



*European Communities
Commission
Background Report*

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HELP FOR SMALL BUSINESSES

Four out of five people, it appears, according to a European Parliament Report, ⁽¹⁾ prefer to work in small or medium-sized firms - with a maximum of 500 employees - than in larger ones. In practice, apart from those working in agriculture or public administration, between a half and two-thirds of working people are employed in these smaller firms in the Community today.

Since the end of the War, however, the small business has been tolerated rather than encouraged. The conventional wisdom has favoured bigness and rationalization in the interests of technology and efficiency. Now, in a period of high unemployment - currently 6 million people in the Community are without jobs - this attitude is changing. The authorities have begun to realize that small firms are usually labour-intensive, that they are flexible and adaptable, normally enjoy good staff/management relations and that, rather than go to the wall, they should be encouraged to prosper.

Both the European Parliament and the Economic and Social Committee have urged Community action in favour of small businesses. They cover such a wide variety of structure and product, however, that the Commission has found difficulty in categorising them or devising a common approach to help them.

Now the European Parliament is again pressing for action. The report from the Parliament's Committee on Economic and Monetary Affairs ⁽¹⁾ not only examines the role of small businesses in the Community's economy, but proposes some radical changes in tax and social security contributions to help the small businessman survive. The Commission has also recently introduced changes in Community competition law designed to extend the scope for close co-operation between small or medium sized firms.

It is now working on other measures to benefit the small business in connection with sub-contracting, block exemption of certain patent-licensing, and mergers.

Problems of small businesses

Although West Germany, France, Italy and Belgium have an official definition of an 'artisanat' or small business, the Commission considers any undertaking with a maximum of 500 employees as a small or medium-sized undertaking (SMU). The definition may be arbitrary: certainly it covers a vast variety of activity. But statistical information on small businesses is meagre and any definition has its drawbacks. SMUs, however, have 4 other general characteristics in common:

(1) PE 49.357/fin, 8 February 1978

- * They are often run by independent entrepreneurs, who are usually personally involved in the various stages of the production process;
- * as a rule they serve small markets and supply a specialised product, and are particularly numerous in the distribution sector at the end of the economic chain;
- * they are mostly labour-intensive, with few opportunities of raising productivity by mass production and machines;
- * they do not usually have direct access to the capital market.

The EP Report sees the great strength of SMUs in their servicing and adaptability to local markets and consumer interest. Prospects are particularly favourable to them in the sub-contracting sector and in the repairs and maintenance sectors of consumer products and durables where, in a period of economic restraint, people may prefer to make their domestic purchases last longer than resort to buying new ones.

In other sectors, however, economic recession works to the disadvantage of small businesses. This is particularly so in a period of inflation, when labour costs rise faster than the other elements of the cost price. Between 1973 and 1975 labour costs per unit product rose sharply in some Community countries - from 25 per cent in Germany to 83 per cent in Italy. This has particularly hit SMUs engaged in the retail trade. They have also been affected by the deliberate policy of member governments to raise the incomes of the low-paid, particularly of women and young people.

The EP Report notes that SMUs have relatively little influence on central wage negotiations or on government wage policy. One of the consequences is that rises in productivity are usually taken as the starting point in industry for negotiations for wage increases. This is unfavourable to the small business because often the nature of its work makes productivity an unrealistic criterion. The EP Committee suggests that in future the labour-intensive SMU should have more say in wage negotiations so that better account can be taken of the needs of this sector. Government pricing policies should also differentiate between labour-intensive and other sectors of trade.

While on the plus side SMUs can offer job satisfaction and adaptability, there is also a negative side. Because of their size the administrative echelons may be weak; they have no easy access to capital, and banks may be chary of lending to them; training opportunities are limited, and there can be a tendency to stick to old ways and resist innovation.

The Report suggests that while SMUs do not wish to be given preferential treatment, they want their special characteristics to be taken into account. Though many governments, including Britain, are now beginning to do this, in the past government policy has been focussed mainly on large undertakings, because of the size of their workforce. Now an integration policy is required which enables large, medium-sized and small firms to flourish, and where the special handicaps of the latter, relating to further training, information and financing receive special attention.

Social Security contributions

Both the Economic and Social Committee in 1974* and the EP Report refer to the burden of social security contributions on labour-intensive enterprises and the need to introduce a basic package of social security provisions for the self-employed in all Member States.

The EP Report notes that in general, in all Community countries, the general burden of social security contributions falls relatively heavily on production industries. Today, an important part of social security expenditure is no longer linked to the position of the wage earner, yet payments to non-workers form an element of labour costs. As the costs of contributions rise and are reflected in these costs, so there is the greater incentive to replace men by machines. Where this is not possible in small labour-intensive industries, the small man has to reduce his staff or go out of business, thus adding yet further to unemployment.

