

Modernizing the SME definition: Getting it right for Europe's high growth and innovative businesses

Executive Summary

SMEs are the backbone of the EU economy, driving job creation, innovation and industrial competitiveness across Member States.

However, the **“linked enterprise” concept within the current SME definition**, designed to prevent large corporations from disguising subsidiaries as SMEs, **incorrectly assumes that PE and VC investors exercise the same control as corporate parents.**

In practice, **private capital funds are financial intermediaries** managing diversified portfolios, while **portfolio companies** backed by private capital **do not share operations, management structures or consolidated balance sheets.**

The current formulation forces companies to lose the SME status, despite meeting all other SME criteria. Companies that are identical in size, activity and strategy to other SMEs can therefore be treated differently solely because of their ownership structure.

At the same time, **private capital, as a whole – not just VC – plays a central role in financing SME innovation and growth**, with over 80% of PE-backed companies in 2024 in Europe qualifying as SMEs.

Private capital also shows a proven record of innovation, not just growth: both at the core of the industry – **proven by data connecting intellectual property (IP) creation with private investment.**

When PE/VC-backed companies lose SME status due solely to ownership structure, they risk losing access to regulatory relief, incentives and public support schemes. This **creates a “cliff-edge” effect that discourages risk capital investment at the core of the EU’s innovation and growth agenda, while promoting Europe’s structural overreliance on bank lending.**

Over time, this dynamic **reinforces Europe’s scaleup gap and undermines the development of globally competitive firms.**

To incentivise SMEs to access private capital within the European market, and mobilise private capital investments, **building on the Commission’s 2025 Recommendation on Small Mid-Caps, the SME definition should be clarified to reflect the independence of private capital-backed portfolio companies** where they maintain separate accounts and funds follow defined investment and exit strategies.

Such alignment should also support coherence with forthcoming initiatives, including the 28th regime, the European Innovation Act and the revision of the General Block Exemption Regulation.

In more detail

The EU's economic vitality is very much intertwined with the performance and resilience of its Small and Medium-sized Enterprises (SMEs), which represent the vast majority of the business landscape and serve as the primary engine for job creation and industrial innovation. Central to this ecosystem is the Commission Recommendation 2003/361,¹ establishing the framework for identifying which enterprises qualify as SMEs and thus for preferential treatment, administrative relief, and targeted financial support – under current and upcoming EU programs and initiatives.

However, the current SME definition contains a misalignment between its design objectives and practical effects. The "linked enterprise" concept, intended to prevent circumvention of SME support through dominant influence, creates perverse outcomes when applied to venture capital (VC) and private equity (PE) firms – and especially the latter. This is particularly relevant as the Commission's agenda increasingly relies on mobilizing private investment to scale up Europe's young, fast-growing companies in critical products and services and to advance the Union's competitiveness and autonomy objectives.

As the voice of Europe's PE/VC industry and their investors, Invest Europe is committed to ensuring that the EU's frameworks support the financing needs of the companies driving both innovation and growth. Europe cannot build future-proof policy frameworks that are not anchored in market reality. If innovation, autonomy, and competitiveness are the goal, then the framing of SMEs must be revised to match the financial and operational realities of modern firms, and thus accurately reflect the nature and role of PE/VC investments – as part of its broader agenda.

This paper will:

- look at the issue within the SME definition and deconstruct the flawed analogy between integrated corporate groups and diverse PE/VC portfolios;
 - establish the symbiotic relationship PE/VC and Europe's SMEs, demonstrating that PE investment is SME investment, as well as the nexus between PE/VC and both innovation and growth;
 - articulate the short-term and long-term consequences of the current SME definition;
 - offer a clear path forward to align the SME definition with economic reality, anchored in the recent development from the Recommendation on Small Mid-Cap (SMC) enterprises.
- ***What's the problem and why it needs changing: the misclassification of PE/VC investments in the SME definition***

1. The issue in the SME definition: how private capital ownership leads to a loss of the SME status

A central feature of the current SME definition is that it links SME status not only to a company's size, but also to its ownership structure. In practice, this means that SMEs backed by PE or VC investors can lose SME status solely because of how they are financed.

Under the SME definition, an enterprise is no longer considered "autonomous" if another entity holds between 25% and 50% of its capital or voting rights, without control. In such cases, the company becomes a "partner enterprise". Where an investor exercises a dominant influence, the company is

¹ As per Article 2 of the Commission Recommendation 2003/361, a micro-company has up to 10 employees, and a turnover or balance sheet total of up to €2 million; a small company has up to 50 employees, and a turnover or balance sheet total of up to €10 million; a medium-sized company has up to 250 employees, and a turnover of up to €50 million or a balance sheet total of up to €43 million.

classified as a “linked enterprise”.² A specific exception exists to encourage equity financing: an enterprise may still be treated as autonomous even if the 25% threshold is reached or exceeded by certain categories of investors, including VC companies, business angels and institutional investors, including regional development funds, amongst others, provided that these investors are not linked to the enterprise and, in some cases, that their total investment remains below a defined monetary threshold.³ However, this exception applies only narrowly and does not cover the full range of PE and growth capital structures.

