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Subject: State aid SA.30515 – N 448/2010 – Finland
Amendments to the tonnage taxation aid scheme

Sir,

1. PROCEDURE

- (1) By letter of 12 October 2010 the Finnish authorities notified the envisaged amendments to the tonnage taxation scheme. Additional information was submitted by letters of 20 December 2010, 28 October 2011 and e-mails of 22 November 2010, 24 November 2011, 2 December 2011 and 9 December 2011.

2. DESCRIPTION

- (2) The Finnish Tonnage Tax Act (in force since 2003 and approved by the Commission decision in State aid case N195/2002), has not achieved its objectives.
- (3) The shipping industry found the scheme not enough attractive and inflexible. As a result, there is no single operator under the Finnish tonnage taxation (hereinafter – TT) scheme.
- (4) As the shipping industry has not opted for the TT scheme, the trends predating the scheme have continued, and the contribution of the Finnish fleet to foreign trade transport diminished:

Year	Share of Finnish registered vessels in terms of tonnes transported	Share of Finnish registered vessels in terms of passengers transported
2001	37.4%	62.3%
2009	33.3%	33.9%

Source: Finnish maritime administration

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- (5) To address the above situation, some amendments to TT Act were adopted at the end of 2009 (not yet applicable) whereas additional amendments will be adopted at the beginning of 2012. The new rules will come into force when the implementing regulation of the government will be approved. Those companies which will submit their application within the first 3 months will be able to enter into TT system retroactively, as of 1 January 2011.
- (6) **Flag requirements will be softened** under the new regime. Up to 40% of the tonnage of all of the company's vessels could be registered under non-EU flags¹ in the future.
- (7) According to amended rules, **tax base will be revised downwards** and will be set at a level similar to the one used in other Member States operating TT systems².

Tonnage	0-1000	1001 – 10 000	10001 – 25 000	above 25 001
Taxation base under TT regimes per 100 tons per day in EUR	0,90	0,70	0,50	0,20

The TT rate shall be 26% of the amount of income calculated with respect to the above-described tax base.

- (8) Instead of the previous 50%, now shipping companies will be able to **charter in with crew** 75% of tonnage³ and still be subject to TT with respect to all eligible income from its fleet (income related to maritime transportation of persons and goods and income from eligible ancillary services). Furthermore, shipping companies will even be able to charter in with crew up to 80% of tonnage in the context of an expansion of operations for a limited time period fixed by the Large Taxpayers' Office⁴.
- (9) The norm concerning the **coverage by the TT of ancillary activities** has been restated in the following wording⁵: "*Income derived from activities subject to TT refers [also] to income derived from [...] activities necessary for and closely associated with the company's activity of maritime transportation of goods and passengers, such as*
- *the transport of cargo and passengers from the port area to and from the vessel that is included in the price of the transport service,*
 - *loading and unloading and the associated temporary storage of goods,*

¹ Section 2 (3)4) of the amended TT Act as amended in 2009.

² Section 9 of the amended TT Act as amended in 2009.

³ Section 2 (3)3) of the TT Act as amended in 2009.

⁴ Proposed amendments to Section 30(2) of the TT Act.

⁵ Section 7(1)3) of the TT Act as amended in 2009.

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- *ticket sales and port terminal operations as well as administrative and insurance activities that are closely associated with the transport of passengers or goods*⁶."

Thus, revenues and expenditures directly related to TT beneficiary's eligible maritime transport activities will be covered by TT.

