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Subject: State aid SA. 35401 (2013/N) – Finland
Tax deferral of taxable capital income for Business Angels Scheme

Dear Sir,

1. PROCEDURE

(1) By letter dated 12 September 2012, registered the same day under number SA. 35401 (2012/PN), the Finnish authorities pre-notified to the Commission the above-mentioned measure. On 18 September 2012, a meeting concerning the measure took place between the Commission and the Finnish authorities. On 2 October 2012, the Finnish authorities forwarded to the Commission additional information. The Commission asked the Finnish authorities to clarify certain issues concerning the measure by emails dated 4, 5, 11 and 16 October 2012 as well as by email dated 18 January 2013. The Finnish authorities replied to those emails on 4 and 10 October and provided additional information concerning the measure on 19 December 2012 and on 8, 9 and 30 January 2013.

(2) By the letter dated 1 February 2013, registered the same day under number SA. 35401 (2013/N), the Finnish authorities notified the measure in accordance with Article 108(3) of the Treaty on the Functioning of the European Union[1] ("TFEU") for assessment under Article 107 (1) of the TFEU, in light of the Community guidelines on State aid to

[1] OJ L 115, 09.5.2008, p. 92.

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promote risk capital investments in small and medium-sized enterprises[2] ("RCG"). Additional information was provided by the Finnish authorities on 4 February 2013.

2. DESCRIPTION OF THE MEASURE

2.1. Objective

(3) In order to address an equity gap for small enterprises in Finland, the measure provides a tax incentive to private individuals (natural persons) who invest equity directly into target enterprises established in Finland. The aim of the measure is to support new innovative businesses.

2.2. Legal basis, granting authority, duration and budget

(4) The legal basis of the measure is the Act on Risk Capital Tax Deferral (*Laki sijoitustoiminnan veronhuojennuksesta verovuosina 2013 - 2015 (993/2012 vp*).[3]

(5) The aid granting authority is the Ministry of Finance of Finland. Aid is awarded automatically once the qualifying objective criteria are fulfilled. There is no discretion available to the awarding authority in the granting of aid.

(6) The duration of the measure is three years. The measure will remain in force until 31 December 2015. The Finnish authorities committed to apply the necessary appropriate measures after the expiry of the current RCG. The Finnish authorities will not put the measure into effect until the Commission has taken a decision authorising it.

(7) The total budget in the form of tax revenues forgone is estimated at EUR 12 million per year during the years 2013 – 2015. According to the Finnish authorities, the recapture of the provided tax relief during the 15 following years would bring back about 80 % of the forgone tax revenues.

2.3. Eligible investments

(8) Investments eligible under the measure are those made exclusively in the form of equity through the acquisition of newly issued shares in the target enterprises (100 % equity investments). The investments exclude replacement capital and buy-outs.

(9) There is no minimum holding period required for an investor to hold the shares of the target enterprise. However, according to the Finish authorities, an exit will usually happen 8 to 10 years from the date of the investment[4].

(10) The eligible investments are limited to EUR 2.5 million per target enterprise over a period of 12 months and must fulfil all requirements set out in the present decision.

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2 OJ C 194, 18.8.2006, p. 2-21.

3 The proposal was adopted by the Finnish Parliament on 18 December 2012 and confirmed by the President of the Republic on 28 December 2012. The Act will be promulgated by a separate statute after the Commission has approved the measure.

4 The Finnish Business Angels Network (Fiban) conducts an annual study on the investment policies of its members. The latest study dates from 2011 and confirms that the estimated holding period of investments was around 8 and up to 9 years in duration. https://www.fiban.org/

2.4. Form of aid

(11) Under the measure, the eligible investors will obtain a tax relief of 50 % of the amount of their investment in the newly issues shares of the target enterprises from their capital income ("deduction"). The deduction from capital income at the moment of the investment will be considered capital income in full upon the sale of the shares ("withdrawal of the deduction"). The Finnish authorities therefore consider this tax incentive as a tax deferral.

