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**Subject: State Aid SA.53469 (2019/N) – Estonia
State aid in favour of maritime transport**

Sir,

1. PROCEDURE

- (1) On 12 February 2019, after informal contacts, the Estonian authorities pre-notified an envisaged special taxation scheme for maritime transport activities carried out by ship operators and ship managers (hereinafter: “the Tonnage Tax scheme”), as well as an envisaged scheme partially reducing labour-related costs for seafarers and their employers involved in such maritime transport activities (hereinafter: “the Seafarer Scheme”). By correspondence of 5, 10, 18 April 2019 and 10 June 2019, the Estonian authorities clarified a number of details concerning the above-mentioned measures.
- (2) By notification of 16 August 2019, Estonia notified, in accordance with Article 108(3) of the Treaty on the Functioning of the European Union (“TFEU”), the envisaged measures. By letter of 29 August 2019, the Commission sent a request for information to which the Estonian authorities replied on 4 September 2019. On 25 October 2019, the Estonian authorities agreed to extend the deadline to adopt a decision on the case until 15 December 2019.
- (3) For reasons of urgency, Estonia has exceptionally accepted that the decision be adopted and notified in English.

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2. DESCRIPTION OF THE MEASURES

2.1. Introduction

- (4) There is currently no special taxation scheme based on tonnage for shipping companies or other special income tax or social contributions scheme for seafarers or shipping companies in the area of maritime transport activities applicable in Estonia. A previous seafarer State aid scheme, which the Commission approved on 24 January 2013 (case SA.35825 (2012/N))¹, expired on 31 December 2015.
- (5) The purpose of the envisaged Tonnage Tax Scheme and Seafarer Scheme (hereinafter: “the measures”) is to raise the international competitiveness of the Estonian and, as a result thereof, the European shipping industry and maritime sector as a key sector of the economy in the international market.
- (6) For these reasons, the Estonian authorities plan to establish a Tonnage Tax Scheme for shipping companies (ship operators and ship managers), as an alternative system to the standard corporate income taxation in Estonia, and a special regime of seafarers’ labour taxes (personal income tax, social tax, unemployment insurance premiums, and mandatory funded pension contributions). Activities other than eligible activities would be subject to standard corporate income taxation and personal income tax as well as regular social security contributions. A table summarizing the current and the envisaged system is provided below:

Table 1: comparison between the current tax treatment and the new special tax treatment for shipping companies (ship operators and ship management companies)

Special tax treatment for shipping companies (tonnage tax)		
Category of tax	Current treatment	New special treatment
Corporate income tax	Deferred taxation: shipping companies (like all undertakings) do not pay income tax directly on profits. The 20% income tax is paid by the undertaking upon distribution of profits.	The existing income tax scheme will remain in place, but as an alternative it will be possible for ship operators and ship managers to opt for taxation on the basis of the Tonnage Tax Scheme. The company will not pay income tax additionally on income taxed under the Tonnage Tax Scheme, nor are distributed profits subject to corporate tax obligation.
Special tax treatment for seafarers and their employers (shipping companies)		
Category of tax	Current treatment	New special treatment

¹ State aid SA.35825 (2012/N) – Estonia – prolongation of the reimbursement scheme for the social tax in the maritime freight transport sector. The scheme expired on 31 December 2015 and the Estonian authorities confirmed that the last aid granting decision under the previous scheme was made on 13 August 2013.

Social tax (employer's tax)	33% of earnings	20% on a tax base of up to 750 euros
Unemployment insurance premiums (employer's share of 0.8% and employee's share of 1.6%; the employer withholds the premiums from the earnings)	2.4% of earnings	2.4% on a tax base of up to 750 euros ²
Funded pension contributions (employee's payment; employer withholds the premiums from earnings)	2% of earnings	2% on a tax base of up to 750 euros
Personal income tax (employee's tax; employer withholds tax from the pay or employee pays the tax)	20% of earnings	0% (on both residents and non-resident seafarers)

- (7) The Estonian authorities expect that aid recipients will in general be small and medium-sized shipping companies, but it is not excluded that large companies will also apply for the schemes.
- (8) The schemes are planned to bring vessels under the flag of Estonia as a Member State of the European Economic Area ("EEA"), and eventually under the flag of any other Member State of the European Economic Area.

