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Subject: State aid – SA.37912 (2013/N) – Croatia
Introduction of a tonnage tax scheme in favour of international maritime transport

Sir,

1. PROCEDURE

- (1) By letter dated 9 December 2013, the Croatian authorities notified the Commission, in accordance with Article 108(3) of the TFEU, of their intention to introduce a tonnage tax scheme in favour of international maritime transport. In the notification letter, the Croatian authorities referred to the Community guidelines on State aid to maritime transport¹ (hereinafter 'the Maritime Guidelines') as the applicable EU legal text that would provide an explicit legal basis for the authorisation of the notified measure.
- (2) The Croatian authorities complemented the notification by letter dated 6 March 2014.
- (3) The Commission considered the notification incomplete and therefore requested additional information by letter of 30 April 2014. The Croatian authorities provided information by letter of 30 May 2014.
- (4) The Commission requested further additional information by letter of 9 July 2014. The Croatian authorities responded by letter of 28 August 2014.

¹ OJ C 13 of 17.1.2004, p.3.

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- (5) As the Commission still considered the notification incomplete, it requested further information by letter of 23 October 2014. The Croatian authorities responded by letter of 5 December 2014.
- (6) The Commission requested further information by letter of 22 January 2015. The Croatian authorities responded by letter of 17 February 2015.

2. DESCRIPTION OF THE NOTIFIED SCHEME

2.1. Legal basis, eligible beneficiaries

- (7) The Croatian tonnage tax scheme (hereinafter 'the scheme') is a system for settling profit tax liability. Eligible undertakings may opt for a tax calculated on the net tonnage of the fleet that they operate (tonnage tax) instead of being taxed on the actual profit of their maritime transport activities under the standard Croatian profit tax system.
- (8) Only legal entities which are liable to corporate tax in Croatia and are engaged in international maritime transport by ship or in an activity assimilated thereto may opt for that alternative system. Eligible undertakings, vessels and activities are described in further detail in Section 2.5 below.
- (9) Croatia introduced the scheme in 2014, on the basis of amendments to Articles 429-429i of the Maritime Code².
- (10) Pursuant to Article 429a of the Maritime Code, the tonnage tax is a tax assessed and payable instead of the profit tax, as regulated by the Act governing the profit tax, regardless of the actual profit or loss generated during the fiscal period for which the tonnage tax liability is determined.
- (11) Provisions regulating the procedure and the manner of exercising the right to participate in the tonnage tax regime are set out in a governmental decree issued by the Croatian Minister of Maritime Affairs, Transport and Infrastructure.³
- (12) The notified measure succeeds the corporate income tax exemption that existed during 2005-2013 and which is not within the scope of the present assessment.

2.2. Objectives of the scheme

- (13) The objective of the Croatian tonnage tax system is to preserve the shipping sector in Croatia and to maintain jobs and maritime expertise.
- (14) According to the Croatian authorities, statistical data collected by the Croatian Ship-Owners Association for 2005-2013 and covering all ships managed from Croatia show a clear need for fiscal advantages for ship-owners and other ship operators. In the

² Official Gazette 181/04, 76/07, 146/08, 61/11, 56/13.

³ Official Gazette 90/13.

years 2005-2010 following the introduction of the measure preceding the scheme and largely comparable to it (the profit tax exemption), the Croatian authorities observed positive developments in terms of tonnage managed from Croatia; a negative trend was however observed during the last three years 2011-2013. The Croatian authorities believe that this trend was the result of the financial crisis which had developed into a shipping crisis fuelled by tonnage oversupply. Therefore, the Croatian authorities deem the continuation of fiscal benefits essential, in order to contain the recent decline and preserve the maritime cluster and know-how in the country.

- (15) According to data provided by the Croatian authorities, Croatian shipping companies currently employ around 2 216 seafarers on ships in international trade and 400 personnel in administration (all staff has Croatian citizenship).

2.3. Budget

- (16) The Croatian authorities estimate that due to the current situation in the maritime transport sector, which is characterised by low profits, no or only a small advantage in form of foregone tax revenues will stem from the scheme at least in its early phase. The Croatian authorities hope that in the long run the sector will come back to robust profitability. On the basis of data for the pre-crisis period 2005 – 2008, foregone tax revenues are estimated to amount to HRK 144 million (~EUR 19 million) per year when the sector comes back to robust profitability.

2.4. Duration of the scheme

- (17) The scheme entered into force on 1 January 2014, pursuant to Art. 140 of the Croatian Law on amendments to the Maritime Code.
- (18) The final tax settlement for the fiscal year 2014 will however only take place in 2015, as is the case with the profit tax, to which the scheme is an alternative. In the interim, eligible undertakings have effected tonnage tax advance payments for the fiscal year 2014.
- (19) The Croatian authorities notified the scheme for a 10-year duration, until 31 December 2024 inclusive.

2.5. Eligibility criteria

2.5.1. Eligible activities and eligible ships

- (20) The scheme covers only maritime shipping operations (namely maritime transport of freight and passengers) as well as exploration and providing other services related to activities at sea. The Croatian authorities confirmed that ships engaging in 'exploration and providing other services related to activities at sea' means ships servicing offshore installations (such as liaison ships, stand-by and supply vessels), cable-laying vessels, pipeline layers and research vessels. The Croatian authorities declared that shipping companies cannot participate in the scheme with any ancillary activities such as loading/unloading services or road haulage as part of the journey, nor can they declare for the tonnage tax margins earned from bought-in non-shipping services. Selling both shipping and ancillary activities in one package will render profits from the entire activity ineligible for the tonnage tax scheme.

