Large Enterprises in the European Economy and their role in regional support programs

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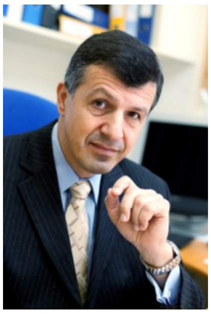

Dear readers,

The European Union has since the beginning been primarily an economic cooperation project. Therefore economic recovery, support of productivity and long-term competitiveness is the ultimate challenge the European policy makers are facing at the moment.

One of the European policies that make an important contribution to the European economy is the EU's cohesion policy. The regulatory framework for this policy, that constitutes the largest expenditure item in the EU's budget for investments in the real economy, is subject of a revision in the conjunction with the adoption of the new multiannual financial framework for the programming period 2014 - 2020. Hence, the European institutions have to decide how to modernize the cohesion policy framework in order to boost the European economy for the benefit of the European society.

One of the important questions in this context is the extent of support targeted on private actors. These actors are currently overburdened by high taxes and public debts that hinder their performance and cause concerns for shareholder investing in Europe.

It is disputable in this context to what extent the cohesion policy should keep actively interfering with private economy or should be streamlined and targeted solely on public sector and precursors of growth such as public infrastructure. However, it is undisputable that if we keep the Keynesian paradigm, we have to secure equal conditions on the market for all companies, either small, or medium or large. Any geographically targeted support has to be based on the quality and required sustainability of the project, and its potential contribution to the job creation and economic growth.

This study shows that large companies generate substantial portion of Europe`s value added and give jobs to significant part of the European society. It demonstrates that discriminatory approach towards large enterprises could impede innovation and reduce the competitiveness of other European companies, SMEs in particular, by excluding them from vital global partnerships in collaborative innovation and by reducing their access to advanced technology. In this context it provides European policy makers with valuable feedback and desired direction indicator for shaping cohesion policy reform.

I wish you enjoyable reading.

Oldřich Vlasák

Vice-President of the European Parliament

ECR Group Coordinator in the Regional Development Committee

Dear friends,

You are opening the study that was initiated by the Confederation of Industry of the Czech Republic. As the most important association of employers in the Czech Republic we represent interests of a wide range of our members – thirty sector federations and about 1600 enterprises, which employ more than 800 thousand workers.

The Confederation consists of a number of enterprises, which differ in size, field of activity and interests. In spite of these facts they all share the belief that business needs to be done in the just environment. Their common objective is to produce goods and offer services requested by customers. This is Alfa and Omega of the prosperity.

Economic growth is collective endeavour of all producers and service providers regardless their size. In our opinion small enterprises are firmly embedded in the value chains of larger enterprises. It is thus obvious that without their projects there would be no contracts for those small ones.

We initiated this study to highlight such interconnectedness. Our opinion is supported by similar findings from abroad; they are included in the analysis.

Currently, there is an ongoing discussion among the European Union and its Member States about the final shape of the next programming period of the Cohesion Policy 2014 – 2020. It is thus important to point out that economic growth of individual countries and the EU as a whole cannot be limited by supporting only one part of employers – small enterprises. This is a strong argument and I believe that European lawmakers will take it into consideration.

Zdeněk Liška

Director General

Confederation of Industry of the Czech Republic

EXECUTIVE SUMMARY

In the new period of Cohesion Policy for 2014 – 2020, under the heading "the thematic concentration" the European Commission proposes to curb support for Larger Enterprises (LEs)[1] in two key areas. First, by excluding them from the productive investments[2] from European Regional Development Fund (ERDF), and second, by limiting initial investment aid[3] for LEs in the new Regional Aid Guidelines (RAG) (1) so that such aid will be allowed only in `a` regions (those most in need). Moreover, operating[4] aid in those regions will only be available for Small and Medium Enterprises (SMEs)[5] and support for large investment projects[6] that are mainly undertaken by LEs will be capped. This paper highlights a number of serious problems with the rationale for and potential impact of this decision by the Commission. Specifically,

- The body of evidence presented by the European Commission is extremely narrow and limited and as such does not clearly demonstrate the lack of effectiveness of productive investments awarded to LEs in a way that justifies the exclusion of LEs from access to productive investment within ERDF and further limitation of regional aid support to LEs. In particular, to ensure the success of the regional development strategies and to achieve the objectives of Cohesion Policy, it is much more important to assess and consider how many jobs are created, what is the quality of those jobs, and the overall sustainability of projects rather than merely focusing on the LE/SME distinction;

- There is huge potential for an adverse impact from the limitation of investment support to LEs that can actually work against the objectives the Commission is trying to achieve through Cohesion Policy and Regional Development Fund, as well as the broader objectives the Europe 2020 strategy. In particular, given that LEs generate substantial portion of EU value added and employment, limiting support may reduce the ability of LEs to support overall growth and employment in the EU;

- It appears that the Commission has overlooked the significant linkages between LEs and SMEs that characterise today's global business environment whereby the collaboration, cooperation and connections between SMEs and LEs in mutually interdependent, complex value and supply chains, innovative and other activities in regional, national and global business ecosystems. The effective functioning of these ecosystems and value chains is essential for supporting economic growth, employment and innovation in SMEs and limiting the support to LEs as proposed by the Commission has the potential to negatively impact SMEs and again work against the objectives the Commission is trying to achieve.

On the basis of the above issues, this paper strongly recommends that in a spirit of subsidiarity it should be left up to the Member States/Regions/Cities to select the particular projects that have the highest potential to achieve the objectives of Cohesion Policy in particular regions rather than constraining their ability to choose projects that may more effectively achieve the objectives by forcing them to exclude them merely on the basis of the size of the enterprise. Thus the legislative proposals for new period of Cohesion Policy should not curb support for LE, but instead, maintain the current status that retains the power of decisions on investment support programmes to individual MS.

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[1] *Based on the 6 May 2003 Commission Recommendation 2003/361/EC regarding the SME definition, large enterprises for the purposes of this document are understood to mean those with more than 250 employees and a turnover of > € 50 million / balance sheet total of > € 43 million.*

[2] *"Productive investments" are also called "Initial investments". In regional aid their purpose is to secure either productive investment (initial investment) or job creation, which is linked to investment. Thus this method favors neither the capital factor nor the labour factor (Information from the Commission - Guidelines on national regional aid" Official Journal C 074, 10/03/1998 P. 0009 – 0018).*

3 "Initial investment" means an investment in material and immaterial assets relating to the setting-up of a new establishment; the extension of an existing establishment; diversification of the output of an establishment into new, additional products; a fundamental change in the overall production process of an existing establishment (Guidelines on National Regional Aid for 2007-2013, 2006/C 54/08).

4 "Operating aid" is aimed at reducing a firm's current expenses and is normally prohibited under Regional Aid. Exceptionally, it may be granted in regions eligible under the derogation in Article 87(3)(a) provided that it is justified in terms of its contribution to regional development. It should in principle only be granted in respect of a predefined set of eligible expenditures or costs (e.g. replacement investments, transport costs or labour costs) and limited to a certain proportion of those costs (Guidelines on National Regional Aid for 2007-2013, 2006/C 54/08).

5 The category of micro, small and medium-sized enterprises (SMEs) is made up of enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding 50 million euro, and/or an annual balance sheet total not exceeding 43 million euro (Commission Recommendation 2003/361/EC).

6 A 'large investment project' is an 'initial investment' with an eligible expenditure above EUR 50 million. A large investment project will be considered to be a single investment project when the initial investment is undertaken in a period of three years by one or more companies and consists of fixed assets combined in an economically indivisible way.

INTRODUCTION

In the last decade a lot of effort has been dedicated to supporting the growth of the European economy, generating employment, reducing the disparities among regions and creating an inclusive society. One of the key instruments for achieving these objectives has been Cohesion Policy. In the new programming period, in addition to focusing on the development of "lagging" regions, Cohesion Policy will also become the main instrument for achieving the objectives of the EU's Europe 2020 strategy to improve Europe`s competitiveness in an increasingly challenging global economic environment.