2.4.1. Current legal framework in Finland

(12) In accordance with the current legal framework in Finland, the capital gains derived from the shares are regarded as investment income in all cases. The taxable capital gain is calculated by deducting the acquisition costs from the net sales price of the shares[5]. The capital gains tax rate is 30 %. If the amount of capital income exceeds EUR 50 000, the capital gains tax rate is 32 %.

2.4.2. Tax deferral

(13) As a result of the measure, private individuals may deduct 50 % of the amount of the investment into the new share capital of the target enterprise from their net capital income from other sources (rental income, dividends, interest, capital gains, etc.). The investment is considered to be realised when the share issue has been registered.

(14) The deduction must be at least EUR 5 000 and cannot exceed EUR 75 000[6]. The investor may invest in several target enterprises, but the deduction cannot exceed EUR 150 000[7] per tax year in such cases.

(15) The same target enterprise may receive investments from several investors. In such a case, however, the tax deduction applies only to the investments up to the amount of EUR 2.5 million per target enterprise over a period of 12 months.

(16) The deduction can be taken during tax years 2013 – 2015. If the deduction cannot be taken in full in the year of the investment, the remainder can be deducted from capital income within three subsequent years.

(17) The deduction will be withdrawn upon the sale of the shares. The amount of the initial deduction granted to investors (i.e. 50 % of the amount of investment into the new share capital of the target enterprise) will be subtracted from the amount of the acquisition costs of the shares. Subsequently, the difference will be subtracted from the net sales price of the shares[8].

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5 I.e. the sales price minus the acquisition costs; if the acquisition costs are less than 20 % of the sales prices, a minimum deduction of 20 % is applied to the sales price instead of the real costs.

6 I.e. the amount of the investment must therefore be between EUR 10 000 and 150 000 to qualify under the measure.

7 I.e. the total amount of those investments cannot exceed EUR 300 000.

8 For example:
Year 2013 - investment into the newly issued shares in the amount of EUR 150 000.
- amount of the deduction from the capital income (i.e. 50% of the investment) = EUR 75 000
Year 2014 – deduction of EUR 65 000

(18) In this manner, the deduction granted at the moment of acquisition is withdrawn as a result of the higher taxation at the moment of the sale of the shares. Consequently, if the sale of the shares results in a loss, that loss will be smaller than without the withdrawal of the deduction.

(19) The deduction will also be withdrawn where: (i) the shares are donated or inherited or otherwise disposed of without remuneration; (ii) the target enterprise ceases its business activities or (iii) the investor moves out of Finland. In the last case, the payment of the tax incurring as a result of the withdrawal of the deduction is deferred until the investor sells the shares or moves out of the European Economic Area (EEA).

2.5. Eligible investors

(20) All private individuals (natural persons) who are generally liable for taxation in Finland are eligible for the tax deferral under the measure. Investments will be made directly into the target enterprises.

(21) The eligible investors shall not be connected with the target enterprises receiving investments.

2.6. Target enterprises

(22) The measure is targeted exclusively at small enterprises[9], falling within the Community SME-definition[10] and incorporated as limited liability companies in Finland (*Osakeyhtiö*) or legally equivalent capital companies in the EEA, which are subject to income tax (the "target enterprises"). The target enterprises must have been established less than six years before the investment.

(23) Foreign companies with a permanent establishment in Finland are also eligible under the measure.

(24) To be eligible under the measure, the target enterprises may not be publicly listed enterprises[11].

Year 2015 – deduction of EUR 10 000

Year 2018 – sale of the shares at the net price of EUR 170 000

Under the current legal framework in Finland, the taxable capital gain is the net sales price minus the acquisition costs of the shares (EUR 170 000 – EUR 150 000 = EUR 20 000). The taxable capital gain therefore equals EUR 20 000.

