Corona Matching Facility and package of measures for start-ups and SMEs

AFTER A LONG WAITING PERIOD: APPLICATION FOR 2 BILLION EURO PACKAGE OF MEASURES HAS NOW STARTED IN BOTH PILLARS

Summary

- Structure and content of the package of measures
- Conditions for eligibility
- Eligibility and application process

The liquidity supply to bridge the corona pandemic has so far been lacking, especially for innovative start-ups and young technology and growth companies. These companies were hardly able to benefit from the corona support programs launched in March, as they almost without exception did not meet the eligibility conditions for the programs. In particular, financing through borrowed capital and the house bank principle provided for in the existing support programmes is not a realistic option for start-ups. After a long lead time and the concrete announcement of the ministries involved at the beginning of April and in the course of May, these companies now have a full opportunity to submit applications for the subsidies.

The package of measures, which is specifically tailored to start-ups, is based upon two pillars. The aim is to reach a large proportion of German start-ups in order to strengthen these and thus also support technological advancements in Germany as a business location. The first pillar of the package is the "Corona Matching Facility" (matching fund). This pillar is aimed at young companies that have already been financed by private venture capital funds (VC funds) or are planning such financing for their further growth. Venture capital financing is an important source of finance for young companies. Investments used by VC funds to finance start-ups in the form of equity capital or convertible loans can be topped up with federal funds under Pillar I. Applications for Pillar I can be submitted to KfW Capital or the European Investment Fund (EIF) since 14 May.

Start-ups and small SMEs that cannot yet rely on VC funds as their investors and therefore do not have access to the Corona Matching Facility are to be supported with mezzanine or equity financing under Pillar II of the package of measures. Since 8 June, the KfW has been providing the promotional institutions of the federal states with global loans with indemnity against liability for this purpose. This enables the regionally well-integrated and networked promotional banks of the federal states and SME investment companies to provide and refinance promotional instruments that are specifically tailored to the federal states. The arrangement will differ in the individual federal states. Both open and dormant equity investments are planned for implementation. However, details are not yet known. The public funding share in Pillar II is a maximum of 800,000 euros per company for each financing. In contrast to Pillar I, here there is the possibility, but not the obligation, for additional investors to make additional funding available to start-ups and SMEs.

Objective of the package of measures

Additional public funding is provided through the Corona Matching Facility via KfW Capital and the EIF, and KfW Global Loans via the state development institutions, in order to make investments more attractive and ensure that start-ups can be provided with sufficient funds. In spite of the crisis, young companies should be able to continue on their current growth path even if the additional economic impairments would otherwise not allow them achieve this.

Requirements for the legitimate claim on the part of the start-up

As recipients of the funding, the measures are aimed directly at start-ups that are worthy of support: the start-ups supported by the funding from both pillars must fulfil further requirements in addition to a sustainable business model. The company must have a "strong German connection" and the financing requirement must have been triggered by the Corona crisis. By definition, a "strong connection to Germany" exists if the company has its registered office or head office or the focus of its business activities in Germany or at least half of the full-time employees work here. Moreover, as required by most other corona support programmes, the company must not have been in financial difficulties as defined by the EU as of 31 December 2019. Individual financial or strategic investors may not hold a majority stake in the start-up. The programme does not impose any additional requirements such as minimum limits on the duration of market activity, turnover or number of employees. Financial assistance through Pillar II is subject to an additional restriction: it is only available to companies with group sales of up to EUR 75 million. The aim, but not the prerequisite, of the Pillar I and II funding instruments is to bridge liquidity problems that have only arisen due to the corona pandemic situation.

Eligible applicants for Corona Matching Facility (Pillar I)

Applications must be submitted directly to KfW Capital by the private VC funds and not by the start-up concerned. Applications may be submitted by European VC fund managers with a German portfolio that already existed before the crisis. An extension of the programme to VC funds based outside Europe is currently being discussed. Both follow-up investments in existing portfolio companies and new investments are eligible for matching. So-called corporate VC funds should not be eligible for application. There has been much criticism of this in various discussions, whereby it has been signalled that requests from corporate VC funds will not be fundamentally rejected, but that attention will be paid during the application process to whether a corporate VC fund is structured similarly to a classic VC fund and pursues similar investment strategies. It is not a prerequisite that the public venture capitalists KfW Capital or the European Investment Fund are already investors in funds of VC fund managers. If the applying VC fund manager is not yet accredited, the verification process provided for by the funding programme must be carried out before the funds are approved. This verification process consists of a concise due diligence of the VC fund manager, together with the details of the funds for which the matching is requested by the CMF institution (KfW Capital or the EIF).

Conditions for the implementation of the investments for the Corona Matching Facility

Together with the start-up and any other investors, the VC fund managers first decide which financial engineering instrument to choose. Equity or equity-like instruments are possible choices, e.g. in the form of convertible loans. After a general request from the VC fund, an NDA has to be signed and the fully completed application with supporting documents has to be sent to the CMF institution. During the application process, the matching quota for each fund managed by the VC fund manager must already be defined. Upon receipt of the application documents, the CMF institution then submits a co-investment and trust agreement to the VC fund manager for review. At the same time, the CMF institution carries out its audit of the applicant and requests further documentation as necessary. If the verification process is successful and all aspects of the co-investment and trust agreement are finally negotiated between the applicant and the CMF institution, the co-investment and trust agreement shall be concluded. Subsequently, the financing round or the convertible loan agreement with the start-up can be concluded by the VC fund and the

funds can be drawn from the Corona Matching Facility. The Corona Matching Facility can be drawn upon, provided that the application and signature of the financing documents has been completed by 31.12.2020. However, it also applies retroactively from April 2, 2020, provided that the documentation of the financing round includes an extension through the use of the Corona Matching Facility. In relation to the CMF institution, the accredited VC fund manager assumes a role as trustee for the public federal funds. Management fees or carry are not paid for the fiduciary management of the federal funds and the investments made from them. Then again, the VC fund manager is free to decide, among other things, on the form and timing of the exit of his investments matched with the federal funds.

Pillar I matching quota

The applicant VC fund managers determine the matching ratio for their portfolio companies and their new investments at the outset. However, the matching ratio for new investments must not be higher than for existing companies. The matching ratios thus selected by the VC fund manager are binding for all further investments until 31 December 2020. The matching quota with public CFM funds is usually 50%. However, the VC fund manager can also decide to deviate from this and opt for a lower or higher matching quota. The maximum matching ratio can be 70 %, but in relation to the specific investment in a start-up only if the matching portion of the total financing round does not exceed 50. The higher quota is therefore only possible if private, non-matched investments from further investors join the round. If other public investors also participate in the financing round, the total share of public funds may not exceed 70% of the round.

Mandatory tender offer for VC funds under pillar I

VC fund managers applying under the Corona Matching Facility will have a tender obligation until 31 December 2020 for all further financing rounds of CMF-eligible portfolio companies of the accredited VC fund. The same principle is valid for new investments, but does not apply if matching is applied for retroactively.

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