Similar to non-European economies, the EU has been focusing on support of SMEs (small and medium enterprises[7]) as a key way to achieve economic and employment growth, as well as to foster and improve our innovation performance. Thus, a number of programmes and policies have been created and legislation implemented to support SMEs.

In the new period of the Cohesion Policy for 2014 – 2020, under the heading "the thematic concentration" the European Commission plans to increase this support by excluding LEs from access to productive investments from the European Regional Development Fund. The European Commission argues that such support provided to LEs is not effective and has a relatively low impact on regional development This change is accompanied by more stringent rules for regional aid that are currently under preparation in the DG Competition that will exclude LEs from operational aid and from initial investment aid in more developed regions (1).

This paper highlights a number of serious problems with the rationale for, and potential impact of, this decision by the Commission. Specifically, the paper sets out a specific evidence to demonstrate that the Commission's decision:

- Is based on an extremely narrow and limited body of evidence and that does not provide sufficient rationale or justification for the decision;
- Actually goes against both the objectives and context of Cohesion Policy and Europe's growth and jobs

[7] *Micro, small and medium-sized enterprises are defined by (20) according to their staff headcount and turnover or annual balance-sheet total:*
*A **medium-sized enterprise** is defined as an enterprise which employs fewer than 250 persons and whose annual turnover does not exceed EUR 50 million or whose annual balance-sheet total does not exceed EUR 43 million.*
*A **small enterprise** is defined as an enterprise which employs fewer than 50 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 10 million.*
*A **microenterprise** is defined as an enterprise which employs fewer than 10 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 2 million.*

agenda in the Europe 2020 strategy. and reduces the chance of fostering structural change in less developed EU regions that can be achieved by LEs strategic investments;

- Is likely to have an adverse impact on SMEs given the interconnections and mutual interdependence between SMEs and LEs and;
- Would negatively impact the ability of the EU to attract Foreign Direct Investments (FDI) from outside the EU in what is an increasingly competitive global investment landscape and thus place the EU at a disadvantage in attracting FDI from key extra-EU regions that are becoming increasingly significant sources of FDI.

This paper is structured as follows. The first section analyses in detail the Commission`s rationale and reasons underpinning the decision to exclude LEs from ERDF and limit their access to support from Regional Aid schemes. We focus in particular on the specific references that are quoted in the Commission`s documents. The body of evidence presented by the European Commission is extremely narrow and limited and, as such, does not clearly demonstrate the lack of effectiveness of productive investments awarded to LEs in a manner that justifies the exclusion of LEs from access to productive investment within ERDF and further limitation of Regional Aid support to LEs.

The second section of the paper focuses on the positive impact and benefits that LEs can have directly on the European economy, as well as indirectly on SMEs and other enterprises. We focus in particular on the role of LEs in regional economic ecosystems and draw on case study evidence from the Brno City Municipality in the Czech Republic that demonstrates the effectiveness of investment incentives granted to large enterprises in terms of fostering structural changes in the region and supporting the shift into higher value added activities that has boosted local SMEs` growth.

In the third section, we examine the role of SMEs and LEs in the European economy including their contributions to value added and employment. We argue that on the basis of existing evidence, there is no one size fits all view on the impact and role of SMEs merely by examining the overall relative importance of SMEs in the European economy. A high proportion of SMEs in some countries, for example, in Greece, Italy, Portugal, Spain, and Hungary, does not necessarily mean that their economies are more competitive, innovative and growing in comparison to countries where the number of SMEs is lower, such as in the U.S., U.K., Germany, Finland, and Denmark. The quality of SMEs and the particular sectors they are operating in is clearly also important in determining their overall impact on employment, value added and innovation, as well as the impact of the business and policy environments that affect them in individual Member States.

We conclude by setting out the detail behind our recommendation to maintain the existing approach that leaves the decision about investment support programmes to individual MS and regional or local government authorities.

1 ANALYSIS OF COMMISSION`S ARGUMENTS

The aim of this chapter is to:

- Demonstrate that the evidence presented by the Commission, in terms of it's relevance and scope, does not serve as a sound basis for implementing the proposed change of policy and;
- Assessing the validity of the reasons outlined by the Commission as the basis for excluding LEs from support.

According to the European Commission`s proposal LEs are to be excluded from the scope of ERDF in the area of productive investments connected with job creation. The Commission also proposes limiting support for LEs to "a" type regions (those that are least developed) and plans to exclude LEs from operating aid for all regions, and cap the amount of support for larger investment projects (LIP) that are mainly undertaken by LEs.

These proposed decisions are set out in the draft legislation for ERDF (2) EC where the word **"primarily"** is left out from the provision. That means that an access to productive investments (PI) is granted only to SMEs (see Annex B for details). The key reasons for Commission's decision are described in document (2) and the rationale for limitation of access of LEs to investment and operating aid are also outlined in Non-paper revising Regional Aid Guidelines (1):

Reasons for exclusion of large enterprises from productive investments presented in ERDF (2):

- ***Lack of economic impact:*** *Supporting LEs with cohesion policy or other public resources does not guarantee better performance or growth. The added value in terms of increasing productivity and growth of providing support to large enterprises decreases notably over time.*

- ***Relocation:*** *The use of incentives through ERDF can create tensions between the regions and Member States due to a perception that there are winners and losers in terms of employment and economic activity. Secondly, it is often the case that there is no net benefit in terms of employment at the EU level, since activity has simply been moved rather than additional activity created.*
- ***Difficult to monitor/prove durability of operations:*** *Difficult to prove that supported operations of LEs provide long-term benefits to the regions, in which they are located, because investment decisions by LEs are made on a global basis and as part of a broader strategy of operations and SMEs are closely tied to the region they operate.*

Commission document **(1):Non-paper revision of regional aid guidelines**

…. ***At the same time, for projects implemented by large enterprises, potential distortions of trade and competition are higher than for projects implemented by SMEs.***

- (7) An important concern in the context of regional investment aid for large enterprises is that ***these firms would often have made the investment concerned even without financial support***, rendering such support both ineffective and costly. This 'deadweight' cost can occur in all forms of business support (in both SMEs and large enterprises). However, ***it is more likely to occur for aid to large enterprises. There is a growing body of evidence suggesting that regional investment aid is more effective and efficient when geared towards SMEs.*** In part, this can be attributed to the observation that access to finance is more often a problem for SMEs than it is for large enterprises. From this perspective, ***financial support to SMEs can be expected to make more of a difference than financial support to large enterprises.*** Large enterprises typically have more leverage (bargaining power) vis-`a-vis public authorities, as they are relatively more important to the region than individual SMEs. The efficiency of financial support given to large firms, as measured e.g. in terms of cost per job created, may be adversely affected as a result.
- (9) The possibility for Member States to grant non-degressive and non-temporary operating aid in outermost regions and low population density areas would be maintained as such aid enable to address well-identified problems and does not generally raise major competition concerns. As the current provisions on operating aid in `a` regions have been used in only one measure (in Eastern Germany) and in view of the strong distortive effect of operating aid to large enterprises, ***the possibility to grant 'general' operating aid in 'a' regions would be limited to SMEs*** and under conditions similar to those laid down in paragraphs 76-79 and 82-83 of the current RAG.....

1.1 SCOPE AND RELEVANCE OF EVIDENCE USED BY THE COMMISSION

First, the Commission document (1) notes (on page 3) that "a growing body of evidence" suggesting that regional investment aid is more effective and efficient when geared towards SMEs". All the sources listed by the Commission were analysed in depth and the detail results are presented in Annex A of this study.

The analysis shows that five of seven documents the Commission refer to analyse the effectiveness of R&D public incentives, mostly at the nation state (and not regional) level. Therefore, these are only slightly relevant in the context of regionally targeted support. Only two are relevant in the context of regional support impact analysis and they actually analyse single regional support program in a single EU country/region. Therefore the general applicability of these conclusions to the whole of the EU is not possible from such limited evidence.

None of these works analyses subsidies granted within the cohesion policy framework. They also do not consider whether the subsidies granted contributed to the achievement of the overall policy goals of Cohesion Policy.