- (21) By way of amendment, the Croatian authorities will include in the scope of the tonnage tax scheme revenues from chartering out ships on a 'bareboat' basis ('bareboat chartering out'). The purpose of that amendment is to allow some short-term flexibility for eligible shipping companies, i.e. companies engaged in maritime transport. Bareboat chartering-out must however not exceed 20% of the tonnage of the entire company's fleet covered by the tonnage tax.
- (22) For the purposes of the application of the tonnage tax system, Article 429 of the Maritime Code defines an eligible ship as a ship authorised, pursuant to a navigation category assigned and documents issued, to navigate outside internal maritime waters and the territorial sea of the Republic of Croatia for the purpose of engaging in maritime shipping operations, exploration and providing other services related to activities at sea.
- (23) The following shall not be considered ships for the purposes of tonnage taxation:
- yachts⁴,
 - fishing vessels,
 - technical waterborne craft⁵.
- (24) As regards the eligibility of tugboats, the Croatian authorities committed to amend the Maritime Code, to clarify, firstly, that only tugboats engaged in 'maritime transport' for more than 50 % of their operational time during a given year are eligible for support under the scheme, and secondly, that towage activities which are carried out *inter alia* in ports, or which consist in assisting a self-propelled vessel to reach port are not considered 'maritime transport'. The present version of the Maritime Code already limits the scope of application to maritime transport of freight and passengers. The proposed amendment's more precise wording will however prevent any misinterpretation of the scope as regards towage activities.
- (25) The Croatian authorities assume that in practice, most of the ships benefiting from the scheme will fall under NACE code 5020 – 'Sea and coastal freight water transport'; half of them being bulk carriers. Passenger ships⁶ falling under NACE Code 5010 – 'Sea and coastal passenger water transport' are nevertheless eligible, too.
- (26) Eligible ships shall meet, as a minimum, the safety standards prescribed in the Croatian Maritime Code and have a valid certificate, usually issued by an EU recognised organisation. In that respect, the Croatian authorities asserted that the

⁴ A yacht is, according to the Article 5 (20) of the Maritime Code, defined as a waterborne craft for sports and recreation, regardless of whether it is used for personal needs or commercial activities, exceeding 12 m in length and intended for a longer stay at sea, and which is authorized to carry no more than 12 passengers in addition to the crew. Therefore, any yacht which falls under the above definition is excluded from the tonnage tax regime.

⁵ Technical waterborne craft, according to the definition set out in Article 5 (12) of the Maritime Code is a ship with or without a mechanical propulsion intended to carry out technical operations (dredger, floating crane, floating dock, rigs for the research and exploitation of the seabed, and alike).

⁶ According to the definition in Article 5 (8) and Article 429 (2) of the Maritime Code, a passenger ship is a mechanically propelled ship which can carry more than 12 passengers.

Maritime Code is in line with all relevant international standards and EU-law. The Croatian authorities pointed out that the Republic of Croatia, as a member state of the International Maritime Organization (IMO) and the International Labour Organization (ILO) had ratified all relevant instruments adopted within those organisations.

- (27) The Croatian authorities, as a signatory to the Paris Memorandum of Understanding on Port State Control (Paris-MoU), explained that they are checking all requests for participation in the tonnage tax scheme against the Paris-MoU database for possible cases of non-compliance with the MoU's shipboard living and working conditions, navigation safety, security protection and sea pollution prevention standards. Accordingly, ships are only eligible if they have not been banned from leaving port more than twice over a three-year period for non-compliance. In that context, the Croatian authorities pointed to the Directive on port State control⁷ and declared that ships will not be admissible if their track record is not in line with Art. 16 of the Directive.

2.5.2. Eligible undertakings

- (28) Pursuant to Article 429a of the Maritime Code, *"the tax payer subject to the tonnage tax shall be a legal person with a registered office in the Republic of Croatia or with the actual management and supervision of its operations located in the Republic of Croatia, provided that it meets the criteria stipulated by the Maritime Code and declares that, instead of the profit tax, it will pay the tonnage tax in respect of the profit generated by:*

a) the economic activity of its own ships, or those owned by dependent ship-owning companies⁸, leased ships⁹ or chartered ships¹⁰;

b) providing ship management services, provided that the ship manager in respect of the ship is a company under the IMO's International Safety Management Code¹¹;

c) the sale of ships participating in the tonnage tax regime and their equipment, and income related to shares in majority-owned shipping companies¹² engaging in

⁷ Directive 2009/16/EC of 23.4.2009, OJ L 131 of 28.5.2009, p.57.

⁸ Ship-owning subsidiaries of tonnage tax beneficiaries, incorporated in certain jurisdictions abroad, fully owned by the beneficiaries. The subsidiaries exclusively serve as special purpose vehicles (SPV) through which beneficiaries acquire ships. The SPV's ships are included in the tax assessment at the level of the tonnage tax beneficiary. See also recital (30).

⁹ Ships leased on bare-boat basis.

¹⁰ Time or voyage-chartered ships.

¹¹ Under the IMO's International Safety Management Code. "The Company" defined as the ship-owner or any person, such as the manager or bareboat charterer, who has assumed responsibility for operating the ship. I.e. in Croatia only companies performing the joint provision of both technical and crew management for a same vessel ('full management'). Such companies act as classic 'ship-owners' as far as transport operations are concerned.

¹² In particular ship-owning SPVs (*supra note 11*).

an economic activity with ships whose net tonnage is included in the assessment of the Croatian tonnage tax. (Article 429a (1))."