2.2. The Estonian maritime sector

- (9) In 1993, Estonia had 79 internationally trading cargo ships flying under the Estonian flag. The last large cargo vessel³ left the Estonian flag in 2014. As a result, there is currently not a single cargo vessel under the Estonian flag engaged in international shipping, which has resulted in a decrease in the number of jobs on vessels sailing under the Estonian flag as well as in the Estonian onshore sector.
- (10) At the moment, only 18 EEA trading passenger ships of 500 GT or more are registered in Estonia⁴, while no internationally non-EEA trading passenger ships nor trading cargo of 500 GT or more are registered under the Estonian flag.

² Resident seafarers from third countries (i.e. countries that are not EU and EEA Member States) will be exempted from unemployment insurance premiums, as they have no possibility of receiving unemployment insurance benefits.

³ Cargo vessel of gross tonnage (GT) 500 or more.

⁴ The Estonian authorities also added that 475 "other vessels" are registered in Estonia. These include fishing vessels, small crafts and ships for domestic transport. These vessels are not eligible under the envisaged scheme.

According to the Estonian authorities, a direct implication of this is that around 5000 Estonian seafarers are not able to find employment on Estonian-flagged vessels and cannot generally access the Estonian social security system nor do they pay tax obligations in Estonia, as they are employed mostly on non-EEA flagged vessels.

- (11) The Estonian authorities therefore wish to take measures to stimulate the Estonian shipping industry, which in their view requires tax differentiation because, like in other Member States of the EU, the Estonian shipping industry is competing with third countries whose tax levels are considerably lower and/or where crewmembers do not pay any labour taxes.

2.3. Objectives and estimated aid impact

- (12) The ultimate goal of the envisaged reform is, through bringing internationally trading cargo and passenger ships of 500 GT or more under the flag of Estonia or any other Member State of the European Economic Area, to retain and increase shipping expertise with the aim of developing the maritime cluster, thus creating new jobs in the maritime sector for EEA citizens, supporting innovation, attracting investments and, finally, increasing tax revenue as well.
- (13) In a first stage, the legal acts will be amended to change the principles concerning taxation of undertakings operating in the shipping sector (ship operators and managers) and crew members (seafarers). At a second stage, other measures will be carried out in conjunction with the special tax treatment, such as electronic, convenient digital government services that will motivate shipping companies to register their ships in Estonian ship registers. Only the special tax regime (the first stage of the reform) is subject to the notification.
- (14) With the implementation of the notified measures, Estonia aims at contributing to the general objectives set out at Section 2.2 of the Maritime Guidelines, more in particular the following:

Improving a safe, efficient, secure and environment friendly maritime transport

- (15) The Estonian authorities submit that it will be ensured that the only ships that can be added or maintained in the registers⁵ are those that are in good technical condition, comply with international requirements, and do not harm the reputation of Estonia as a flag state.
- (16) In addition, Estonia has already acceded to the major conventions ensuring maritime safety and security and protection of the marine environment, while only in a few cases the ratification is currently in process⁶. The Estonian State commits that Estonian-flagged ships will comply with the ratified conventions.

⁵ The Estonian authorities submitted that following the reform, the current register of bareboat chartered ships will remain, and a second register of bareboat chartered ships will be created as a separate register.

⁶ Estonia is on the Paris MoU White List and therefore recognized as a quality flag. Paris MoU on Port State Control, White, Grey and Black List, available online at the following link: <https://www.parismou.org/detentions-banning/white-grey-and-black-list>

- (17) Also, to implement the Tonnage Tax Scheme, the ship operator or the provider of the ship’s technical management service must have assumed responsibility for organizing the maritime safety and technical service of a ship meeting the established conditions and has a corresponding certification. In addition, in order for the Tonnage Tax Scheme to be implemented, the provider of the crew management service must comply in full with and apply all the requirements of the Maritime Labour Convention (“MLC”) of the International Labour Organization; all the ships and crews managed by the service providers specified in the foregoing clauses must comply with international standards and requirements arising from the law of the European Union related to maritime security and safety, training and certification of seafarers, environmental conservation and working conditions on a ship (clause 52¹ (3) 1) and subsection 52¹ (13) of the Draft Income Tax Act).