The body of research quoted by the Commission is in its majority focused on R&D subsidies, whereas the investment program where the Commission plans to limit support for LEs is much broader than R&D (i.e. productive investment in various thematic areas).

After analysing the evidence provided by the Commission it is possible to conclude that none of these documents offer a substantial basis to justify measures that would significantly limit investment support for LEs as proposed in ERDF and RAG by the Commission.

The Commission`s decisions to exclude LEs from PI related to job creation from the scope of ERDF as well as to limit their access to Regional Aid, are not justified by the research findings presented by the Commission as the specific studies quoted do not clearly prove the ineffectiveness of productive investments or subsidies awarded to LEs.

1.2 ASSESSING THE VALIDITY OF REASONS UNDERPINNING RATIONALE FOR EXCLUDING AND LIMITING SUPPORT TO LEs

There are a number of problematic issues with the various assertions made by the Commission justifying the rationale for excluding and limiting support to LEs.

Firstly, the view of the Commission that providing incentives through EU Structural Funds, especially to larger organizations, merely promotes the relocation of work from mature member-states to less expensive, emerging member-states, and thus produce no net-benefit in terms of employment and wealth creation for Europe, is questionable.

While it is clear that Cohesion Policy should not promote the relocation of enterprises within the EU, the Commission's view underestimates the complexity of major investments by LEs. In reality there is a multitude of factors beyond incentives in the decision making matrix, such as the quality and cost of labour, real estate costs, quality of infrastructure, regulatory considerations, tax regime, labour code, and overall business regulations; as well as political variables, such as stability and the quality of governance. As such, the relocation of an enterprise solely on the basis of taking advantage of incentives within the EU is not compatible with common and sound business decisions. However, as more and more locations outside of the EU offer comparable operating environment such as the availability of a skilled workforce, costs, rule of law, good infrastructure etc. incentives can be a critical determining factor in the decision of where to locate. As such, the EU overall may lose as LEs may look to regions outside EU that compete aggressively attractive investment packages.

It is evident that LEs are in better position to move their operations globally But do they really do this on the scale that would justify their complete exclusion from access to PI? There is no objective evidence presented in Commission`s document that would support this view. Moreover, the Council Regulations and legal provisions of many MS already cover the relocation issues.

The Council Regulation (EC) No 1083/2006 ensures that Community funding does not support relocation within the European Union (article 42) and if Cohesion Policy support is provided for investment by LEs, that undergo a substantial modification of the cessation of a productive activity within five years those funds have to be paid back (article 57).

- Also, in a number of programmes provisions were negotiated with Member States that exclude larger or all companies from receiving ERDF support in case of delocalisation. In cases where there is a suspicion that there are irregularities in the use of Structural Funds, the Commission starts investigations.

Secondly, in relation to the assertion in the Commissions document (1) that "the potential distortions of trade and competition" are to be higher (in LEs) "than for projects implemented by SMEs" we disagree on a number of dimensions. Even though large projects are in most cases carried out by LEs, it is not accurate to imply that all LE projects are "potentially more distortive", then SME projects. LEs initiate and run particular regional projects without regional market-distortion effects in the same way as SMEs do (e.g. design, prototyping centres etc.)[8]. Potential distortion effects are connected with the nature of regional project itself and this should be evaluated within this context, not in regards of the overall size (LEs vs. SME) of the company implementing it.

Thirdly, the Commission is also concerned about the difficulty of monitoring and the durability of operations of LEs in terms of proving that supported operations of LEs provide long-term benefits to the regions. The detailed reasoning of the Commission in (2) is presented as follows: "In practice, these provisions are relatively easy to apply in the case of SMEs, whose economic activity is closely tied to the region in which they operate. In contrast, large multinational enterprises need to make investment decisions on a far more global basis and by definition make location decisions as part of a broader strategy of operations. This increases the burden of monitoring on the part of the Commission and the Managing Authorities."

Excluding LEs from productive investment support based on the fact that there "is the burden of monitoring" does not provide sufficient justification to exclude LEs from support. A more appropriate policy response would be to improve the monitoring processes so that real benefits are measured. We address in detail in next section the questionable validity of excluding LEs on the basis of the long-term benefits that they provide.

[8] *We investigate this issue and outline evidence to support this in the next section on the role of LEs in national and regional economic systems.*

2 ROLE OF LES IN THE NATIONAL AND REGIONAL ECONOMIC ECOSYSTEMS

One of the major shortcomings of the Commission's analysis is that it fails to analyse or investigate the relationship between LE activity and the objectives of Cohesion Policy to determine whether the proposed exclusion of LEs may indirectly hamper the achievement of these objectives. The aim of this section is to address this shortcoming in two key ways.

- Firstly we examine the broad impact of LEs in the areas that are relevant for the objectives of Cohesion Policy. We outline how, given the nature of current business and value ecosystems whereby significant linkages exist between LEs and SME, excluding LEs could have detrimental impacts for SMEs and again work against the overall objectives of Cohesion Policy and the Europe 2020 strategy. Included in this is an analysis of the benefits of the ecosystems created by LEs & SMEs;
- We support this evidence with two specific case studies. The first case study example is based on an evaluation of the current funding period conducted in the Czech Republic that clearly shows the benefits provided by LEs in achieving several key regional objectives. The second case study is the Brno City Municipality where investment incentives granted to LEs led to the transformation of the Brno region from a declining manufacturing site to e Central Europe high tech hub.

The objectives of the new period of the Cohesion Policy are (among others):

The objectives of the new period of the Cohesion Policy (3)

- To support the delivery of the Europe 2020 strategy – specifically job creation, competitiveness, economic growth, improved quality of life and sustainable development
- To concentrate funds on the areas and sectors where they can make the most difference as the expression of the EU`s solidarity with less developed countries and regions
- To reduce the significant economic social and territorial disparities that still exist between Europe`s regions to prevent undermining some of the cornerstones of the EU, including its large single market and its currency, the euro.

EU regional policy is an investment policy. It supports job creation, competitiveness, economic growth, improved quality of life and sustainable development. In the new programming period it should also support the delivery of the Europe 2020 strategy – smart, inclusive and sustainable growth.

If the European Commission would like to pursue greater focus on Cohesion Policy and Europe 2020 strategy objectives, it is necessary to take into consideration the numerous dimensions across which LEs contribute to achieving of these objectives. We now examine some of these key channels.

2.1 IMPORTANCE OF LES, AND LE AND SME ECOSYSTEMS FOR COHESION POLICY AND EUROPE 2020 STRATEGY OBJECTIVES.

The linkages between LEs and SMEs help to support employment in the latter – if support for LEs is reduced, the ability of SMEs to sustain and create employment will be adversely impacted.

In addition, there are also positive spillovers from large firms to firms of other sizes. Evidence shows that FDI leads to substantial productivity gains for domestic firms and the size of FDI spillovers is economically important, accounting for about 11 % of productivity growth in U.S. firms between 1987 and 1996 (4). In the U.K, estimates suggest that a 10 % increase in foreign presence in a U.K. industry raises the total factor productivity of that industry's domestic plants by about 0.5 % (5).

Inter- and intra-industry knowledge spillover effects from large enterprises can also be significant. This huge benefit is completely overlooked and omitted from the Commission's analysis.

LEs` investment in the region is always connected with the transfer of LEs global know-how and technology, which then remains in the region in the form of skilled local workforce and technical equipment available for not only local SMEs, but for a broad spectrum of firms. In short, a wide range of economic players – large and small – will benefit from the positive spillovers from LEs. Indeed, survey evidence from Ireland shows that the majority of the SME IT founders had multinational backgrounds and attributed their experience and skills gained while working for MNCs [9] as key motivating factors in their decision to go into business. The majority of the SME founders considered their multinational backgrounds and the range of skills they gained as being very important to their company (6).