Where an investor does not qualify for the “autonomous” exception, the SME status of the portfolio company must be assessed by aggregating data with that of the investor to determine if it still fits within the SME ceilings. For “partner enterprises”, data is added proportionally based on the percentage of interest in the capital or voting rights, for “linked enterprises”, 100% of the data from the linked investor (and any other enterprises that investor controls) is added to the company’s own totals.

For PE- or growth-backed SMEs, aggregation with the investor’s data almost inevitably pushes the combined figures beyond SME ceilings. As a result, companies that remain SMEs in operational and economic terms lose SME status because they are assessed as part of a much larger economic group.

2. Why the SME definition approach is incorrect: key differences between private capital and trade groups

By implicitly assuming that private capital investors function in the same way as corporate parent companies, the definition conflates two different models of ownership and control: financial investment and industrial group integration.

Treating PE/VC-backed companies as if they were subsidiaries of corporate groups ignores the legal, economic and operational reality of private capital investment and leads to outcomes that are misaligned with the objectives of SME policy. PE/VC is about value creation, not about integrating companies into a parent organization.

Key differences between PE and corporate groups illustrate this misalignment.

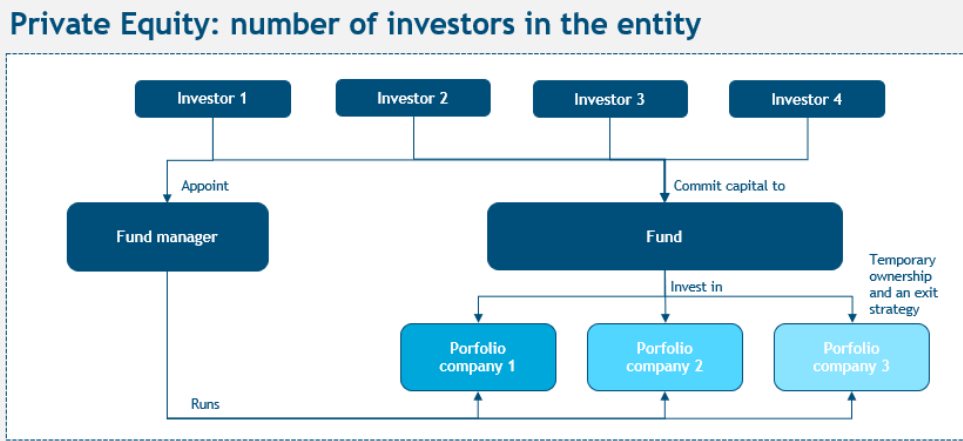
a. Differences in the ownership model

PE/VC firms act as intermediaries for a diverse pool of investors who commit capital to a fund. The fund manager, the general partner (GP) – is appointed to run the fund with a long-term exit strategy. The investors – limited partners (LPs), such as pension funds, insurers, or endowments – have no ability to exercise control over portfolio companies.

In a corporate group, the parent company holds and controls subsidiaries indefinitely.

² As per Article 3(3) of the Commission Recommendation 2003/361, a link is established if the investor: holds a majority of the voting rights, has the right to appoint or remove a majority of the management or supervisory body, exercises dominant influence via a contract or the company's memorandum/articles of association

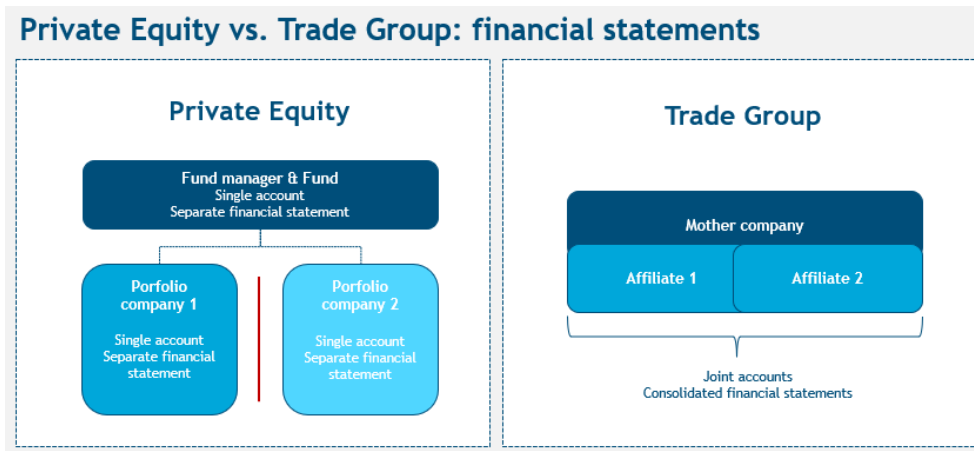
³ The monetary threshold refers to business angels and stands at EUR 1,250,000.



b. Differences in the accounts and financial reporting

Funds and portfolio companies maintain entirely distinct accounts. Each portfolio company prepares its own financial statements and is not consolidated into a single group balance sheet. Funds themselves are separate legal and accounting entities, with clear contractual boundaries, as they are investments.