- (10) **Exceptionally, income from bare-boat chartering of ships could in the future be treated under the TT in the context of a short-term surplus in capacity experienced by a TT beneficiary**⁷. Notably the TT beneficiary will be able to rent out for a period of up to 3 years temporary excess capacity stemming from the fluctuation in demand for its own shipping services and count the relevant revenue under the TT system. Given the above conditions, the income from ships specifically bought for renting out purposes will not be covered by TT. In addition, the Finnish authorities will introduce the requirement that the proportion of bare-boat chartered out ships should not exceed 20% of the company's fleet under TT. Furthermore, the forthcoming amendments to TT Act will introduce the requirement that independently of bare-boat chartering out activity and chartering in of ships with crew, the TT beneficiary will always have to operate itself at least 20% of the fleet it has under TT (i.e. the share of ships chartered in with crew together with ships chartered out without crew should not exceed 80% of the fleet under TT).
- (11) The new rules also provide that, under certain conditions, **towing vessels will be accepted under the regime**⁸ provided that at least 50% of the operational time the vessel performs the transportation of goods or passengers (i.e. less than 50% of the income in the tax period should come from activities carried out in ports and from the provision of assistance to self-propelled vessels in order to reach port). Only the tugboats registered in an EU ship register could be accepted under TT.
- (12) **Introduction of the possibility to carry forward**, for the purposes of corporate income taxation, **past losses related to activities non-eligible under TT**. I.e. after the company enters the TT system, it will not have to restart corporate income taxation for its non-eligible activities from zero. Under the new rules⁹, the company's losses shall be regarded as concerning activities subject to income tax to the extent that it is obvious that the losses have been incurred with respect to activities subject to income tax. Those losses that could not be exactly allocated to the maritime and non-maritime activities would be allocated proportionally to the net assets assigned to the two types of activities¹⁰.

⁶ I.e. TT beneficiary will account under TT *inter alia* the cost related to ticket sales, insuring cargo, etc. as well as corresponding additional receipts from the clients (the latter shouldn't necessarily be separately invoiced).

⁷ Proposed amendments to Section 8.(1)4) of the TT Act.

⁸ Proposed amendments to Section 8(3) of the TT Act.

⁹ Section 6(2) and 6(3) of the TT act as amended in 2009.

¹⁰ I.e. the same approach will be used as the one chosen with respect to over-depreciation.

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- (13) With the proposed amendments, **a maritime transport company within a group would be able to opt for the TT scheme** independently of the taxation regime applicable to the other maritime transport companies of the same group, provided it engages in either passenger or freight transport as separate business entity and under separate business management¹¹. For example, in the future, groups would be able to choose to leave all passenger transport outside the TT scheme¹². The context underlying this new provision is that very often passenger transportation activities are loss-making and relevant losses are covered only thanks to the sale of goods on board of ships. Application of TT regime to transportation revenues of such companies would place such companies in worse situation than under the normal corporate income taxation regime. All the earlier approved ring-fencing measures¹³ will stay in force to exclude abuses. These *inter alia* include the application of market conditions to the relations between tonnage tax companies and other companies of the same group. The rule on thick capitalisation as approved by the Commission in 2003¹⁴ would continue to apply as well. Companies opting for tonnage tax will be required to do so for a minimum period of ten years. They will not be able to treat part of their eligible ships under TT and another part under the normal corporate income taxation. All the eligible income and expenditures from eligible ships of the TT beneficiary would have to be covered by TT (the so called "all or nothing rule").
- (14) The amended TT regime also clarifies the **rules on the issue of group subsidies in a situation of a company under TT regime**¹⁵. In a situation when the eligible company provides a group subsidy to another company of the group, the amount of this subsidy is capped at the level of profits of the contributing company subject to corporate income taxation (i.e. profits from non-eligible activities). Any group subsidy received by a company subject to TT shall always be regarded as its income from non-eligible activities and subject to corporate income taxation.
- (15) Under the amended rules, **dividends of shipping companies under TT will** become subject to general regulations governing dividends (under the old rules the dividends were always taxed, even in cases when the recipient company was subject to corporate income taxation; this, in turn, often nullified the benefit of TT). In other words, in the future dividends would be taxed as if the company was liable for normal income tax. This would

¹¹ Section 3(3) of the TT Act as amended in 2009.

¹² It should be noted that even if it is decided to enter passenger shipping activities under TT, sales of goods automatically fall under the corporate income taxation.

¹³ See Commission's 2003 decision in case N195/2002.

¹⁴ The rule on 'thick capitalisation' limits tax optimisation possibilities within a group of companies where at least one company is subject to TT and at least one - subject to normal corporate income taxation. Notably, it ensures that a group of companies cannot predominantly finance their activities under the TT rules with shareholders' equity, while activities in other companies taxed under the standard rules are financed with borrowed capital where the interest expenditure would be tax deductible.