- (29) The afore quoted Article 429a (1) a and c implies that the following profit categories are treated equally:
- profits from ships entered in the tonnage tax regime either directly owned by the shipping company and ships indirectly owned by the shipping company or through its dependent subsidiaries;
 - proceeds from sales of directly owned ships and sales of ships owned by a dependent subsidiary, where the sale was executed by a transfer of shares of the subsidiary (ship-owning company) rather than the transfer of the ship itself.
- (30) According to the Croatian authorities, the above described equal treatment of shipping companies and their subsidiaries abroad is due to the following peculiarity of the Croatian shipping sector: Croatian shipping companies usually incorporate subsidiaries in certain jurisdictions abroad¹³ which they fully own and which exclusively serve as special purpose vehicles (SPV) through which they acquire ships. Thus, the international shipping banks would obtain sufficient collateral from the SPV, such as pledge of shares, resignation of directors, pledge of the earnings accounts, and which is further backed by the corporate guarantee of the Croatian shipping company concerned; the asset of the company, i.e. the ship, would also be safe from the general creditors of the parent company. The Croatian authorities asserted that all subsidiaries of Croatian shipping companies are such SPVs.
- (31) All revenues received from the operation of an eligible ship are shown in the consolidated financial documents of the parent company regardless of whether the revenues have been received directly by the parent company or by the subsidiary. Both directly and indirectly owned eligible ships are operated by the parent company. In particular, income related to shares or stakes in ship-owning companies will only be eligible for tonnage taxation if such shipping company is controlled by the tonnage tax beneficiary and operate ships entered in the tonnage tax regime.

2.6. Strategic and commercial management of the tonnage taxed fleet from the EEA

- (32) The actual management and supervision of the operations of eligible undertakings must be situated in the Republic of Croatia. The Croatian authorities committed to amend the scheme's legal text in the sense that ships included in the tonnage tax scheme shall be strategically and commercially managed from an EU or EEA Member State.

2.7. Training requirements

- (33) Article 429b of the Maritime Code, obliges eligible undertakings to prepare annual trainee boarding plans. Such plans set out the minimum number of deck or engine

¹³ In particular in jurisdictions applying Anglo Saxon law, like Malta and Liberia.

trainees, citizens of either the Republic of Croatia or another EEA Member State, who must be on board within a single calendar year, as well as a provisional schedule of their boarding of individual ships.¹⁴

- (34) Eligible undertakings are obliged to report to the Croatian authorities on the implementation of the annual trainee boarding plan.

2.8. Tonnage tax rates

- (35) With the notified scheme, the Croatian authorities intend to charge for each vessel a lump sum tax, determined on the basis of its tonnage (Article 429e of the Maritime Code); the annual rates are as follows:

Table 1

| Net Tonnage | | | | |
|--|--|-------------------------------------|------------------------------------|-----------------------------------|
| 0-1000 | 1001-10000 | 10001-25000 | 25001-40000 | >40000 |
| HRK 270.00 (~35,44 €) per 100 NT | HRK 230.00 (~30,19 €) per 100 NT | HRK 150 (~19,69 €) per 100 NT | HRK 95 (~12,47 €) per 100 NT | HRK 55 (~7.22 €) per 100 NT |

- (36) In respect of any ship for which the taxpayer has paid the tonnage tax or its equivalent abroad, the tax actually paid abroad shall be accounted for as part of the domestic tonnage tax for up to the amount of the domestic tonnage tax payable for the ship concerned, pursuant to Article 429.g (6) of the Maritime Code. According to the Croatian authorities, this provision is necessary to avoid double tonnage taxation of ships owned by eligible undertakings through their affiliated companies abroad.

2.9. 'Flag-link' requirement

- (37) The Croatian authorities have submitted detailed statistics on the composition of fleets of all tonnage tax payers that already registered for the scheme. According to that data, the shares of EEA flagged vessels of the Croatian tonnage taxed fleets are above 60% with the exception of only one tonnage tax beneficiary whose relevant rate is at 45%.
- (38) The same statistics show that all tugboats accepted under the Croatian tonnage tax scheme are EEA flagged. The Croatian authorities committed to nevertheless amend the scheme's legal text in order to specify that only EEA flagged tugboats will be accepted under the scheme.
- (39) The Croatian authorities verify the flagging of tonnage taxed vessels:
- during the introduction of new vessels into the tonnage tax scheme;
 - by the Ministry responsible for Maritime Affairs which performs random checks;

¹⁴ The minimum number of trainees in the annual plan must be in a 1:10 ratio to the total number of officer posts on all ships the eligible undertaking included in the scheme. The minimum number of trainees shall be taken on board within a single year for a total of as many days as the minimum number of trainees multiplied by 183 days.

-by the Tax administration which performs random checks.

- (40) In addition eligible undertakings are obliged to report to the Croatian authorities every change related to the number, tonnage, nationality and ownership of the ships participating in the scheme, as well as changes of any fact which is necessary to meet the requirements of the tonnage tax regime, within a period of 15 days from the day when the change occurred.
- (41) The Croatian authorities committed to introduce binding provisions that will oblige all tonnage tax beneficiaries who have less than 60% of their fleet under EU/EEA flags to maintain or increase their share of EU/EEA flagged ships compared to the situation as at entry into the tonnage tax scheme. No new companies will be accepted to the tonnage tax scheme without having a share of its fleet under EEA flags. All applications submitted after 1 July 2013 will be subject to that obligation.
- (42) Even if currently Croatian shipping companies are not involved in time/voyage chartering activities, the Croatian authorities committed to introduce early 2015 the requirement that, independently of the respect of the general flag-link rule, no more than 75% of a beneficiary's may consist of non-EEA time or voyage chartered vessels.

2.10. Avoidance of cross-subsidisation of non-eligible activities

- (43) The scheme provides for the following ring-fencing measures to avoid the spill-over of the scheme's advantage into non-eligible activities in Croatia or in other countries:
- (44) Firstly, the taxpayers subject to the tonnage tax are obliged to provide separate accounting coverage of any activities other than those that generate eligible profits.
- (45) Secondly, the arm's length principle/market pricing is ensured in accounts of tonnage tax beneficiary when the company has both eligible and non-eligible activities.
- (46) Thirdly, the taxpayer subject to the tonnage tax is obliged to apply the arm's length principle to any transactions with its affiliates if the latter do not participate in the tonnage tax regime.
- (47) Fourthly, any ineligible activities and profits are subject to the Croatian regulations governing the profit tax (Article 429a (2) of the Maritime Code).
- (48) Fifthly, eligible undertakings have to stay in the tonnage tax scheme for at least 10 years. Prior to the expiry of each ten-year period, an (re)application for the subsequent ten-year period may be submitted.
- (49) Lastly, the Croatian authorities committed to introduce by early 2015 an 'all-or-nothing rule' in the sense that all eligible ships of a tonnage-taxed undertaking and its group must be covered by the scheme. According to the Croatian authorities each of the present beneficiaries has brought all its eligible ships under the scheme.