If the deduction was granted to the investor in years 2015 and 2016, the capital gain is corrected with the amount of the deduction, i.e. in EUR 75 000 (the sales price minus the acquisition costs reduced by the amount of the actual deduction: EUR 170 000 – [EUR 150 000 – EUR 75 000] = EUR 95 000). Therefore, the taxable capital gain after the sale of the shares will amount to EUR 95 000, that is EUR 75 000 more than according to the standard rules.

9 "Small enterprise" refers to an enterprise which employs at most 50 people and which has a maximum turnover of EUR 10 million or a maximum balance sheet of EUR 10 million.

10 The beneficiaries of the measure are undertakings qualifying as SMEs within the meaning of the Commission Regulation (EC) No 800/2008 of 6 August 2008 declaring certain categories of aid compatible with the common market in application of Articles 87 and 88 of the Treaty (General block exemption Regulation); OJ L 214, 9.8.2008, p.3 and the applicable Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises; OJ L 124, 20.5.2003, p. 36-41.

11 As defined in the Finish Income Tax Act (*Tuloverolaki 30.12.1992/1535*), section Section 33a.

(25) According to the Finish authorities, the measure is not sector specific. The target enterprises should not, however, be engaged in banking, insurance, real estate investments, investments in stock markets and farming.

(26) Investments in enterprises in the shipbuilding[12], coal[13] and steel industry[14] are also excluded. The Finnish authorities confirmed that investments under the measure will not support export-related activities and investments will not be contingent upon the use of domestic preference to imported goods.

(27) Enterprises which find themselves in financial difficulties within the meaning of the Community Guidelines on State aid for Rescuing and Restructuring Firms in Difficulty[15] are also not eligible for investments under the measure.

(28) To be eligible under the measure, the target enterprises may not be established as result of a merger, diffusion or transfer of assets as defined in Sections 52 – 52 d of the Business Income Act[16].

(29) The Finnish authorities confirmed that the definition of seed, start-up and expansion capital for the purposes of the measure will be in accordance with the Commission's definition of these terms, as set out in section 2.2 (e), (f) and (h) of the RCG, namely:

§ Seed stage financing refers to financing provided to study, assess and develop an initial concept, preceding the start-up phase.

§ Start-up capital refers to financing provided to companies, which have not sold their product or service commercially and are not yet generating a profit, for product development and initial marketing.

§ Expansion capital refers to financing provided for the growth and expansion of a company, which may or may not break even or trade profitably, for the purposes of increasing production capacity, market or product development, or the provision of additional working capital.

(30) According to the Finnish authorities, the target enterprises shall formulate a detailed business plan. The business plan shall contain details of the product, sales and profitability development and establish the *ex-ante* viability of the project, illustrating its profit-driven character. Together with the investor, the target enterprises shall draw up an exit strategy, indicating the time and the means of an exit.

2.7. Cumulation with other aid

(31) The Finnish authorities undertake to reduce the relevant aid ceilings or maximum eligible amounts by 50 % in general and by 20 % for target enterprises located in

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12 As defined in the Framework on State aid to Shipbuilding, OJ C 317, 30.12.2003 p. 11-14.

13 High, medium and low grade category A and B within the meaning of the internal codification system for coal laid down by the UN Economic Commission for Europe.

14 As defined in Annex I of the Guidelines on National Regional Aid for 2007-2013, OJ C 54, 4.3.2006, p. 13-45.

15 OJ C 244, 1.10.2004, p. 2

16 The Business Income Tax Act (*Laki elinkeinotulon verottamisesta 24.6.1968/360*).

assisted areas during the first three years of the first risk capital investment and up to the total amount received, where the capital provided to a target enterprise under this measure is used to finance initial investment or other costs eligible for aid under other block exemption regulations, guidelines, frameworks, or other State aid documents.

(32) This reduction does not apply to aid intensities provided for in the Community Framework for State aid for Research and Development[17] or any successor framework or block exemption regulation in this field.

2.8. Monitoring and reporting

(33) The Finnish authorities undertake to comply with the reporting and monitoring requirements set out in point 7.1 of the RCG and, in particular, to submit to the Commission annual reports containing a summary table with a breakdown of the investments made under the measure, including a list of all the beneficiaries of risk capital measures.

