602 201	13 661 768	8 100 772	Industrie des fabrications métalliques
[illegible] 222 421	*2 054 437*	*26 628 792*	*5 350 504*	*31 979 296*			*Total*
[illegible] 481 656	*124 949*	*1 001 896*	*193 439*	*1 195 335*	*1 216 617*	*634 938*	*Industrie de la transformation des matières plastiques*
[illegible] 311 421	*251 966*	*840 480*	*119 106*	*959 586*	*822 041*	*398 880*	*Industries manufacturières n.d.a.*
[illegible] 058 056	*1 100 176*	*4 166 608*	*212 555*	*4 379 003*	*4 231 341*	*1 826 816*	*Industrie de la construction (6)*
							Electricité, gaz, eau
[illegible] 159 374	820 851	2 956 740	2 944 415	5 901 155	6 965 267	9 194 107	Electricité (sauf autoproduction) (7)
[illegible] 431 211	257 524	297 102	1 138 297	1 435 399	1 830 905	1 570 216	Industrie du transport et de la distribution publique du gaz
55 268	691	45 121	9 671	54 792	38 915	18 353	Production et distribution de chaleur et de vapeur
[illegible] 212 790	28 103	131 920	507 792	639 712	345 748	2 867 042	Industrie de l'eau
[illegible] 643	*1 107 169*	*3 430 883*	*4 600 175*	*8 031 058*			*Total*
[illegible] 144 632	*9 891 601*	*66 890 729*	*17 575 285*	*84 466 014*	*76 984 813 (8)*	*48 180 319 (8)*	*Total général*

(4) Y compris l'industrie de la filterie.
(5) Y compris le montage de constructions métalliques.
(6) Non compris les investissements de la société d'énergie nucléaire franco-belge des Ardennes (SENA).
(7) Les totaux généraux comprennent les renseignements confidentiels qui n'ont pas été publiés pour certaines activités ou qui ont été regroupés avec d'autres données.

Tableau 13. – REPARTITION DES DEPENSES D'INVESTISSEMENTS SELON LA TAILLE DES ETABLISSEMENTS (ANNEE 1971).

SPECIFICATION	Industries extractives	Industries alimentaires, boissons, tabac	Industries chimiques, caoutchouc, raffinage du pétrole	Bois	Papier	Impression	Cuirs et peaux	Industrie textile
20 à 49 personnes :								
Nombre de déclarants	58	385	115	342	72	179	59	368
Nombre de personnes occupées	1 873	12 249	3 699	10 254	2 228	5 597	1 769	11 819
Montant (en 1 000 F)	157 505	709 008	402 523	278 118	142 461	208 444	16 255	387 008
En %	9,1	11,2	2,1	20,5	5,8	18,7	17,0	10,8
50 à 99 personnes :								
Nombre de déclarants	29	175	64	147	43	73	20	211
Nombre de personnes occupées	2 144	11 894	4 893	10 140	2 884	4 889	1 306	14 687
Montant (en 1 000 F)	296 119	812 631	387 764	351 091	130 261	151 897	9 291	486 932
En %	17,1	12,8	2,0	25,8	5,3	13,7	9,7	13,6
100 à 499 personnes :								
Nombre de déclarants	32	188	118	75	55	61	12	265
Nombre de personnes occupées	6 809	38 508	26 278	12 586	12 334	11 669	2 518	54 325
Montant (en 1 000 F)	961 614	2 605 125	10 464 138	594 916	847 185	408 050	69 922	1 889 173
En %	55,5	41,0	53,5	43,8	34,4	36,7	73,3	52,9
500 personnes ou plus :								
Nombre de déclarants	14	32	33	5	11	10	—	25
Nombre de personnes occupées	37 973	26 411	38 977	4 357	8 107	7 851	—	24 119
Montant (en 1 000 F)	317 171	2 219 871	8 276 450	134 926	1 343 588	343 560	—	812 955
En %	18,3	35,0	42,4	9,9	54,5	30,9	—	22,7
Total :								
Nombre de déclarants	133	780	330	569	181	323	91	869
Nombre de personnes occupées	48 799	89 062	73 847	37 337	25 553	30 006	5 593	104 950
Montant (en 1 000 F)	1 732 409	6 346 635	19 530 878	1 359 051	2 463 495	1 111 951	95 468	3 576 068
En %	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0

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Tableau 13 (*suite*)

SPECIFICATION	Habillement	Industrie des minéraux non métalliques	Sidérurgie et métaux non ferreux	Industrie des fabrications métalliques	Autres industries manufacturières	Construction	Electricité gaz, eau etc.	Total
20 à 49 personnes :								
Nombre de déclarants	537	172	14	733	198	1 059	75	4 366
Nombre de personnes occupées	17 044	5 095	401	21 722	6 078	32 875	567	133 270
Montant (en 1 000 F)	171 921	353 869	21 593	527 538	273 248	719 599	4 214 551	8 583 611
En %	20,3	11,7	0,2	3,9	14,0	15,7	21,6	9,4
50 à 99 personnes :								
Nombre de déclarants	20,1	74	10	346	88	373	9	1 863
Nombre de personnes occupées	13 719	5 119	708	24 139	6 039	25 113	662	128 336
Montant (en 1 000 F)	126 786	295 093	91 699	745 552	326 991	655 692	161 141	5 028 913
En %	15,0	9,8	0,8	5,6	16,8	14,3	0,8	5,5
100 à 499 personnes :								
Nombre de déclarants	180	84	19	382	85	261	18	1 835
Nombre de personnes occupées	32 108	16 948	4 723	82 503	16 060	49 616	3 809	370 791
Montant (en 1 000 F)	439 365	975 399	175 443	2 960 861	1 172 156	1 982 995	1 583 332	27 129 671
En %	52,0	32,4	1,5	22,2	60,1	43,1	8,1	29,8
500 personnes ou plus :								
Nombre de déclarants	7	27	31	109	6	36	15	361
Nombre de personnes occupées	4 416	28 663	84 284	184 985	4 719	35 354	25 696	515 912
Montant (en 1 000 F)	107 302	1 389 777	11 380 407	9 130 654	176 378	1 238 650	13 577 948	50 419 [illegible]
En %	12,7	46,1	97,5	68,3	9,1	26,9	69,5	5[illegible],3
Total :								
Nombre de déclarants	925	357	74	1 570	377	1 729	117	8 425
Nombre de personnes occupées	67 287	55 825	90 116	313 349	32 896	142 958	30 734	1 148 312
Montant (en 1 000 F)	845 374	3 014 138	11 669 142	13 364 605	1 948 773	4 596 936	19 536 972	91 191 895
En %	100,0	100,0	100,0	100,0	100,0	100,0	100,0	100,0

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EQUITY FINANCING PROBLEMS
OF SMALL AND MEDIUM-SIZED
ENTERPRISES (SME's) IN DENMARK.

1. Comparison of financial structures of SME's and large enterprises

1.1. From the table below which only covers handicrafts and smaller industries employing less than 75 workers it will be seen, that long-term debt (normally mortgage loans in real property credit associations) accounts for well over 40 per cent of the total liabilities of these enterprises, while short-term loans (mainly bank loans and trade creditors) account for about 30 per cent. The figures are subject to certain reservations however, as they originate in balance sheets from enterprises, which have been granted Government loans pursuant to the Act on loans to hardicrafts and smaller industries (see 4.1.) These enterprises are normally characterized by a more intentive management than the typical small and medium-sized enterprises.

	1971 %	1973 %
Short-term debt capital	30	29
Long-term debt capital	43	40
Equity	27	31
Total liabilities	100	100

Source: Håndværksundersøgelse 1958-73, Del I. Teknologisk Institut.

1.2. The table below shows the corresponding figures of joint-stock companies with a share capital of more than D.kr. 250.000. The major part of these enterprises employ more than 75 workers.

	1971 %	1973 %
Short-term debt capital	55	53
Long-term debt capital	11	9
Equity	34	38
Total liabilities	100	100

Source: Statistiske efterretninger 1974, No.53, and Statistisk Årbog 1975.

A comparison between these two tables shows a significant difference in the ratio of short-term debt capital to long-term debt capital of the SME's as compared to that of the larger enterprises.

1.3. As to the differences between industrial sectors of small and medium-sized enterprises the following figures give some indications on the degree of self-financing (equity as a percentage of total liabilities). As the data on which these figures are based derives from the same enterprises as mentioned under 1.1. they are subject to the same reservations.

	1971 %	1973 %
Manufacturing enterprises	28	31
Repairs	29	34
Building and construction	25	29
Retail Trade	22	29
Total average	27	31

Source: see 1.1.

2. Sources of external equity finance for SME's.

2.1. SME's are primarily organized as individual enterprises. When they are organized as joint-stock companies the founder and his family often hold the controlling interest. However, there seems to be a tendency towards organizing the SME's as private companies which are in the main subject to the same regulations as the joint-stock companies. An important difference between these two types of enterprises however is, that joint-stock companies have to hold a share capital of least D.kr. 100.000, while private companies only must have to have a contributed capital of D.kr. 30.000.

2.2. The private sector is dominant as to the financing of SME's and the governmental sector only very exceptionally (if ever) holds shares or other equity capital in SME's (nor in other enterprises).

2.3. When joint-stock companies wish to raise equity finance on the Stock Market a share capital of the issuer of at least 24

D.kr. 1 million is required. SME's therefore very seldom (if ever) have shares quoted on the stock exchange.

2.4. The Danish Government recently has considered it necessary to increase the financial resources available to the SME's cf. remarks under 4.1. At the present moment (September 1975) it is considered too early to evaluate the effect of these measures, as they were taken this summer and came into force only on the 1st August 1975. However, it must be emphasized that the financial problems of the SME's may often be refered to problems of management. Because of the financial problems and the closing down of many enterprises as a result of the recession an emergency consulting service open to the SME's was established on an experimental basis in the spring of 1975 through a special grant from the Council of Technology under the Ministry of Trade and Industry. It often appeared, that when the consultants from this service were able to assist the owner of an SME in explaining the total situation of his enterprise to his bank, the bank would give the necessary credits. In many cases therefore financial problems are due to management problems, and the methods for solving these are not financial aid but service, aids by consultants of various kinds, management training etc. However, this is a general problem not necessarily connected with the size of the enterprises. Furthermore the group of enterprises belonging to the category of SME's is a very heterogeneous group and it may in many cases be of a limited value, from an industrial policy point of view, to use the criterion of the size of an enterprise only.

