EUROPEAN UNION

Committee of the Regions

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OPINION

Green Paper on the long-term financing of the European economy

THE COMMITTEE OF THE REGIONS

- welcomes the Commission's timely Green Paper on the long-term financing of the European economy, and welcomes the move to launch a wide-ranging debate in the form of a public consultation on how the supply of long-term financing can be improved and the system of financing long-term investments in Europe strengthened and diversified with a view to the EU's future development;
- shares the Commission's view that the European financial sector has been less successful since the financial crisis at channelling savings into long-term investments; the financial crisis and the present weak macroeconomic environment in particular have created a climate of uncertainty and risk aversion especially felt by cash-strapped Member States;
- is also concerned that specific local and regional-level circumstances are not given enough attention in provision of long-term financing and in measures typically taken to promote long-term investment;
- has reservations about EU moves to restrict competition and the leeway of governments in some areas of investment that are especially important to local and regional authorities. The coordination process and authorisation procedures are too time-consuming and complicated, which makes Europe less competitive internationally and increases the appeal of other parts of the world to investors.

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<u>Reference document</u>

Commission Green Paper on the long-term financing of the European economy
COM(2013) 150 final

Opinion of the Committee of the Regions – Green paper on the long-term financing of the European economy

I. GENERAL COMMENTS

THE COMMITTEE OF THE REGIONS

Smart and inclusive growth

1. welcomes the Commission's timely Green Paper on the long-term financing of the European economy, and welcomes the move to launch a wide-ranging debate in the form of a public consultation on how the supply of long-term financing can be improved and the system of financing long-term investments in Europe strengthened and diversified with a view to the EU's future development;

2. shares the Commission's view that the European financial sector has been less successful since the financial crisis at channelling savings into long-term investments; the financial crisis and the present weak macroeconomic environment in particular have created a climate of uncertainty and risk aversion especially felt by cash-strapped Member States;

3. supports the Commission's view that Europe faces the pressing task of returning the EU to the path of smart, sustainable and inclusive growth. At the same time, the Committee believes that more heed should be given to specific local and regional circumstances as well as the challenges faced by SMEs;

4. emphasises that far-reaching, all-round cooperation between the EU institutions, the Member States, cities and regions, local and regional authorities, and interest groups, based first and foremost on subsidiarity and proportionality, will be pivotal to overcoming the economic crisis, facing new challenges and setting and achieving common goals;

5. believes that increasing the average value added by businesses from the productive economy in job-rich sectors could be an effective way to boost economic growth. Strengthening such businesses with the help of innovation and simplified conditions for access to capital could have a profound impact on the economy as a whole;

6. notes that the knowledge-based assets of the world's biggest companies (listed on the S&P 500 index) already make up 80% of their company value. Drivers of growth are mainly to be found in sectors of the economy with the greatest potential for global expansion: the green economy; agriculture (including efficient use of local biological resources and the bio-economy); the silver economy; products and services linked to healthcare and social services; IT applications; and business and lifestyle applications from the creative sector. In the USA, for example, a large share (almost 60%) of the new jobs created over the next ten years may

be linked to products and services that do not even exist yet. The economic benefits of re-using or adding value to public sector information through IT applications could amount to as much as EUR 140 billion annually, which would boost GDP accordingly[1];

7. points to its earlier, related opinions on *Synergies between private investment and public funding at local and regional levels*[2]; *Mobilising private and public investment for recovery and long term structural change: developing public-private partnerships*[3]; a *Programme for the competitiveness of enterprises and small and medium-sized enterprises (2014-2020)*[4]; *Creating greater synergies between EU, national and subnational budgets*[5]; and *The role of local and regional authorities in promoting growth and boosting job creation*[6];

II. VIEWS OF THE COMMITTEE OF THE REGIONS

The supply of long-term financing and characteristics of long-term investment

8. agrees with the Commission's analysis, which is essentially that investors face a lack of legal certainty and are very cautious in their investments. They prefer short-term, more liquid investments, and above all investments in private assets. Financial institutions are often focused on fast-developing emerging markets with low wage costs;

9. is concerned about the rapidly growing competition for foreign capital, because indebted countries urgently need new sources of capital to make growth-enhancing investments and service existing debt. Attention should not, or not just, be focused on loans, but also on other sources of capital;

10. points out that the municipalities and regions play many different roles in financial markets, making their own long-term investments, as well as investing to a greater or lesser degree on their own account, for instance through municipal undertakings or for industrial policy reasons. Municipalities and regions are also themselves investments on the financial markets;

11. notes that the public sector operates on the financial markets in a different environment and with different objectives than does the private sector. The need for a return on investment, the investment horizon and risk tolerance, for example, are very different for public and private investors. The Commission should therefore pay particular attention to public sector activity where long-term financing is concerned;

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1 European Commission, Public Sector Information - Raw Data for New Services and Products (http://bit.ly/wa4AR).