By contrast, corporate groups consolidate their subsidiaries (“affiliates”) into one set of financial accounts. Subsidiaries are part of one permanent group structure, integrated into the parent company’s balance sheet and strategy.

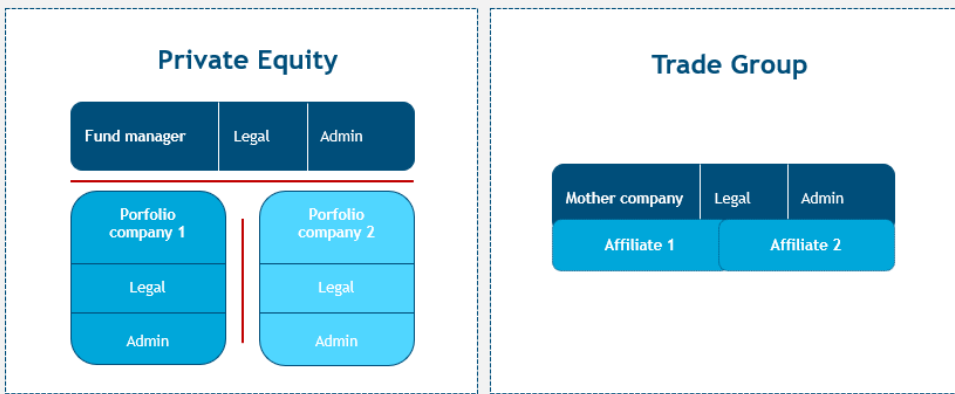


c. Differences in the organizational structure

PE/VC-backed companies do not share centralised management, joint services, or common legal and administrative structures. Each portfolio company operates entirely independently, with its own legal advisers, administrative functions, and management team. The fund manager sits outside this structure, providing capital and board-level guidance, but does not integrate services or decision-making across companies. Portfolio companies are stand-alone businesses.

In contrast, trade groups centralize these functions at the parent company level. Legal, administrative, and management services are pooled and coordinated for all affiliates, ensuring group-wide integration and oversight.

Private Equity vs. Trade Group: management

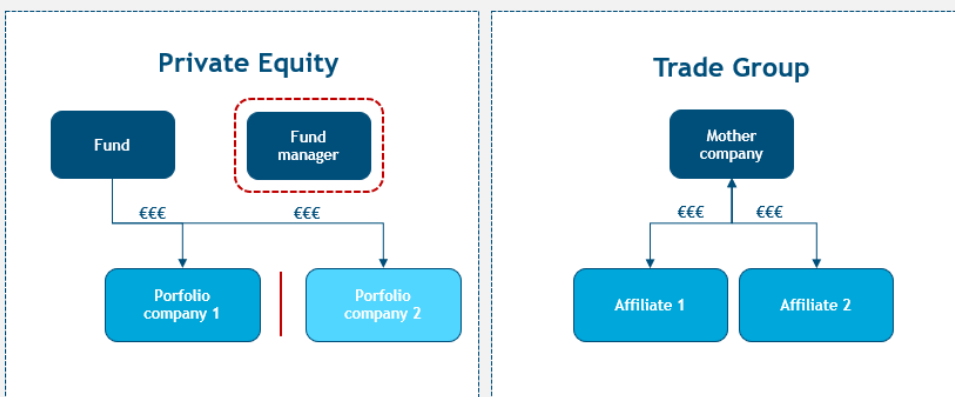


d. Differences in financial aid and capital allocation

Each portfolio company receives its own direct investment allocation from the fund, and those resources cannot be reallocated between companies. If a portfolio company faces economic difficulties, it generally cannot rely on financial support from the fund manager or from other companies in the portfolio. There are no portfolio-wide cash pools or intra-group guarantees.

Trade groups have a parent company that can move resources freely between affiliates. Profits from one subsidiary can be redirected to support another, or group-level guarantees can be used to stabilize weaker units. This capacity for cross-subsidization is one of the defining features of corporate groups, but it does not exist in the PE/VC model.