In addition there is the positive impact that the presence of LEs can have on innovation in SMEs and other enterprises. For example, the entry of foreign companies into a domestic region has a positive spillover effect on local firms' innovation - FDI inflow to a sector can also intensifies knowledge sourcing activities

[9] *MNC – multinational company*

from other firms and from within the incumbent itself. Evidence from Estonia has shown that a 10 % higher entry rate of foreign owned firms is associated with 4 % increase in incumbents‘ probability of engaging in process innovation (7).

In terms of the obstacles to SMEs growth, in addition to limited access to financial capital, technology inefficiencies and human resources inefficiencies are also significant. LEs´ knowledge spillovers can contribute to the strengthening of SMEs´ absorptive capacities. As SMEs acquire higher capabilities, they are able to reach the large firms´ requirements, which are mainly related to delivery time, large volume, quality increase, and price reduction. The exclusion of LEs from investment support as proposed by the Commission fails to take into account the other channels through which LEs can address these barriers to SMEs growth. Indeed no analysis is offered by the Commission outlining the relative magnitude of these barriers in a way that would justify the exclusion of LEs on the basis that the capital barrier is the most significant (8).

Participation in global value chains can bring stability to SMEs and allow them to increase productivity and to expand their business. While some SMEs directly engage in foreign trade, others link with international markets by entering the value chain of an MNC. Compared with “going it alone,” partnering with MNCs provides advantages such as increased sales and enhanced firm reputation, access to new markets through the MNC’s established channels, leveraging the MNC’s technical knowledge and other expertise, improved quality and productivity to meet MNC supplier standards; and a stronger base for future growth.

Evidence shows that LEs make sustained efforts to connect with SME suppliers, invest resources in supplier development activities, implement collaborative models of supplier relationship management, introduce supplier diversity programs, and participate in SME product development teams. In most MNC-SME linkages, the MNC partners supply considerable assistance to small businesses in the early stages of their relationship to upgrade their processes and products.

The Berman Group (9) notes that in the Czech Republic “small and medium businesses operate always in symbiosis with large companies and with the frame of procurement of large companies very often prosper”.

The Federation of Austrian Industries (10) declares that “in the case of Austria the top 150 so-called “leading competence units” (LCUs) are large enterprises accounting for 23 % of industrial production, 18 % of total added value and 37 % of total R&D investments in Austria. Around 122,000 SMEs operate in networks with these 150 LCUs.” The Federation also finds (11) that leading competence units are part of the core substance of the Austrian economy. Through their demand for high-quality input, they become the focal points of entire business networks. In conjunction with SMEs they act as pacemakers for growth and innovation, thus creating prosperity and employment in Austria.

The pace of positive social change and quality of life across regions is increasing due to primarily LEs. It is connected to the adoption of so called more integrated business model - one that's socially responsible as well as highly relevant to a company business mission. This trend hastens the development of innovative, cost-effective solutions to challenges like health, environmental protection, employee well-being and community development. It leads to the societal and economic progress and has the power to unleash the next wave of global growth (9).

As the Commission stated many times in its various documents and in its responses to the Parliamentary questions (12) “a primary objective of Cohesion Policy is growth and the creation of new jobs in particular regions and Member States. Any support for productive investment has to be seen in this context. Promoting job creation and economic growth can be achieved in many ways — from the setting up of small enterprises to supporting larger companies - ecosystems, value chains. It also pointed that in a spirit of subsidiarity it is up to the Member States to select projects, which would contribute to reaching the programme's objectives. Also it stressed that “it should up to the managing authorities to carry out a fair and transparent selection of the most suited projects and monitoring their added value. The Commission should ensure that the Member States respect the legislation in force” (12).

The evidence we have outlined above illustrates very clearly that **LEs contribute to Europe 2020 strategy and Cohesion Policy targets and objectives.** It also highlights the negative impact that the proposed change would have on the ability of ability of the EU to achieve the Commission’s objective to provide more effective support to SMEs, as well as also reducing the capacity of MS to implement the Europe 2020 strategy agenda and to fulfil Cohesion Policy objectives in accordance with specific needs of their regions.

If LEs are to be excluded from the access to the productive investments and their access to the Regional Aid further limited, it may be detrimental to the ability of the EU and individual MS to achieve the objectives of Cohesion Policy and Europe 2020 strategy, especially with regards to the employment and R&D targets as stated in Europe 2020 strategy.

As EU countries are already evaluating outcomes of their investment support strategies of 2007 – 2013 period of EU Funds and current results are consistent with the evidence we have presented here, that is, they show that the role of LEs is important for national economies. Thus, the possibility for LEs to access productive investment and to Regional Aid schemes should be maintained in the ERDF legislation for 2014 - 2020. We argue that there is no need to exclude any type of entity from access to productive investments. The main criterion should be how the projects/investments contribute to Europe 2020 strategy and Cohesion Policy objectives, as well as to Regional needs and specifics.

From the perspective of regional policies it is necessary (beyond supporting SMEs) to also support the whole business ecosystem. As the situation differs in individual EU countries and their regions, the Member States should be able to maintain their freedom to design strategies to fulfil Cohesion Policy and Europe 2020 strategy objectives and targets in accordance to their local needs and specifics. **The final decision about investment policies should be left on the Member States and regional authorities.** The Commission should ensure that they respect the legislation in force.

2.2 LE ROLE IN NATIONAL STRATEGIES

In this sub-section, we provide an example of an evaluation of the current funding period conducted in the Czech Republic. Some these outcomes are in contradiction with the reasons of the European Commission regarding the exclusion of LEs from PI and limitation of their access to Regional Aid.

Analysis of priorities and needs of different areas supported by the EU structural funds under the responsibility of the Ministry of Industry and the EU structural funds (9)

Main findings

... Small and medium businesses operate always in symbiosis with large companies - and with the frame of procurement of large companies very often prosper. In the Czech Republic, as shown our socio-economic analyses, the LE domestic sector is relatively weak: (i) large firms are compared to international competitors are still relatively small, (ii) The vast majority of large companies is among "traditional" companies that are still suffer from the effects of prior periods, (iii) most of the great Czech domestic firms are undercapitalized and (iv) is also lagging behind their technological equipment.

... Although small businesses in terms of mass and number of supported projects dominate in investment programs crucial to the competitiveness of Czech companies and the economy, large businesses at the same time in these programs are of great importance. Support for the middle and large business should survive because it is possible that in the aggregate represent a potential growth more important than small business. At the same time another surveys in the field of innovation and competitiveness in the business sector shows that the Czech and medium-sized and large businesses, especially those owned by Czech entities have similar growth problems, such as small businesses...

... Strengthening the SME sector is thus in our view necessarily linked with growth and development of large firms. But they still do not achieve significant growth, up to a large extent due the same reasons that small businesses - non-technical competencies, under-development and relying mainly on their own knowledge resources, or on existing know-how. Support for large firms in principle does not require specific tools, barriers are largely similar to those of SMEs. It is therefore to make available the interventions, or at least part of it, to large companies.

... Aid limited to small or small and medium sized enterprises could have a negative impact on the competitiveness of the Czech Republic as a whole. On the other hand, the support for LE has to be highly targeted and must serve to their growth and penetration into new markets and significant improvement of their position internationally.

... Public support should be given only those large companies that are able to offer in return for significant growth associated with the creation of jobs, with the expansion and qualitative transformation of production.

Extracts from Berman Group analysis (9) listed above also provide information on employment and growth characteristics based on the different size of companies in the Czech Republic – see Table 1. It documents that LEs in the Czech Republic created more jobs than small companies. Therefore, the assumption of lower effectiveness of LEs in job creation has not been proved in the case of this country.

The case of the Czech Republic show that LEs contribute significantly to job creation and to the economic development of the country by nurturing a conducive ecosystem for SMEs, specifically through facilitating technology transfer, innovation and export capacities. The decision to exclude LEs from productive investments could thus have a negative impact on ability of the country to fulfil Europe 2020 strategy objectives.