¹⁵ Section 23 of amended TT act, explaining how the Act on Group Subsidies in Taxation (Laki konserniavustuksesta verotuksessa, 825/1986) would apply to the companies under tonnage taxation for its eligible activities.

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make the tax relief a final measure instead of just deferring taxation as is the case under current legislation.

- (16) **Rules on the over-depreciated ships being transferred to the TT system will be restated¹⁶.** Pursuant to the Finnish tax legislation, any Finnish company can depreciate each year up to 25% of the remaining value of the pool of machinery and other equipment, including ships¹⁷. This implies that part of assets (notably ships) may be over-depreciated as of the entry into TT. Upon the shipping company's entry into TT, a capital gain value is fixed for each ship entering the TT system¹⁸. If the previously over-depreciated ship is sold before full 9 years being spent in the TT system, the tax administration will establish the capital gain at the moment of the sale (the difference between the ship's sales value and the tax value at the moment of the entry into TT). The taxable amount will, however, be capped at the level of the capital gain as at the moment of the entry into TT system. In addition, the maximum value subject to the capital gains taxation will every year be decreased by 1/9¹⁹ under certain conditions²⁰. The capital gain value calculated according to the principles described above will be taxed 3 years after the moment of the sale, if the relevant amount is not reinvested in ships²¹. The above-mentioned tax relief with respect to the earlier over-depreciated ships will only be provided within the limits of the aid ceiling stipulated in Chapter 11 of the Maritime guidelines.
- (17) All the other conditions of the scheme as approved by the Commission in 2003 will remain applicable. Inter alia the rules to prevent the so called "thick capitalisation" will stay in force. The relaxation of the thick capitalisation provisions initially planned on the basis of 2009 amendments to TT Act will not be implemented as the new amendments to TT Act will re-introduce the initial wording on the "thick capitalisation". Also aid ceiling requirements would stay in force.

¹⁶ Proposed amendments to Section 15 of TT Act.

¹⁷ This rule however doesn't apply to the ships acquired in the year preceding the entry into TT: only the change in the market value between the acquisition date and the date of the entry into TT can be depreciated.

¹⁸ The value of capital gain for a specific ship is determined as the difference between the market value of ship and the ship's proportion of the remaining value of the equipment and machinery's pool under fiscal rules (for tax purposes, equipment and machinery are depreciated in Finland on a pool basis).

¹⁹ I.e. if the ship is sold 5 years after the entry into TT system, the maximum taxable amount will be $1 - 5/9 = 4/9$ of the ship's over-depreciation value as established at the moment of the entry into TT.

²⁰ The value of the capital gain related to the ship depreciation during the 5 years preceding the entry into TT can be gradually "written-off" (1/9 reduction every year) only if it does not concern ships bought during the last year preceding the entry into TT and did not reduce taxation of non-maritime activities during the last 5 years preceding the entry into TT.

²¹ If the TT beneficiary reinvests capital gains in the new ships, the latter have to be kept until the end of the 9th year in TT or replaced again in the case of the sale. Otherwise, the capital gain will be taxed.

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3. ASSESSMENT OF THE MEASURE

3.1. *Existence of aid within the meaning of Article 107(1) of the TFEU*

- (18) The notification concerns a State aid scheme, a predecessor of which has been authorized by the Commission²². The current modification of the existing scheme does not alter the Commission's assessment that the scheme as well as its modification constitutes State aid within the meaning of Article 107 (1) TFEU.