2.11. Specific rules on transition between two taxation systems

- (50) The notified scheme applies from 2014 in continuation of the expired corporate tax exemption scheme. According to the Croatian authorities, the expired scheme in

essence corresponded to a tonnage tax and had existed for 9 years. The Croatian authorities explained that due to that previous system, shipping companies cannot introduce any previously over-depreciated ships into the new tonnage tax scheme ('ships with hidden tax liabilities'¹⁵). Furthermore, new entries would be unlikely in the coming years¹⁶.

- (51) The Croatian authorities committed to introduce the rule that a ship would be ineligible if any hidden tax liability exists at the moment of application for tonnage taxation, unless the applicant negotiates with the Ministry of Finance measures to bring the tax alleviations in line with the permitted level. In particular, the Croatian authorities will amend the scheme's legal text in order to ensure:
- the calculation of hidden tax liabilities as a difference between the accounting value of a ship at the moment of entry into tonnage taxation and its tax value;
 - that hidden tax liabilities are written off only within the aid ceiling. Notably, after each fiscal year, the data would be gathered on tax amounts paid by the beneficiary company in tonnage tax and any other taxes (payments related only to eligible activities). Hidden tax liabilities could then be reduced by the total sum of tax payments;
 - that the remaining hidden tax liability is taxed when a ship with such liabilities is sold. However, if the ship is sold with a view of being replaced with a new one, taxation of the remaining tax liability may be postponed by up to 3 years. The new ship would then be assigned the remaining hidden tax liability as established for the sold ship.
- (52) In addition, the Croatian authorities committed to clearly stipulate by way of amendment to the scheme's legal text, that upon the exit of companies from the tonnage taxation the tax value of shipping assets is determined as if they had all the time been under the corporate income tax regime. In that context, the Croatian authorities will further amend the scheme's legal text in the sense that the tax value of shipping assets shall take into account the depreciation of ships while under tonnage taxation system, so that upon the exit of companies from tonnage taxation, the cost of wear and tear of ships while under the tonnage tax system cannot be used to reduce corporate income tax payments.
- (53) The Croatian authorities have initiated the procedure for the relevant amendments before 2015, so that the amended version of the scheme's legal text would be in force early 2015.

2.12. Controls and Sanctions

- (54) Eligible undertakings are obliged to notify the Croatian authorities within 15 days of any changes related to the number, tonnage, nationality and ownership of ships

¹⁵ Liabilities which might arise from the difference in the accounting/market value of the ship and its tax value at the moment of the entry into the tonnage tax regime.

¹⁶ Two shipping companies which did not enter tonnage taxation were not eligible under the Croatian rules (e.g. companies not having ships which trade internationally)

participating in the scheme, as well as of changes of any facts relevant for its qualification to pay the tonnage tax¹⁷.

- (55) The Croatian authorities committed to introduce¹⁸ mandatory annual compliance declarations for all controllable parameters such as type of vessel, activities performed with the vessel, net tonnage, days in use, flag, types of operation and respect of the aid ceiling.
- (56) A tonnage tax payer forfeits the right to pay the tonnage tax instead of the profit tax from the time it ceases to comply with the scheme's eligibility criteria (Article 429d of the Maritime Code). A taxpayer who forfeits that right prior to the expiry of the ten-year participation period shall pay a sum equal to the profit tax for the entire tax assessment period for which it forfeits the right; if the profit tax liability is lower than the tonnage tax, the difference will not be refunded.
- (57) Any taxpayer who forfeits the right to pay the tonnage tax may not reapply for participation in the scheme for a period of five years, unless it forfeits that right for non-compliance with the scheme's safety, shipboard living and working security and pollution prevention standards (Article 429b(1) of this Code), in which case the taxpayer may not reapply for a period of five years, only in respect of the particular ship which does not comply with said standards.
- (58) If an undertaking voluntarily leaves the tonnage taxation scheme and agrees to enter profit taxation, the undertaking, pursuant to Article 429d (4) of the Maritime Code, cannot re-enter the tonnage tax for a period of 5 years.

2.13. Cumulation

- (59) In respect of the cumulation of aid from the notified scheme with aid from other public measures, including relief from labour-related costs, the Croatian authorities declared that:
- Firstly, no direct aid schemes exists in favour of Croatian ship-owning companies.
 - Secondly, Croatian seafarers are obliged to pay social contributions in Croatia if they are residents in Croatia; no relief applies.
 - Thirdly, apart from the notified scheme, the only other tax derogation applicable in the maritime sector is the income tax exemption for seafarers who sailed on ships in international trade for more than 183 days in a tax year. The Croatian authorities consider that measure a support to seafarers rather than to shipping companies.

¹⁷ Rules of 21.06.2013 on the procedure and manner of exercising the right to participate in the tonnage tax regime (Ministry of Maritime affairs, transport and infrastructure)

¹⁸ Rules of 21.06.2013 on the procedure and manner of exercising the right to participate in the tonnage tax regime (Ministry of Maritime affairs, transport and infrastructure).

- (60) The Croatian authorities therefore concluded that the total aid¹⁹ for the benefit of shipping companies does not provide higher benefit than the full exemption from taxes and social contributions of shipping companies and seafarers would represent.