The Parliamentary Committee suggests that some reform is needed which will shift the basis of assessment for social security contributions from the labour factor to added value, so as to achieve a more balanced spread among companies. This means that the amount to be collected from a company in social charges should be calculated not only on the basis of the wage bill but also partly on the basis of the added value of these companies. While admitting the disadvantages of the scheme - notably that it could provide less incentive to modernize and increase productivity - the Committee suggests that, in the present climate, this may be less important than retaining jobs.

While accepting that no such radical change could be introduced immediately, the Committee believes that the subject should be aired now with a view to reform in the future.

Community action

The Commission believes that help for small businesses is essentially a matter for national governments, but in the last few months it has taken specific action to try and help them at Community level by expanding the scope of the Business Co-operation Centre and relaxing certain restrictions affecting competition policy.

The Business Co-operation Centre

The Centre - or 'marriage bureau' as it is sometimes called - was set up in 1973 to help small and medium sized companies co-operate to their mutual profit across national boundaries inside the Community.

Between May 1973 and November 1976 the Centre answered 2,000 requests for information and processed about 350 requests for co-operation. In the end, however, only 50 inter-firm agreements were achieved, of which nearly half (24) concerned British companies. Indeed, British firms have accounted for more enquiries to the Centre than any other country, totalling just under 30 per cent of all enquiries in 1976.

Last year, however, the Commission decided to give the Centre a more active role. Its work it felt was too passive and spread too thin. In future it

* CES 731/74 D/Rab hn, 16 July 1974 and Opinion, CES/1158/77 pk 23 November 1977.

will concentrate on special sectors for 'matching' companies, depending on growth and advantages to competition and, instead of waiting for enquiries from firms, may initiate discussion where co-operation agreements appear to be of mutual advantage. In addition, following requests from non-Member countries, and subject to certain conditions, the Centre can now put Community firms in touch with non-Community ones, and vice-versa.

Competition policy

Article 85 of the EEC Treaty prohibits agreements or concerted practices between firms that result in restriction or distortion of competition within the common market. In 1970, however, the Community of the Six agreed to exclude small business agreements from the general provisions of the Treaty,⁽¹⁾ subject to ceilings on turnover. Many small businesses also benefit by block exemptions allowed under the Article for specialised agreements relating to a particular product.⁽²⁾

The Commission has recently taken two important measures designed to extend scope for co-operation between small firms under these heads.

The qualifying aggregate annual turnover relating to minor agreements has been raised from 15 million units of account to 50 mua (£10m. to £34m) provided, as before, the combined market share does not exceed 5 per cent. The Commission has decided to more than treble the original threshold, not only to take account of inflation, but because experience shows that the aggregate turnover of small and medium sized firms taking part in agreements of minor importance does not, in fact, exceed this new limit.

The second of the Commission's measures widens the scope of block exemptions for specialization agreements, as from 1 January 1978 for five years. The largest aggregate market share which may be held by firms qualifying for exemption is increased from 10 to 15 per cent, and their maximum aggregate annual turnover is increased from 150 mua to 300 mua (£100m. to £200m.) The Commission believes that these changes should be of particular benefit to medium-sized firms which are not members of large corporate groups.

Role of the European Investment Bank (EIB)

The Community makes funds available to industry through its various Funds and the EIB. Some of these benefit SMUs, but in general too little use is made of these opportunities.

To try and remedy this the European Council last March asked the EIB to examine ways of expanding its operations to counter Community economic problems and in December last year the Bank agreed to lend £20 million (30.6 million units of account) to Britain to help finance small and medium industrial ventures in the UK development areas. The mandate was signed between the Bank and the Secretary of State for Industry and the appropriate departments for Scotland, Wales and Northern Ireland.

Priority is to be given to projects carried out by small and medium-sized companies which will create or safeguard employment in these areas.

(1) OJ No. C 64, 2 June 1970 and OJ No. C 313, 29 December 1977.

(2) Regulation (EEC) 2779/72, OJ No. L 292, 29 December 1972 and OJ No. L 338, 28 December 1977.

Loans will amount to between £30,000 and £2.6 million and may cover up to 50 per cent of the fixed asset costs involved in a project. The terms agreed by the Bank will be for 7 years; after two years deferment, repayment will be by equal six-monthly installments of capital and interest. The interest rate has been fixed at 7.5 per cent.

Though the loans will be disbursed in foreign currencies, the Government will safeguard borrowers from the effects of any fluctuations in exchange rates; it will also provide the EIB with the necessary security, in the form of a guarantee for each loan. The Government will make a charge of 1 per cent for this service.

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