TABLE 1 – EMPLOYMENT CHARACTERISTICS (IN THOUSANDS OF EMPLOYEES) OF THE CZECH REPUBLIC BASED ON THE SIZE OF THE ENTERPRISE

	2004	2005	2006	2007	2008	Index 2007/2004
Small & Micro	521.7	516.7	505.9	521.7	528.8	101.4
Medium	993.0	1009.2	1022.3	1056.3	1067.0	107.5
Large	1604.3	1608.7	1629.8	1670.2	1689.1	105.4
Total	3119.0	3134.6	3158.0	3248.2	3284.9	105.3

SOURCE: (9)

2.2.1 CASE STUDY EVIDENCE FROM BRNO, THE CZECH REPUBLIC

BRNO

The transformational role of LEs in regional economies and their contribution to its ecosystem is clearly demonstrated in the case of Brno City Municipality.

In 90ties of the last century Brno witnessed decline in its manufacturing industry with disastrous effect on employment and growth. Before the collapse of manufacturing in 1995 the unemployment rate was 1.3 %. After 1995 it rose to 8.1 % and peaked in 2003 at 10.9 %. In total, Brno lost of 245,000 jobs, the majority of which was in industrial production.

Within the framework of the national investment scheme, Brno City Municipality founded an industrial zone and technological park to attract strategic (large) investors. The City offered an investment support program together with quality infrastructure, a competitive cost structure and sufficient numbers of graduates in technical fields.

The result was positive: a number of large companies , (including Honeywell, s. r. o. Daikin Device Czech Republic, s. r. o. IBM Global Services Delivery Center Czech Republic, SILICON GRAPHICS, Motorola Solutions CZ, Vodafone Czech Republic) came to Brno, despite the fact it was unknown location for such investments. As a result, unemployment fell to an impressive 5.7 % by the end of 2008.

The economy of Brno City Municipality has completely restructured and by doing so created some 240,000 jobs.

The role of LEs in the transformation of the Brno region was indispensable. As we have been in beginning of the economic decline in the 90th years concentrated to attract the large investment project (mostly provided by LEs) it helped us to build the sustainable regional economy ecosystem attracting and incorporating the vast number of SMEs acting in the LE value chains or independently and sharing the R&D potential of Brno universities enabled by original LE investments.

Marie Zezůlková, Brno City Municipality.

Below are further opinions regarding the importance of LEs in the revitalisation of Brno.

The core activities of our company are strategic outsourcing services – remote administration and support of servers and applications, network services and End User Support.

We have started in 2001. Incentives from the Czech government were approved in 2001 and 2006. EU incentives were approved in years 2009 and 2010 approval for 2011 request is pending. Since 2005 until now company increased the number of own employees by more than 2.000 people.

Most of key suppliers have either their head office or branch office in the South Moravia region. Their supplies involve rent of buildings, utilities, education courses, recruitment of new employees, subcontracted employees. Their supplies represent a great majority of third party services supplied to the company.

Pavel Dočekal, IBM Global Services Delivery Center Czech Republic,s.r.o.

GTS Brno part of GTS Group 100 % owned by Lufthansa Passage. GTS Brno provides call and support services for LH Group customers in CEE countries, Russia and Germany. GTS in part Load control secures Flight documentation for over 120 airports worldwide.

Initial investment was over 30 mil CZK and started 2005. Investment support from Czech government based on program. Current total number of employees is 290 with plans to reach 300 in 2012.

We are an example of the locally founded SME supported by its mother LE continually growing to become LE due to the increasing regional support and available skilled workforce.

Roman Tesař, *Global Tele sales Brno s.r.o. (Lufthansa)*

Based on the business success, large companies in Brno are closely cooperating with SMEs and universities and contributing to creation of R&D clusters and facilities.

3 ROLE OF LEs & SMEs IN THE EUROPEAN ECONOMY

The aim of this section is to provide an overview of the relative importance of both LEs and SMEs in terms of the enterprise population as well as the contribution to value added, employment, productivity and efficiency.

On the basis of the evidence presented, we conclude that the application of a one size fits all policy toward SMEs and LEs will have different impacts and effects in different Member States and so may in effect work against the objectives of the Commission as part of ERDF, Cohesion Policy and the Europe 2020 strategy.

3.1 PRODUCTIVITY OF EU LEs AND SMEs

We begin by examining a number of indicators[10] related to basic business productivity and efficiency measures overall for the EU and for individual Member States. Wage adjusted labour productivity ratio in Table 2 varies from 122.6 % (EL). to 255 %(LV).

[10] *Data presented in this chapter are mostly based on mostly on publicly available Eurostat source and It should be noted that in comparison with the data sources covering the SME the statistical coverage of the LE is much smaller.*

TABLE 2 – BUSINESS ECONOMY OVERVIEW; PRODUCTIVITY AND PROFITABILITY, NON-FINANCIAL BUSINESS ECONOMY,2006

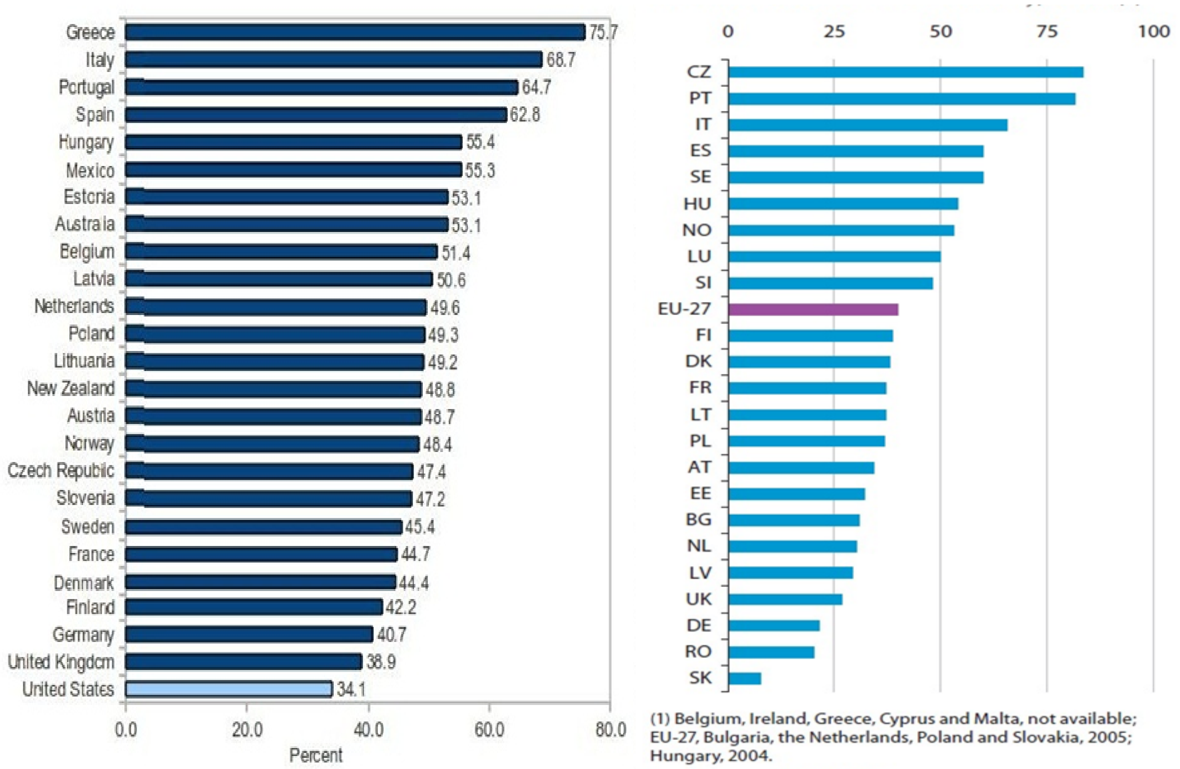
	Apparent labour productivity (EUR thousand per person employed)	Average personnel costs (EUR thousand per employee)	Wage adjusted labour productivity ratio (%)	Gross operating ratio (%)
EU-27	43.5	28.8	151.1	10.8
BE	62.8	44.2	142.2	8.0
BG (1)	5.4	2.6	204.7	9.2
CZ	19.1	11.4	166.8	10.7
DK	65.9	39.1	168.8	12.0
DE	53.6	35.7	150.4	10.4
EE	17.6	9.2	191.0	10.1
IE (1)	83.5	:	:	:
EL	26.9	21.9	122.6	12.2
ES	38.6	26.1	148.0	11.4
FR	54.2	40.6	133.5	7.3
IT	41.6	31.2	133.1	11.2
CY (1)	32.9	21.2	155.3	14.4
LV	13.6	5.3	255.7	13.9
LT	10.7	6.1	177.4	10.2
LU	68.7	43.0	160.0	7.7
HU	16.6	9.8	169.4	8.6
MT	:	:	:	:
NL (2)	50.8	33.5	151.6	9.7
AT	56.6	37.4	151.2	11.0
PL (1)	16.1	7.6	210.7	14.9
PT	21.6	13.3	162.2	9.2
RO (1)	7.0	3.6	194.4	10.0
SI	26.4	18.0	146.8	9.0
SK	18.8	8.7	216.9	11.0
FI	65.0	40.1	162.2	10.4
SE	59.4	43.9	135.3	9.4
UK	60.5	33.9	178.5	14.4
NO	109.2	51.3	212.8	17.9

