

10 ideas for the future of Europe's digital economy – "SMEs as the engines of digital change"

The creation of the European Digital Single Market is a crucial condition for a successful digitalisation of our economy. In this strategy paper, The European Digital SME Alliance presents its ideas for Europe to regain digital sovereignty. European SMEs, leaders in the ICT markets and vehicles of digital enablement for the society as a whole, are at the centre of this strategy.

The digitalisation of economy and society leads to profound changes of economic structures. Value chains shift, business organisations and workflows find new ways and the competitiveness of companies is newly defined. Buzzwords such as "Cyber-physical-systems" or "Big Data" are paradigms of an industrial revolution, which will sooner or later affect all sectors of the economy, as well as our society.

The dynamism of Small and Medium sized Enterprises is a driving force of Europe's economy. However, too many barriers still prevent these companies from having a single EU internal market. The Joint Research Centre of the European Commission recently highlighted in a study¹, how numerous national markets and the differing legal systems are contrary to growth and modernization of digital companies. Only 7% of all small and medium sized enterprises are able to offer their services outside their national markets. The digital revolution poses new challenges to businesses, as well as legislators, in today's interconnected world.

Digitalisation – the foundation of tomorrow's prosperity

Progress and innovation are the keys for our future prosperity. More than 60% of innovations within the EU over the last 10 years were driven by IT and this trend is rising. Thus, digitalisation will be the

foundation of our prosperity in the future. The strategic groundwork for this has to be laid down now.

European companies are faced with fundamental changes. In the SME driven European economy, numerous national champions have emerged. Many of them have become leaders in their countries and are active on the global markets.

10 ideas for the future of Europe's digital economy:

1. A European Digital SME Hub to connect SMEs as an answer to the dominance of large IT business groups
2. Unified European contract law
3. Introduction of a European capital company
4. Tax: reduction of VAT cross-border obstacles, retention of profits and fight multinational tax avoidance
5. Enabling a modern and data-driven economy
6. Modernization of access to finance, especially initial and growth capital
7. Unified regulation of the digital infrastructure
8. SME friendly standardization policy
9. Unified European framework on copyright and improvement of the European patent law
10. Digital skills for SMEs

¹ International Trade in Online Services, Institute for Prospective Technological Studies
Digital Economy Working Paper, 2015
<https://ec.europa.eu/jrc/sites/default/files/JRC97233.pdf>

SMEs are having problems expanding in other European countries. A recent study² of the European Commission highlights that the digital sales between 2010 and 2014 increased exponentially, but are only generated by a few companies. Currently, more than 50% of the e-commerce that involves more than one EU country happens through just 1% of the websites. Those sales happen most likely on global platforms such as Amazon, eBay or Alibaba. Moreover, 54% of all digital services in the EU are rendered by US companies.

In conclusion, the EU Digital Single Market, if existing, is controlled and exploited by non-European companies. It is high time for Europe to conceive its strategy for regain our digital sovereignty.

Digital SMEs: Enablers of an industrial revolution

The population of Europe's digital SMEs in a nutshell³

- ICT contributes nearly 50% of EU productivity growth
- The population of digital SMEs is approximately 1.1M enterprises in the EU
- An estimated 41% share of digital SMEs is innovative, equal to more than 300,000 companies.
- High involvement of digital SMEs in the industrial value chain: the share of SMEs value added in digital manufacturing in the EU is about 36%, while the comparable share in ICT services is 33%.
- The contribution of digital SMEs to European R&D investments is considerable: 14%, equal to €2.9 Billion, is the share of SMEs in the total ICT Manufacturing R&D business expenditure.

Digital SMEs provide the majority of jobs in Europe's ICT sector and generate 40% of the volume of sales. Digital SMEs play a central role as partners and suppliers of Europe's 23 Million ICT-user SMEs. Small and medium sized IT companies are the digital enablers that will activate the next industrial revolution in Europe.

Despite the role played by Europe's digital SMEs, large multinational business groups currently dominate the EU Digital Single Market.

Thus, we call on legislators and policy makers to concentrate on measures that allow SMEs to exploit the potential of Digital Single Market and to become leaders in the global digital markets.

10 ideas for the future of Europe's digital economy

1. A European Digital SME Hub

The German government is discussing the idea to create the German IT Mittelstand Centrum, a hub that will serve the community of German digital SMEs by promoting digitalisation of SMEs and offering support for the creation of SME consortia.

Similarly, Europe should recognise the key role of its digital SMEs as innovators that compete with large multinational ICT companies. Many European politicians and business leaders have tried to boost Europe's digital economy by replicating the Silicon Valley model, whereas they should have conceived a model that is based on Europe's features and strengths.

In particular, Europe does not have the same market size and access to capital as the US. However, our unique strength lies on the thousands of small hidden champions that constitute a dynamic and interconnected ecosystem. Therefore, Europe should build on its strengths and define specific actions to build on them.

Our proposal is the creation of a European Digital SME Hub that supports the dynamic creation of SME networks that put together resources and skills of different companies. Strengthening the networking opportunities of digital SMEs builds on the asset of our eco-system and allows companies to be stronger together.

