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EDITORIAL

Dear reader

D&I - 115 Years of Insight

This year Dittmar & Indrenius celebrates its 115th anniversary. Since 1899 we have served businesses in Finland with an ambition for excellence.

From the outset Dittmar & Indrenius was closely connected to the industry and the banking and finance sectors. Along the years, the firm established itself as a leading law firm capable of serving the growing domestic industry and international companies operating in Finland. The firm was often involved in cases that were the first of their kind in Finland.

Still today we are dedicated to the interests of our clients and to quality. Our work is as international as ever and our clients operate in a global economy where business requirements change rapidly. Although our ambition for excellence dates back to the early days of the firm, we challenge ourselves to look ahead, question old ideas and develop innovative ways to address the needs of today's marketplace.

This year we have, in addition to assisting clients in a number of exciting matters, appointed two new partners and a Director of Client Relations, launched a new practice focusing on IPR issues and deepened our cooperation with our pro bono partner, President Martti Ahtisaari's Crisis Management Initiative, one of the world's leading private conflict resolution organisations.

In this D&I Quarterly, we discuss topical legal issues in the field of Finnish commercial law focusing on tax, competition and public procurement. If you have any questions concerning any of the issues discussed, do not hesitate to contact the author or any of your regular contacts at the firm.

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TAX & STRUCTURING

> SUPREME ADMINISTRATIVE COURT RULING IN A LANDMARK CASE REGARDING RECLASSIFICATION OF AN INTRA-GROUP LOAN

by Kai Holkeri

Kai Holkeri

Kai Holkeri heads D&I's Tax & Structuring practice. He advises corporate clients on structuring and tax optimisation of M&A transactions, financial transactions, and incentive schemes as well as general corporate tax and tax litigation.

The Finnish Supreme Administrative Court provided its ruling on 3 July 2014 in a landmark case regarding the reclassification of an intra-group debt into equity by virtue of the domestic transfer pricing provision in Section 31 of the Tax Assessment Procedure Act. The Court dismissed the argumentation of the tax authorities and upheld the earlier decision of the Administrative Court.

The rule in Section 31 generally provides that all transactions between related parties are to reflect the arm's length principle. Section 31 does not, however, include a specific provision regarding the reclassification of the legal form of an instrument in circumstances where the legal form agreed between related parties would deviate from that what would have been agreed between unrelated parties.

The case involved a Finnish company that had received a subordinated accounting hybrid loan from its Luxembourg parent company. The Finnish company had recorded the subordinated loan as equity in its IFRS accounts. The hybrid loan bore interest at a rate of 30 percent. The company had determined the interest rate based on a benchmark study of comparable loans on the market.

The tax authorities had claimed that the legal form of the loan agreed between related parties was to be disregarded, and that the loan was to be reclassified as equity pursuant to the domestic transfer pricing rule and the OECD Transfer Pricing Guidelines. In such case, the interest on the loan would have become non-deductible for the Finnish company.

The Court stated a reclassification of the loan into equity was not possible under the domestic transfer pricing provision alone. The Court further noted that it had not been demonstrated or even alleged by the tax authorities that the case was to regarded as tax avoidance. The fact that the OECD Transfer Pricing Guidelines (Sections 1.65, 1.66 and 1.68) could in theory have allowed a reclassification of the legal form of the loan into equity was not relevant because a tax treaty cannot broaden the tax base from that determined under the domestic tax provisions. Consequently, the arm's length principle included in Article 9 of the tax treaty between Finland and Luxembourg only regarded the arm's length pricing of the instrument, not the classification of the instrument.

The case is likely to provide considerable support for Finnish companies in comparable situations, and it is expected to have material precedential value for many of the currently pending transfer pricing disputes.

TAX & STRUCTURING

> FATCA AGREEMENT AND THE EXCHANGE OF TAX INFORMATION BETWEEN FINLAND AND THE U.S.

by Hanna-Mari Manninen and Jasper Kuhlefelt

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Legislation on the implementation of the FATCA agreement between Finland and the U.S. is currently being prepared by the Ministry of Finance. From the point of view of most financial institutions, FATCA will require, amongst others, more thorough identification procedures of their clients' U.S. tax residency as well as compliance with the IRS's registration requirements.