3. Fiscal policies

3.1. The present provisions on depreciation for taxation purposes have had a positive influence on the self-financing and consequently on the investments of the enterprises also in the SME's.

3.2. The rules of depreciation have not been modified to allow for the effect of inflation.

3.3. The double taxation (company tax as well as income tax of the shareholders) of joint-stock companies and private companies generally may restain the financing through shares. On the other hand the major part of SME's are organized as individual enterprisos and thoroforo not subjoot to oompany taxoo.

3.4. As far as fiscal policies are concerned there are no special provisions for the SME's.

3.5. As mentioned above there ase special rules of taxation as to joint-stock companies and private companies. The company tax is a fixed percentage - at the present moment (September 1975) 37 per cent - of the taxable income of the companies. But on top of that the shareholder is taxed of his dividend.

4. Initiatives to solve the problem

4.1. The only measures implemented solely for the benefit of the SME's are the "Act No.211 of 28th May 1975 on loans to handicrafts and smaller industries" and the"Act No. 341 of 26th June 1975 on State guarantee for short-term loans to handicrafts and smaller industrial firms". Under the provisions of the former Act the Ministry of Trade and Industry may, within an annual amount of D.kr. 40 millions grant loans with a view to furthering modernization and rationalization. These loans, on which interest for the time being is fixed at 9 per cent, are granted to enterprises with up to 75 employers for up to 15 years, except loans for the purchase of machinery which have to be repaid over a maximum of 10 years.This act has replaced a similar act operating with an annual amount of D.kr. 20 million, which have proved to be a successful measure. According to the latter act a State guarantee can be extended for short-term loans from banks to handicrafts and smaller industrial firms within a total amount of D. kr. 200 million.The loans must be used for an extensive reconversion to new productions or to new markets. Loans for which State guarantee is extended cannot exceed D.kr. 250.000 and the duration of the State guarantee is limited to 5 years from the raising of the loan. The State guarantee is limited to 50 per cent of the loan, while the rest of the risk is covered by the lending banks who also administer the arrangements. It is too early to express an opinion of the effects of this measure.

4.2. For the present no new initiatives are under consideration within the governmental sector.

NOTE ON THE FINANCING OF SMALL AND MEDIUM-SIZED ENTERPRISES (S.M.E.) IN FRANCE

I. COMPARISON OF THE FINANCIAL STRUCTURES OF S.M.E. AND LARGE ENTERPRISES

S.M.E. have relatively little scope for self-financing, are unable to call on the capital market and are discriminated against by financial institutions when it comes to long-term borrowing so that they find it more difficult than large enterprises to increase their permanent capital; as a result they resort more and more to short-term borrowing.

These are the conclusions which can be drawn from statistics provided mainly by the central offices monitoring borrowers' balance sheets of a number of financial institutions (Banque de France, Crédit National ...). It should however be noted that these statistics are fairly fragmentary and that experience has shown that the samples prepared by these offices are more representative of large than of small or medium-sized enterprises.

The figures given in this document should therefore be regarded more as a pointer to trends rather than the result of exhaustive statistical research.

1) S.M.E. find it more difficult than large enterprises to increase their permanent capital

In the aggregated balance sheets, long-term funds (permanent capital) account for 48% in the case of S.M.E. compared with 55% for large enterprises.

These difficulties in raising long-term funds are experienced both in calling upon shareholders or in resorting to financial intermediaries.

1.1. It is more difficult for S.M.E. than for large firms to call upon existing or new shareholders for capital

Shareholders in small enterprises (family business) have limited financial resources so that it is often difficult for them to contribute fresh capital. In addition, shareholders of this type are wary about any capital contributions from outside which might cause them to lose their majority holding in their companies.

Potential shareholders are discouraged by the low dividends distributed by S.M.E.: 60% of S.M.E. compared with 30% of large enterprises, do not distribute any dividend at all.

The ratio of distributed profits to equity capital seldom reaches 3% in S.M.E., whereas 6% is not an uncommon figure for large enterprises. The former cannot call on the capital market by share issues, because their small financial scale excludes them from the stock market.

1. 2 Financial institutions discriminate against S.M.E. when granting long-term loans

They are discriminated against because of the lender's assessment of the risk involved: the bigger the borrower the less the risk of insolvency; the large enterprises have a variety of resources, they are well known and constitute an economic, or even a political force by virtue of the number of people they employ.

By diversifying their operations, large enterprises are able to spread risks so that their overall profits are less subject to chance.

In relative terms, S.M.E. owe less than large enterprises to financial intermediaries; the coefficient of indebtedness;

$$\frac{\text{debts owed to financial intermediaries}}{\text{equity capital}}$$

is 0.75 for S.M.E. compared with 0.83 for large enterprises.

1. 3 Although their small size is a handicap when seeking outside finance, it facilitates direct relations between the enterprise and its owners

Direct relations between the enterprise and its owners, who often manage the business means that ancillary resources, medium-term certificates and current account advances of members make up a larger proportion of the firm's own resources: 40% as against 20% for large enterprises.

2) S.M.E. are resorting increasingly to short-term borrowing

43% of borrowings by small enterprises are short-term, compared with 32% for large enterprises making the structure of borrowing by the former less secure. 28

It can be said that the average rates of interest charged to S.M.E. are higher than those charged to large enterprises:

The ratio $\frac{\text{financing costs}}{\text{total debts outstanding}}$

shows that in recent years the average interest rate for S.M.E. has been 5.5% against 4.4% for large enterprises.

Faced with these financial constraints, S.M.E. have a more rapid turnover of current assets, particularly work in progress: turnover period for S.M.E. is one month compared with three months for large enterprises.

The structures of the various industrial sectors are so different that it is impossible to pinpoint any significant differences in the financing of S.M.E. and large enterprises on a sector - by - sector basis: a S.M.E. in light engineering will employ 200 workers which corresponds with a large enterprise in the distribution sector.

II. EXTERNAL SOURCES OF EQUITY CAPITAL FOR S.M.E.

1) Main external sources of equity capital

The Sociétés de développement régional (S.D.R.), the Institut de Développement Industriel (I.D.I.), venture capital companies such as E.E.D. and SOFINNOVA, finance companies with wider interests such as SOPROMEC and BANEXI, the provincial stock exchanges and the Paris over-the-counter market are the main external sources of equity capital for enterprises.

1.1 The S.D.R. seem best suited to meet the requirements of S.M.E.

The S.D.R., bodies governed by private law, were set up in 1955 to provide capital to enterprises in the provinces which found it difficult to borrow on the capital market, and to promote the economic development of all the French regions. Their task is, therefore, to acquire holdings in the capital of local enterprises. The S.D.R. can intervene financially in four different ways: acquire holdings up to a limit of 25% of the capital of the S.D.R. in respect of any single enterprise and up to 35% of the capital of the enterprise; grant loans from their own funds; grant long-term loans from capital raised by group borrowing, provide guarantees.

The acquisition of holdings has taken second place to the granting of loans, partly as a result of the difficulties encountered by the S.D.R. in mobilizing savings in the regions and the reluctance of enterprises to go to outside sources to increase their capital, for fear of losing their independence.

1. 2 The Institut de développement industriel (I.D.I.)

The I.D.I. was formed in 1971 as a "public" limited liability company by the State, a number of specialized crédit institutions (Crédit national, Crédit agricole, the S.D.R.) and various banks, in order to help strengthen industrial structures. The Institute, which had an initial capital of FF 332 million, later raised to FF 532.8 million, has the task of acquiring holdings in industrial S.M.E. which are expanding rapidly but which need equity capital.

1. 3 Venture capital companies

This type of company can step in from the moment an enterprise is formed, by acquiring a capital holding of between 10 and 50%. These companies are interested in enterprises employing advanced or original technology.

EUROPEAN ENTERPRISES DEVELOPMENT (E.E.D.) was set up in 1964 with the assistance of Paribas, Suez, Worms and the three big nationalized banks; its shareholders now include about 50 European and American banks. It is only interested in products which have reached, or are already beyond the prototype stage.

SOFINNOVA

The shares in this company, which was set up at the end of 1971 to finance innovations are held by insurance companies, banks and industrial groups; by 1975 its capital had been increased from FF 2.5 million to FF 39 million. Staffed by engineers and experts in the evaluation of innovation projects, the company assists expanding small enterprises and innovators who do not have an existing enterprise at their disposal.

It operates by acquiring holdings in the capital of enterprises, setting up "groupement d'intérêt économique" (G.I.E.) and making loans. It maintains close links with the "Association Nationale pour la Valorisation de la

Recherche" (ANVAR) (National Association for the Application of Research), the I.D.I., the S.D.R. and finance or portfolio investment companies.

1. 4 Finance companies with wider interests; SOPROMEC, BANEXI

*The "Société de promotion économique"(SOPROMEC) was set up in 1964 by the Groupe des Banques Populaires to increase the resources of S.M.E. by acquiring direct capital holdings (50% of its interventions)and by granting personal loans to heads of enterprises. The system of these loans works as follows:

- the loansis granted not to the enterprise but to its head who can then subscribe for/all increase in its capital;
- the head of the enterprise assumes personal responsibility for repayment of the loan from his own resources;
- the contract concluded with SOPROMEC is a conventional loan agreement specifying the duration of the loan, the period of repayment and the rate of interest,

*BANEXI (capital: FF 70 million), a subsidiary of the B.N.P., was set up to carry out rescue operatins by acquiring holdings in industrial enterprises.

Two-thirds of its capital is used for operations, involving property or large enterprises and one-third for holdings in S.M.E. At present BANEXI has 70 different holdings worth a total of FF 320 million.

The bodies providing finance are faced with a number of problems:

- the yield on holdings in S.M.E. is inadequate, as the latter distribute low dividends, out of profits which are often fairly modest to achieve a maximum degree of self-financing;
- it is difficult for them to pull out again, and risks are high.

1. 5 Provincial stock exchanges and the over-the-counter market

*There are six provincial stock exchanges: Lyon, Nancy, Lille, Marseille, Bordeaux, Nantes. They are relatively unimportant compared with the Paris Exchange, accounting together for only 3% of total stock market business. Their purpose is to help finance S.M.E. Anxious to improve their image and to make managements realize that there is no loss of

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prestige in having their company quoted on a provincial exchange, the various stock exchanges have undertaken an information campaign based not only on statistics but also on an analysis of the various companies listed on their markets.