² Alaveras and Martens, 'Online services trade in the EU Digital Single Market', JRC/IPTS Digital Economy Working Paper, forthcoming 2015

³ Study on Innovative ICT SMEs in Europe, IDC, 2006

The main functions of the European Digital SME Hub are the following:

- > Supporting the creation of digital SME consortia with legal and market expertise
- > Advisory support for SMEs on digitization

The hub will connect small and medium sized digital companies and foster ad hoc cooperation on specific projects. In the same way, cooperative approaches for developing "virtual factories" can be strengthened. The hub will be an institution that facilitates and reduces the transaction cost of creating virtual factories where SMEs work together.

The Digital SME Hub provides opportunities for small companies to form trans-national consortia with other SMEs in a "plug and play" way. Such consortia can take part in bigger competitions or tenders and thus compete with multinational ICT companies.

Finally, by providing advisory support for SMEs on digitization, the Digital SME Hub, pursues a complementary approach: on one hand it connects companies and on the other hand it convey the message of digitalisation. Hence, it will be a multiplier for digitalisation and thus will strengthen the EU's digital economy altogether.

2. A unified European contract law

Cross-border trade is still a huge problem for smaller companies. Due to different legal regimes in the respective states, contracts between companies in different countries become a bureaucratic and costly effort.

This very often prevents our SMEs from exploiting the potential of the internal market. Even when SMEs perceive profit opportunities outside their countries, they often decide not to pursue them because of the high costs and burdens of establishing contracts according to different national laws. The project to solve this problem – a unified European contract law – was discussed at length by the EU and finally not pursued after 2013.

More recently, following the adoption of the Digital Single Market Strategy, a limited version of this contract law was pursued by the European

Commission: A European law that is very focused on the interest of consumers: the sellers of digital goods may refer to their respective national laws when selling products online, while the framework for consumer protection will be tackled later. The European Digital SME Alliance believes that this approach is short-sighted. A full European contract law that goes beyond the national laws of the respective states needs to be established in order for all companies to benefit for the EU internal market.

3. Introduction of a European capital company

The European Commission plans on establishing a European single member company (Societas Unius Personae - SUP) to create a suitable counterpart for the European Company (SE), which is only interesting for large business groups.

However, forming a single shareholder company is a viable option only for very small companies. Instead, SMEs that work in an international context require a European private capital company. In fact it is important, especially for mid-sized IT companies, to gain access to a European legal company structure accepted and trusted equally well in all European member states. The creation of a European Capital company would address the need of these companies.

The plans for the Societas Privata Europaea (SPE) would have matched the needs of these mid-sized IT companies. However, similarly as the plans for EU contract law, this initiative was not concluded. Thus, the European Digital SME Alliance advocates for a resumption of SPE on the agenda of EU.

4. Tax: reduction of VAT cross-border obstacles, retention of profits and fight multinational tax avoidance

For the European Digital SME Alliance, the different tax regimes on VAT are a central problem for the internal market. Paying VAT in the country, where the product is sold, generates huge bureaucratic obstacles for companies that are forced to bear unnecessary additional costs. This discourages companies to do business abroad and prevents the integration in the internal market.

Therefore, the European Digital SME Alliance welcomes the Commission's plan to reduce the distortion of the market by harmonizing the existing rules concerning Europe-wide sales and in doing so include non-European companies in the tax regime ending their tax advantages. The place of taxation has to be the place, where profit is made.

The argument that this change would favour companies in certain countries compared to others is an unjustified excuse. Not only the benefits deriving from having the same taxation on national and cross-border sales would be huge, but also there exists many other costs that are dramatically different from country to country and that certainly have much higher impact than a minor percentage difference in VAT, such profit tax, energy cost, labour cost, etc.

Moreover, tax incentives and support measures should be provided for companies that invest in digitalisation. For instance, profit up to 100.000 € which is reinvested in digitalisation, should be exempt from taxes. Such measures on reinvestment can trigger considerable investments comparable to the impact of reinvestments at the time of Germany's economic recovery after World War 2.

The European Digital SME Alliance calls on the EU and Member States to intensify coordination and efforts to fight against tax avoidance by multinational companies. Europe's digital SMEs often face unfair competition from foreign large enterprises that exploit the advantages of different national systems to pay less or even no taxes.

5. Enabling a modern and data-driven economy

The European Digital SME Alliance welcomes the Commission's proposal in its Digital Single Market strategy communication, to strengthen the modern data-driven economy in Europe and the cross-border data traffic with concrete actions. This includes useful proposals for initiatives with a smaller impact, such as an efficient and affordable cross-border parcel delivery service or the reduction of special forms of geo-blocking which result from unjustified national laws as to allow citizens and businesses to purchase online products independently from where they are.

However, the results of such actions may not be sufficient to have an impact of Europe's digital economy.

Data-driven business models depend on other essential factors, such a clear and positive regulatory framework. Enabling a modern data driven economy is key for Europe's competitiveness and digital leadership on the global markets.