(34) The measure will not be applied before its full text has been published on the internet. The Finnish authorities communicated an internet address where the measure will be published (http://www.finlex.fi).

(35) The Finnish authorities undertake to maintain for at least ten years detailed records regarding the granting of aid for the risk capital measure, containing all information necessary to establish that the conditions laid down in the RCG have been observed, notably as regards the size of the tranche, the size of the company, the development stage of the company (seed, start-up or expansion), its sector of activity (preferably at four digit level of the NACE classification), as well as information on the other criteria mentioned in the RCG.

3. ASSESSMENT OF PRESENCE OF STATE AID

(36) The Commission has assessed the notified measure under Article 107(1) TFEU and, in particular, in light of the RCG, which provide for the specific requirements in the area of State aid to promote risk capital investments in SME's.

(37) In order for a risk capital measure to fall within the scope of Article 107(1) TFEU, four cumulative criteria must be met:

- § the measure must involve the use of State resources;
- § the measure must confer an advantage on its recipients;
- § that advantage must be selective in that it is limited to certain undertakings;
- § the measure must distort or threaten to distort competition and be likely to affect trade between Member States.

[17] OJ C 323, 30.12.2006, p. 1.

(38) In line with section 3.2 of the RGC, in its assessment of whether a risk capital measure constitutes State aid, the Commission will consider the possibility that the measure may confer aid on at least three different levels:

- § aid to investors;
- § aid to an investment fund, investment vehicle and/or its manager;
- § aid to the enterprises in which investment is made.

3.1. State aid to investors

(39) Article 107(1) TFEU only applies where an advantage is conferred on an undertaking. In the present case, the eligible investors which can benefit from the measure are private individuals (i.e. natural persons) generally liable for taxation in Finland (see recital **(20)** above) and not undertakings. Article 107(1) TFEU is not therefore applicable at this level of the risk capital measure.

(40) The Commission therefore concludes that there is no State aid within the meaning of Article 107(1) TFEU at the level of investors.

3.2. State aid to target enterprises

(41) By granting a tax deferral to private individuals on the condition that they invest directly into target enterprises, those enterprises receive investments in amounts and on conditions different from what they would have been able to obtain under normal market conditions. The measure therefore facilitates the provision of risk capital to the target enterprises which would otherwise not be available, or at least not to the same extent, in the absence of the measure[18]. The measure therefore confers an advantage on the target enterprises.

(42) Moreover, since the measure involves a tax deferral it should be considered to constitute State resources as it involves foregone tax revenues for the Finnish State. The measure should also be considered selective as only investments in certain qualifying SMEs are eligible for the deduction (see recital **(22)** above). Finally, since it cannot be excluded that the target enterprises are active in intra-EU trade, the measure should be considered likely to distort or threaten to distort competition and likely to affect trade between Member States.

(43) Since all cumulative criteria of Article 107(1) TFEU are fulfilled, the Commission concludes that there is State aid within the meaning of that provision at the level of the target enterprises in which the eligible investments are made.

3.3. Lawfulness of the aid

(44) By notifying the measure prior to its implementation, the Finnish authorities have respected Article 108(3) TFEU.

[18] Case C-156/98 *Germany v Commission* [2000] ECR I-6857.

4. COMPATIBILITY ASSESSMENT

4.1. Criteria for assessing the compatibility of the measure

(45) Considering that the measure constitutes State aid at the level of targeted enterprises, the Commission must examine whether this aid is compatible with the internal market. Article 107(3)(c) TFEU provides that aid to facilitate the development of certain economic activities may be considered to be compatible with the internal market where such aid does not adversely affect trading conditions to an extent contrary to the common interest. Since the measure concerns the provision of risk capital to small enterprises, the RCG should be applied to this compatibility assessment.