The conditions with which companies wishing to raise equity capital on the stock market must comply, make a fair number of medium-sized companies turn to the over-the-counter market instead.

*Although it acts as a kind of acclimatizing market, the/Paris over-the-counter market is often regarded with some reservations by companies which would like to be quoted on the official market for reasons of prestige. The main problem facing the financial intermediairies on this market is to make a daily market so that shareholders can mobilize their investments.

2) The relative importance of finance provided by the private and public sector

Direct financial assistance from the public sector to S.M.E. is rare: loans from the "Fonds de Développement Economique et Social", regional development premiums.

This aid is not usually granted on the basis of the size of enterprise but rather on purely industrial criteria (promotion of productive investment) or regional planning considerations.

Most of the finance provided by the public sector is granted indirectly through bodies governed by private law (the S.D.R.. Crédit National, Crédit Hôtelier). These bodies lend money to S.M.E. at subsidized rates of interest. As the available statistical instruments for analysing what benefit these loans represent to S.M.E. are inadequate, it is difficult to measure accurately the relative importance of finance provided by the private and public sectors.

3) The minimum requirements for enterprises wishing to raise equity capital on the stock market are set out below:

3. 1 When applying for an official quotation:

- Any French company wishing to have its shares officially quoted for the first time must apply both to the "Chambre Syndicale des

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Agents de Change" (Stockbrokers' Association) and the "Commission des Opérations de Bourse" (C.O.B.); a file must be submitted to the former and a letter sent to the C.O.B. containing the company's application and specifying the number and origin of the securities which the shareholders intend to put on the market on the day of introduction.

- The number of securities offered must, as a rule, be equivalent to 25% of the share capital.

3. 2 When the application is examined

- The C.O.B. asks the company applying for its shares to be officially quoted to appoint a specialized firm to audit its accounts in accordance with the rules laid down by the profession.

- The Chambre Syndicale is responsible of examining the file on the application for a quotation and presenting its conclusions to the C.O.B.

- The "Collège" (executive organ) of the C.O.B. then receives from its own staff all the relevant facts on which to base its judgment, i.e.:

  - the study and opinion of the Chambre Syndicale des Agents de Change;

  - information compiled by the C.O.B.'s own staff when the company's accounts were being audited, or obtained in contacts with the management of the company of the auditors.

The C.O.B.'s decision depends on a number of factors relating to the size of the company issuing the shares, the quality of its management and its external control, its past performance, profit-making capacity and future prospects.

The likelihood of there being a sufficiently large market in the securities concerned is also taken into account.

The Collège considers the case and decides whether or not the company's shares should be officially quoted. If it decides in favour, it designates the place of negotiation and approves the information document submitted by the company.

4. To what extent do existing sources of finance meet the requirements of S.M.E.?

Current statistics on the financing requirements of S.M.E. and the extent to which these are met by drawing on existing sources are not sufficient to enable this question to be fully answered. However, new instruments of analysis to cover this area are to be introduced as part of the preparation of the Seventh Plan and the reform of enterprises, particularly in conjunction with the central offices monitoring borrowers' balance sheets of a number of financial institutions (Banque de France, Crédit National, Caisse des Dépôts et Consignation, etc.)

III. FISCAL POLICY

1) Influence of present fiscal policy on self-financing

1. 1 All the profits of partnership - whether distributed or not - are charged to personal income tax which each partner must pay in proportion to his share in the business. In this respect the system can be said to promote neither distribution of profits nor self-financing.

The profits of companies liable to corporation tax are all taxed at a rate of 50%. The distributed portion of these fprofits is in addition subject to income tax in the hands of the shareholders, even though this is reduced by the amount of the tax credit granted with the dividend; the total tax liability (corporation tax + personal income tax) on distributed profits is thus higher as a rule than that on retained profits. It can thus be said that the tax credit, at its present rate, merely reduces the extra burden on distributed profits and that, overall, it is less costly to plough back profits directly than to distribute them and then have to call on shareholders for fresh capital! Seen from this anglà, it appears, contrary to a view often voiced, that self-financing is in fact encouraged.

This conclusion must, however, be qualified somewhat because the effect of the tax arrangements varies according to the structure and size of the enterprise involved.

It may thus be to the advantage of the owner/managers of a company to distribute dividends among themselves rather than plough back the profits directly, and then make this money available to the company in the form of current account advances; the interest they would then receive is deductible from the company's taxable profits and may, in addition be discharged from income tax if flat-rate payment is made.

1. 2 Declining-balance depreciation and temporary deductions for investment undoubtedly make self-financing easier. However, the benefits of this are felt more by large enterprises with a policy and programme of continuous renewal and development than by S.M.E.

2) <u>Has fiscal policy been adjusted to take account of the effects of inflation?</u>

There have been no new measures motivated by inflation and based, for example, on a revaluation of balance sheets.

There has been no change in the permanent provisions on the valuation of stocks (reserves for price increases, reserves for price fluctuations), or in declining - balance depreciation.

An investment allowance, however, has just been introduced in France, as in most countries, to encourage enterprises to invest and hence to stimulate economic activity.

3) <u>Does fiscal policy influence capital increases?</u>

3. 1 Capital can be increased by injecting fresh capital or capitalizing reserves.

Capital duty in the first case has now been harmonized within the Community.

In France capitalizing reserves is subject to an increased rate of capital duty which exempts shareholders from income tax on the bonus shares received.

It is difficult to make an overall assessment of what effect these measures have on the behaviour of companies and their shareholders. Circumstances vary. In the case of owner/managers it may be claimed that the situation tends if anything to discourage any increase in capital on their part, whether it be through the contributinn of fresh capital or through the capitalization of reserves, so that current account financing is often preferred.

3. 2 Another factor which may influence increases in capital is the difference between the taxation of shares (i.e. financing from internal resources) and the taxation of bonds.

Borrowing brings advantages to the enterprises interest payments are deductible from taxable profits, and the cost of repayment is reduced by inflation.

Despite the effects of inflation on his capital the bondholder often prefers a higher income (on which he may pay tax under the flat-rate arrangement discharging him from further liability) to a smaller dividend and a theoretical capital gain on shares which he will find very difficult to realize if the shares are not quoted.

4) Has any special provision been made for S.M.E.?

Apart from the flat-rate and simplified systems (taxes assessed on the basis of actual turnover and profits), available to enterprises whose turnover does not exceed FF 500 000 (flat-rate) or FF 1 000 000 (simplified), there are no tax provisions applying specifically to S.M.E.

5) Are there any special provisions based on the legal form of enterprises?

As in most other countries, the taxation of profits in France varies according to the legal form of the enterprise concerned: sole propriortorships and partnerships are liable to personal income tax; "private" limited liability companies and "public" limited libility companies are subject to corporation tax.

However, the main provisions relating to the basis of assessment for these taxes - valuation of stocks, depreciation, treatment of capital gains - are identical.

IV. INITIATIVES WHICH MAY HELP TO SOLVE THE PROBLEM

1. Initiatives taken over the last five or ten years and their results

1. 1 Setting-up of the Institut de Développement Industriel (I.D.I.)

The vesting letter of 31 March 1970 assigned to the I.D.I. a role of national interest: in selecting industries and enterprises for the purpose of granting assistance, the Institut must take account of the priorities of the Government's industrial policy and bear in mind regional planning considerations.

It must give priority to medium-sized firms which may find it very difficult, owing to lack of sufficient equity capital, to raise the capital needed to improve their rate of growth. It may also be called upon to play a part in certain restructuring operations by exercising its finfluence on negotiations or contributing capital.

. An account of the I.D.I.'s achievements since 1970 is given below:

Since its inception I.D.I. has examined 1,126 applications for assistance. Applications are now received at the rate of about 150 per year. They increasingly involve firms at the top end of the medium-sized category with annual sales of more than FF 50 million. Almost three-quaters of the applications concern problems of expansion, either through internal growth or through amalgamations. I.D.I. has thus come to act as an industrial development consultant even in cases where it cannotbecome financially involved.

Financial assistance provided by I.D.I. totalled FF 219,9 million in 1970-71, FF 177.8 million in 1972, FF 102.7 million in 1973 and FF 96.8 million in 1974, a grand total of FF 597.2 million. I.D.I. has been deliberately selective in its approach: with the exception of the initial period, it has on average approved new financial assistance in ten or twelve of the cases considered.on average.

The Institut assists mainly medium-sized enterprises: 85% of the companies associated with the I.D.I. have a turnover of less than FF 150 million; the majority of its operations involves enterprises with sales of between FF 10 million and FF 40 million; the amounts invested in each firm vary between FF 1 million and FF 11 million.

I.D.I. assists all industrial sectors, with a particularly high proportion in engineering, wood, furniture and "miscellaneous" industries. In more than three - quarters of the cases dealt with assistance has taken the form of capital holdings, thus exerting a multiplier effect by enabling the firms concerned to raise additional funds from institutions. granting long- and medium-term credit.

I.D.I. tries to arrange its withdrawal from enterprises after a fairly short period, depending on individual circumstances and the position of the shareholders. By 31 December 1974, programmed withdrawals for 85% of its total investments had been arranged; the average length of its intervention is almost six years.

I.D.I. has carried out studies to provide it with detailed information about the various industrial sectors and their subsectors.

1. 2 <u>The Sociétés de Développement régional (S.D.R.), set up in 1955, seem best suited to meet the requirements of S.M.E.</u>

The sole purpose of the S.D.R. was originally to help finance industrial enterprises in regions of under-employment or inadequate economic development by acquiring holdings in their capital. They could also be instrumental in the launching of new enterprises. Their activities have since been extended: the Finance Act of 1960 removed the obligation to acquire capital holdings as a condition of granting loans. In 1971 the S.D.R. were authorized to give assistance by acting as guarantors in the mutual medium-term credit system managed by the Caisse Nationale des Marchés de l'Etat; they have also been authorised to lend to the "SICOMI" (Sociétés d'investissement dans le Commerce et l'Industrie) set up specially to enable the S.D.R. to carry out property leasing transactions.

The S.D.R. enjoy a number of tax advantages; tax exemptions, guaranteed dividends, subsidized interest rates.

They are subject to a number of requirements: they must have a capital of at least 250 million old francs, fully paid up; any holdings they acquire may not exceed 25% of their own capital in respect of any single enterprise and 35% of the capital of the enterprise.