2 CdR 272/2013.

3 CdR 21/2010.

4 CdR 98/2012.

5 CdR 1778/2012.

6 CdR 1186/2012.

12. is also concerned that specific local and regional-level circumstances are not given enough attention in provision of long-term financing and in measures typically taken to promote long-term investment;

13. has reservations about EU moves to restrict competition and the leeway of governments in some areas of investment that are especially important to local and regional authorities. The coordination process and authorisation procedures are too time-consuming and complicated, which makes Europe less competitive internationally and increases the appeal of other parts of the world to investors;

14. calls for long-term investments by municipal and regional authorities that create jobs, promote technological innovation and green growth, and develop energy, transport and communications infrastructure to be facilitated and encouraged, including in difficult economic times;

Enhancing the long-term financing of the European economy. The capacity of financial institutions to channel long-term finance. Commercial banks

15. points out that the December 2012 European Council Conclusions[7] stress that "the possibilities offered by the EU's existing fiscal framework to balance productive public investment needs with fiscal discipline objectives" should be further "exploited" in the preventive arm of the Stability and Growth Pact. Reiterates, against this backdrop, its call for separation of current spending and investment in the budget deficit calculations so as to avoid investments with long-term net benefits being impeded;

16. is pleased that banks are slowly re-establishing their capacity to make long-term investments, but notes that so far funds for local investment have only been made available under wholly inadequate conditions;

National and multilateral development banks and financial incentives

17. feels that is important for national and multilateral development banks to (a) support strategically important investments, especially in infrastructure and energy provision, and (b) pursue counter-cyclical financial policies, which means retaining capital in periods of economic growth and substantially boosting investment during economic crises;

18. agrees that excessive consolidation of banks should be prevented at EU level, but at the same time recommends stepping up cooperation so as to pool free capital for investment at local and regional level;

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7 European Council Conclusions of 13 and 14 December 2012, I. Economic Policy, point 2.

19. advocates linking investment aimed at sustainable growth to long-term checks, and calls for provisional investment plans to be continued. In the long term, project bonds would also ensure sustainability at local and regional level;

20. believes that long-term investments at local and regional level can also be supported by complementing policy tools and frameworks with efforts to cut red tape, develop online communication and streamline the decision-making process;

Institutional investors

21. agrees that institutional investors play a key role in long-term financing, and on the need for compliance with the Solvency II Directive. Clearly, the greater the sums invested, the greater the role played by these investors. At the same time, it has to be ensured that available funds are invested in the economy of the EU, and not that of Asia or other parts of the world;

The cumulative effects of regulatory reform on financial institutions

22. underlines that current and future reform of supervisory rules will produce long-term, cumulative effects. The regulatory system must be thoroughly thought-out and its possible repercussions over time – including at local and regional level – closely followed;

The efficiency and effectiveness of financial markets in offering long-term financing instruments

23. notes that capital market financing of long-term investment in Europe can be improved by strengthening the EU's single market for capital, developing infrastructure supporting the local and regional financial institutions and ensuring effective investor protection, and that pension funds investing in local and regional development should be included;

24. considers that there is a need to develop further investment products or packages of potential investments (such as road / utility projects) that could make them more amenable to direct investment by pension funds;

25. believes there is a pressing need to lift labour productivity. It needs to constantly adapt to an ever-changing economic environment. In such an environment it can be beneficial if employees are able and want also to function as shareholders and investors with an interest in long-term investment in the company that employs them; in case of local investments, especially in energetic and environmental sectors, there is need for establishing investment constructions, where the local and regional community may appear as a financing actor also, and not just as a consumer;

26. underlines that it might be beneficial for change and local development if employees are also shareholders and investors, should they should so wish and should the possibility for such

participation even exist in the market structure concerned. Legislative reform and greater transparency can play a supportive role to encourage employees to participate in this way;

27. is convinced of the need to more clearly include micro companies and SMEs, improve transparency at trade centres, and involve investors. The share of the market for loans outside the financial sector should be expanded and access to the market for SME loans made easier;

28. underlines that the EU's securitisation market can be revived if there are controls on how financial institutes invest capital, and if harmonised, transparent rating methods are used to ensure that the only capital that counts is that which is properly collateralised. Implementing these measures should free up capital which can be invested, and the liquid project bond market for SMEs should also be guaranteed;

Cross-cutting factors enabling long-term saving and financing

29. believes that creating different models for special savings accounts within the EU, and the potential advantages of such models, are linked to the question of how to guarantee interest on savings.