(46) Section 4.2 of the RCG lists the types of risk capital measures the Commission believes are capable of encouraging market investors to provide risk capital to target enterprises and are likely to result in investment decisions being taken on a commercial (that is, a profit-driven) basis, among which point 4.2(d) mentions fiscal incentives to investors to undertake risk capital investment. Given that the measure provides a fiscal incentive to private individuals investing directly into the target enterprises, the measure falls within the scope of the RCG.

(47) Section 2.1 of the RCG requires the exclusion of aid to enterprises in difficulty, and to enterprises in the shipbuilding, coal and steel industry. Furthermore, the RCG do not apply to aid to export-related activities, namely aid directly linked to the quantities exported, to the establishment and operation of a distribution network or to other current expenditure linked to the export activity, as well as aid contingent upon the use of domestic in preference to imported goods. The measure complies with section 2.1 of the RCG in this respect (see recitals **(26)** and **(27)** above).

(48) The measure also complies with point 2.2(b) of the RCG, which defines private equity investments as investments in companies not listed on a stock market (see recital **(24)** above).

(49) The investments made under the measure concern newly issued shares exclusively, which excludes replacement capital and buy-outs (see recital **(8)** above) so that the measure also complies with the definition of venture capital under point 2.2(i) of the RCG and private equity under point 2.2(b) of the RCG.

4.2. Assessment under Section 4.3 of the RCG

(50) The Commission will declare a risk capital measure compatible under Article 107(3)(c) TFEU only if it concludes that the aid measure leads to an increased provision of risk capital without adversely affecting trading conditions to an extent contrary to the common interest. To determine this, the Commission applies a balancing test, set out in point 1.3 of the RCG, which examines the potential positive effects of the measure in reaching an objective of common interest against its potential negative effects in terms of distortion of competition and trade. The Commission will consider that the incentive effect, the necessity and proportionality of aid, required as part of this balancing test, are present in a risk capital measure and that the overall balance of the measure is positive where all the conditions of Section 4.3 of the RCG are met.

4.2.1. Maximum level of investment tranches

(51) Point 4.3.1 of the RCG stipulates that tranches of finance, whether wholly or partially financed through State aid, must not exceed EUR 2.5 million per SME over each period of 12 months. As pointed out in recital (**10**) above, the maximum annual investment tranche per target SME will be EUR 2.5 million. Therefore, the condition of point 4.3.1 of the RCG is met.

4.2.2. Restriction to seed, start-up and expansion financing

(52) According to point 4.3.2 of the RCG, the risk capital measure must be restricted to provide financing up to the expansion stage for small enterprises, or for medium-sized enterprises located in assisted areas. It must be restricted to provide financing up to the start-up stage for medium-sized enterprises located in non-assisted areas.

(53) As pointed out in recital **(22)** above, the measure is targeted exclusively at small enterprises, falling within the Community SME-definition, up to their expansion stage. The measure does not apply to medium-sized enterprises. The definition of seed, start-up and expansion capital for the purposes of the measure, as set out in recital (**29**), complies with point 2.2 of the RCG. Therefore, the conditions of point 4.3.2 of the RCG are met.

4.2.3. Prevalence of equity and quasi-equity investment instruments

(54) Point 4.3.3 of the RCG requires that the risk capital measure must provide at least 70 % of its total budget in the form of equity and quasi-equity investment instruments into target SMEs. As pointed out in recital **(8)**, considering that 100 % of the investments made by investors into the target enterprises will be made in the form of equity, the measure complies with point 4.3.3 of the RCG.

4.2.4. Participation by private investors

(55) Point 4.3.4 of the RCG stipulates that at least 30 % of the funding of the investments made inside assisted areas, and respectively 50 % in other areas, must be provided by private investors. Under the measure, the total amount of funding of the investments in the target enterprises is provided by private investors. Therefore, the conditions of point 4.3.4 of the RCG are met.

4.2.5. Profit-driven character of the investment decisions

(56) Point 4.3.5 of the RCG provides cumulative criteria to assess if investment decisions under the measure are profit-driven.