(1) 2005.
(2) 2004.

SOURCE: (13)

Figure 1 shows the relative importance of employment in SMEs, as well as the relative number of SMEs per 1000 inhabitants. The key point that can be taken from this chart is that there is massive variation in how important SMEs are for supporting employment as well as huge differences in the relative number of SMEs, and as a result, the impact that they have will differ significantly across countries. When we consider the productivity values in Table 2 in conjunction with the information in Figure 1, it is clear that there is no systematic linkage or relationship between the relative importance of SMEs, either in terms of contributing to overall employment, or in terms of the relative number per head of population, and the performance of economies overall in terms of productivity. The countries with high proportion of SMEs, for example, Greece, Italy, Portugal, Spain, and Hungary, are not necessarily more productive in comparison to the U.S., U.K., Germany, Finland, and Denmark where the number of SMEs is lower. This highlights very clearly that productivity will be determined by a range of factors in Member States, other than merely the presence of SMEs. There is thus **no rationale to apply a "one size fits all" approach to achieving the objectives of Cohesion and Regional Development Policies by focusing merely on firm size as a basis for allocating support.**

FIGURE 1: SHARE OF EMPLOYEES IN ENTERPRISES WITH 1-50 EMPLOYEES, 2007 AND NUMBER OF SMES PER 1000 INHABITANTS, NON-FINANCIAL BUSINESS ECONOMY, 2006



SOURCE: (15) AND (13)

In addition to examining productivity at the aggregate level, it is also important to examine differences across sectors and industries. Table 3 sets out details of the value added, persons employed and efficiency distribution for a number of different sectors in the European economy based on the company size. The table shows that in total (non financial business economy) large enterprises are responsible of 42.3 % value added and 32.6 % persons employed.

SMEs are in total thus responsible for 57.7 % of value added and 67.4 % of persons employed. Micro SMEs (as an important part of the overall SME sector) are responsible for 21 % value added and 29.7 % persons employed. When we calculate overall global efficiency ratio (value added % / persons employed %), we will find that large enterprise are more efficient (1.3), than SMEs (0.86)[11], that is, they make a much larger relative contribution to value added given their size compared to SMEs.

Thus **even though SMEs employ more people, LEs produce relatively more value per employee.** This key result is valid for the majority of sectors included in the Eurostat study. The implication of this result is that by limiting support for LEs, the Commission will be limiting support for the enterprises that make a much more efficient contribution to value added and employment and thus the relative impact of growth in value added and employment in SMEs at the EU level in aggregate will be relatively smaller than similar growth in LEs.

[11] *For micro SMEs is that ratio even lower (0.71).*

TABLE 3 – BUSINESS ECONOMY OVERVIEW; VALUE ADDED, EMPLOYMENT, EFFICIENCY IN NON-FINANCIAL BUSINESS ECONOMY, 2006

	Value added (%)					Persons employed (%)					Efficiency Ratio				
	SME	*Micr.*	*Small*	*Med.*	**Lar.**	**SME**	*Micr.*	*Small*	*Med.*	**Lar.**	**SME**	*Micr.*	*Small*	*Med.*	**Lar.**
Non-financial business economy	57.7	21	18.9	17.8	42.3	67.4	29.7	20.7	17	32.6	0.86	0.71	0.91	1.05	1.3
Industry	42.5	7.3	14.1	21	57.5	57.2	13.2	19.6	24.4	42.8	0.74	0.55	0.72	0.86	1.34
2 Mining and quarrying	35.7	11.9	9.3	14.5	64.3	31.6	5.5	13.3	12.9	68.4	1.13	2.16	0.7	1.12	0.94
3 Food. beverages & tobacco	45.5	8.2	14.8	22.6	54.5	62.5	16.3	21.2	25	37.5	0.73	0.5	0.7	0.9	1.45
4 Textiles. clothing. leather & footwear	74.5	14.1	28	32.4	25.5	75.3	17.7	26.3	31.2	24.7	0.99	0.8	1.06	1.04	1.03
5 Wood & paper	58.3	11.5	19.9	27	41.7	73.5	21.8	24.9	26.7	26.5	0.79	0.53	0.8	1.01	1.57
6 Fuel processing & chemicals	22.3	1.2	5	16.1	77.7	33.8	3.2	8.8	21.8	66.2	0.66	0.38	0.57	0.74	1.17
7 Rubber & plastics	57.4	4.8	19	33.6	42.6	64.1	7.8	22	34.3	35.9	0.9	0.62	0.86	0.98	1.19
8 Other non-metallic mineral products	52.5	7.3	18.5	26.7	47.5	64	14.5	22.1	27.5	36	0.82	0.5	0.84	0.97	1.32
9 Metals & metal products	62.4	11.2	24.9	26.4	37.6	72.1	17.6	28.2	26.4	27.9	0.87	0.64	0.88	1	1.35
10 Machinery & equipment	50.7	6.2	16.5	28	49.3	56.7	9.5	18.6	28.6	43.3	0.89	0.65	0.89	0.98	1.14
11 Electrical machinery & optical equipment	38	5.9	12.2	19.9	62	47.6	10.9	15.1	21.7	52.4	0.8	0.54	0.81	0.92	1.18
12 Transport equipment	13.8	1.4	3.5	8.8	86.2	20.8	2.7	5.8	12.4	79.2	0.66	0.52	0.6	0.71	1.09
13 Furniture & other manufacturing	72.6	18.3	26.3	27.9	27.4	76.8	25.6	25.7	25.5	23.2	0.95	0.71	1.02	1.09	1.18
14 Network supply of electricity. gas & steam	19.8	5.1	4.4	10.3	80.2	17.6	2.2	4.3	11.2	82.4	1.13	2.32	1.02	0.92	0.97
15 Recycling & water supply	47.2	9.3	16.6	21.3	52.8	52	9.1	16.3	26.6	48	0.91	1.02	1.02	0.8	1.1
16 Construction	82.8	33	32.1	17.7	17.2	88	41.5	30.6	15.9	12	0.94	0.8	1.05	1.11	1.43
Non-financial services	63.5	27.7	19.8	15.9	36.5	68.4	35.2	19.5	13.7	31.6	0.93	0.79	1.02	1.16	1.16
17 Motor trades	78.8	28.7	29.1	21	21.2	88.2	42.6	29.1	16.5	11.8	0.89	0.67	1	1.27	1.8
18 Wholesale trade	76.9	23.7	29.4	23.8	23.1	82.1	32.9	29.1	20.1	17.9	0.94	0.72	1.01	1.18	1.29
19 Retail trade & repair	56.4	31.5	16.3	8.6	43.6	65.1	42.7	15	7.4	34.9	0.87	0.74	1.09	1.16	1.25
20 Accommodation & food services	76.5	35.5	27.2	13.8	23.5	82.4	44.7	26.8	10.9	17.6	0.93	0.79	1.01	1.27	1.34
21 Transport and storage	51.5	16.9	18	16.6	48.5	59.3	23.8	19.2	16.3	40.7	0.87	0.71	0.94	1.02	1.19
22 Media & communications	21.8	5.2	7.6	9.1	78.2	35.3	11.6	11.6	12.1	64.7	0.62	0.45	0.66	0.75	1.21
23 Real estate. renting & leasing	85.7	52.4	16.7	16.7	14.3	84.8	53.5	17.4	13.9	15.2	1.01	0.98	0.96	1.2	0.94
24 Research & development	41.7	7	10.2	24.5	58.3	54.2	11.8	15.8	26.6	45.8	0.77	0.59	0.65	0.92	1.27
25 Business services	66.6	29.1	20.1	17.5	33.4	64.5	31.3	16.7	16.6	35.5	1.03	0.93	1.2	1.05	0.94

