

# IfM-Position Paper

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## Mittelstand policy in a social-ecological market economy

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The Covid-19 pandemic, the war in Ukraine, supply chain problems, climate change, digitalisation are all currently causing increased uncertainty in Mittelstand companies. In the short term, Mittelstand policy can cushion risks to the existence of Mittelstand companies or individual subgroups with the help of a sectoral, individual company, or size-related measures. However, with a view to the necessary long-term transformation to a climate-neutral economy, a regulatory approach and the design of framework conditions that focus on Mittelstand companies in their entirety are preferable. After all, Mittelstand companies are not only a pillar of the economy but also make significant contributions to society and democracy in our country.

A particular challenge for economic policy is to develop the framework conditions in a way so that climate-neutral value creation is achieved and, at the same time, Mittelstand companies are not unduly burdened.

### Mittelstand-friendly climate policy

One of the priorities of Mittelstand policy is to support the transition to CO<sub>2</sub>-neutral value creation. Mittelstand companies and environmental protection are no longer at odds. In detail, an IfM survey in the manufacturing sector in 2021 (Dienes et al. 2021) found that most companies are "pro-climate protection" and also implement such policies. More than 50 per cent of them have already realised environment-related process innovations between 2018 and 2021. Almost 40 per cent had launched environmental product innovations. However, less than 28 per cent of the Mittelstand companies surveyed stated that they had sufficient resources for this (non-Mittelstand: 32 per cent). Their higher propensity for ecological innovation is probably due to the unique characteristics of Mittelstand companies (that is, unity of ownership and management).

Institut für  
Mittelstandsforschung

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**Mittelstand policy can strengthen this proactive approach of Mittelstand companies.** Appropriate environmental policy should give companies leeway for innovative solutions and not force them into a tight corset of regulations and prohibitions.

Flexible climate policy instruments such as CO<sub>2</sub> pricing in form of a Pigovian tax or emissions trading can be used preferentially, but attention must be paid that this does not lead to an additional burden on companies. In other words, the revenues should ideally be refunded to the payers in a way that is compatible with incentives.

**Mittelstand companies are often indirectly affected by new sustainability obligations directed at large companies**

Currently, the European Commission is introducing several additional reporting obligations for companies. Although companies with up to 500 employees or, from 2023, up to 249 employees are formally exempt from "non-financial reporting,"<sup>1</sup> the planned Non-Financial Reporting Directive only applies directly to large companies. However, they are already indirectly affected and must, for example, increasingly provide information to larger companies, who are already forced to report on the social and environmental impacts of their activities, to demonstrate their sustainability activities. In addition, in 2024, the EU will consider whether the non-financial reporting obligation should be extended to SMEs. An extension of the reporting obligations to small and medium-sized companies is therefore likely in the future.

**One example of a regulation that could potentially disadvantage Mittelstand companies concerns the regulations on financing sustainable investments.** Since this year, credit institutions have to prove the sustainability of their loan portfolios based on the so-called Green Asset Ratio (GAR).<sup>2</sup> Due to the current regulation, regional banks with a traditionally high share of SME clients may be at a competitive disadvantage. Their loan portfolios appear less "green" compared to commercial banks, with relatively large companies already subject to reporting requirements in their loan portfolios. Ultimately, regional banks may restrict lending to smaller Mittelstand companies to increase their

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<sup>1</sup> Non-Financial Reporting Directive (NFRD), implementation in Germany via the CSR Directive Implementation Act (CSR-RUG)

<sup>2</sup> The GAR puts the corporate loans granted by the credit institution, which flow into taxonomy-compliant - sustainable - economic activities, in relation to the total loan portfolio. While the "green loans" of large companies are in the numerator of the GAR, all loans, including those granted to SMEs, are included in the denominator.

GAR. It should be considered whether loans to SMEs should be excluded from the GAR calculation to avoid credit hurdles from the outset.

### **Thinking bureaucracy and climate protection together**

Less bureaucracy means more resources are available for original business activities and dealing with current challenges. Even though economic policy has prioritised the reduction of bureaucracy over the past two decades, Mittelstand companies perceive the bureaucratic burden as high. They criticise the density of regulation, question the sense of many regulations, and every fourth company deliberately does not comply with individual bureaucratic requirements (Holz et al. 2019).

However, the transformation of the (Mittelstand) economy towards a climate-friendly economy cannot proceed without further regulation. The following aspects are essential to ensure that environmental regulations will not cause procedural cost depressions and disproportionately increase the compliance burden for small enterprises:

- Existing regulations must be reviewed continuously for their effectiveness and burden intensity for Mittelstand companies and adjusted if necessary. Equally, an ex-ante consideration of the indirect effects of new national and European/supranational regulations on Mittelstand companies should take place, even if Mittelstand companies are formally excluded.
- It must be assessed whether a compliance burden for reporting obligations is appropriate. Policy makers must remember that the bureaucratic effort for Mittelstand companies is higher than for larger companies due to its fixed cost character. Therefore, the goal should be a cost burden proportional to the economic strength of Mittelstand companies to avoid competitive disadvantages compared to larger companies. Threshold values may not always be sufficient for this.
- The transparent dissemination of information on new regulations to the Mittelstand and the implementation of environmental policy measures must be made as simple as possible. It would therefore be helpful to involve representatives of Mittelstand companies in shaping legislation in the run-up to legislative initiatives.

### **Literatur**

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