Reporting to begin next year

Finland signed an agreement with the United States on the implementation of the U.S. Foreign Account Tax Compliance Act ("FATCA") on 5 March 2014. Under the agreement, the Reporting Finnish Financial Institutions ("RFFIs") such as credit institutions, investment firms, fund management companies and certain insurance companies are required to identify their U.S. customers and report their investments and holdings to the Finnish Tax Administration, which will then provide this information annually to the U.S. Internal Revenue Service ("IRS"). The reporting will begin in 2015 regarding information collected from the beginning of 2014.

Registration with the IRS required

The agreement requires the RFFIs to comply with the applicable registration requirements on the IRS's FATCA registration webpage. The RFFIs that have not already done so should register with the IRS as soon as possible in order to obtain a Global Intermediary Identification Number ("GIIN") before 1 January 2015. The GIIN serves to demonstrate that the RFFI complies with the requirements of the FATCA agreement. An RFFI demonstrating significant and continuous non-compliance with its obligations under the FATCA agreement may face a 30% withholding tax on certain U.S.-source payments made to it.

Intergovernmental exchange of tax information spreading globally

As at September 2014, already 42 countries have signed agreements with the U.S. on the implementation of the FATCA and a further 59 countries have reached agreements in substance. FATCA will later also automatically expand the exchange of tax information between the EU countries. According to the EU directive 2011/16/EU on administrative cooperation in the field of taxation, where a member state provides a wider cooperation to a third country than that required by the directive, it may not refuse to provide such wider cooperation to any other member state.

In addition, a Standard for Automatic Exchange of Financial Account Information (more commonly known as the Common Reporting Standard, or the CRS) has been developed in the context of the OECD with the intergovernmental agreements on the implementation of the FATCA as a basis. To date more than 65 jurisdictions have agreed to the implementation of the CRS.

More onerous obligations on financial institutions to be expected in the future

The intergovernmental FATCA implementation agreements can be seen as an onset to a global automatic exchange of information relating to taxation. The FATCA represents the direction of the upcoming development within the EU and OECD. For most individual financial institutions, this development will likely lead to increasing compliance and reporting obligations in the foreseeable future.

COMPETITION & PUBLIC PROCUREMENT

> MARKET COURT IMPOSES LARGEST NATIONAL FINE TO VALIO FOR PREDATORY PRICING

by Hanna Laurila and Toni Kalliokoski


Hanna Laurila

Hanna Laurila heads the firm's Competition & Public Procurement practice. She advises domestic and international corporate clients in a wide range of competition and public procurement matters. She has also extensive experience in commercial contracts including distribution arrangements.


Toni Kalliokoski

Toni Kalliokoski is a senior associate in D&I's Dispute Resolution and Competition & Public Procurement teams. He specialises in competition litigation and antitrust damages. He also practises real estate law as well as corporate and commercial law.

On 26 June 2014, the Market Court imposed a EUR 70 million fine on the Finnish dairy company Valio for predatory pricing on the milk market. The Court found that Valio made a strategic decision to drop the wholesale price of fresh milk below costs to foreclose the Finnish fresh milk market from imported milk and continued this practice for almost three years.

Valio, the biggest milk processor in Finland, is owned by dairy co-operatives which in turn are owned by dairy farmers. Valio collects over 80% of all raw milk in Finland. It is the market leader in nearly all dairy products and has a market share above 50% in the fresh milk market. Consequently, Valio was found to hold a dominant position in the fresh milk market. Valio's main competitor in Finland is Arla Ingman, which since 2008 has been a part of the Arla Foods group.

Prices could be compared to actual total costs and average variable costs in the market concerned

LRAIC method and effects-based analysis was not used

The Court upheld the Competition Authority's traditional approach to compare Valio's wholesale prices with total costs and average variable costs in the fresh milk market.

The Court did not follow recent EU case law such as Post Danmark which examined whether reduced prices covered long run average incremental costs (LRAIC) and whether anticompetitive effects of low prices could be established above those costs. The LRAIC method was considered more relevant for natural monopolies. Valio's arguments on the fixed nature of raw material costs due to Valio's obligation to process all the raw milk produced by its owner co-operatives were not accepted. The Court stressed that this was not a legal obligation but a historical practice accepted by Valio's management.

Valio argued that variable raw milk cost used in the comparison should be lower since, due to the co-operative nature of the business, the price paid for raw milk included also profits on more lucrative products than fresh milk. This argument was rejected.