SOURCE: AUTHORS, BASED ON DATA FROM (13)

Furthermore, there are additional pieces of work to support the conclusion that there is no rationale to for focusing merely on firm size, and on SMEs in particular, as a basis for allocating Cohesion Policy and ERDF support, as well as an exclusive focus on this sector of economy as a sustainable source of growth. We have highlighted two particular pieces of work that reflect this view based on evidence from the EU and further afield on the economic impact of SMEs. It is important to note that the conclusions regarding the merit of focusing on SMEs are equally applicable to policies focused at regional as well as national levels.

The small start big (14)

If you`re talking about an economic indicator in which the U.S., U.K., Germany, Finland, and Denmark are the bottom and Greece, Italy, Portugal, Spain, and Hungary are at the top, then you`re looking at an economic indicator in which you want to be at the bottom. The economically more successful countries are less dominated by small firms. That shows that the link between entrepreneurship and small businesses is much weaker than is often posited

Entrepreneurs boost the economy by exploiting new ideas and business models in order to turn a profit. The ones that do this well don`t stay small; they grow rapidly, helping to disseminate new technologies and create jobs. If your economy has a lot of small firms, that`s an indication that some part of this process is broken. If you look at the Italian example, for instance, you find that a lot of small Italian firms are retail and service enterprises protected from competition by onerous regulation.

Rethinking the Boosterism About Small Business (16)

...In the popular imagination, small firms are more nimble, more innovative, and more virtuous than blue-chip companies that employ thousands. Yet the notion that small business is the force behind prosperity is not true. The longer the U.S. and other countries cling to this myth, the harder it will be to carry out the kinds of economic policies that might actually stimuli job growth. In the U.S. in 2007 there were around 6 million companies with workers on the payroll. Ninety percent of those businesses employed fewer than 20 people, according to analysis of the latest census data by Erik Hurst and Ben Pugsley of the University of Chicago (17). Collectively, those companies accounted for 20 percent of all jobs. Most small employers are restaurateurs, skilled professionals or craftsmen (doctors, plumbers), professional and general service providers (clergy, travel agents, beauticians), and independent retailers. These aren`t sectors of the economy where product costs drop a lot as the firm grows, so most of these companies are going to remain small. And according to Hurst and Pugsley`s survey evidence, the majority of small business owners say that`s precisely their intent – they didn`t start a business for the money but for the flexibility and freedom. Most have no plans to grow.

Detailed SME landscape statistics provided in this study questions the straightforward understanding of SMEs as a single entity. It applies especially to micro enterprises that are in EU responsible for at about one third of the SME added value and 44 % of persons employed in SMEs. The heterogeneity of SMEs as a group (16) is not reflected in the view that all SMEs play a similar role as a force for economic development.

The differences in productivity and flexibility between micro-enterprises and other SMEs needs to be taken into account when developing policy focused on SMEs, as well as when

distinguishing policy for and comparing SMEs and LEs.

In addition, concentrating policies that exclusively support SMEs, especially in countries with high SME densities and weaker economies, may have perverse consequences by actually directly undermining the ability of these countries to achieve the objectives of Cohesion Policy and Europe 2020 strategy, as well indirectly impacting their ability to achieve the objectives by reducing their attractiveness as locations for LE investments in an increasingly competitive and globalized economy.

STUDY CONCLUSIONS AND POLICY IMPLICATIONS

The purpose of this study has been to analyse the arguments underpinning, and provide an overall review of, the plans by the European Commission under "the thematic concentration" of the ERDF whereby the Commission plans to exclude larger enterprises from access to productive investment for job creation. The Commission further plans to limit LE access to Regional Aid in draft Regional Aids Guidelines. The main conclusion of the paper is that these measures are not aligned with the objectives of, and do not fit with, the context of Cohesion Policy and the Europe 2020 strategy agenda.

Specifically, this paper highlighted a number of serious issues with the rationale underlying this perspective and the potential for perverse impact from employing this approach. We showed that the decision is based on an extremely narrow and limited body of evidence that does not provide sufficient rationale or justification for the decision. There is also a number of problematic issues with the various assertions made by the Commission regarding relocation, trade and competition distortions, and monitoring of LE operations to prove long term benefits. In total, they do not provide a sufficient basis to exclude LEs in the manner the Commission plans to after 2014.

One of the most serious problems with the Commission's approach is the real potential of actually reducing the chance of fostering structural change in less developed EU regions that could be achieved by allowing for legitimate LE strategic investments. We showed the broad positive impact of LEs in areas relevant to the objectives of Cohesion Policy. Further we demonstrated how, given the nature of current business and value ecosystems, there are significant positive linkages between LEs and SMEs. Thus, excluding LEs could have detrimental impacts for SMEs and work against the overall objectives of Cohesion Policy and Europe's growth and jobs agenda the Europe 2020 strategy.

We further supported our analysis with additional examples and case studies, including an evaluation of the current funding period conducted in the Czech Republic and the powerful example of the Brno City Municipality. These clearly show the benefits provided by LEs in achieving several key regional objectives and demonstrate effectiveness of investment support provided to LEs. The structural changes in the regional economy and its transformation into higher value added sectors by building a critical mass of know-how has not only created a significant number of jobs, but also nurtured the rise and prosperity of local SMEs.

In addition, the evidence we presented highlighting the many benefits that arise from LEs individually, as well as through their linkages with SMEs, points the real potential that the Commission's plans may negatively impact the ability of the EU to attract Foreign Direct Investments (FDI) from outside the EU in what is an increasingly competitive global investment landscape. This would put the EU at a competitive disadvantage in attracting FDI from key extra-EU regions that are becoming increasingly significant sources of investment.

We also provided a brief statistical overview of the role of SMEs and LEs in the European economy that illustrated how a more balanced view is needed when accessing their contribution to economic growth - a high proportion of SMEs in some countries, for example in Greece, Italy, Portugal, Spain and Hungary,) does not necessarily mean that their economies are more competitive or productive in comparison to countries where the number of SMEs is lower, such as the U.S., U.K., Germany, Finland, and Denmark.

Thus, the main **conclusion of the study is that for successful regional development strategies, the number of jobs created by the project, its quality and sustainability are the vital variables. They should thus form the basis for the decision as to whether to grant support for those projects. Size of enterprise is not a vital variable. Our evidence clearly shows that there is no firm rationale to exclude any type of entity from access to productive investments or further limit access of LEs to Regional Aid Schemes. The main criterion should be how the projects/investments contribute to Europe 2020 strategy and Cohesion Policy objectives, as well as to the regional needs and specifics and most importantly then, the Legislative proposals for the new period of Cohesion Policy should maintain the current status that retains the power of decisions on investment support programmes to individual MS and regional authorities.**

ANNEX A – DETAILED ANALYSIS OF RESEARCH WORKS AND STUDIES PROVIDED BY COMMISSION AS A BASE FOR ITS ARGUMENTATION

Commission Staff Working Paper – Executive Summary of the Impact Assessment accompanying the Proposal for a Regulation concerning the ERDF and the Cohesion Fund (18)

…"Empirical evidence shows that direct aid for SMEs is more effective, while 'for larger companies crowding out of private investment may prevail over positive effects.' The funding of productive investments of large enterprises where public intervention is not necessary has led to criticisms that funding is given to firms which do not actually need it, and that the funding is therefore crowding out private investment instead of having added value"…

- Noted "empirical evidence" is not provided/ documented. Such statement is also irrelevant when trying to focus an support aid for specific region**.**

C. Criscuolo, R. Martin, H. Overman, J. Van Reenen (2011), "The causal effects of an industrial policy", mimeo Centre for Economic Performance, London School of Economics for recent research on the effectiveness of the Regional Selective Assistance (RSA) program in the UK (19)

- Study analyzing results of the UK RSA programme to support manufacturing jobs. Study period between 1986 and 2004.
- Only one country covered.
- UK is not proper case to be used as it is developed country with small "convergence" regions. Therefore using the results as a key case for exclusion of large enterprises in less developed regions in other countries is not appropriate.
- Only manufacturing jobs / plants were taken under consideration (no services, value adding sectors etc.).
- Details of RSA programme are not presented. Is it really comparable to other countries?