3. ASSESSMENT OF THE AID

3.1. Existence of aid under Article 107(1) of the TFEU

- (61) Pursuant to Article 107(1) of the TFEU, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.
- (62) The notified tonnage tax scheme enables shipping companies to reduce the corporate income tax they would otherwise have to pay in case the company is profitable. The Commission therefore considers that the notified regime confers a selective economic fiscal advantage to undertakings active in the international maritime transport.
- (63) By implementing the scheme, the Croatian authorities are foregoing tax revenues. Hence, the fiscal advantage is granted through State resources and it is imputable to the State.
- (64) Shipping activities are essentially carried out on a worldwide market. In addition, the markets for both maritime cabotage routes and maritime services are fully liberalised.²⁰ Thus, services provided by shipping companies benefiting from the notified scheme are open to competition within Member States, between Member States and between Member States and third countries. Consequently, the notified scheme threatens to distort competition and could affect trade between Member States.
- (65) Therefore, the Commission considers that the scheme under examination constitutes State aid within the meaning of Article 107(1) of the TFEU.

3.2. Assessment of the notified aid measure

- (66) Pursuant to 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.

¹⁹ Except for aid for training aid, restructuring aid, aid related to public service obligations and start-up aid for new short sea shipping services.

²⁰ As from 1 January 1993: Council Regulation (EEC) No 3577/92 of 7 December 1992 applying the principle of freedom to provide services to maritime transport within Member States (maritime cabotage), OJ L 364 of 12.12.1992, p. 7; Council Regulation (EEC) No 4055/86 of 22 December 1986 applying the principle of freedom to provide services to maritime transport between Member States and between Member States and third countries, OJ L 378, 31.12.1986, p. 1.

- (67) Specific criteria to assess the compatibility of State aid to maritime transport are set forth in the Guidelines on State aid to maritime transport²¹ (hereinafter "the Maritime Guidelines").
- (68) Section 3.1 of the Maritime Guidelines applies to the fiscal treatment of ship-owning companies and specifically mentions tonnage tax, generally defined as a system of replacing the normal corporate tax system by a tonnage tax where the ship owner pays an amount of tax linked directly to the tonnage operated, irrespective of actual profits or losses. The notified scheme described above is a tonnage tax scheme in the sense of Section 3.1, 4th paragraph, of the Maritime Guidelines.
- (69) The Commission has therefore assessed the compatibility of the notified scheme with the internal market on the basis of the Maritime Guidelines.

3.2.1. Objective in the common interest

- (70) Section 2.2, 1st paragraph, of the Maritime Guidelines provides for specific objectives in the Community [EU-] maritime interest that may be supported with aid schemes.
- (71) Based on information provided by the Croatian authorities, the Commission finds that the scheme contributes to the following objectives in accordance with the Maritime Guidelines:
- Eligibility criteria described above in recitals (26), (27) help improving a safe, efficient, secure and environment-friendly maritime transport;
 - Eligibility criteria described above in Section 2.9 encourage the flagging or re-flagging to Member States' registers;
 - Available data (recitals (14), (15) above) suggests that the scheme is contributing to the consolidation of the maritime cluster in Croatia, protecting and promoting employment for EU/EEA seafarers;
 - The obligation to carry out seafarer training (Section 2.7 above) will help maintaining and improving maritime know-how).

- (72) In conclusion, the scheme contributes to a number of objectives in the common interest.

3.2.2. Competition with flags of convenience; improvement of the fiscal climate for shipping companies

- (73) Section 3.1, 1st paragraph, of the Maritime Guidelines suggests that the creation of conditions allowing fairer competition with flags of convenience seems the best way forward to avert the flagging out of vessels and also corporate relocation, due to the low-tax environment in third countries.

²¹ OJ C 13, 17.1.2004, p. 3.

- (74) As was described above in recital (14), a comparable measure preceding the scheme is likely to have brought about an initial positive trend in terms of tonnage managed from Croatia. A negative trend followed, most likely due to a shipping crisis fuelled by tonnage oversupply, as a corollary of the financial crisis.
- (75) Against this backdrop, the Commission finds that aid through the notified scheme is needed to bring about a material improvement which the market in all probability would not deliver itself.
- (76) Section 3.1, 1st paragraph, of the Maritime Guidelines suggests that the fiscal climate in many third countries is considerably milder than within Member States, which has resulted in there being an incentive for companies not only to flag out their vessels but also to consider corporate relocation.
- (77) Given that the scheme in question is a special measure to improve the fiscal climate for ship-owning companies in Croatia, the Commission has no doubts that the scheme is the appropriate policy instrument.

3.2.3. Provision of fiscal incentives to stimulate competitiveness

- (78) Section 3.1, 5th paragraph, of the Maritime Guidelines provides for the legal presumption that, *inter alia*, a system of replacing the normal corporate tax system by a tonnage tax is a fiscal incentive to stimulate the competitiveness of the EU shipping industry.
- (79) Available information (recital (14) above) shows that the scheme preceding the notified scheme, and in essence comparable to it, had an incentive on beneficiaries to manage more tonnage from Croatia than without the aid.
- (80) The Commission has no doubts that the scheme will have an incentive effect on beneficiaries to pursue activities in the common interest.

3.2.4. Eligibility for aid

- (81) The Commission assessed whether aid under the scheme is exclusively aimed at the beneficiaries, ships and activities permitted by the Maritime Guidelines, and is limited to the necessary minimum and transparent.

3.2.4.1. Eligible activities and eligible ships

- (82) The Commission assessed whether activities eligible for aid under the scheme are 'maritime transport' activities in the sense of Section 2, 3rd paragraph, of the Maritime Guidelines, namely "*transport of goods and persons by sea*", as further specified in Section 3.1, 12 paragraph *et seq.*, of the Maritime Guidelines and as developed in the Commission's decision practice on the basis of the Maritime Guidelines.
- (83) As was described above in recital (20), ships involved in "*maritime shipping operations*" are admitted to the scheme. According to available information, this includes the transportation of freight and passengers and in so far is in line with the Maritime Guidelines.