30. is concerned that a compulsory or partly compulsory European savings account could be met with scepticism in some Member States, while voluntary accounts would arouse little public interest. In choosing a model for a special EU savings account, priority should clearly be given to the one best able to restore low levels of confidence and contribute to the Europe 2020 employment and growth objectives at local and regional level;

Taxation

31. a coordinated European approach for applying a lower tax rate to capital investments should be considered;

32. takes the view that to create the right incentives for long-term saving, consideration should be given to tax advantages at national level that incentivise rapid reinvestment of profits, long-term investment, and capital investments in micro companies and SMEs; it would make sense to distinguish between income from capital and income from other sources here. Consideration could also be given to lowering tax rates and exempting long-term financial savings;

33. recommends drawing on previous positive or negative experience when assessing the utility of reducing corporate income taxation on businesses. In some Member States, for example, all profits are presently exempt from taxation, regardless of whether or not they are reinvested, with only some forms of deployment in which money leaves the company incurring taxation, such as dividends, special benefits and natural benefits, etc. The result is an estimated effective tax rate of 4-5%. Such a system does not encourage local investment;

34. points out that a number of surveys on investment decisions place the taxation regime in fourth to sixth place in terms of priority. They suggest that there are other, more important factors, such as local availability of labour and appropriate skills, availability of energy and water, etc., low basic business costs, and other factors that directly or indirectly impact on business, such as corruption and the like;

35. advises the Commission to consider the possibility of not taxing reinvested profits and income from interest, and of granting tax exemptions to research, development and environmental projects;

36. also supports increased coordination to simplify the corporate income taxation system, expand the tax base and reduce tax rates. State intervention in the economy and in people's lives should be restricted, giving businesses and citizens increased responsibility for their financial position and thereby encouraging a range of collective activities;

Accounting principles

37. notes that fair value accounting principles are not applied in all Member States. They are used by companies that operate in several EU Member States simultaneously. Fair value accounting principles have not yet brought about any change in investor behaviour;

38. steps should be taken to ensure the stability of accounting principles based on market-based assessments of assets and liabilities over long-term funding periods, and alternative measures should be planned to allow risk-free long-term financing with a view to the market value of assets and their sources;

Corporate governance arrangements

39. believes that granting tax concessions on dividends would be one way of inducing long-term engagement on the part of shareholders. Distributing a larger share of dividends to shareholders who place their dividends in long-term investments would achieve the same result. There should also be tax concessions for long-term investment in local and regional developments;

40. is convinced that where incentives for asset managers prove counter-productive, accounting transparency should clearly be improved to ensure trust between the public, business owners, business management and employees;

Information and reporting

41. believes that efforts to more closely integrate financial and non-financial information that helps businesses gain a clearer overview of their long-term financial position so that they can

make better decisions should not be coupled with a move away from quarterly reporting, given the current pace of life and the opportunities offered by the digital age. Moreover, it enables assessment of an evolving situation before problems pile up or before remedying those problems becomes much more expensive;

42. recommends considering the scale and scope of quarterly indicators with regard to all the possibilities offered by the digital age. At the same time, it is important for the specialist media not to publish data in a biased manner, but in an objective, trustworthy manner, with comprehensible summaries, expert contributions and brief analyses included where necessary;

43. believes that economics and statistics already provide adequate indicators for long-term comparison, which makes applying, checking and analysing existing indicators a time-consuming task. Deploying new indicators would not appear to make much sense, therefore. Of course, this could change if a particularly informative indicator or benchmark median were identified;

The ease of SMEs to access bank and non-bank financing

44. agrees that SMEs have more limited access to financing than large companies do, and in several Member States face the added difficulty of legislation that is discriminatory in many respects;

45. recommends considering the possibility of a public exchange or of developing an Internet-based bond market where everyone would be free to invest in local or regional development without having to go through brokers;

46. advises SMEs to make use of additional lenders, such as credit cooperatives, building societies and similar small financial institutions, whose share of the market in most countries in Eastern Europe is, regrettably, rather small, and whose development is often not promoted by the state. Some Member States offer a bank deposit guarantee, for example, but exclude credit cooperatives;

47. proposes for local and regional governments, economical advocacy organisations, organisations having authority on public wealth and money market organisations to create local and regional cooperatives, which can supply alternative sources of funds for local and regional long-term financing;

48. calls on the Commission to study the legal reforms that are necessary and fit to allow credit cooperatives to function efficiently, and to draft legislative proposals accordingly;

49. is convinced that such a network of small financial institutes could be the solution to many local and regional problems, and that steps must be taken to ensure that SMEs receive a

guaranteed share of risk capital. At the same time, thought should be given to large-scale use of credit guarantees;

50. underlines that the development of an EU legal framework for alternative, non-bank sources of SME financing would, under certain conditions, clearly benefit local and regional development, since the current legal framework does more to constrain SMEs than benefit them.

Brussels, 9 October 2013

The President
of the Committee of the Regions

Ramón Luis Valcárcel Siso

The Secretary-General
of the Committee of the Regions

Gerhard Stahl

III. PROCEDURE

Title	Opinion on the Green paper on the long-term financing of the European Union
Reference(s)	COM (2013) 150
Legal basis	Article 307(1) TFEU
Procedural basis	Optional referral
Date of Commission letter	8 May 2013
Date of President's decision	27 March 2013
Commission responsible	Commission for Economic and Social Policy (ECOS)
Rapporteur	Uno Silberg (EE/EA), member of Kose Rural Municipality Council
Analysis	21 May 2013
Discussed in commission	27 June 2013
Date adopted by commission	27 June 2013
Result of the vote in commission	Majority
Date adopted in plenary	9 October 2013
Previous Committee opinions	
Date of subsidiarity monitoring consultation	N/A

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