Their activities are characterized by two main features:

- the very small proportion of funds raised by increasing capital: a total of FF 183 million by the end of 1973;
- the growing predominance of funds raised by collective borrowing: funds raised in this way totalled FF 5,655 million by the end of 1973.

The S.D.R. have therefore failed to a certain extent in their task of attracting savings to enable them to acquire holdings in the capital of regional S.M.E. Instead they have largely become credit institutions and now play a major role in lending to a certain category of enterprise on Government subsidized terms.

2) Further action currently planned by the public authorities or the private sector

There is a need for new financial structures channelling savings into investment in medium-sized enterprises. The solution advocated would involve setting up specialized investment companies, SODIMI, along the lines put forward in the draft law presented by Mr. D'Ornano in 1973.

SODIMI securities would initially be subscribed to by private investors, particularly institutional investors, and would subsequently be introduced on the capital market. These investment companies would operate mainly by subscribing to shares and ordinary or convertible bonds.

The SODIMI would try to establish, on the over-the-counter market, a market in the securities of medium-sized enterprises which they had bought or subscribed to, thus giving investors the opportunity to acquire a direct interest in such companies. The SODIMI would bring new life to these markets, as they could act as permanent buyers or sellers. The SODIMI could only operate effectively, however, if they were granted certain tax concessions.

The responses set out below do not extend to enterprises other than those engaged in manufacturing activities. They also relate, in the main, to small as opposed to medium-sized enterprises i.e. projects employing up to about 50 people. However, it is quite reasonable to assume that the same comments could apply to medium-sized enterprises employing up to, say, 100 people.

1. Comparison of financial structures of SME's and large enterprises.

(a) Typical financing of fixed asset investment would be as follows: 35% equity; 35% grant; 30% long term loan. Working capital normally provided by way of short term bank accommodation. The long term loan element is generally a high interest bearing loan with, in many cases, conversion to equity rights.

(b) The financing of larger enterprises is similar in structure to that of smaller enterprises but the long term and the short term loan elements are significantly different. The loan elements are made up of one or more of the following combinations: Leasing; Preference Share; Straight Loan. Because of the scale of their operations and the possibility of access to international sources of finance, large enterprises sometimes have an advantage over smaller units in being able to secure finance on more favourable terms.

(c) In so far as there are differences between industrial sectors they arise for two reasons i.e. the capital intensity of the project and profitability. In sectors where the fixed asset investment is high in relation to total capital employed it is generally easier to secure loan capital at better terms so that the cost of debt may be cheaper. The more profitable sectors of industry generally have a higher equity debt ratio than the normal or low profitability sectors.

2. Sources of external equity finance for SME's

(a) In practical terms there are no real sources of external equity for small enterprises. The financial institutions including the government backed Industrial Credit Company do have equity investment arms but generally they do not invest directly in the equity of small companies. Where, however, they provide long term loans to small enterprises they invariably carry equity conversion rights.

(b) The importance of private versus government sources of finance can be gauged from the fact that grants can represent a significant portion of fixed asset investment. Grants in this context are tantamount to equity. It can therefore be said that governmental sector and private sector are of equal importance since grants generally match equity. Apart from grants the other source of government finance is the Industrial Credit Company which provides loan capital rather than equity.

(c) The minimum requirements for raising equity finance on the Stock Market are as follows:-

(1) The company must have a market value of at least £500,000
(2) The value of the stock offered to the public must be at least £200,000.
(3) The percentage of the total equity of the company offered to the public must be at least 35%.

(d) The needs of most small enterprises are adequately catered for by the existing structure. There are, however, examples of projects which either failed to materialise or are inhibited in their growth because of their lack of permanent finance.

3. (a) Ireland's system of taxation on coRporate income is at present made up of two taxes, i.e. Corporation Profits Tax at rates of 7½% for the first £2,500 and 23% on the balance and Income tax at a rate of 35%. Corporation Profits Tax ranks as a deduction in computing income for income tax purposes and accordingly the total imposition varies from approximately 40% to 50% depending on the amount of taxable profits. Dividends paid out of these profits are deemed to be paid out after deduction of Income Tax at 35% which is available for set off or repayment in accordance with the circumstances of the beneficial owners. A Bill to replace these two taxes by a single Corporation Tax at 50% with a tax credit of 35/65 ths is at present before Parliament. The proposed new system would be a change in form but not in level of the present corporate taxes or tax credit. These systems, which correspond to a partial imputation system, ~~which correspond to a partial imputation system~~, are considered to assist self-financing in case of private companies employing its shareholders in a managerial or technical capacity as the maximum rate of personal tax is 77%. On the other hand, in the case of larger enterprises whose equity is more widely held, a "classical" system might be more conducive to the retention of profits.

(b) Fiscal policies in Ireland had been modified to allow for inflation, in effect, in two important respects.

(1) Companies engaged in the manufacture of goods, construction, farming, or the sale of plant and machinery to such companies may claim as a trading expense a deduction where the value of their trading stock at the end of the accounting period exceeds that at the beginning. The deduction is equal to the amount of the increase in stock valuation less 20% of the trading profits for the period, subject to the proviso that the deduction cannot be greater than the amount of the trading profits of that accounting period. The relief applies to accounting periods ending between 5 April 1973 and 5 April 1975.

(2) The accelerated depreciation provisions whereby the total cost of new plant and machinery can be written off in the year of purchase effectively goes some way to remove the problem of the treatment for tax purposes of inflation in respect of the cost of fixed assets.

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(c) Fiscal policies affect the way in which capital is raised to the following extent:

dividend payments are not deductable in computing taxable profits: whereas, generally speaking, interest payments are deductable.

(d) The first £2,500 is chargeable at only 7½% instead of 23% for corporation profits tax. Under the proposed Corporation Tax the Rate ~~note~~ on profits not in excess of £4,000 will be 40% and there is a provision for a measure of relief on profits between £4,000 and £10,000.

(e) Business is normally carried out under three legal forms.

(1) limited company
(2) partnership
(3) sole trader.

The method of computing income is similar in all three cases and the principal difference lies in the rates of tax. The limited company is taxed at the rates previously indicated. In the other two cases the income is treated as the earned income of the relevant person. Accordingly, the fiscal advantages of the various forms is largely dependent upon the amount of profits earned, as this in turn determines the tax rates.

4. Initiatives to resolve the problem.

The principal initiative at Government level over the past five to ten years has been the establishment of the Small Industry Division within the I.D.A. This Division provides advisory and financial services to help viable small-scale manufacturing enterprises to solve problems obstructing their growth, and to facilitate the establishment of new firms. Projects assisted normally employ less than 50 persons with a fixed asset investment of less than £200,000. Financial incentives include capital grants towards the cost of fixed assets and grants towards the cost of training workers in skilled industrial processes.

LAWS GOVERNING FINANCIAL ARRANGEMENTS AND CREDIT FACILITIES OR TAX CONCESSIONS FOR S.M.E. IN ITALY

In recent years the competent authorities have introduced a number of laws making provision for enterprises wishing to restructure, reorganize or convert their production possibilities to obtain finance on easy terms.

These measures, which are part of the broader process of industrial development to keep pace with international competition are listed below:

Law No 274 of 18 May 1973, amending Law No 1470 of 18 December 1961, and providing additional funds, includes provision for the financing of industrial programmes involving the conversion, transformation and restructuring of enterprises, provided this is in the general interest and of economic and social value.

Law No 1101 of 1 December 1971 contains a series of measures designed to promote improvements in the productive structures of the textile industry and to help enterprises in this industry to build up operations to a scale which will enable them to remain competitive in present-day conditions.

Under Law No 1101 - the credit clauses of which were extended to other productive industries within the meaning of Article 9 of Law No 464 of 8 August 1972 - three types of programmes may qualify for financial assistance on easy terms;

a) - restructuring of reorganization plans carried out by textile enterprises

b) - plans for converting some or all facilities to other operations, being implemented by textile enterprises in areas where the textile industry is predominant;

c) - Plans for the construction of new industrial plant and the extension of existing plant for activities other than textile manufacturing.

Law No 184 of 22 March 1971 provides for the establishing, under the Istituto Mobiliare Italiano, of "working capital"to be used to help carry out restructuring undertaken by individual enterprises or, preferably by groups of enterprises in productive industries where there are rationalization or efficiency problems.

Law No 623 of 30 July 1959 - subsequently amended and supplemented - provides for the financing of and tax concessions for S.M.E. in certain depressed areas of Italy.

Law No 713 of 24 December 1974 lays down special concessions for small and medium-sized industries.

Finally, there is the "Finanziaria Meriodinale", set pp in April to establish, develop, expand and reorganize companies in southern Italy, particularly small and medium-sized ones.

FINANCING OF SMALL AND MEDIUM-SIZED ENTERPRISES IN THE GRAND DUCHY OF LUXEMBOURG

Generally speaking, it is difficult to answer at all fully the question regarding the financing of S.M.E. in Luxembourg.

Because of a lack of statistical data in this field the replies to the EEC questionnaire cannot be based on quantitative data but must take the form of a general description of the financing of S.M.E. We have had to enlist the aid of experts in tax legislation.

1. The comparison of the financial structures of S.M.E. and large firms has not been possible, until recently, except in the industrial sector, as large commercial enterprises in the distribution sector have only appeared, with one or other rare exceptions, in recent years.

It can be said quite categorically that S.M.E. in the industrial sector, including artisanal enterprises, have for a long time been self-financed by depreciation and reinvested profits. Only part of the working capital has been financed by short- or medium-term liabilities, i.e. trade credit and overdrafts on current account. The same is true of large firms, the main representative of which, ARBED, sought virtually no loans until 1967.

Commercial S.M.E., which normally have fewer fixed assets than industrial enterprises, have been self-financed, mainly by reinvesting profifs. When necessary, the owners or new associates

.../...

have invested capital to supplement self-financing.

The situation has changed in all sectors since the end of the sixties. Keener competition in a rapidly expanding economy, the progressive integration of the country into the Community, rising labour costs and general cost inflation have caused many problems which S.M.E. and large firms alike have had to face by taking major restructuring, modernization and rationalisation measures. Capital requirements have increased as a result. These could not be met solely by self-financing, which has been eroded by the depreciation of money, and the financial structures of firms have therefore altered radically. The proportion of own funds used to finance firms is now shrinking and being replaced by funds from other sources; large firms are having to borrow on the capital market and S.M.E. are resorting to bank loans and mortgages.