- (84) Ships involved in *exploration* and *providing other services related to activities at sea* are also admitted, as described above in recital (20). The latter activity involves vessels servicing offshore installations (such as liaison ships, stand-by and supply vessels), cable-laying vessels, pipeline layers and research vessels. In the light of maritime-aid case practice²², the Commission has no objections against including such types of vessels in the scheme.
- (85) *Ancillary activities* (recital (20) above) and *yachts, fishing vessels and technical waterborne craft* (recital (23) above) are excluded from the scheme.
- (86) Revenues from *bare-boat chartering out* as described above recital (21) will be allowed under the scheme, in order to introduce an element of limited flexibility. The Croatian authorities committed to amend the scheme by the following limitations, in order to ensure that companies which are to a significant extent or even exclusively engaged in chartering out vessels, and thus cannot be considered to be engaged in maritime transport in the sense of the Maritime Guidelines, are excluded from the benefit of the tonnage tax scheme: Firstly, bare-boat chartering out activities must be related to temporary excess capacity; secondly, temporary excess capacity must be related to the beneficiary shipping company's own shipping services, for a period of up to 3 years; thirdly, excess capacity specifically acquired (bought or chartered) for chartering-out purposes is ineligible for tonnage taxation; lastly, the proportion of bare-boat chartered-out capacity should not exceed 20% of the shipping company's fleet under the tonnage tax scheme.²³
- (87) Bare-boat chartering out as proposed by the Croatian authorities is in line with the Maritime Guidelines, as the objectives in the common interest spelled out in the Maritime Guidelines "*maintaining and improving maritime know how and protecting and promoting employment for European seafarers*" and "*contributing to the consolidation of the Maritime cluster established in the Member States while maintaining an overall competitive fleet on world markets*" are safeguarded.
- (88) Pursuant to Section 3.1, 14th paragraph, of the Maritime Guidelines, the *towing at sea* of other vessels, oil platforms, etc. falls under the definition of 'maritime transport' if more than 50 % of the towage activity effectively carried out by a tug during a given

²² In its decision of 13.1.2009 in C 22/07, Denmark, the Commission accepted the inclusion of supply voyages with persons or equipment from harbour to installation on the continental shelf and back again, the transport of oil products (etc.) from the continental shelf to shore installations, tasks in connection with anchoring, cable-laying activities.

In its decision of 30.6.2004 in C 20/2003, Belgium, the Commission accepted the inclusion of vessels servicing offshore installations (such as liaison ships, stand-by and supply vessels).

In its decision of 27.4.2010 in N 714/2009, The Netherlands, the Commission accepted the inclusion of cable layers, pipeline layers, research vessels and crane vessels.

²³ According to the Commission's decisional practice, revenue from bareboat chartering-out activities is eligible for tonnage taxation provided such activities are necessary to reduce fleet overcapacities and are of a temporary nature; see e.g. Commission Decision of 11.12.2002 in State aid N 504/02, Ireland, recital (28); Commission decision of 13.5.2003 in State aid 737/2002, France, recital (2); Commission decision of 20.12.2011 in State aid N 448/2010, Finland, recital (32).

year constitutes 'maritime transport'; waiting time may be proportionally assimilated; towage activities which are carried out *inter alia* in ports, or which consist in assisting a self-propelled vessel to reach port do not constitute "maritime transport" for the purposes of this communication.

- (89) With respect to *tugboats*, the Commission welcomes that the Croatian authorities have committed to propose by 2015 clarifying amendments to the scheme's text, the Maritime Code, to ensure that only those tugboats are eligible which are involved for more than 50 % of the operational time during a given year in activities that constitute 'maritime transport' and that towage activities which are carried out *inter alia* in ports, or which consist in assisting a self-propelled vessel to reach port, do not constitute 'maritime transport'.
- (90) The Commission positively notes that only ships meeting EU/international standards relating to security, safety, environmental performance and on-board working conditions will be admitted to the scheme. *Inter alia*, the Commission notes that ships with an unsatisfactory track record in the sense of the Port State control rules are excluded from the scheme.
- (91) The Commission is satisfied that each and every ship under the Croatian tonnage tax scheme is commercially and strategically managed from the EEA and that the Croatian legislation will be further clarified in this respect to ensure that the relevant principle is always observed.
- (92) In conclusion, eligible activities and ships are in accordance with the Maritime Guidelines.

3.2.4.2. Eligible undertakings

- (93) Section 3.1 of the Maritime Guidelines implies that only ship-owners operating their own ships and other ship operators, such as charterers and ship managers in respect of vessels for which they have been assigned the entire crew and technical management, are eligible for fiscal aid such as tonnage taxation. As was described above in recital (28), the scheme is in line with this requirement. In particular, the benefits of tonnage taxation will be limited to providers of maritime transport service and to ship managers which assume from the owner the full responsibility for the vessel's operation.
- (94) The Commission welcomes that beneficiaries will have certain training obligations, as described above in Section 2.7. Said obligations clearly foster the attainment of the Maritime Guidelines' objectives, in particular maintaining and improving maritime know-how and protecting and promoting employment for European seafarers, and thus augments the aid's positive effects.
- (95) The Commission assessed whether the coverage of capital gains from the sale of ships, as described above in recital (29), is in line with the Maritime Guidelines. According to the Commission's decision practice, capital gains from the sale of ships are part of

the usual business of shipping companies and therefore can be included in a tonnage-tax scheme.²⁴