(57) Firstly, a significant involvement of private investors providing investments on a commercial basis, directly or indirectly, into the equity of the target enterprises must be present. As regards the present measure, all of the capital delivered through the measure is provided by private investors investing directly into the target enterprises (see recital **(20)** above). The State is not involved in investment decision-making, apart from setting out the rules for the purpose of tax incentives under the measure (see recital **(5)** above). Therefore, the condition of point 4.3.5(a) of the RCG is met.

(58) Secondly, pursuant to point 4.3.5(b) of the RCG, a detailed business plan for each investment, establishing a project's *ex-ante* viability, must exist. As indicated in recital **(30)**, each target enterprise is required to have a business plan, containing details of the product, sales and profitability development and establishing the *ex-ante* viability of the project. Therefore, the condition of point 4.3.5(b) of the RCG is met.

(59) Thirdly, as set out in point 4.3.5(c) of the RCG, a clear and realistic exit strategy must exist for each investment. The Commission notes that, under the measure, there must be a clear and realistic exit strategy assessed individually for each investment (see recital (**30**) above). Therefore, point 4.3.5(c) of the RCG is met.

(60) Therefore, the conditions of point 4.3.5 of the RCG are met.

4.2.6. Commercial management

(61) The measure concerns exclusively direct investments into the target enterprises by natural persons. There is no fund or fund manager involved. Point 4.3.6 of the RCG is therefore of no relevance to the present measure.

4.2.7. Sectoral focus

(62) According to point 4.3.7 of the RCG, the Commission may accept a sectoral focus for risk capital measures. This provision is not applicable, since the measure does not have a sectoral focus.

4.2.8. Conclusion

(63) In light of the above, the Commission concludes that the measure complies with the criteria set out in Section 4.3 of the RCG.

4.3. Cumulation

(64) The measure also complies with the cumulation rules of section 6 of the RCG. Where capital provided to the target enterprises under the measure is used to finance initial investment or other costs eligible for aid under other block exemption regulations, guidelines, frameworks, or other State aid documents, the relevant aid ceilings or maximum eligible amounts will be reduced by 50 % in general and by 20 % for target enterprises located in assisted areas during the first three years of the first risk capital investment and up to the total amount received. This reduction does not apply to aid intensities provided for in the Community Framework for State aid for Research and Development or any successor framework or block exemption regulation in this field.

(65) The Finnish authorities have confirmed that they will apply these cumulation rules, see recital **(31)** above. Therefore, the conditions of section 6 of the RCG are met.

4.4. Reporting and monitoring

(66) Section 7 of the RCG lays down the conditions for the provision of annual reports on risk capital measures and for the publication and recording obligations of the Member States.

(67) The Finnish authorities have undertaken to comply with the reporting and monitoring obligations, see recitals **(33), (34)** and **(35).**Therefore, the conditions of section 7.1 of the RCG are met.

4.5. Conclusion

(68) The Commission concludes that the notified measure fulfils the conditions set out in the Community Guidelines on State aid to promote risk capital investment in small and medium-sized enterprises.

(69) Moreover, the Commission acknowledges that the Finnish authorities committed to apply the necessary appropriate measures after the expiry of the current Community Guidelines on State aid to promote risk capital investment in small and medium-sized enterprises.

(70) The Commission has therefore found the measure to be compatible with the internal market pursuant to Article 107(3)(c) of the TFEU.

5. CONCLUSION

(71) The Commission has accordingly decided to consider the aid to be compatible with the Treaty on the Functioning of the European Union.

(72) The Commission reminds the Finnish Government that, in accordance with Article 108(3) of the TFEU, all plans to refinance, alter or change this aid measure must be notified to the Commission.

(73) The Commission reminds the Finnish Government to provide an annual report on the implementation of the measure.

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/competition/elojade/isef/index.cfm.

Your request should be sent by registered letter or fax to:

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Yours faithfully,
For the Commission

Joaquín ALMUNIA
Vice-President