S. Wallsten (2000; for the US) "The effects of government-industry R&D programs on private R&D: the case of the Small Business Innovation Research program" RAND Journal of Economics, 31, 82-100 (20)

- US Study - different funding approach then in the EU, no regional impact analysis.
- Analysis was limited only on R&D support impact.

X. González, J. Jamandreu, and C. Pazó (2005; for Spain) "Barriers to innovation and subsidy effectiveness", RAND Journal of Economics, 36, 930-50 **(21)**

- Data source 1990-1999 - old data sample.
- Only one country analyzed – Spain.
- Analysis was limited only on R&D support impact.

S. Lach (2002; for Israel) "Do R&D subsidies stimulate or displace private R&D? Evidence from Israel" Journal of Industrial Economics, 50, 369-90 (22)

- Data source - Israeli manufacturing firms in the 1990s - old data sample.
- Israel - not EU - different conditions.
- Analysis was limited only on R&D support impact.

R. Bronzini and E. Iachini (2010; for Italy) "Are incentives for R&D effective? Evidence from a regression discontinuity approach", mimeo Bank of Italy **(23)**

This study is targeted to overall effectiveness of public incentives in R&D.

- Analysed sample is not balanced - majority of companies are of "Machinery and equipment" sector.
- Analysis was limited only on R&D support impact.
- Study provides information, that impact of public incentives has been measured in a number of studies with mixed results ("out of nineteen micro-econometric studies surveyed, half found no effect. Examining the papers published in the last decade we found a similar balance: out of total of eleven, just six confirm a positive role for public incentives")

H. Gorg and E. Strobl (2007; for Ireland) "The effect of R&D subsidies on private R&D" Economica, 74(294), 215-234 **(24)**

One of the conclusions of this study was that company size does not impact the effectiveness of foreign investments into the region .

- Analysis was limited only on R&D support impact.

„… evidence for foreign establishments suggests that grant provision causes neither additionality nor crowding out effects of private R&D financing, regardless of the size of the subsidy."

ANNEX B – DETAILED COMPARISON OF THE CURRENT AND PROPOSED LEGISLATION

Detailed comparison of the current and proposed legislation is provided in the following tables:

TABLE 4 – DETAILED COMPARISON OF THE CURRENT AND PROPOSED LEGISLATION OF EUROPEAN REGIONAL DEVELOPMENT FUND

European Regional Development Fund **Topic: Scope of Support**	
Current text	**Proposed text**
Article 3 **Scope of assistance** 1. The ERDF shall focus its assistance on thematic priorities. The type and range of actions to be financed within each priority shall reflect the different nature of the Convergence, Regional competitiveness and employment and European terri- torial cooperation objectives in accordance with Articles 4, 5 and 6. 2. The ERDF shall contribute towards the financing of: . (a) productive investment which contributes to creating and safeguarding sustainable jobs, primarily through direct aid to investment **primarily** in small and medium-sized enterprises (SMEs); *Source: (25)*	*Article 3* **Scope of support from the ERDF** 1. The ERDF shall support: **(a)** productive investment, which contributes to creating and safeguarding sustainable jobs, through direct aid to investment in small and medium-sized enterprises (SMEs); *Source: (26)*

TABLE 5 – DETAILED COMPARISON OF THE CURRENT AND PROPOSED LEGISLATION OF REGIONAL AID RULES (INITIAL INVESTMENT AID)

Regional Aid Rules Topic: Initial Investment Aid	
Current text	**Proposed text**
4.1.2. Aid ceilings (maximum aid intensities) for aid to large companies In the other Article 87(3)(c) regions, the ceiling on regional aid must not exceed 15 % GGE. This is reduced to 10 % GGE in the case of regions with both more than 100 % of average EU-25 GDP per capita and a lower unemployment rate than the EU-25 average, measured at NUTS-III level (based on averages for the last three years, using Eurostat data) (45). *Source: (27)*	**3.1. Material scope of the RAG** (6) Regional aid consists of initial investment aid or, in certain circumstances, operating aid, which, in both cases, are targeted at specific regions in order to redress regional disparities. While aiming to promote cohesion within the EU, the distortive effects of this aid have to be kept to the minimum and the Commission has to ensure that the positive effects of the aid outweigh its negative effects. As the 'a' regions are those most in need it is desirable to ensure that it would be possible to grant investment aid to all type of companies. As 'c' regions are more developed from an EU perspective, the contribution to regional development of initial investment projects is proportionally less important. At the same time, for projects implemented by large enterprises, the potential distorsions of trade and competition are higher than for projects implemented by SMEs. **(8)** Therefore, the direct negative effects of aid in favour of projects implemented by large enterprises are more likely to outweigh any positive externalities. **As a consequence, regional investment aid would be limited to SMEs only in these regions.** *Source:* (1)

TABLE 6 – DETAILED COMPARISON OF THE CURRENT AND PROPOSED LEGISLATION OF REGIONAL AID RULES (LIP, OPERATING AID)

Topic: LIP Larger Investment Projects	
Current text	**Proposed text**
4.3. Aid for large investment projects For the purpose of these guidelines, a 'large investment project' is an 'initial investment' as defined by these guidelines with an eligible expenditure above EUR 50 million (54). *Source:* (27)	(11) Current practice shows that large investment projects (LIP, i.e. projects with eligible expenses above EUR 50 million) are mainly undertaken by large enterprises. **Due to the significant potential distortive effects of aid for these projects, such aid is currently subject to an adjusted regional aid ceiling on the basis of the following scale (for SMEs, no bonus may be granted)**: Eligible expenditure Adjusted aid ceiling Up to EUR 50 mio 100 % of regional ceiling For the part between EUR 50 mio and EUR 100 mio 50 % of regional ceiling For the part exceeding EUR 100 mio 34 % of regional ceiling *Source:* (1)
Topic: Operating aid	
Current text	**Proposed text**
5. Operating aid Regional aid aimed at reducing a firm's current expenses (operating aid) is normally prohibited. Exceptionally, however, such aid may be granted in regions eligible under the derogation in Article 87(3)(a) provided that (i) it is justified in terms of its contribution to regional development and its nature and (ii) its level is proportional to the handicaps it seeks to alleviate (69). It is for the Member State to demonstrate the existence and importance of any handicaps (70). In addition, certain specific forms of operating aid can be accepted in the low population density regions and the least populated areas. Operating aid should in principle only be granted in respect of a predefined set of eligible expenditures or costs (71) and limited to a certain proportion of those costs. *Source:* (27)	(9) The possibility for Member States to grant non- degressive and non-temporary operating aid in outermost regions and low population density areas would be maintained as such aid enable to address well-identified problems and does not generally raise major competition concerns. As the current provisions on operating aid in 'a' regions have been used in only one measure (in Eastern Germany) **and in view of the strong distortive effect of operating aid to large enterprises, the possibility to grant 'general' operating aid in 'a' regions would be limited to SMEs and under conditions similar to those laid down in paragraphs 76-79 and 82-83 of the current RAG.** *Source:* (1)

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