- (96) Nevertheless, a differentiated treatment should be applied to ships which were over-depreciated when entering a tonnage taxation system (as compared to depreciation based on the normal life-span of the ship) and thus bear hidden tax liabilities. In that respect, the Commission notes that as explained above in Section 2.11, hidden tax liabilities will be duly established by the tax authorities at the moment of the entry into the tonnage tax system and that alleviations with respect to such liabilities, if any, would be taken into account for the permitted aid ceiling. Moreover, the Commission notes that Croatia has committed to amend the scheme, as noted in recitals (52) and (53) above. The Commission deems such amendments a satisfactory solution to address potential cases of hidden tax liabilities.
- (97) According to the Commission decision on the Maltese tonnage tax scheme²⁵ shareholder revenues related to stakes in shipping companies do not constitute income arising from *shipping activities*, but rather income arising for the shareholders from their *investment activities*. Therefore, an exemption from taxation at shareholder level is not in line with the Maritime Guidelines. The Commission, however, notes the peculiarity of the Croatian shipping sector described above in recital (30), namely that shipping companies usually incorporate abroad subsidiaries as SPVs through which they acquire vessels, and which then own and, eventually, sell these vessels. Based on information provided by the Croatian authorities, the Commission finds that such SPV's are mere instruments which serve the sole purpose of satisfying the exigencies of international shipping banks. Hence, SPVs are not effectively in charge of any maritime transport activity. Rather, such activity will be fully exercised by the parent company owning such SPV. Admitting to the scheme ships indirectly owned by the shipping company through such SPVs, and thus treating them equally with directly owned ships, is in line with the Maritime Guidelines as the Croatian maritime companies perform their shipping activities with ships placed in SPVs. In the same vein, the Commission accepts the equal treatment of proceeds from the sale of a directly owned ship with the proceeds from the sale of a ship owned by a subsidiary-SPV, where the sale was executed by a transfer of shares of the subsidiary rather than the transfer of the ship itself.

3.2.4.3. Tonnage tax rates

- (98) Section 3.1, penultimate paragraph, of the Maritime Guidelines stipulates that, in order to keep an equitable balance of tonnage tax rates, the Commission will only approve schemes giving rise to a tax-load for the same tonnage fairly in line with the schemes already approved.
- (99) The Commission notes that the notified tonnage tax rates (see 2.8 above) differ from the ones applied by most Member States in so far as the rate in question is not based

²⁴ See e.g. Commission decision of 30.6.2004 in C 20/2003, Belgium.

²⁵ Commission decision of 25.07.2012 to initiate the formal investigation procedure in State aid case SA.33829 (C/2012), OJ C289 of 25.09.2012, see in particular recitals 91-94

on the so-called 'notional profit'²⁶. Nevertheless, the Commission notes that the ultimate level of taxation for Croatian companies is not significantly lower than the rates the Commission had approved for other Member States including Cyprus, for which the Commission had approved a similar lump-sum taxation system²⁷:

Table 2

| | Net Tonnage | | | | |
|---------|-----------------------|-----------------------|-----------------------|-----------------------|----------------------|
| | 0-1000 | 1001-10000 | 10001-25000 | 25001-40000 | >40000 |
| Cyprus | 36,50 € per 100 NT | 31,03 € per 100 NT | 20,08 € per 100 NT | 12,78 € per 100 NT | 7,30 € per 100 NT |
| Croatia | 35,44 € per 100 NT | 30,19 € per 100 NT | 19,69 € per 100 NT | 12,47 € per 100 NT | 7,22 € per 100 NT |
| Poland | 34.68€ per 100 NT | 24.27€ per 100 NT | 13.87€ per 100 NT | 6.94€ per 100 NT | 6.94€ per 100 NT |

- (100) Moreover, the ultimate tax burden from the Croatian tonnage tax is not smaller than the one the Commission had approved for Poland²⁸.
- (101) The Commission deems acceptable that under the scheme, tonnage tax or its equivalent paid abroad in respect of the same vessel are taken into account for the purpose of the application of the domestic tonnage tax (see above recital (36)), to avoid double taxation.
- (102) In conclusion, the Commission finds the notified Croatian tonnage tax rates to be overall in line with the rates approved for other Member States.

3.2.4.4. Flag link

- (103) One of the objectives of the Maritime Guidelines is that flagging or re-flagging to Member States' registers be encouraged through the aid. Accordingly, Section 3.1, 8th and 14th paragraphs, of the Maritime Guidelines require that at least part of a beneficiary undertaking's fleet flies EU/EEA flags (the 'flag-link requirement').
- (104) According to available information (described in 2.9 above), no shipping company neither entered, nor will enter the scheme without having a share of its fleet under EEA flags, and all tugboats which entered the scheme are EEA flagged tugboats.²⁹ The Commission welcomes the commitment of the Croatian authorities to introduce binding provisions that will ensure that also in the future, Croatian shipping companies continue to contribute sufficiently to the EEA flagging objective of the

²⁶ Notional profit is based on a lump sum determined on the basis of the net tonnage of each ship, to which is then applied the national corporate tax rate.

²⁷ Commission decision of 24.3.2010 in N 37/2010, Cyprus.

²⁸ Commission decision of 18.12.2009 in C 34/07, Poland.

²⁹ With respect to the single beneficiary with a 45% EEA-flagged share, the Commission notes even this ratio is better than the EEA average.

Maritime Guidelines and that no non-EEA tugboats are accepted under the tonnage taxation.

- (105) In addition, the Commission notes that the Croatian authorities will lay down additional requirements in the sense that no more than 75% of a beneficiary's fleet may consist of non-EEA time or voyage chartered vessels. Thus, aid to time/voyage charterers will contribute to the objectives of the Maritime Guidelines (either EEA flagging or maintenance of maritime know-how through a certain percentage of own maritime transport operations). The Commission accepts this commitment as the same approach was accepted by the Commission in the Commission's initial decision in the French tonnage tax case³⁰ and equivalent approach was accepted in the Commission's 2015 decision³¹.
- (106) In conclusion, the scheme is, and will remain, in line with the flag link requirement of the Maritime Guidelines and thus will contribute to an objective in the common interest, namely the flagging or re-flagging of ships to Member States' registers.

3.2.4.5. Restriction of aid to shipping activities; avoidance of spill-over into non-shipping activities

- (107) Pursuant to Section 3.1., last paragraph, of the Maritime Guidelines, in order to facilitate the development of the shipping sector and employment in the Community interest, fiscal advantages through tonnage tax schemes must be restricted to shipping activities; any spill-over of aid into non-shipping activities must be prevented.
- (108) On the basis of available information on the controls and sanctions put in place by the Croatian authorities (described above, Section 2.12), the Commission concludes that preferential tax treatment through the scheme is restricted to eligible activities in the sense of the Maritime Guidelines.