3.2. *Compatibility assessment*

- (19) Under Article 107(3)(c) of the TFEU, aid to facilitate the development of certain economic activities may be considered compatible with the internal market, where such aid does not adversely affect trading conditions to an extent contrary to the common interest, and thus provides a possible basis for an exemption from the general prohibition of State aid. The Commission considers Article 107(3)(c) of the TFEU to be the appropriate legal basis applicable to the notified scheme.
- (20) The appropriate legal basis for compatibility assessment is Article 107(3)(c) TFEU, implemented by the Guidelines on State aid to maritime transport²³ (hereinafter "the Maritime Guidelines") The Maritime Guidelines determine the conditions under which Member States are allowed to set up certain State aid schemes to support their maritime transport industry in the pursuit of general objectives, such as:
- improving a safe, efficient, secure and environment friendly maritime transport;
 - encouraging the flagging or re-flagging to Member States' registers;
 - contributing to the consolidation of the maritime cluster established in the Member States while maintaining an overall competitive fleet on world markets;
 - maintaining and improving maritime know-how and protecting and promoting employment for EU/EEA seafarers; and
 - contributing to the promotion of new services in the field of short sea shipping following the White Paper on Community transport policy.
- (21) Section 3.1 of the Maritime Guidelines specifically mentions tonnage tax schemes as examples of fiscal measures that "*have been shown to safeguard high quality employment in the on-shore maritime sector*", and may thus be considered compatible with the internal market“.

²² State aid case N195/2002.

²³ OJ C 13, 17.1.2004, p. 3.

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- (22) However, the Maritime Guidelines lay down certain criteria, which such schemes must meet to be considered compatible with the internal market.
- (23) The Commission will thus assess below whether each modification of the existing aid scheme fulfils the criteria established by the Maritime Guidelines and the Commission's decision making practice.
- (24) Regarding the **new rules on the flag requirement** the Commission notes that even after relaxation of the rules, that TT beneficiaries will be obliged to have at least 60% of their tonnage registered in the EU. Therefore, the Commission is of the opinion that this modification is in compliance with the requirements of the Chapter 3.1 of Maritime guidelines²⁴.
- (25) **Concerning the new rules on tax base under the TT system**, the Commission notes that according to the amended rules, the tax base will be revised downwards and will be set at a level similar to the level used in other Member States operating TT systems:

Tonnage	Taxation base under TT regimes per 100 tons per day in euro					
	FI	NL ²⁵	DE ²⁶	DK ²⁷	UK ²⁸	ES ²⁹
0-1000	0,90	0,908	0,92	0,94	0,97	0,90
Between 1 001-10 000	0,70	0,681	0,69	0,67	0,73	0,70
Between 10 001-25 000	0,50	0,454	0,46	0,40	0,48	0,40
Between 25 001-50 000	0,20	0,227	0,23	0,27	0,24	0,20
Above 50001	0,20	0,050	0,23	0,27	0,24	0,20

The TT rate shall be 26% of the amount of income calculated with respect to the above-described

Therefore, the principle laid down in Chapter 3.1 of the Maritime guidelines that the Commission should approve only schemes giving rise to a tax-load for the same tonnage fairly in line with the schemes already approved is complied with.

- (26) **As regards the the new maximum permissible limit with respect to the charter in with crew to 75% of tonnage (80% in the context of expansion of operations**, the Commission notes that chartering in with crew is used for the purpose of acquiring a 'critical mass' of ships and better market coverage, allowing shipping companies to become a factor in a given market. It allows a shipping company to serve clients with regards to transport of large cargo amounts, where a given shipping company does not

²⁴ Commission communication C(2004) 43 — Community guidelines on State aid to maritime transport (OJ C 13 of 17.1.2004).

²⁵ Commission decision in case N 738/95 as amended by the decision in case N457/2008.

²⁶ Commission decision in case N396/1998.

²⁷ Commission decision in case N563/2001.

²⁸ Commission decision in case N790/99.

²⁹ Commission decision in case N736/2001.

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have sufficient capacity on their own ships (and could thus not accept the contract at all). In this manner time charter contributes to employment on board the shipping companies' own ships. Chartering in with crew makes possible to penetrate new markets without running the risk related to immediate acquisition of new tonnage for that purpose.