2. Unlike the large firms, S.M.E. in Luxembourg are unable to expand their capital by issuing new shares. They have no common banking institution of their own and therefore have no access to the stock market. Restructuring is the only possibility left open to them. Individual S.M.E. are forming companies by taking on one or more active or sleeping partners who are prepared to invest in the company. Most of these restructuring operations are exempt from tax, since under certain conditions the law does not require the increased capital to be declared.

It is difficult to quantify the effects on the financing of S.M.E. of interventions from public funds (capital grants, subsidies to offset borrowing charges and temporary tax arrangements).

.../...

The dwindling number of S.M.E. - going out of business or losing their trade to powerful joint-stock companies - should be sufficient proof that existing possibilities of financing no longer meet the requirements of S.M.E. Of course they can still resort to loans. Many firms, however, find too many obstacles here: either they cannot provide the requisite guarantees on their own or the financial charges are too high.

3. Undistributed profits are subject to the same tax as distributed profits. Although legislation on tax relief for investment was intended to assist all firms regardless of their size, some measures affect S.M.E. more than large firms.

The value of fixed assets has been raised twice since the Second World War under the tax law. There are no plans at the moment to increase it again to offset current inflation, but, certain tax reductions - essentially of a temporary nature - may remain in force as a compensatory measure.

4. No special laws have been passed with regard to S.M.E. or in respect of the legal status of firms.

The principal measures adopted during the last ten years which have a direct or indirect influence on financing or increasing the share capital of S.M.E. are:

- certain tax rebates and allowances, which have been described above;
- easier terms for the acquisition of land or premises by firms setting up new operations or relocating existing operations;

.../...

- premiums allowed on savings for young traders and artisans setting up business for the first time;
- capital grants paid to existing firms for investment projects which are completely or partly self-financed;
- loans for the purchase of equipment and interest subsidies, i.e. a State contribution towards the borrowing costs which varies according to trades and occupations.

These measures have certainly helped the investment projects of S.M.E. but they have not provided the initial stimulus for them, or at least not for all of them. The creation, extension and modernization of firms has been carried out in the past largely due to the personal efforts of the heads of companies, to the improvement of productivity and to the general economic upswing. Furthermore, the effect which certain aids might have had on the creation of equity capital has been lessened by the tax burden, since such aids, as far as their repercussion on the financial situation of firms is concerned, are - just as in neighbouring countries - subject to income tax just like business profits.

There is a danger that the measures taken up to now will prove inadequate in the present troubled economic climate and a large number of S.M.E. may be swept away, since they will not be able to hold their own against the onslaught of firms with large capital resources.

Apart from a few self-defence initiatives which have been taken here and there, resulting in regroupings and mergers of firms, no new safeguard measure has yet been envisaged by the public authorities to protect S.M.E.

SURVEY OF THE FINANCING OF SMALL AND MEDIUM-SIZED ENTERPRISES (S.M.E.) IN THE NETHERLANDS

1. A small enterprise has no access to either the money or capital market. A typical S.M.E. is financed from private capital, including profits, and from bank credit.

- A large undertaking can go to the money and capital market.
- The different treatment given to the various branches of industry depends on the nature of the particular sector. An undertaking in a weak branch of industry generally finds it more difficult to obtain credit than an undertaking in a branch in which business is flourishing.

2. The most important external sources of share capital are equity investment companies. These may be either private or public. State equity investment companies take only minority shares. Several of these companies exist in the public sector in the Netherlands. Furthermore, the authorities have very recently created an institute for so-called "subordinate" loans ("achtergestelde lening") with a view to improving the capital structure of weak enterprises. Here, the creditors have priority over the provider of the so-called "subordinate" loan should the undertaking concerned go bankrupt. The provisional maximum amount earmarked for this purpose is Fl 500 million. The minimum amount per loan to be provided by the Nationale Investerings Bank (national investment

.../...

bank) is Fl 250 000 - which is the limit for the Krodiëtbeschikking Midden- en Kleinbedrijf, which also gives subordinate loans.

- The private sector probably has the largest relative share in the financing of S.M.E. (statistical data not available).

- Not applicable; small enterprises are not admitted on to the stock market.

- No answer can be given.

3. The present high rates of taxation leave little room for self-financing. However, the authorities do to a certain extent encourage smaller enterprises to finance themselves, and have, to this end, made it legally possible for the self-employed to build up a fiscal reserve for their retirement. This reserve can in fact be reinvested in the enterprise. Furthermore, those self-employed persons whose profits are below a certain figure benefit from an allowance for the self-employed, which means that a certain amount of the invested capital is exempt from capital taxation.

Private companies and limited liability companies (besloten en naamlose Vennootschappen) are better able to finance themselves-even without such measures - since in their cases retained profits are usually subject to a lower rate of taxation than in the case of private undertakings.

- Income tax rates, which are of particular importance to privately owned enterprises are officially adjusted each year to take into account the rate of inflation recorded. No adjustment may exceed 80 %.

.../...

- The returns on an enterprise's capital naturally depend on the proportion of the profits claimed by the tax authorities. The effects of this are mitigated by the extension of the investment allowance and the opportunity for the premature writing-off of industrial premises. However, the latter measure is applicable only outside the "Randstad" area (the highly industrialized Western zone of the Netherlands).

- The above-mentioned fiscal reserve for retirement benefits and the allowance for the self-employed are in fact intended primarily for S.M.E.

- Yes. The fiscal reserve for retirement benefits and the allowance for the self-employed are applicable only to privately operated enterprises in which profits are subject to income tax, and therefore not to limited liability companies.

4. The measures referred to in point 3 were drawn up during this period specifically for S.M.E. They should have certainly met with some success, although it is not yet possible to ascertain to what extent.

- The Government has set up a study committee (Chairman: Prof. Hofstra), whose task it is to investigate the effect of inflation on the levying of taxes, with special attention being paid to the concept of fiscal profits.

FINANCING OF SMALL FIRMS IN THE UK

NOTE BY THE DEPARTMENT OF INDUSTRY

INTRODUCTION

1 This note briefly describes how small firms are financed in the UK. It has been prepared in accordance with the schema proposed by DGIII/A/4 of the Commission of the European Communities, and is to be considered, together with similar notes by other member countries at the next meeting of small firms officials to be held by the Commission in November 1975.

2 For the purpose of this note, Equity and Debt are as defined in the footnote to the DGIII schema. Small firms are those in the manufacturing, distribution and service sectors excluding agriculture, the professions and financial services, conforming to the size limits defined for statistical and descriptive purposes only in the Report of the Bolton Committee of Enquiry on Small Firms published in 1971. These size limits, showing adjustments of turnover where appropriate to allow for present day values are at Appendix 1.

FINANCIAL STRUCTURE AND COMPARISON WITH LARGE ENTERPRISES

Finance of a Typical Small Firm

3 Data published by the Bolton Committee based on a sample survey of small firms accounts for the years 1964 and 1968 is summarised in the Tables at Appendix 2. These show the composition of the average balance sheet of:

(a) the survey group as a whole; and

(b) sub-divisions of the group according to legal status of the business and broad industrial sectors.

Table (a) also compares average balance sheets for the survey group and for quoted companies.

4 According to these data, the average small firms derives about 90% of its long term finance from equity sources and from owners loans, and 70% of its short term capital from trade creditors. Another 23% of short term finance is provided by bank loans and overdrafts, and the balance from miscellaneous credit sources such as debts for services, taxes due and borrowings from private individuals.

5 Variations/....

5 Variations occur, of course, within this average. Bolton found, for example, that unincorporated businesses tend to borrow less from the banks than do companies, and that a substantial proportion of small firms do not borrow at all. On the other hand, he also found evidence to suggest that fast growing firms rely to a much greater extent than the average on external borrowing from banks and elsewhere.

Finance of a typical large firm

6 The information on the financial structure of large enterprises in the United Kingdom is obtained from the published annual accounts of companies. These accounts are drawn up to give a true and fair view of a company, and assets and liabilities held are valued at book value, which represents either the historic cost when purchased or the value when last revalued, and are net of accumulated depreciation. The depreciation charge is generally calculated on a straight line basis over the life of the asset and is not the amount of depreciation allowed for taxation relief as in many other European countries. The method of valuing assets and depreciation affects the size of profits and thus the size of revenue and capital reserves, and this plus other differences in accounting conventions makes intra-country comparisons of the financial structure of companies based on company accounts very difficult if not impossible.

7 The Bolton Committees analysis of the average quoted company balance sheet showing the proportion of funds derived from various sources is incorporated in Table (a) of Appendix 2. The relative importance of the various forms of debt in relation to the value of shareholders' interest, that is share capital and revenue, capital and tax reserves from 1964 to 1973, for large listed industrial and commercial companies operating mainly in the United Kingdom is shown in Table 1 of Appendix 3. Listed companies which include quoted companies, are those whose securities have been admitted to the Official List of the United Kingdom Stock Exchange (see paras 17-23).

8 The ratio of long term loans plus bank borrowing rose over the period 1964-1970 and then fell back in 1971 and 1972 before increasing again in 1973. There is likely to have been a further small increase in 1974 because companies had very large increases in bank borrowing. At least part of the rapid increase in this borrowing relative to shareholders' interest after 1964 resulted from the 1965 Finance Act which made it more advantageous to raise loan capital than equity, and the slowing down after 1970 is in part probably associated with the faster increase in creditors relative to debtors, so that by 1973 creditors were greater than debtors.

9 There/....

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9 There is considerable variation between companies and industries of the ratio of debt to shareholders' interest as is shown by Table 2 of Appendix 3. These figures, however, need to be treated with caution because first they are based on only a limited number of companies, and second companies are classified by their main activity and therefore the figures for a particular industry can include a significant amount of the activity of another industry group.

Differences between Industrial Sectors

10 Though the Bolton Committee found that there were variations in the financial structure of small firms between industries, it did not regard them as significant enough to draw comment. It is notable, however, that unincorporated manufacturers appear to have a lower proportion of equity to total finance than unincorporated non-manufacturers, whereas for corporate small firms the opposite appears to be the case. The relevant proportions are shown in Table (b) of Appendix 2.

SOURCES OF EXTERNAL EQUITY FINANCE

Major Sources

11 So far as is known, no information is available about the proportion of equity finance provided from external sources or the proportion of funds available from external sources that are invested in small firms by way of equity holdings. However, research commissioned by the Bolton Committee showed that external funds comprise a very small proportion of total assets employed by the small firms sector, and that institutional funds tend to be concentrated on the expanding firm.