3.2.4.6. Aid limited to the minimum; transparency

- (109) Pursuant to Section 2, 2nd paragraph, of the Maritime Guidelines, State aid must always be restricted to what is necessary to achieve its purpose and be granted in a transparent manner.
- (110) As regards restriction to the necessary minimum, Section 11, 2nd paragraph, of the Maritime Guidelines sets a maximum level of aid, in order to avoid cumulation of aid to levels which are disproportionate to the objectives of the Community common interest and could lead to a subsidy race between Member States: total aid³² for the benefit of shipping companies may not provide any benefit greater than the benefit represented by a reduction to zero of taxation and social charges for seafarers and a

³⁰ Commission decision of 13.05.2003 in State aid case N737/2002, OJ C38 of 12.02.2004

³¹ After removal of the confidential information the decision will be published on http://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=3_SA_14551

³² Except for aid for training, restructuring aid, aid related to public service obligations and start-up aid for new short sea shipping services.

reduction to the level specified in Section 3.1, penultimate paragraph, of the Maritime Guidelines of corporate taxation of shipping activities.

- (111) According to information provided by the Croatian authorities, the only support measure in the maritime sector that supplements the tonnage tax system in question is the income tax exemption for individual seafarers described above in recital(58).
- (112) For the purpose of the assessment of the present tonnage tax scheme, the Commission finds that the income tax exemption for individual seafarers³³ does not affect compliance with the permitted aid ceiling.
- (113) The Commission also notes that any additional advantage in the form of alleviations of hidden tax liabilities will be handled within the limits of the aid ceiling (see recital (51) above).
- (114) As regards transparency, the Commission finds that the mechanism of the notified tonnage tax system (Sections 2.1, 2.5 above), and in particular the calculation of tax rates (Section 2.8 above), are transparent.
- (115) In conclusion, the Commission finds that the aid is limited to the minimum necessary, and is granted in a transparent manner.

3.2.5. Distortions of competition

- (116) Pursuant to Section 2, 2nd paragraph, of the Maritime Guidelines, Aid schemes should not be conducted at the expense of other Member States' economies and must be shown not to risk distortion of competition between Member States to an extent contrary to the common interest.
- (117) As was demonstrated above under Section 3.2.4.3, the notified tax rates do not significantly deviate from hitherto approved rates. Available information does not suggest that the scheme nurtures neither the flagging out nor corporate relocation from other Member States to Croatia.
- (118) In conclusion, the Commission finds that the scheme does not risk to distort competition contrary to the common interest.

4. CONCLUSION

- (119) The Commission regrets that the Croatian authorities have implemented the scheme prior to the Commission's authorisation (see Section 2.4, above). Nevertheless, having regard to the analysis set out above, the Commission concludes that the scheme under examination is compatible with the Maritime Guidelines.

³³ This income tax exemption for seafarers may be subject to a separate compatibility assessment by the Commission at a later stage, on the basis of Section 3.2 of the Maritime Guidelines.

5. DECISION

(120) The Commission concludes that the notified tonnage taxation scheme is compatible with the internal market on the basis of Article 107(3)(c) of the TFEU, as clarified by the Commission in the Maritime Guidelines. It has accordingly decided not to raise objections to the implementation of the scheme. The Commission adopted this decision on the basis of the Croatian authorities' commitments to clarify/amend the scheme, in the sense that:

- tonnage tax beneficiaries who have less than 60% of their fleet under EU/EEA flags are obliged to maintain or increase their share of EU/EEA flagged ships compared to the situation as at entry into the tonnage tax scheme;
- no new company is accepted to the tonnage tax scheme without having a share of its fleet under EEA flags;
- bare-boat chartering out activities must be related to temporary excess capacity; temporary excess capacity must be related to the beneficiary shipping company's own shipping services, for a period of up to 3 years; excess capacity specifically acquired (bought or chartered) for chartering-out purposes is ineligible for tonnage taxation; the proportion of bare-boat chartered-out capacity should not exceed 20% of the shipping company's fleet under the tonnage tax scheme;
- only tugboats engaged in 'maritime transport' for more than 50 % of their operational time during a given year are eligible for support under the scheme;
- only EEA flagged tugboats are accepted under the scheme;
- ships included in the tonnage tax scheme shall be strategically and commercially managed from an EU or EEA Member State;
- hidden tax liabilities for each ship of a company entering tonnage tax system are established and no alleviations are provided with respect to these liabilities beyond the aid ceiling;
- upon the exit of companies from the tonnage taxation the tax value of shipping assets is determined as if the shipping assets had all the time been subject to the standard taxation system;
- no more than 75% of a beneficiary's fleet may consist of non-EEA time or voyage chartered vessels;
- all eligible ships of a tonnage-taxed undertaking and its group must be covered by the scheme ('all-or-nothing rule');
- beneficiaries submit mandatory annual compliance declarations for all controllable parameters such as type of vessel, activities performed with the vessel, net tonnage, days in use, flag, types of operation and compliance with the aid ceiling.

- (121) The Commission reminds Croatia to inform the Commission of the final text of the amended scheme.
- (122) The Commission further reminds Croatia to submit annual reports on the application of the scheme.
- (123) Finally, the Commission reminds the Croatia to inform the Commission pursuant to Art 108(3) of the TFEU on all plans to alter this aid scheme, e.g. in order to include any non-shipping activities in the scheme, with the exception of the amendments committed by the Croatian authorities, enumerated above.

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European Commission
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State Aid Registry
B-1049 Brussels
Fax (32-2) 296 12 42
Stateaidgreffe@ec.europa.eu

Yours faithfully,
For the Commission

Margrethe Vestager
Member of the Commission