- (27) The Guidelines themselves do not mention any limitation to the inclusion of ships chartered in with crew under tonnage tax schemes. The companies which charter in such ships would still be considered as providers of maritime transport services even if they use for this purpose ships and personnel of other companies. Therefore such companies would normally be covered by the scope of the Maritime guidelines.
- (28) In past decisions, the Commission has authorised schemes covering companies with a ratio between tonnage of owned vessels and tonnage of vessels chartered-in with crew of up to 3:1³⁰, 4:1³¹ or, under very strict conditions 10:1³². That ratio has been intended to avoid situations where tonnage tax companies eventually become pure maritime brokers, without any responsibility for the crew management and the technical management of vessels that they operate. If tonnage tax companies were to operate only vessels chartered-in with crew, they would lose their know-how in terms of the crew management and technical management of vessels, in contradiction with one of the objectives set out in section 2.2 first subparagraph fourth indent of the Guidelines, namely "maintaining and improving maritime know-how".
- (29) Limitation imposed on the Commission with respect to ships chartered in with crew has been meant also to make it easier to keep on-shore activities related to the vessels under TT within the Community/EEA. Here the objective pursued is to contribute "to the consolidation of the maritime cluster established in the Member States" in line with section 2.2 first subparagraph third indent of the Guidelines.
- (30) As the Finnish authorities impose the necessary limitation on chartering in with crew, the Commission therefore considers that the relevant changes to the Finnish TT Act are in line with the Maritime guidelines.
- (31) The **revised list of ancillary activities** as described in paragraph 9 of the present decision is in line with the Guidelines as interpreted in the Commission's decision-making practice concerning TT schemes³³. The relevant activities are indeed closely related, ancillary to maritime transport. Very often, they are even billed in a single invoice by the maritime transport companies to their clients. The new legislative provisions indeed ensure that companies exercising the relevant activities as main activities would not benefit from the TT. Therefore, the Commission accepts that the relevant amendments to the TT Act are compatible with the Maritime guidelines.

³⁰ See e.g. Commission Decision No C20/2003.

³¹ See e.g. Commission decision in case N 563/2001.

³² See e.g. Commission's decision in case C 2/2008.

³³ See e.g. point 26 of the Commission decision in case N 37/2010.

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- (32) As regards the introduction of the conditional possibility to include revenues from bare-boat chartering out of ships on a temporary basis (up to 3 years) under TT, the Commission considers it justified to offer limited flexibility for TT beneficiaries in situations of short-term overcapacity in their own shipping activity. In this context, it should be mentioned that the administrative burden of taking ship out of TT/ reintroducing it back into TT may be disproportionate for short-term contracts compared to the potential tax gain. The Commission notes that the Finnish authorities follow the same principles as those applied in the Irish TT³⁴. Notably, the TT beneficiary will be able to benefit from the relevant possibility only exceptionally, in the context of temporary excess capacity stemming from the fluctuation in demand for its own shipping services and the income from ships specifically bought for renting out purposes will not be covered. In addition, the Commission notes that the Finnish authorities will introduce the requirement that the proportion of bare-boat chartered out ships should not exceed 20% of the company's fleet under TT. Furthermore, independently of bare-boat chartering out activity and chartering in of ships with crew TT beneficiary will always have to operate itself at least 20% of the fleet it has under TT (i.e. the share of ships chartered in with crew together with ships chartered out without crew should not exceed 80% of the fleet under TT). Therefore, the relevant option will be available only to genuine shipping companies performing "maritime transport" activities³⁵ i.e. to the "transport of goods and persons by sea" and eligible for support under the Guidelines. The Commission thus concludes that the proposed changes are in line with the Maritime guidelines, in particular with their objective to encourage flagging and reflagging to Member States' registers.
- (33) The Commission notes that in introducing **conditional possibility to cover revenues from towage vessels by TT system** Finland strictly follows the wording of the Maritime Guidelines. Namely, towing vessels will be accepted under the regime provided at least 50% of the operational time the vessel performs the transportation of goods or passengers (i.e. less than 50% of the income in the tax period should come from activities carried out in ports and from the provision of assistance to self-propelled vessels in order to reach port). Only the tugboats registered in an EU ship register could be accepted under the TT. Therefore, the Commission considers that the proposed change is in compliance with the Maritime Guidelines.
- (34) With regards to the **introduction of the possibility to carry forward under corporate income taxation system losses incurred with respect to non-eligible activities** the Commission notes that the Maritime Guidelines only prohibit that losses occurred while under TT cannot be used to reduce corporate income tax bill for non-eligible activities. As the introduced modification will not have such effects it is compliant with the Maritime guidelines.

³⁴ See e.g. Commission's decision in the Irish TT case (N504/2002).