12 The main external sources of equity finance are private individuals, though their importance is declining with the decrease in the number able to invest substantial sums; institutions such as insurance companies, pension funds and merchant banks; and for fast growing firms with an earlier prospect of obtaining a public quotation, a small number of venture capital companies, usually offshoots of merchant banks or insurance companies.

13 Of the latter the most important is the Industrial and Commercial Finance Corporation Ltd (ICFC) established in 1945 by the Bank of England and major clearing banks, which provides finance to small and medium sized businesses in amounts ranging from £5000 to £500,000 or more; It is thought that the investment by ICFC since its founding of over £375m in some 3000 small and medium sized companies (the proportion invested as equity in small firms is unknown) exceeds the combined amount invested by other equity or venture capital companies having an interest in the small firms sector.

14 Many institutional investors, including ICFC, make it their policy never, or only rarely, to intentionally acquire a controlling interest in companies in which they invest, but the size of an equity holding can vary considerably. The Bolton Committee researchers found 1 merchant bank that tries to restrict its holding to 15% or less, but it is estimated that 25-30% is a more typical figure.

15 Equity/.....

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15 Equity capital may sometimes be sought to provide capital to pay Capital Transfer Tax (formerly Estate Duty) without breaking up the business. Certain institutions, of which the Estate Duty Investment Trust (EDITH) is best known, specialise in buying minority interests for this purpose. EDITH is not normally prepared to invest less than £20,000 in any company, and its investments are effectively restricted to companies earning before-tax profits of £15,000 per annum and upwards. Though this kind of investment has tended to remain static in the past, the introduction of Capital Transfer Tax in 1975 may see a growth in demand in the future.

Relative Importance of Government and Private Sector Sources

16 Though small firms are eligible for aid under the Government's regional development programmes, the amount of help given in the form of equity investment since the passage of the Industry Act 1972 is nil. The only other potential source of government equity is the National Research and Development Corporation (NRDC) which provides funds to assist the exploitation of inventions, and which invested £3m in the form of equity in companies of all sizes in 1973.

The Minimum requirements for Raising Equity on the Stock Market

17 A company seeking equity finance on the Stock Market for the first time is required to provide certain specified information in a form approved by the Stock Exchange. Additionally when the company is admitted to the Official List, it enters into a 'Listing Agreement' under which it is required to maintain a regular supply of information to its shareholders and the investing public.

18 Applications for a Stock Exchange listing are considered from companies whose listed securities are expected to have an initial aggregate market value of at least £500,000. This may be made up of more than one class of security but an application will not normally be considered in respect of any single security whose initial market capitalisation is expected to be below £200,000. In exceptional cases a lower initial capitalisation may be acceptable where the Council of the Stock Exchange are satisfied as to marketability.

19 At least 35% of any class of issued equity capital or securities convertible into equity capital is required to be in the hands of the public, that is, persons who are not associated with the Directors of major shareholders. In the case of very large issues the Council of the Stock Exchange may be prepared to allow a lower percentage.

20 The/....

20 The usual methods by which vendors or Companies obtain a listing and raise finance for securities, previously privately held, are by "offers for sale" or "placings". (There are also facilities for introducing to the market securities which are already widely held, possibly being quoted on one of the Provincial exchanges, for raising additional funds or making acquisitions by the issue of further securities of a class which is already listed and for the conversion of securities and the exercise of options and warrants.)

21 In the case of "offers for sale" (and the less common "prospectus issue") a prospectus is required, which after approval by the Stock Exchange must be issued and advertised. A card based on the prospectus is also required to be inserted in the statistical services. This enables the offer to be made to the public by an issuing house or broker (or by the company itself in the case of a "prospectus issue") or securities already in issue or for which they have agreed to subscribe.

22 A placing is the sale of or obtaining subscription for securities by an issuing house or broker through the market and to or by their own clients. This method is generally only allowed where there is not likely to be a significant public demand for the securities and where the expected market value of the securities to be placed does not exceed a prescribed maximum amount fixed from time to time by the Stock Exchange. (At present this amount is £500,000). This concessionary method of obtaining a listing may be favoured by small firms as it avoids the necessity of producing a full prospectus and is less expensive than the other methods.

23 Appendices 4 and 5 show the expected contents of a prospectus and the requirements the Stock Exchange insists that a company should comply with to obtain a listing.

Adequacy of Existing Sources of Equity Finance

24 The Bolton Committee examined the needs of small firms for external finance, including equity, in considerable detail. It found that the main limitations on most small firms ability to raise equity or long term funds are a lack of knowledge of the sources of finance available, the increased cost of overheads (the "transaction" cost) when applied to smaller firms and the lack of management and accounting procedures which would enable investors and lenders to accurately assess the potential rewards and risks involved. It also found that there was no imperfection in the supply of finance to warrant either the creation by Government of a new institution or the way existing ones are organised. It concluded therefore that though some small businesses would/....

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would be unable to find finance of the type they need, at the price they can afford to pay, any deserving firm would eventually find a source from which it could obtain finance though not necessarily in the form of equity, on proper terms. Broadly this position still obtains today, though it is kept under frequent review.

FISCAL POLICIES

Effect of Current Fiscal Policy on Self-Financing

25 The corporation tax system which has operated in the UK with effect from financial year 1973 is an imputation system under which part of the company's liability to corporation tax is imputed to the shareholder by way of a tax credit which satisfies the basic rate income tax liability of the shareholder in respect of the dividends received from the company. To ensure that this credit is always covered by tax actually paid by the company, a company that pays a dividend must at that time make an advance payment of corporation tax equal to the amount of the credit that the shareholder will be able to claim. This advance payment can be set off against the company's liability to corporation tax for the period in which the dividend is paid.

26 Prior to financial year 1973 the system in operation was a classical system under which the liabilities of company and its shareholders are completely separated.

27 Thus the imputation system does not discriminate against distributed profits as did the classical system since the latter involved full economic double taxation of profits (first in the hands of the company when earned and secondly in the hand of the shareholders when distributed). As the imputation system involves even-handedness of treatment for profits whether distributed or undistributed it is likely that it leads to a higher level of distribution than would the classical system and therefore reduces retentions of profits available for self-financing.

28 For the closely owned company (ie one controlled by 5 or fewer persons or by its directors) this tendency has in the past been reinforced by the enforcement of distributions through the so-called shortfall provisions requiring close companies to distribute a minimum percentage of their profits. These provisions still exist, but are of less significance following the introduction of the imputation system and their effect has in any case been mitigated by changes in the law which have removed many companies from the liability to shortfall assessment. There have also always been provisions for lower distributions than the required minimum when the need for higher retentions can be demonstrated, and the Bolton Committee was satisfied that these have been very well/....

well and sympathetically administered by the tax authorities.

29 Capital taxation in the UK consists of a tax on capital gains following the actual or deemed disposal of assets, introduced in 1965, and a tax on the transfer of capital in the form of gifts either during the lifetime of the donor or on his death. An annual wealth tax is at present under consideration. Companies as well as individuals are subject to tax on capital gains. Capital Transfer Tax and the proposed Wealth Tax are chargeable to individuals only.

30 These taxes may affect the self-financing capability of small firms either through their effect on individual owners and shareholders as is argued in the case of Capital Transfer and Wealth Taxes, by leading to the distribution of profits in preference to their retention in the business, or when the tax is paid out of the income of the business, by reducing the surplus available for reinvestment. However, as these taxes have only just, or have yet to, become a reality, time alone will tell whether these dangers materialise. A different, but related, danger lies in the possibility that assets will be realised as a means of overcoming liquidity problems arising from a liability to tax. However, the Bolton Committee recognised in the context of capital gains that disposal of a share of the equity is a more likely course which, if adopted, would have no effect on the ability of a business to finance itself from its own resources.

Modifications of Fiscal Policy to allow for Inflation

31 There has been no general modification of fiscal policy to allow for the effects of inflation, though following publication of the Report of the Committee on Inflation Accounting in September this year, consideration is being given by the Government to its fiscal implications for the corporate sector and for the business community as a whole. Three specific measures that have been adopted to mitigate the effects of inflation from which small businesses benefit are:

(1) raising the profit limits in 1974 governing the eligibility of companies to qualify for the small firms rate of Corporation Tax (see para 35 below);

(2) introduction of stock appreciation relief whereby profits arising from inflationary increases in the value of stocks and work in progress are excluded from liability to tax;

(3) doubling of the exemption from Capital Gains Tax on business assets disposed of on retirement.

Effect/.....

Effect of Fiscal Policy on the Raising of Capital

32 There are three aspects of fiscal policy that affect the raising of capital. The first results from the lack of discrimination against distributed profits that is inherent in the imputation system. This permits the market to have a less restrained influence over the distribution and reinvestment of profits and those businesses which have good profit expectations will presumably find it easier to attract capital.

33 The second factor which acts contrary to this is the disparity of treatment between distributions in respect of equity capital and interest payments in respect of borrowed funds. Whereas dividends must be paid out of taxed profits interest payments are allowable in computing corporation tax profits. [See example at Appendix 6.] The result is clearly that equity funds are a more costly form of finance than borrowed funds. The effect is however less marked under an imputation system than under a classical system and the change to the imputation system should have resulted in a greater proportion of finance being raised through equity rather than borrowing than would otherwise have been the case. As this is however only one of many factors to be considered in financing decisions it is not possible to quote data in support of this. The gap between the cost of equity and borrowed funds is less in the case of companies which can take the benefit of the small company's rate of corporation tax, (see paragraph 35). The disparity of treatment also disappears when the shareholder is itself a body liable to corporation tax. If the income that it receives is in the form of a dividend then the tax credit that it receives covers its full liability to tax in respect of the dividend since dividends flowing from one UK company to another are not liable to corporation tax. If however, the income is in the form of interest on monies loaned the tax credit is allowed against the company's corporation tax liability the additional tax payable cancelling the more favourable treatment afforded to the interest payment in the hands of the paying company.

34 The third aspect is Stamp Duty. Although Stamp Duty is payable on the transfer of both loan stock and shares there is no duty chargeable on the issue by a company of debentures or loan stock comparable to the duty chargeable on the issue of share capital. The rate of duty payable on the issue of share capital is one per cent. This disparity of treatment will again be one factor to be taken into account when considering whether to raise funds by an issue of shares or by borrowing.