Private Equity vs. Trade Group: aid

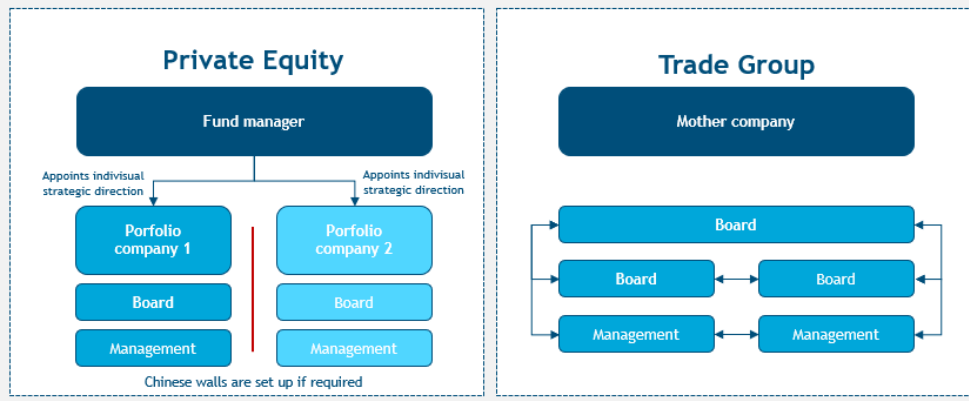


e. Differences in operational management

PE/VC managers take on meaningful risk to provide strategic guidance and support, in order to build long-term value, especially through the Board. However, each portfolio company has its own independent board and management team, responsible for day-to-day decisions and operations. Companies remain fully separate.

In a corporate group the parent company exercises direct oversight across subsidiaries. Boards and management teams are interconnected, and operational decisions are coordinated at group level. This creates a unified chain of command that does not exist in the PE/VC industry.

Private Equity vs. Trade Group: day-to-day management

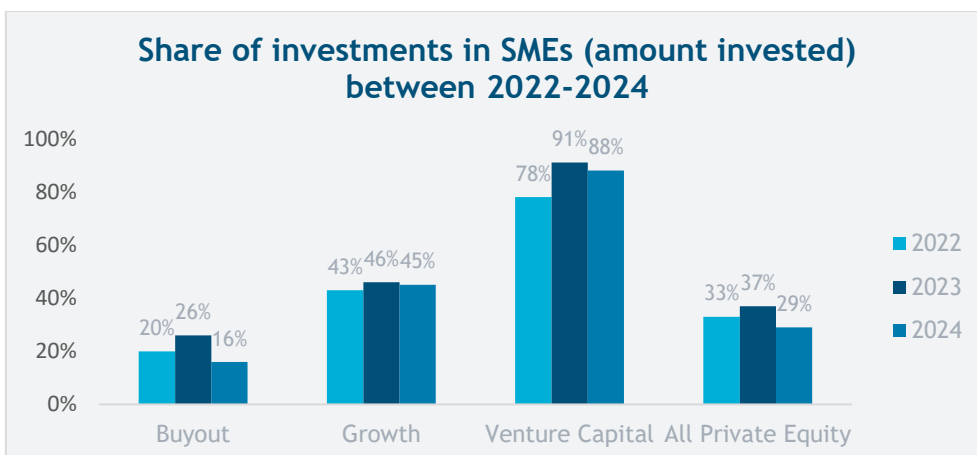
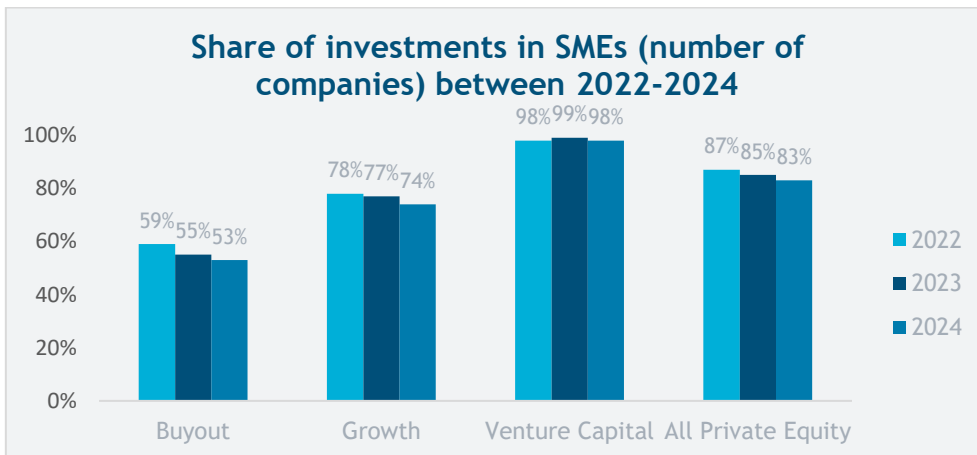


- **Why the SME definition matters for Europe’s growth and innovation**

Within Europe’s SME ecosystem, private capital is not a peripheral stakeholder. It is a primary source of long-term capital – for both innovation and growth – for the very companies that sit at the center of the EU’s competitiveness agenda.

