

Shipping Group newsletter*

Norway

19. December 2008

Approval by ESA of the new Norwegian tonnage tax system and proposed amendments to fulfil conditions for the approval

Background

The EFTA Surveillance Authority (ESA) has on 3 December 2008 approved the introduction of the revised Norwegian tonnage tax system with permanent tax exemption for qualifying shipping profits.

The approval is conditional on that Norway implements certain amendments to the present rules. On this background the Ministry of Finance has on 4 December 2008 issued a discussion document in which the following amendments to the present tonnage tax system are proposed:

- Introduction of a ten year "lock-in period"
- A requirement that all qualifying companies within the same group should make the same election (tonnage taxation or ordinary taxation)
- A requirement that tonnage taxed companies that deliver so-called door-to-door services cannot charge a margin related to the land or air transport services
- An extension of the scope of qualifying companies to cover companies resident in an EEA state that are only engaged in activities in Norway that are considered qualifying under the tonnage tax system.

Ten year lock-in period

Formally the introduction of a ten year "lock-in period" implies that a tonnage taxed company is required to stay within the tonnage tax system for a minimum number of years (as is also the requirement under several other EU/EEA tonnage tax systems).

The background is that the tonnage taxed companies should commit themselves to maintaining within the EEA area for a certain period of time.

However, the company may in practice still choose to exit the tonnage tax system before the end of the ten year period. It is likely that companies that exit the Norwegian tonnage tax system e.g. intend to transfer their business activities from Norway or have losses that can be offset against profit in other group companies. However, a former tonnage taxed company cannot receive group contributions with tax effect the year it exits the tonnage tax system and the two following years.

If the company exits the tonnage tax system before the end of the ten year period, the exit in itself will not have any tax consequences, except that the company will be subject to ordinary taxation at 28% from the year it exits the system. It is not proposed that the tonnage taxation for the previous years should be revised even if the company exits the tonnage tax system before the end of the lock-in period.

On the other side the company will not be permitted to enter into the tonnage tax system again before the end of the ten year period, i.e. if the company exits the tonnage tax system after the end of year 5 it must remain subject to ordinary taxation for 5 years before it is allowed to enter into the tonnage tax system again.

The tax value on the assets will be stepped up to market value at the time of the exit from the tonnage tax system. A possible gain/ loss upon transfer of the assets will therefore be limited to a possible change in the value and depreciations after exit from the tonnage tax system.

The ten year lock-in period is proposed to be effective from 1 January 2007.

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All qualifying companies within the same group must make the same election (tonnage taxation or ordinary taxation)

It is proposed that all qualifying companies within the same group (more than 50% joint ownership or control) must make the same election as to whether the companies should be subject to tonnage taxation or ordinary taxation.

If a company that has claimed tonnage taxation in its tax return is acquired by a group that has not yet filed the tax return, the election made by the company that is acquired should according to the discussion document not influence the new owner group's election.

In case of mergers the surviving company's lock-in period should be continued. In case of de-mergers both companies should continue the lock-in period. In case the de-mergers should be to an existing company, the existing company's lock-in period should be continued.

It is explicitly stated that transfer of business assets and business (partially) will not influence the lock-in period.

Since the Norwegian tonnage tax system does not permit illegal assets or ordinary taxed income in a tonnage taxed company, except financial income, companies that do not fulfil all conditions for tonnage taxation will not be considered qualifying.

The requirement therefore only applies to group companies that fulfil all requirements for tonnage taxation, i.e. companies that own illegal assets or are engaged in illegal activities are not covered by the requirement, even if the companies are also engaged in activities that would in their nature qualify for tonnage taxation.,

Ordinary taxed group companies may therefore remain subject to ordinary taxation if they acquire at least one asset that is illegal within the tonnage tax system, for example shares in non listed companies that are not subject to tonnage taxation. Alternatively the company can engage in illegal business activities. Since the new rule is proposed to enter into force 1 January 2009 it should be sufficient to acquire illegal assets or engage in illegal business activities within the end of 2009.

A company that has previously exited the tonnage tax system within the end of the first ten year period

(regardless of whether the exit was voluntary or compulsory) will not qualify for tonnage taxation, and therefore not be considered qualifying.

If a company exits the tonnage tax system after the end of the ten year "lock-in period", all group companies must exit the tonnage tax system – at least the group companies have fulfilled the "lock-in period".¹

According to the discussion document a tonnage taxed company's compulsory exit due to a violation of the conditions for tonnage taxation, or voluntary exit before the end of the "lock-in period", will not have any consequences for the other group companies. The reason is that these companies will no longer qualify for tonnage taxation. Consequently other group companies may still remain within the tonnage tax system.

The proposed rule is proposed to be effective from 1 January 2009.

Door-to-door transportation

According to regulations issued by the Ministry of Finance (FSFIN § 8-13-1 (1) e) a tonnage taxed company may be engaged in so-called door-to-door transportation if the land or/ and air transportation is carried out by a non tonnage taxed company. In case the parties are related it is presupposed that the pricing should be arm's length.

According to ESA's state aid guidelines state aid should only be given to shipping activities, i.e. not to land and/ or air transportation. On this basis the Ministry of Finance proposes that a tonnage taxed company that delivers door-to-door services cannot charge a margin related to the land or air transport services. However, it will still be permitted to sell door-to-door transport services, if the land and/ or air transportation is carried out by an ordinary taxed company – either a related company or an unrelated subcontracting party.

The amendment is proposed to be effective from 1 January 2007.

¹ If the company that exits the tonnage tax system, but not all group companies, have fulfilled the "lock-in period" the question arises whether also the companies that have not fulfilled the "lock-in period" (that are in principle required to stay within the system for ten years) should be forced to exit the tonnage tax system. In our opinion there are arguments that these companies should not be forced to "violate" their obligation to stay within the tonnage tax system. However, this question is not discussed in Ministry of Finance's discussion paper.

Foreign companies resident within the EEA

Under the present rules only Norwegian incorporated private and public limited companies are qualifying subjects under the tonnage tax system.

It has been considered doubtful whether this requirement is compatible with Norway's EEA obligations.

On this basis the Ministry of Finance proposes that foreign companies resident within the EEA that correspond to Norwegian private and public limited companies that only have qualifying shipping income in Norway, should be considered qualifying. The foreign company may not, unlike Norwegian tonnage taxed companies, have financial income that is taxable to Norway. In other words the proposal is based on that excess liquidity should be deposited abroad/ allocated to the main office abroad.

It is explicitly stated that companies incorporated abroad, but tax resident in Norway, should not qualify for tonnage taxation.²

The new legislation where after Norwegian companies resident within the EEA are considered qualifying under the tonnage tax system is proposed to be effective from 1 January 2008.

² Originally the background for limiting the scope of the tonnage tax system to Norwegian incorporated private and public limited companies was that companies formally incorporated abroad will not be subject to Norwegian corporate legislation. It was assumed that would imply that Norwegian tax authorities would have limited possibilities to ensure that dividends distributed were subject to taxation.

After the introduction of the new Norwegian tonnage tax rules with permanent tax exemption for qualifying shipping income we cannot see that this argument is relevant. Further, companies resident within the EEA area will generally be subject to corporate legislation that is very similar to Norwegian corporate legislation.

On this background it is difficult to see the background for this limitation, especially if the company in question is incorporated in an EEA state.

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