³⁵ As defined in Regulation (EEC) No 4055/86 and in Regulation (EEC) No 3577/92.

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- (35) As to the newly introduced possibility for a **maritime transport company within a group would be able to opt for the TT scheme independently of the taxation regime applicable to the other maritime transport companies of the same group**³⁶, the Commission notes that indeed such possibility appears justified. Very often passenger transportation activities are loss making and relevant losses are covered only thanks to the sale of goods on board of ships. Application of TT regime to transportation revenues of such companies would place such companies in worse situation than under the normal corporate income taxation regime and would be at odds with the goals of the Maritime guidelines. The Commission also notes that the set of ring-fencing measures as mentioned in paragraph 12 of the present decision and further detailed in the Commission decision in case N195/2002 will be in force to limit abuses. Therefore, the Commission considers that the proposed change is in compliance with the Maritime Guidelines.
- (36) **The Commission considers that the reformulated rules on the issue of group subsidies in a situation of a company under TT regime** respect the ring-fencing principles as set in the Maritime guidelines. Any group subsidy received by a company subject to TT shall always be regarded as its income from non-eligible activities and subject to corporate income taxation. In a situation when the eligible company provides a group subsidy to another company of the group, the amount of this subsidy is capped at the level of profits of the contributing company subject to corporate income taxation (i.e. profits from non-eligible activities). Therefore, the Commission considers that the proposed new wording of the rules on group subsidies is in compliance with the Maritime Guidelines.
- (37) The Commission considers as justified the **repeal of the previous rules according to which dividends were always taxed, even in cases when the recipient company was subject to corporate income taxation (measure which in many cases nullified the benefit of TT)**. This measure is clearly necessary to make the Finnish TT system functional and is in line with the approach chosen in other Member States having TT systems. Therefore, the Commission considers that the proposed change is in line with the Maritime guidelines.
- (38) The Commission notes that **the rules proposed by the Finnish authorities with respect to the earlier over-depreciated ships of the genuine shipping companies**³⁷ **entering TT** are comparable to those already accepted by the Commission³⁸. The way these rules are formulated discourages ship acquisition transactions ahead of entry into TT with the sole aim of obtaining tax gains, while allowing smooth integration into TT system (if companies opting for TT would have to settle immediately the hidden tax liabilities they had upon the entry into TT, at least in the short-term, they would be in a less

³⁶ provided it engages in either passenger or freight transport as separate business entity and under separate business management.

³⁷ In line with the Finnish TT Act provisions, only companies performing transportation of goods and passengers by sea can enter TT system (i.e. intermediary companies, such as ship lessors described in the Commission's decision on the Spanish tax lease system – SA.21233, cannot enter TT).

³⁸ See e.g. Commission decision in the UK tonnage tax case (N790/99).

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advantageous situation than staying under the normal taxation rules). Chapter 3.1. of the Maritime guidelines "Fiscal treatment of ship-owning companies" does not limit Member States' choice as to the instruments used to de-tax maritime companies profits provided other requirements of the Maritime guidelines are respected, including the aid ceiling stipulated in Chapter 11 of the Maritime Guidelines. As this is the case, the Commission considers that the proposed change would be in compliance with the Maritime guidelines.

- (39) All other conditions approved by the Commission in its 2003 decision remain applicable.
- (40) It should be noted that chapter 13 of the Guidelines specifies that the Guidelines will be reviewed within seven years of their date of application, and this review is currently underway. The notified modifications will thus cover a period after this review has been carried out. Consequently, should the Guidelines be modified following this review with respect to their provisions covering the notified modifications, the Commission may request appropriate measures in order to align them with the new provisions of the Guidelines.

Conclusion

- (41) In light of the foregoing considerations, and the considerations already developed in the previous Commission decision approving the initial TT scheme, the Commission concludes that the Finnish TT scheme as amended is in line with the Maritime guidelines and with Article 107(3)(c) TFEU.

4. DECISION

The Commission has accordingly decided:

- to consider the notified amendments of the existing aid scheme to be compatible with the Treaty on the Functioning of the European Union.

If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site: http://ec.europa.eu/eu_law/state_aids/state_aids_texts_fi.htm

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Yours faithfully,
For the Commission

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