1. Who finances SMEs: private capital is structurally SME-focused across all investment stages

Across all segments of the private capital market – from VC to growth and buyout funds – investment activity is structurally concentrated on SMEs. It is the core business of the European private capital industry.



Source: Invest Europe / European Data Cooperative (EDC)⁴

Data from Invest Europe and the EDC show that VC invests almost exclusively in SMEs, reflecting its role in financing early-stage and innovative companies.⁵ This structural focus is already implicitly recognized in EU rules through the “partner enterprise” treatment applied in certain contexts.

However, the SME focus of private capital extends well beyond VC alone. Growth capital funds consistently invest a very high share of their activity in SMEs, both by number of companies and by capital deployed. Even in buyout strategies – often perceived as targeting only large corporates – a majority of portfolio companies are SMEs by number, with the SME share remaining consistently above 50%. While larger investment tickets naturally account for a higher proportion of capital in bigger firms, the volume of SME exposure remains economically significant.

Overall, between 2022 and 2024, more than 80% of all European PE-backed portfolio companies were SMEs, and approximately one-third of total PE capital was invested in SMEs. These figures have remained broadly stable over recent years, although a gradual decline can be observed in both the number of SME investments and the share of capital deployed, particularly at the buyout stage.

In this context, the impact of the SME definition, including the treatment of “linked enterprises”, cannot be dismissed as marginal. The way SME status is determined affects a substantial share of the private equity ecosystem and, by extension, the majority of companies financed through private capital – the firms expected to drive Europe’s economic transformation.

2. What finances innovation: private capital plays a central role in enabling innovation

Access to equity finance is closely linked to innovation outcomes, not just growth. This relationship is widely recognized in economic and innovation policy analysis, including at EU and OECD level.

Evidence extracted by Eurostat in September 2025 shows that while debt remains the most widely used form of financing in general, equity financing plays a disproportionately important role in funding innovation. Between 2020-2022, only a small share of EU enterprises used debt specifically to finance innovation activities, while a smaller but more innovation-intensive group raised equity. Among companies that raised equity, around half used it fully or partially to fund innovation or R&D activities – a significantly higher proportion than among firms relying on debt.⁶

This reflects the inherent risk profile of innovation projects. Innovation investment involves uncertainty, long time horizons and asymmetric outcomes. Equity financing allows this risk to be shared with investors, making it structurally more suitable for innovation than debt financing, regardless of company size. Data shows that innovation-active firms are significantly more likely to seek and obtain equity financing than non-innovation-active firms, underscoring the central role of equity investors in enabling innovation.⁷

⁴ Invest Europe (2025), *Investing in Europe: Private Equity activity 2024*, Invest Europe, published 8 May 2025; Invest Europe (2024), *Investing in Europe: Private Equity activity 2023*, Invest Europe, published 10 May 2024; Invest Europe (2023), *Investing in Europe: Private Equity activity 2022*, Invest Europe, published 3 May 2023.

⁵ Within Invest Europe’s data universe, SMEs are defined as companies with fewer than 250 full-time equivalent staff. The same categorization is used within Eurostat.

⁶ Eurostat (2025), *Enterprises – access to finance and public funding for innovation purposes*, Statistics Explained, European Commission. Retrieved from https://ec.europa.eu/eurostat/statistics-explained/index.php?title=Enterprises_-_access_to_finance_and_public_funding_for_innovation_purposes (accessed 16 January 2026).

⁷ *Ibid.*

Public funding remains important, but it also does not close this gap. While more than a quarter of EU firms receive some form of public support, only a small fraction of enterprises rely on public funding specifically for innovation or R&D.⁸

Private capital, therefore, plays a critical role in addressing this market failure by providing risk-bearing finance where debt and public instruments fall short.

3. Where does innovation happen: innovation and growth are interconnected, extending beyond VC

Policy discussions on innovation often rely on an implicit distinction between “innovation” and “growth”, or on a narrow association of innovation with VC alone. While innovation and growth are not identical concepts, in practice they are deeply intertwined. One does not automatically guarantee the other, but neither can be sustained without the other. A understanding of innovation must extend beyond the narrow lens of startup creation and product invention. Innovation takes different forms, including the form of economic transformation within established companies – through digitalization, organizational change, process optimization and the adoption of new technologies.

Innovation policy that focuses exclusively on early-stage invention risks overlooking how innovation is translated into productivity gains and competitiveness. In practice, innovation becomes economically meaningful only when firms are able to scale, invest, professionalize and expand into new markets – processes that require sustained access to long-term risk capital.