Special Provisions for Small Firms

35 Successive Governments have accepted the Bolton Committee conclusions that small firms neither need nor desire preferential treatment of any kind, but in accordance with/...

with the Committee's main recommendation have tried to avoid any action that inadvertantly discriminates aginst the sector. Fiscal measures from which small firms benefit are therefore either generally available, or are designed to avoid discrimination resulting from size. The main provisions are:-

(1) a so-called 'small firms rate' of Corporation Tax for profits up to £25,000. Between £25,000 and £40,000, profits are taxed on a sliding scale between the "small firms", and the standard rate. Above £40,000 the standard rate applies. Current "small firm" and standard rates are 42% and 52%. It should be noted that profits are charged at a single rate according to the band in which the total profit falls. For example, if profits exceed £25,000, but not £40,000 the whole profit is chargeable at a single rate on the sliding scale. Similarly if profits exceed £40,000, the whole profit is charged at 52%, ie there is no banding;

(2) though Capital Transfer Tax is an individual and not a business liability, measures have been included to facilitate the transfer of small business interests, and to encourage their transfer during the lifetime of the donor in the interests of orderly succession. These are:

  (a) a lower rate of tax on lifetime transfers up to £500,000 in value provided they are made at least 3 years before the donor's death;

  (b) provision for tax to be paid by the donee;

  (c) provision to pay tax by interest free instalments over 8 years up to a value of £250,000.

(3) Capital Gains Tax due on disposal of certain types of business interest may be paid by interest free instalments over 8 years.

Special Provisions for Different Legal Forms of Business

36 Under UK taxation provisions the proprietors of unincorporated businesses whether sole-proprietors or partnerships are assessed to income tax in respect of their profits at the rate of tax applicable to the personal circumstances of the proprietor ie after deduction of allowances, at the basic rate and, if appropriate, the higher rates. Where the profits of the business are substantial, because income tax is chargeable on the full amount of business profits regardless of whether they are distributed, an unincorporated business is unfavourably treated in comparison with a company as regards undistributed/......

undistributed profits but more favourably treated as regards distributed profits.

37 Secondly the favourable treatment that corporation tax affords to borrowed funds does not have the same effect in respect of unincorporated businesses liable to income tax. Although the interest payments are deductible in computing the business profits liable to income tax the interest itself is assessable to income tax in the hands of the recipient. Moreover, because the interest but not the business profits will be investment income chargeable to investment income surcharge, there is a bias in favour of direct proprietorial investment in an unincorporated business rather than investment by way of loan.

INITIATIVES TO RESOLVE THE PROBLEM

<u>Initiatives taken with the past 5 to 10 years</u>

38 The major initiative taken in the small firms field in this period was the setting up in 1969 of the Bolton Committee of Enquiry on Small Firms to examine the role of small firms in the national economy, and in particular their profitability and the availability of finance. The Committee eventually reported in 1971.

39 The policies adopted by UK Governments since that time have been in accordance with the Committee's conclusions referred to in paragraph 35 , and many of the Committee's recommendations have now been implemented.

40 The Committee was broadly satisfied that adequate sources of equity capital were available to small firms and made no recommendations on this point. Several changes in tax legislation which would affect retained profits were recommended and where it has been possible in the context of wider economic and social policies, these changes have been introduced.

41 An important initiative taken in 1974 by the Bank of England in association with the English and Scottish clearing banks as joint owners of Finance for Industry Ltd (FFI) was the expansion of FFI's capacity to provide medium term finance for investment by British industry. The aim is to make £1000m available for this purpose by way of loans financed by various means from market and bank sources. Though it is envisaged that the vast majority of these loans will be to medium and large sized firms, some additional facilities are expected to be provided to the small firms sector through the FFI's subsidiary, ICFC Ltd.

New/.....

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New Initiatives being Examined within the Public and Private Sectors

42 One of the duties of the Small Firms Division of the Department of Industry is to keep under review the needs of the small firms sector and to determine whether special measures to assist the sector might become necessary, particularly during the current period of inflation. At the present time, consideration is being given to a number of proposals for helping small firms, based on a recent assessment of the health of the sector and of the range of feasible financial and fiscal measures available. For obvious reasons, however, no details of the possibilities being examined can be disclosed though some discussion of the range of potential measures may be possible at the meeting to be held later in the year.

Small Firms as Defined by the Bolton Committee

Industry	Definitions adopted in the report (figures relate to 1969)	Turnover updated to 1974 levels
Manufacturing	200 employees or less;	
Retailing	turnover £50,000 or less	turnover £86,000 or less
Wholesale Trades	turnover £200,000 or less	turnover £306,000 or less
Construction	25 employees or less	
Mining/Quarrying	25 employees or less	
Motor Trades	turnover £100,000 or less	turnover £172,000 or less
Miscellaneous Services	turnover £50,000 or less	turnover £86,000 or less
Road Transport	5 vehicles or less	
Catering	All excluding multiples and brewery managed public houses.	

Table (a)

Balance sheet structure of small firms compared with quoted companies

	Per cent of total assets/capital and liabilities			
	Small Firms (1968-69)		Quoted Companies (1967)	
Tangible fixed assets	31.5		40.4	
Goodwill	2.6		2.8	
Trade Investments			3.1	
Total Fixed assets		34.1		46.3
Stocks and w.i.p.	24.9		24.4	
Debtors	27.0		23.0	
Cash	7.8		3.8	
Investments			2.1	
Other Current assets	6.3		0.3	
Total Current assets		65.9		53.7
Total Fixed and Current Assets		100.0		100.0
Ordinary shares	28.2		20.9	
Preference shares	1.5		2.3	
Capital and revenue reserves	23.3		29.3	
Directors' loans	3.4			
Future tax reserves			2.8	
Total capital and reserves		56.4		55.8
Minority interests			2.4	
Long term loans	5.1		12.5	
Bank loans and overdrafts	8.6		6.2	
Creditors	26.7		18.5	
Other current liabilities	3.3		4.5	
Total liabilities		43.6		44.2
All Capital and Liabilities		100.0		100.0

Source: Bolton Report, Chapter 2.

Table (b)

Small firms: structure of balance sheets of companies and unincorporated firms in manufacturing and in non-manufacturing

	Per cent of total assets/capital and liabilities							
	Manufacturing				Non-manufacturing			
	Incorporated		Non-incorporated		Incorporated		Non-incorporated	
Tangible fixed assets	34.8		37.5		27.6		39.4	
Goodwill	0.9		2.0		2.2		5.0	
Total Fixed Assets		35.7		39.5		29.8		44.3
Stocks and w.i.p.	21.2		16.6		28.1		19.4	
Debtors	29.9		28.0		30.4		15.6	
Cash	6.8		10.0		6.4		12.3	
Investments and other currents assets	6.5		5.9		5.4		8.5	
Total current assets		64.3		60.5		70.2		55.7
All Assets		100.0		100.0		100.0		100.0
Ordinary shares	18.2				18.4			
Preference shares	1.9				1.9			
Capital and revenue reserves	33.3				27.8			
Directors' loans	4.4				4.9			
Capital and Reserves		57.8		60.5		53.0		67.6
Long term loans	3.6		2.0		4.3		5.6	
Bank loans	7.9		4.3		9.7		6.0	
Creditors	25.9		28.2		30.1		17.2	
Other current liabilities	4.8		5.2		3.0		2.9	
Total Liabilities		42.2		39.5		47.0		32.4
All Capital and Liabilities		100.0		100.0		100.0		100.0

Source: Bolton Report, Chapter 2.

Table 1

Debt as a proportion of shareholders' interest[1]

Listed companies in manufacturing, distribution and other services

Per cent/£ million

	NUMBER OF COMPANIES	Bank Loans	Long-term loans	Total loans	Creditors[2] less debtors	Shareholders interest (
		per cent of shareholders' interest				£m
1964	2,233	9.0	15.7	24.7	- 7.4	14,468
1965	2,198	10.5	16.7	27.2	- 7.2	15,666
1966	2,109	11.7	19.7	31.5	- 8.2	15,993
1967	1,993	11.7	22.8	34.6	- 9.2	15,928
1968	1,829	12.5	24.6	37.1	- 9.8	15,899
1969	1,701	15.0	25.0	40.0	- 7.8	17,390
1969	1,366	14.8	26.3	41.1	- 7.4	16,906
1970	1,309	17.0	27.0	43.9	- 4.6	17,687
1071	1,239	15.2	27.4	42.6	- 1.8	19,177
1972	1,168	14.9	27.0	41.9	- 1.1	21,856
1973	1,116	18.1	26.3	44.4	2.5	25,409

Notes.

(1) Ordinary and preference shares plus revenue, capital and tax reserves, plus minority shareholders' interest, ([illegible]

(2) Short-term loans other than bank loans are included in creditors

Source: Department of Industry analysis of company accounts published in Business Monitor, M3, Company Finance, covering large listed companies operating mainly in the United Kingdom in manufacturing, distribution construction and certain other services. Companies whose main interests are in agriculture, mining, shipping, property, finance, and those operating mainly overseas are not included. The series covers all companies in scope with:

1964 - 69 Net assets of £½ million or more or gross income of £50,000 or more in 1964

1969 - 73 Net assets of £2 million or more or gross income of £200,000 or more in 1968

Debt as a proportion of shareholders' interest(1)

Listed companies by industry – 1973

Per cent/£ million

	Number of companies	Bank loans	Long-term loans	Total loans	Creditors(2) less debtors	Shareholders' interest (1)
		per cent of shareholders' interest				£m
Food	33	23.6	24.6	48.2	9.4	2036
Drink	44	5.3	29.5	34.8	1.7	1761
Tobacco	3	16.0	63.0	79.0	12.9	691
Chemicals and allied industries	46	12.4	39.4	51.8	– 9.3	2786
Metal manufacture	41	19.1	27.2	46.3	– 7.3	776
Non-electrical engineering	145	19.3	17.2	36.5	– 4.8	1509
Electrical engineering	51	10.6	22.2	32.8	– 1.8	2284
Shipbuilding and marine engineering	7	11.0?	40.6	41.7	111.6	63
Vehicles	36	27.6	25.9	53.5	43.3	805
Metal goods not elsewhere specified	67	17.9	18.8	36.7	– 2.4	1040
Textiles	71	23.1	28.0	51.1	– 2.1	1292
Leather, leather goods and fur	6	28.5	25.0	53.5	15.2	24
Clothing and footwear	35	21.8	16.0	37.8	– 3.9	268
Bricks, pottery, glass cement, etc	41	14.9	22.1	37.0	– 5.4	884
Timber, furniture, etc	25	33.1	7.6	40.7	– 0.8	150
Paper, printing and publishing	66	18.7	26.2	44.9	– 7.3	1534
Other manufacturing industries	43	28.3	20.5	48.9	– 3.5	588
Total manufacturing industries	762	16.9	27.6	44.4	0.3	18491
Construction	84	33.0	17.4	50.4	35.5	860
Transport and communication	16	27.2	16.4	43.6	3.0	240
Wholesale distribution	78	39.9	17.9	57.7	– 1.6	853
Retail distribution	86	8.9	15.8	24.6	0.5	2516
Miscellaneous services	70	24.4	38.9	63.3	10.6	1799
Companies with mixed activities	20	21.9	20.6	42.4	12.7	651
Manufacturing, distribution, etc	1,116	18.1	26.3	44.4	2.5	25409

Notes – see notes to Table 1

The Contents of a Prospectus

(In the case where listing is sought for securities of a company no part of whose capital is already listed.)