Equally efficient competitor could not compete on prices below variable costs

The Court concluded that after the price cuts in March 2010, Valio's wholesale prices did not cover the variable costs of production and sale of fresh milk. As the largest purchaser of raw milk, Valio is able to set the price which its competitors must pay to obtain Finnish raw milk. This price must be taken into account in the application of the equally efficient competitor test used to assess Valio's pricing behavior and likelihood of foreclosure.

Meeting competition argument was rejected

Valio claimed that its price cuts were motivated by its desire to meet competition from Arla Ingman which had obtained significant business with the largest grocery retail chain S Group. The Court rejected this claim. The criteria of efficiency defence were not fulfilled. The Court also pointed out that Valio's price changes were not initiated by customers but were part of Valio's own strategy and that Valio offered additional price reductions to the S Group which was an important customer for Arla Ingman.

Evidence of intent to foreclose competitors widely discussed

The Court found that it is not necessary for the Competition Authority to show intent to foreclose to conclude that pricing behavior is predatory. Further, it was explicitly stated that intent could be presumed since Valio's prices did not cover variable costs. Despite this conclusion, the Court examined in detail the evidence submitted for Valio's intent.

Intent can be presumed if prices do not cover variable costs

It found that Valio's top management made a strategic decision in February 2010 to drop the wholesale prices of fresh milk significantly to foreclose competition on the Finnish market. The finding was based on e-mail correspondence and internal documents found during inspections. According to the judgment, the evidence showed that the purpose of the price cuts was to make importing of milk unprofitable for Arla Ingman, to increase Valio's market share and thereafter raise prices back to a higher level.

Recidivism and seriousness of the infringement explain the historical fine

Valio was ordered to end its abusive pricing and to pay a record fine of EUR 70 million. The Court justified the high fine by the serious nature of the infringement. The Court noted that Valio had offered conditional volume rebates to Arla Ingman's important customer and forced Arla Ingman to sell at an even lower price than Valio, thereby increasing Arla Ingman's losses. The Court also took into account recidivism since Valio had been found guilty of an abuse of dominant position in the milk market in 1998. Furthermore, Valio failed to terminate the abusive pricing behavior even during the investigation.

Payment of fine postponed until final decision

Valio has appealed the judgment in the Supreme Administrative Court. On 19 August 2014, the Supreme Administrative Court ordered, based on Valio's demand, that payment of the fine be postponed while the matter is under consideration in the Court.

COMPETITION & PUBLIC PROCUREMENT

> NEW GENERAL TERMS AND CONDITIONS FOR PUBLIC PROCUREMENT OF GOODS AND SERVICES

by Tuomas Rytkönen

Tuomas Rytkönen

Tuomas Rytkönen is an associate in D&I's M&A & Private Equity team. His main areas of expertise are mergers and acquisitions, energy, infrastructure and natural resources, as well as general corporate and commercial law.

The new general terms and conditions for public procurement of goods and services ("JYSE 2014") were published in July 2014. The three most material changes concern price adjustment, liability caps as well as the service provider's liability towards the service users.

The prices are fixed for 12 months at a time

The first material change is that the price of the goods or services is fixed for only 12 months at a time, when previously the price was fixed for the whole agreement period. The change must be based on the general development of the cost of the good or services. If either party wishes to change the prices, it must suggest new prices no later than three months prior to the end of the 12-month period. If the parties do not agree on the new prices, either party may terminate the contract with a six months' period of notice.

The liability cap is the value of the goods or services multiplied by five

The second material change is the introduction of a liability cap. The liability cap is the calculated value of the goods or services multiplied by five. In fixed-term agreements, the value is calculated based on the monthly average order volume multiplied by the number of months the agreement is in force. In case the agreement is in force until further notice, the value is determined by a 48-month agreement period.

Service provider's liability towards service users is unlimited

The third material change is that the service provider's liability towards the service users is clarified. The service provider must compensate the service users for all damage, direct and indirect, caused by the service provider's breach of the agreement. The liability caps are not applied.

Procurement units should include the relevant JYSE 2014 for goods or services as well as possible deviations from them in the requests for tender. Bidders should carefully consider which clauses they wish to amend. In order to avoid interpretation difficulties, all amendments should be specific.

Information technology service providers should note that also the general terms and conditions for public procurement of IT services are being renewed. The renewed terms and conditions are expected to come into force by the end of 2014.

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