As reflected in the 2025 OECD analysis, the role of SMEs extends well beyond employment and value creation: SMEs are sources of innovation, often pioneering new ideas and technologies that drive economic progress. Innovation, however, does not occur simply because a company is classified as an SME. It depends on managerial capacity, access to technology, the ability to develop and protect innovation assets, and access to international markets – the structural gaps that private capital is designed to address. In this sense, private capital’s role is not merely to increase output, but to change the production function itself: how value is created, how processes are organized, and how innovation is deployed at scale.⁹

This broader concept of innovation is reflected in international frameworks, which recognize “business process innovation” as a key driver of productivity and competitiveness.¹⁰ While private capital excels at financing the creation of new technologies and business models, it also plays a distinct and complementary role by driving large-scale transformation within existing SMEs.

For example, a manufacturing SME backed by PE that deploys advanced digital tools or artificial intelligence across its operations is undertaking innovation at scale, with tangible productivity and efficiency gains that ripple through value chains and regional economies. Restricting the policy narrative – or the application of SME status – to venture-backed companies alone therefore overlooks a substantial share of innovative activity occurring within growth-stage and later-stage SMEs, where a relevant portion of employment and value creation take place.

4. What does the evidence show: innovation outputs confirm private capital’s role across all stages

⁸ *Ibid.*

⁹ OECD (2025), *Unleashing SME Potential to Scale Up: Helping SMEs Scale Up*, OECD Studies on SMEs and Entrepreneurship, OECD Publishing, Paris, <https://doi.org/10.1787/ea948a58-en>

¹⁰ OECD/Eurostat (2018), *Oslo Manual 2018: Guidelines for Collecting, Reporting and Using Data on Innovation, 4th Edition, The Measurement of Scientific, Technological and Innovation Activities*, OECD Publishing, Paris/Eurostat, Luxembourg. <https://doi.org/10.1787/9789264304604-en>

This broader innovation-growth dynamic is also evident in measurable outputs. The relationship between private capital and innovation is mutually reinforcing: both PE and VC respond to, and stimulate, the creation of intellectual property.

Data from Invest Europe and the European Union Intellectual Property Office (EUIPO), demonstrates that companies with existing intellectual property, such as trademarks, attract significantly higher levels of private investment across venture, growth and buyout stages. More specifically, companies with pre-existing trademarks received 55% more investment at the venture stage, 45% more at the growth stage, and 68% more at the buyout stage – every fund stage is part of a continuum of value creation and innovation capability-building. Additionally, a 10% increase in trademark stock correlated with about a 3.4% increase in finance raised.¹¹

At the same time, increased capital investment directly enables further innovation: higher levels of investment are associated with a greater likelihood of subsequent patent and trademark filings. A 10% increase in capital invested raises the odds of subsequent patent filings by around 1% and trade mark filings by around 1.22%, showing that financial backing directly enables new technological and commercial IP creation.¹²

Overall, out of around €809 billion invested in EU27 companies between 2007 and the first half of 2023, 20% went to companies with patents, 40% to those with trademarks, and 15% to firms with both forms of IP protection.¹³ This virtuous circle highlights the role of private capital not only in scaling innovative SMEs, but also in deepening their innovation capacity over time, across all fund stages – an acknowledgment that is not adequately reflected within the current SME definition.

- **The practical consequences of the current SME definition: from firm-level impacts to system-level consequences**

The dynamics elaborated in the previous section unfold against a regulatory framework that continues to apply an SME definition that risks actively deterring PE and VC investment. In practice, the current definition can lead investors to reconsider investments, and SMEs to avoid accepting PE/VC financing altogether, in order to preserve their SME status, which acts as a gateway to a broad range of economic, regulatory and financial advantages that materially shape business models, investment decisions and growth trajectories.

Because access to finance directly shapes an SME's ability to innovate and scale, the design of the SME definition can either support – or, as it currently stands, undermine – EU objectives. The consequences extend beyond individual transactions.

1. The immediate consequences of losing SME status: discouraging private capital investments in high-growth, innovative SMEs

For companies, SME status provides access to a set of cumulative regulatory, financial and institutional conditions that help address capability and scale constraints. This saves time and money, allowing businesses to trade compliance for value creation. For PE/VC investors, the ability of portfolio companies to maintain SME status translates into tangible implications for risk, cost structures and exit potential, affecting predictability and attractiveness.

¹¹ Invest Europe and EUIPO (2024), *Protecting European Innovation: Private Equity's Role in European Intellectual Property Rights*, Invest Europe/EUIPO, Brussels/Alicante, published 20 November 2024.

