

# Shipping Group newsletter\*

Norway

17. March 2009

## Background

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

The approval was conditional on that Norway implemented certain amendments to the present rules. On this background the Ministry of Finance issued a discussion document on 4 December 2008 in which the following amendments to the present tonnage tax system were 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)
- An extension of the scope of qualifying companies to cover companies resident in an EEA state that are only engaged in activities in Norway and are considered qualifying under the tonnage tax system.
- A requirement that tonnage taxed companies which deliver so-called door-to-door services cannot charge a margin related to the land or air transport services

The Ministry of Finance has on 27 February 2009 issued a white paper where it proposes amendments to the tonnage tax rules. The proposed amendments are mainly correspondent to the proposals in the discussion paper. Further the Ministry of Finance's supplementary regulations to the General Tax Act section have been revised on 3 March 2009 by stating explicitly that tonnage taxed companies which deliver so-called door-to-door services cannot charge a margin related to the land or air transport services.

## 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. will have losses that can be offset against profit in other group companies, or intend to transfer its business activities from Norway.

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 of course 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 (5 year restriction period).

It could be possible to transfer assets to another company within the tonnage tax system and/or a new company that enters into the tonnage tax system in Norway or another jurisdiction before the end of the ten year period.

The tax value on the assets will be stepped up to market value at 1 January the exit year. A possible gain/ loss upon transfer of the assets to another company will therefore be limited to a possible change in the value and depreciations after exit from the tonnage tax system.

In case of a merger between two companies the lock-in period or restriction period for the surviving company will be continued. In case of de-mergers the original company's lock-in period or restriction period should be maintained by all newly incorporated companies, while a company that is not newly incorporated should maintain its original lock-in period or restriction period.

The ten year lock-in period is proposed to be effective from 1 January 2007, and it is explicitly stated that the time that a tonnage taxed company has been subject to tonnage taxation prior to 1 January 2007 should not be included when calculating the ten year lock-in period.

**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.

Whether two or more companies belong to the same group should be determined based on the corporate structure at the time the companies file their tax return.

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 not influence the new owner group's election. However, if the company that is acquired has not filed its tax return, it must make that same election as the other qualifying group companies. This applies regardless of whether the other group companies have filed their tax return at the time the company is acquired.

Since the Norwegian tonnage tax system does not permit illegal assets or ordinary taxed income, 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 October 2009 because the company would then have

exceeded the two month deadline for disposing of illegal assets or activities within the end of the year. 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 will 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.

According to the discussion paper 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 background is that these companies will no longer qualify for tonnage taxation. Consequently other group companies may still remain within the tonnage tax system.

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

**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 that is taxable to Norway according to the General Tax Act or the Petroleum Tax Act, should be considered qualifying<sup>1</sup>.

According to the Ministry of Finance this requirement means that the relevant company's business activities must be managed solely from Norway and not from a main office or permanent establishment abroad.

The foreign company may as Norwegian private and public limited companies invest in financial assets in Norway and abroad.

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<sup>1</sup> PricewaterhouseCoopers pointed out that the reference to the Petroleum Tax Act was missing during the public hearing.

It is explicitly stated that foreign incorporated companies that are resident in Norway for tax purposes will not be considered qualifying under the tonnage tax system <sup>2</sup>.

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.

### **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.

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 has changed the supplementary regulations to the General Tax Act on 3 March 2009 by stating explicitly 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 party.

The amendment is effective from 1 January 2007. Consequently any company that has charged a margin in previous tax years will in principle be considered to have

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<sup>2</sup> 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 that were distributed from foreign companies 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 is incorporated in an EEA state.

been engaged in illegal business activities and will consequently in principle be considered disqualified from the tonnage tax system from the year it started the illegal activity. However, it could be argued that the company should be allowed to correct the breach within two months from the Ministry of Finance's announcement of this limitation

### **Contacts**

For more detailed information, please do not hesitate to contact your local PwC contact

#### **National**

Svein T. Sønning  
Partner Tax – Kristiansand. Tel. +47 9526 1071

Rita Granlund  
Partner Assurance – Oslo. Tel. +47 9526 0237

Steinar Hareide  
Partner Tax – Oslo. Tel. +47 9526 0429

#### **Stavanger**

Torbjørn Larsen  
Partner – Assurance. Tel. +47 9526 1096

Kjell Inge Gade  
Partner – Tax. Tel. +47 9526 1175

#### **Bergen**

Jon Haugervåg  
Partner – Assurance. Tel. +47 9526 1300

Dag Saltnes  
Partner – Tax. Tel. +47 9526 0632

#### **Kristiansand**

Torstein R. Robstad  
Partner – Assurance. Tel. +47 9526 1020