In this context, the European Digital SME Alliance warns that the EU data protection directive should limit the restrictions on the use of data only where the processing concerns personal data. As long as data is processed anonymised or pseudonymised, and the re-identification of the data subject is not possible or not practicable, personal data processing should be allowed without explicit consent of the person concerned. If that is not the case, new technologies such as Big Data and the related business models in Europe cannot be realized. As a result, those innovations together with their value chain will be take place elsewhere. Besides, it is important that the data protection rules are applied in a uniform way as to ensure a coherent legal framework for all companies operating in the internal market.

6. Modernization of access to finance

For SMEs the growth investment necessary to reach the EU internal market is at least 10 times higher than in the US. SMEs face additional costs due to different languages, banking and legal systems, taxes and bureaucracy when they access any new national market in the EU.

Moreover the available venture capital in the US is 10 times higher than in the EU. Thus, the inequality between EU and US rises to a factor of 100. For a smaller company with the ambition to grow, this gap is overwhelming.

The EU urgently needs to focus on a better access to growth capital in form of venture capital, stock exchange for digital companies, growth funds or tax reliefs.

7. Unified regulation of the digital infrastructure in Europe

Another key aspect for a digital society and economy is unrestricted access to super fast and reliable telecommunications networks.

The deployment of broadband in the vast European rural areas is a crucial step. Therefore, the European Digital SME Alliance welcomes the revision of the Universal Service Directive and the intention of the Commission to provide incentives for an investment in broadband networks.

An essential target for 2020 should be access to networks with data transfer rate of 1 gigabit per second in 99% of households.

Moreover, it is important that net neutrality is met in Europe without discrimination. Privileged data handling should be restricted to a few selected critical classes of service without discretionary margin for the providers. Moreover, fragmentation of different rules and interpretations at the Member States level must be prevented. The recently approved EU Telecom Package does not establish a sufficient level of clarity and definitions, such that there is concrete risk of diverging applications at national level.

8. Interoperability and standardisation

The European Digital SME Alliance is highly interested in the Commission's plans to reach a better standardisation and interoperability.

In this context, we highlight the importance of standardisation as a way to involve the interested parties in the definition of the specifications that create interoperability. Standards allow companies to benefit from complex technological eco-systems. SMEs take great advantage from developing innovative products and services on standardised technologies, which could not be available for them in a closed proprietary eco-system where technologies are vertically integrated.

However, standards might be seen by SMEs especially if they are too complex or too expensive to comply with. Also, standardisation might be abused by certain parties to restrict the competition on the market.

Hence, for standardisation to deliver a key contribution to Europe's Digital economy, the following recommendations should be taken into account:

Standardisation processes must be open and inclusive, and especially allow the effective participation of SMEs. The European Commission should set clear requirements for Standardisation Bodies to ensure that the processes cannot be abused by certain parties with detriment to the large communities.

SME involvement should be increased. More European companies should exploit their position in ICT standardisation to become global market leaders. Hence, additional public support should be made available especially for creating awareness about standardisation among SMEs and for reducing the financial burden of participating into standardization.

Europe should invest in educating and training standardisation experts that can help European companies, especially SMEs, benefit from involvement in ICT standardization.

The intervention by public authorities, especially the Commission, should be limited to cases where this is justified, punctual and effective. The Commission should work with the industry and the interested parties in order to promote, accelerate or facilitate the development of certain standards, when this has the potential to promote competitiveness of European companies. On the contrary the EC should not impose an agenda on the Standardisation Organisations forcing them to produce standards even without the necessary industry involvement.

9. A unified European framework on copyright

The European Digital SME Alliance welcomes the EU's approach to create a common framework for a more unified copyright. Making business and research results available and simplifying the persecution of copyright violations both cross-border, supports competition and innovation.

At the same time, the EU should expand the European patent law and focus on a careful and unified patent examination.

Furthermore, patentability of software is a very critical aspect that may seriously harm the competitiveness of European digital SMEs. Hence, software patents should be prevented.

10. Digital skills for SMEs

Digital competences are a key pillars for a company's success. In the dynamic ICT market, securing well-qualified employees is a necessity for companies' survival. Whereas multinational IT companies can easily cope with scarcity of skilled staff in one country by moving operations or attracting people from another country, this is not possible for an SME. The search for employees cross-border is made difficult because the focus and level of trainings differ. Approaches to harmonise Vocational Education and Training such as the e-Competence Framework are welcomed by the European Digital SME Alliance. Promoting the use of such solutions would create favourable conditions for SMEs in the internal market.

Moreover, the European Digital SME Alliance pleads for a stronger involvement of social partners and representative industry associations in the Grand and National "Coalitions for Digital Jobs".

The European Digital SME Alliance also calls on governments to further invest in the harmonisation of VET curricula among Member States and especially to make reference to the European e-Competence Framework

A greater availability of skills would create more opportunities for digital companies thus fostering digitalisation of Europe's economy and society. Stronger digital SMEs would secure growth, innovation and full employment.