¹² *Ibid.*

¹³ *Ibid.*

Area	Benefit while SME	Impact when SME status is lost
Regulatory requirements	<p>For SMEs: lighter accounting, reporting and administrative requirements, reduced fixed costs and management distraction</p> <p>For investors: lower compliance costs improved margins, cash flow and capital efficiency across the portfolio</p>	<p>For SMEs: transition to full reporting and disclosure regimes, mandatory audits and expanded compliance infrastructure, increases fixed costs, stricter enforcement regimes and higher penalties for non-compliance</p> <p>For investors: higher operating costs, reduced cash generation and increased regulatory risk that must be priced into the investment</p>
Tax treatment	<p>For SMEs: access to SME-specific tax reliefs, including reduced effective tax rates and R&D tax credits</p> <p>For investors: tax-efficient structures, improved project economics and after-tax returns</p>	<p>For SMEs: higher effective tax burden</p> <p>For investors: lower after-tax returns and reduced attractiveness for investments</p>
Access to specialized services and support	<p>For SMEs: access to free or low-cost targeted advisory services, regulatory guidance, mentoring, networking opportunities, institutional engagement</p> <p>For investors: reduced execution risk and reliance on external advisors</p>	<p>For SMEs: increased fees and costs, as well as reliance on external consultants and legal resources</p> <p>For investors: higher execution costs and operational risk</p>
Procurement opportunities	<p>For SMEs: direct and preferential access to SME-friendly procurement procedures, revenue stability</p> <p>For investors: diversified and predictable revenue streams</p>	<p>For SMEs: reduced competitiveness, and increased uncertainty</p> <p>For investors: reduced attractiveness and constrained growth pathways</p>
Access to public funding and aid	<p>For SMEs: eligibility for innovation grants, guarantees and financing programs, higher de minimis thresholds and more favorable State aid conditions</p> <p>For investors: co-investment and risk-sharing mechanisms, capital efficiency and reduced downside risk</p>	<p>For SMEs: disqualification from ongoing or future support programs and loss of favorable aid conditions</p> <p>For investors: reduced ability to leverage public funding alongside private capital, increased risk and capital intensity of investments</p>

Taken together, these factors make SME investment a compelling and economically rational component of private capital portfolios.

However, when a company loses SME status due to ownership or control criteria, the impact is immediate and often severe. Crossing the SME threshold triggers a disproportionate increase in compliance obligations and operating costs, which simultaneously increases risk, reduces capital efficiency and complicates exit strategies for investors.

In the case of private capital-backed companies, all of this occurs as competitors may still qualify as SMEs and maintain advantages, while the financed firm, although it remains within the SME size thresholds, loses status because of ownership. Additionally, as this transition is not always the result of organic growth, the short adjustment period also does not allow companies and investors the needed time to plan for its consequences.

Faced with this trade-off, some companies choose to limit investment, delay scaling or seek alternative, or suboptimal financing structures. As a result, otherwise value-creating investments may be delayed, downsized or abandoned altogether.

2. The long-term consequences of losing SME status: reinforcing Europe's innovation and scaleup gap

These micro-level distortions contribute to a well-documented macro-level challenge: Europe's persistent scaleup gap.

Europe does not suffer from a lack of entrepreneurship. On the contrary, the continent excels at startup creation, with record numbers of new ventures launched in recent years and about a third of global founders over the past decade.¹⁴

However, it struggles to convert promising young companies into globally competitive scaleups. Invest Europe and EDC's fundraising data shows that the European private capital market experienced a pronounced peak followed by a correction where different fund strategies have followed distinct trajectories. While VC is earlier in the recovery cycle than buyouts and growth equity, capital availability for later stages remains uneven. Although there was a modest rebound in 2024, growth funds remain structurally smaller than they were before the market correction, unlike VC. All while buyout fundraising peaked in 2022 and then declined sharply over the 2022-2024 period, falling by roughly 43%. This suggests that capital is flowing back more readily to early-stage innovation than to the scaleup phase: a weakness in the financing available for scaling companies.¹⁵

The investment data also reinforces this picture. Capital deployment rebounded in 2024 after the 2023 slowdown, but the number of companies financed continued to fall – a shift toward larger tickets for fewer companies, reflecting greater selectivity and risk aversion across the market. However, compared to their 2021 peak, almost half of total growth investments has disappeared. Buyout investment activity has been volatile but recovered in deployment faster than in fundraising, pointing to the use of existing dry powder rather than renewed capital inflows.

The combination of these trends and cyclical exit markets leaves scaleups caught between a recovering venture market and a cautious growth one, reflects an imbalance risks leaving successful venture-backed companies without sufficient capital to scale, even as early-stage innovation continues to thrive.

Market sentiment within the private capital industry reinforces this diagnosis. Investors identify the availability of scaleup finance, fundraising constraints and weak exit environments as the most significant challenges facing the European ecosystem – challenges that mutually reinforce one another and widen the gap with competing jurisdictions, especially coupled with a lower risk-taking attitude, and the lack of adequate market integration.¹⁶

In this context, regulatory frameworks that disincentivize private capital investment at scaling stages risk aggravating this structural problem. When SMEs are penalized for accessing PE or growth capital the result is a self-reinforcing cycle of under-scaling.