Encouraging the flagging or re-flagging to Member States’ registers

- (18) The Estonian authorities submit that the schemes will contribute to the objectives of the Maritime Guidelines by encouraging the flagging or re-flagging to Member States’ registers.
- (19) Estonia forecasted that a number of additional Estonian-flagged vessels would accrue each year to the Estonian registries if all project activities will be successful. The following table summarizes the number of ships estimated to accrue to the Estonian registries from 2020 to 2025.

Table 2: expected ships accruing to Estonian registries

Year	2020	2021	2022	2023	2024	2025
Total ships	18	36	90	162	216	288

Contributing to the consolidation of the maritime cluster established in the Member States while maintaining an overall competitive fleet on world markets

- (20) The Estonian authorities submit that the final goal of the schemes is, through bringing ships under the Estonian flag, to retain and increase shipping expertise with the aim of developing the maritime cluster and the onshore sector, thus creating new jobs in the maritime sector for the citizens of the EEA, supporting innovation and attracting investment. The Estonian authorities add that according to a study on the European shipping sector⁷, one new job aboard a ship will create 3.8 jobs on shore. A table summarizing the impact of the schemes on the maritime cluster for each of the relevant years is also provided in the following section⁸.

Maintaining and improving maritime know-how and protecting and promoting employment for European seafarers

- (21) The Estonian authorities submit that currently there are over 10,000 Estonian seafarers⁹ with a very good education and experience. As such, the shipping sector has a great potential to be one of the engines driving the Estonian economy. For

⁷ Oxford Economics 2014: “The economic value of the EU shipping industry”.

⁸ See table 3, recital (23).

⁹ According to data from the Maritime Administration’s Estonian Seafarers Register.

these reasons, bringing ships under a European Economic Area flag will increase shipping-related know-how and this in turn will support the development of the onshore sector and job creation.

- (22) Thanks to the registration of new ships in the Estonian ship registers, according to the Estonian authorities seafarers will in the future have a greater opportunity to work on Estonian-flagged (and other EEA-flagged) vessels. As Estonian-flagged vessels are subject to Estonian laws, this would allow the State to better protect seafarers' social rights and give Estonian seafarers better access to the State social security system. At the moment, an estimated 5,000 Estonian seafarers work under the flags of foreign countries and a large share of them lack social security as they work on third-country-flagged vessels which do not offer the seafarers adequate levels of social security. As a result of the envisaged changes to the legislation, the social security situation for those Estonian seafarers who currently do not have access to Estonian social security will also improve.
- (23) The Estonian authorities add that at present Estonian seafarers have a problem finding a job when they no longer wish to work at sea. The shipping-related onshore sector has a minimum number of jobs and, because of that, the valuable resource of highly educated experienced maritime specialists gets lost. In view of these circumstances, if for instance seafarers had the opportunity to be hired by shipping companies in other positions (e.g. onshore), know-how would be retained by the sector, the State would receive tax revenue from their earnings and, upon acquiring sufficient experience, they would later be able to establish their own company, which will increase the number of jobs even further. The following table provides an overview of the impact of the measures on Estonian employment.

Table 3: forecasted number of additional jobs

	2020	2021	2022	2023	2024	2025
Total ships	18	36	90	162	216	288
Number of crew members	234	468	1 170	2 106	2 808	3 168
Total jobs in the onshore sector (direct impact)	0	51	152	406	862	1 470
Jobs – other sectors (indirect impact)	0	27	81	216	457	778
Total jobs in the onshore sector (direct and indirect)	0	78	233	621	1 319	2 248
Total employment in Estonia (prediction)	667,000	665,000	663,000	661,000	659,000	657,000
Number of onshore sector jobs created through maritime sector measures, expressed as a percentage of total employment in Estonia,	0.00%	0.01%	0.04%	0.09%	0.2%	0.34%

2.4. National legal basis

- (24) The national legal basis consists in amendments to the Income Tax Act, the Funded Pensions Act, the Social Tax Act and the Unemployment Insurance Act made by the Draft Act on the Amendment of the Law of Ship Flag and Ship Registers Act, Income Tax Act and, in connection therewith, other Acts. These amendments are laid down in the “Draft Act” and in the “New draft Act” (referred to together as “the Draft Act”).¹⁰
- (25) The Estonian authorities confirmed that the Draft Act includes a standstill clause and that the schemes will not enter into force before the approval of the Commission.