A statement by the directors accepting responsibility for the accuracy and adequac the information.

Details of the authorised and issued share capital of the company.

Details of all borrowings by the company.

Details of the directors and secretary, the bankers, brokers, solicitors, registrar trustees and auditors.

The rights of each class of shareholders

A summary of the articles of association concerning directors' powers.

The nature of the business and full details of subsidiaries and other material investments.

A five year record of sales and gross trading income.

A statement of the financial and trading prospects of the company including the assumptions on which any profits forecast is based.

A statement by the directors as to the sufficiency of working capital.

A statement of the amount of the proceeds of the issue and how they are to be appli

A full report by the auditors to the company covering the last five accounting periods and any material changes since the end of the last accounting period.

Full details of any capital issued by the company within the last 2 years whether cash or other consideration.

Full details of any capital which is under option or similar agreement.

Details of preliminary and other expenses incurred in the issue and by whom payable

Details of commissions, discounts, brokerages etc granted within the last two years in connection with the issue of capital in the company.

A statement showing

(a) alterations in the share capital during the last two years.
(b) the interests of each director in the share capital.
(c) details of any other substantial interest in the company's share capital.

Details of directors' service contracts and their aggregate emoluments.

Details of any interests of the directors in any of the assets acquired or sold by the company within the last two years.

A statement of any material litigation pending.

Confirmation of any statements purporting to be based on expert evidence.

Details of material contracts outside the ordinary course of business.

Details of when and where relevant company documents may be inspected.

To issue interim reports not more than 6 months from the date of the notice conve
the A.G.M.

To supplement the annual report of the directors with

(a) information regarding any variation of accounting practices.
(b) a geographical analysis of operations.
(c) particulars about all companies in which the group interest amounts to 20% or more.
(d) a statement of directors' interests and changes in them.
(e) a statement as to whether the company is a 'close' company.
(f) particulars of any contracts in which a director is or was materially interested.

To ensure that service contracts issued to directors are made subject to approval
general meeting and are available for inspection at specified times.

To certify transfers promptly and without charge and similarly to issue certifica
of holdings.

To obtain the consent of the company in general meeting before issuing for cash a
equity capital or securities or entitlements convertible into equity.

To issue to the holders of all securities the details of any circular directed to
the holders of one particular class of the company's securities.

The Listing Agreement

On a company's admission to listing it is required to enter into a "Listing Agreement" with the Stock Exchange. Companies will be requested to renew their Agreement as and when the SE wishes to introduce amendments to the terms.

The Agreement requires a company to give immediate notification of dividends, profits (or losses) and issues of securities and other changes including any information necessary to appraise the position of the company. No price-sensitive information should be divulged in such a way as to place in privileged position anyone outside the company and its advisers. Nor should information be released in such a way that Stock Exchange transactions are entered into at prices which do not reflect the latest available information.

The following are the main requirements specifically covered by the Listing Agreements.

Notification at least ten days in advance, the dates of board meetings at which dividends or statements of profits or losses are likely to be announced.

Notify the SE immediately after the relevant board meetings

(a) Any preliminary profits announcements.
(b) Any decisions regarding dividends or other distributions.
(c) Any proposed change in the capital structure.

Notify the Press the basis ~~the basis~~ of allotment of securities in offers to the public.

Notify the SE immediately

(a) particulars of any material acquisition or realisations.
(b) relevant information under the provisions of the City Code on Take-overs an Mergers.
(c) any changes in directors.
(d) any proposed change in the general character or nature of the business.
(e) any information required by the Companies Act. (Section 33). This concerns the notification to a company of the acquisition of an interest of 10% or more in it by another company.
(f) any change in the status of the company under the close company provisions.
(g) any other information necessary to avoid the establishment of a false marke in its securities.

To issue proxy forms to persons entitled to vote at meetings.

To forward to the SE

(a) proofs, for approval, of all circulars and notices to holders of securitie
(b) all circulars and notices immediately they are issued.
(c) all resolutions passed at AGMs.

Notify the SE if the annual report is delayed more than 6 months after the end of the period to which it refers and the reasons for such delay.

EFFECTS OF TAX ON EQUITY AND LOAN FINANCING (para 33)

Company Profits £100,000

Corporation Tax Rate 52%

Income Tax Basic Rate 35%

Finance required by company £100,000

Return required by investor 10% before tax

	Financed by equity		Financed by borrowing	
	£		£	
Profits	100,000		100,000	
Loan interest	-		10,000	(basic rate tax to be deducted)
CT	52,000		46,800	
	48,000		43,200	
Dividends	6,500	(tax credit 3,500 to shareholders)	-	
Retained Profits	41,500		43,200	

FINANCING OF SMALL FIRMS IN NORTHERN IRELAND
NOTE BY THE DEPARTMENT OF COMMERCE FOR NORTHERN IRELAND

1. In general, the information about the financing of small firms set out in the main paper applies equally to Northern Ireland as it does to the rest of the United Kingdom, although a firm which was considered small by the Bolton Committee (ie one employing up to 200 persons) is quite large in the Northern Ireland context. The main difference lies in the iniatives taken within the past five years to deal with the problems of small firms in Northern Ireland. This difference is reflected in the specifically Northern Ireland institutions - the Local Enterprise Development Unit (LEDU) and the Northern Ireland Finance Corporation (NIFC) which have been set up under devolved legislative powers.

LOCAL ENTERPRISE DEVELOPMENT UNIT

2. LEDU was set up in 1971 (under the Industries Development Act (Northern Ireland) 1971) to promote and assist the expansion of employment in small local enterprises. The Unit is a Company limited by guarantee and funded directly by Government grant. Its remit extends to providing financial and other assistance to firms employing up to 50 persons in the manufacturing sector and to service activities ancilliary to industry, agriculture and tourism. While LEDU is empowered to give assistance by way of equity, it has not, to date, provided funds in this way.

NORTHERN IRELAND FINANCE CORPORATION

3. Although the Northern Ireland Finance Corporation was not established primarily to help small firms, its mandate covers undertakings in all industrial sectors employing 50 or more persons. The NIFC is a statutory body, set up in May 1972 under the Northern Ireland Finance Corporation (Northern Ireland) Order

1972, initially having its main objective the provision of assistance to local companies whose business had been adversely affected by civil disorder. It was recognised that there were a number of firms suffering from serious liquidity problems but which with appropriate assistance had reasonably good prospects of viability in the longer term and had a valuable contribution to make to the Northern Ireland economy. The Corporation, which has available to it funds of up to £50 million, is empowered to assist companies by means of loans, loan guarantees and equity.

4. While the first priority of the Corporation was in the field of survival finance, it has since entered upon a longer term phase of encouraging and assisting new investment through the growth of existing industry, the attraction of new industry and the provision of venture capital. In this wide field, the NIFC acts as a commercially orientated development bank and its power to take equity in undertakings which it assists is thus of increasing importance. The Corporation's powers to take equity has to be seen not only in the light of its objective of providing financial assistance but also in terms of its further aim to increase the indigenous share of the ownership and control of Northern Ireland industry.

5. Since it was set up the Corporation has provided £3.54 million by way of equity, involving 22 firms. Assistance to 10 of these companies has involved 50 per cent or more equity participation.

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KURS FÜR DIE UMRECHNUNG DER NATIONALEN WÄHRUNGEN DER LÄNDER DER GEMEINSCHAFT, DER VEREINIGTEN STAATEN UND JAPANS IN EUROPÄISCHE RECHNUNGSEINHEITEN (R.E.) AM 2.12.1975

EXCHANGE RATE IN EUROPEAN UNITS OF ACCOUNT (U.C.) OF THE CURRENCIES OF MEMBER COUNTRIES OF THE COMMUNITY, THE UNITED STATES OF AMERICA AND JAPAN ON 2.12.1975

TAUX DE CONVERSION EN UNITES DE COMPTE EUROPEENNES (U.C.) DES MONNAIES NATIONALES DES PAYS DE LA COMMUNAUTE, DES ETATS-UNIS ET DU JAPON AU 2.12.1975

TASSO DI CONVERSIONE IN UNITA'DI CONTO EUROPEE (U.C.) DELLE MONETE NAZIONALI DEI PAESI DELLA COMUNITA', DEGLI STATI UNITI E DEL GIAPPONE AL 2.12.1975

OMREKENINGSKOERSEN IN EUROPESE REKENEENHEDEN (RE.) VAN DE NATIONALE VALUTA VAN DE LANDEN VAN DE GEMEENSCHAP, DE VERENIGDE STATEN EN JAPAN PER 2.12.1975

PAYS	MONNAIE NATIONALE (100.000)	U.C. (1)
DEUTSCHLAND (B.R.)	DM.	32.685,-
BELGIQUE/BELGIË	FB.	2.171,-
DANMARK	C.	13.999,-
FRANCE	FF.	19.240,-
IRELAND	L.Ir.	173.375,-
ITALIA	Lit.	125,-
LUXEMBOURG	F.L.	2.171,-
NEDERLAND	FL.	31.892,-
UNITED KINGDOM	L.S.	173.114,-
U.S.A.	Dol.	85.917,-
JAPON	Yen	282,-

(1) 1 U.C. = 1,16 dol.