¹⁴ Atomico (2025), *State of European Tech 2025*, Atomico, London.

¹⁵ Invest Europe (2025), *Investing in Europe: Private Equity activity 2024*, Invest Europe, published 8 May 2025.

¹⁶ Arthur D. Little and Invest Europe (2025), *The Insight: State of the European Private Equity Industry 2025*, published 6 November 2025.

- **Conclusion: our proposed solutions**

The outcomes of the SME definition are not the result of SME policy objectives, but of a structural misclassification. PE/VC investors provide both capital and strategic support; they do not integrate SMEs into industrial groups. By treating private capital-backed companies as if they were subsidiaries of corporate groups, the current definition creates unintended disincentives to equity financing – penalizing businesses for accessing long-term risk capital – distorts investment decisions and contributes to Europe’s scaleup gap, undermining the very goals the SME definition is intended to serve: innovation, productivity and sustainable growth.

The European Commission has already acknowledged this reality. In its May 2025 Recommendation on SMC enterprises, it explicitly recognized that companies backed by both VC and PE funds should not be disadvantaged when certain conditions are met, exactly because of the role these funds play in preserving the ability of European enterprises to finance their innovation and growth.

The proposed independence carve-out for private capital ownership is exactly what has been missing in past the past from the SME definition and should, therefore, be covered within the 2003 Recommendation.

We suggest amending the SME definition to reflect the derogations for PE/VC funds and Alternative Investment Funds (AIFs) as set out in the SMC Recommendation. This would ensure that the current “majority” rules that trigger linkage in the SME definition (as defined in Article 3(3) of the Commission Recommendation 2003/361, prior to any subsequent amendments) do not apply to PE/VC funds – so long as they maintain the required accounting and exit protocols – and that PE funds are not automatically considered “partner enterprises” (as defined in Article 3(2) of the Commission Recommendation 2003/361, prior to any subsequent amendments), thereby also limiting additional proportional aggregation and providing a treatment once reserved only to VC.

Specific wording that can be included from the SMC recommendation concerning the “linked enterprise” status:

*“Where an alternative investment fund as defined in Article 4(1), point (a), of Directive 2011/61/EU has invested into an enterprise, **the following should not be considered “linked enterprises”** for the purposes of point 3.3:*

- a. that enterprise and that alternative investment fund;***
- b. that enterprise and the manager of that alternative investment fund;***
- c. that enterprise and another enterprise in which that alternative investment fund has invested.***

*The first subparagraph applies **provided that all the following conditions are met:***

- a. the alternative investment fund and its manager, and the enterprises concerned maintain separate accounting records;***
- b. the alternative investment fund and its manager have a pre-defined investment strategy to exit the enterprise or enterprises concerned, including by realising their value through the sale of the enterprise or other means.”***

Specific wording that can be included from the SMC recommendation concerning the “partner enterprise” status:

“By way of derogation from point 3.2, an enterprise may be ranked as autonomous, and thus as not having any partner enterprises, even if 25% or more of its capital or voting rights are held by the following investors, provided that those investors are not linked, within the meaning of point 3.3, either individually or jointly to the enterprise in question:

- a. *public investment corporations, **venture capital or private equity funds**, individuals or groups of individuals with a regular venture capital investment activity that invest equity capital in unquoted businesses ('business angels'), provided the total investment of those business angels in the same enterprise is less than EUR 5 000 000;*
- b. *universities or non-profit research centres;*
- c. *institutional investors, including regional development funds;*
- d. *autonomous local authorities with an annual budget of less than EUR 10 million and fewer than 5 000 inhabitants."*

While the SME definition is not the only lever for mobilizing private capital, it remains a longstanding and timely one. The SME definition is embedded across a wide range of existing EU instruments and initiatives – including the General Block Exemption Regulation (GBER), the Rescue and Restructuring Guidelines, EU financing programs, etc. – and will also underpin forthcoming initiatives, such as the 28th regime and the European Innovation Act. Misalignment at this level, thus, risks propagating inconsistencies across the broader policy framework.

To avoid misalignment and legal uncertainty, we suggest prioritizing the review of the SME definition and, where possible, having it preceding the adoption of existing initiatives undergoing further review, as well as the adoption of new initiatives, if they already make use of it or will. This is particularly important where thresholds or criteria may be adjusted subsequently.

A revised SME definition, consistent with current market needs and realities, would signal that Europe supports entrepreneurship throughout the entire lifecycle of a business – not by expanding SME eligibility beyond its intended scope, but ensuring that SME status reflects how companies operate in practice.