2.5. Duration

- (26) The Estonian authorities clarified that according to the standstill clause the new schemes will enter into force on 1 July 2020, subject to a positive decision by the European Commission, and will remain in force for six years. Therefore, the Tonnage Tax and the Seafarer schemes will expire on 30 June 2026. In addition, the Estonian authorities confirmed that prolongation of the schemes will be subject to a new notification to the Commission.

2.6. Tonnage Tax Scheme

- (27) Under the standard Estonian corporate income tax law, corporate profit is not taxed unless it is distributed (as dividends and other profit distributions). The corporate tax rate is 20% for all distributed corporate income. The standard Estonian corporate income taxation system is thus a system of deferred taxation. Therefore, if profits are not distributed, no tax obligation arises.
- (28) Under the envisaged Tonnage Tax Scheme, a resident company that incurs an income tax obligation in Estonia will have the option, as an alternative to the standard corporate income taxation system, to choose tonnage taxation (subsection 52¹ of the Draft Income Tax Act).
- (29) The peculiarity of the Tonnage Tax Scheme compared to the current ordinary procedure is the way taxable income (i.e. the tax base) is determined. While under ordinary procedure the undertaking’s distributed profits are taxed, under the Tonnage Tax Scheme the amount of taxable income derived from international transport of goods or passengers by sea is computed on the basis of the product of the net tonnage of the ship(s) in the undertaking’s use and the tax base ratios to be established based on each vessel’s net tonnage (see recitals (50) and (51)).
- (30) If an eligible undertaking (ship operator or ship manager) opts for the Tonnage Tax Scheme, this is binding for the undertaking until the expiry of the authorisation for State aid granted by the European Commission and as long as the conditions for application of the scheme are met. In case of a ship management company, the Tonnage Tax Scheme can be applied to income from the provision of ship crew management or technical management service corresponding to the applicable

¹⁰ The English translation of the consolidated text is available at: <https://www.riigiteataja.ee/en/eli/ee/519062017011/consolide/current>

conditions (see recitals (34)-(35)). The Estonian authorities clarified that under the Tonnage Tax Scheme, a ship management company will not be subject to rates more favourable than those of the ship operator.

- (31) As regards the financial impact of the Tonnage Tax Scheme, the Estonian authorities provided a summary table of the estimated aid amounts involved over the relevant years:

Table 4: summary of estimated aid amounts (tonnage tax)

Summary: aid amounts calculation						
	2020	2021	2022	2023	2024	2025
Estimated number of ships	18	36	90	162	216	288
Tax load under current legislation (EUR)	90,654	184,935	471,584	865 829	1,177.527	1,601,437
Tax load under new legislation (EUR)	43,532	88,806	226,456	415,773	565,452	769,014
Aid amount (EUR)	47,122	96,129	245,128	450,055	612,075	832,423
Aid intensity	52%	52%	52%	52%	52%	52%

2.6.1. Scope

2.6.1.1. Eligible undertakings

- (32) Under the proposed legislation, any tax resident company¹¹ (ship operators and ship management companies) that incurs an income tax obligation in Estonia will have the option to choose the Tonnage Tax Scheme as an alternative to the ordinary procedure for taxation of income derived from international transport of goods and passengers by sea¹². The residency of the aid recipient is relevant for determining the right and scope of taxation. In accordance with Article 8 of the agreements for the avoidance of double taxation and the prevention of fiscal evasion with respect

¹¹ According to subsection 6(2) of the Income Tax Act, a legal person, excluding a trust fund, is a tax resident if it is established pursuant to Estonian law. A tax resident is also a European public limited company (SE) and European association (SCE) whose location is registered in Estonia. A tax resident legal person pays income tax on the tax objects specified in sections 48 to 52 and withholds income tax on payments listed in Section 41. <https://www.riigiteataja.ee/akt/119112010007?leiaKehtiv>

¹² Based on subsection 13(5) and subsection 52¹(5) of the Draft Income Tax Act, for maritime transport to be considered as international, more than 50% of the voyages must take place (i) between an Estonian port and foreign port; (ii) between an Estonian port and an installation outside of the territorial sea of Estonia; (iii) between ports of a foreign country or foreign countries; or (iv) between a foreign port and a facility located off the shore. In particular, in case a ship provides scheduled passenger services, to be considered international at least 50% or more of the annual port of calls of the ship must be located outside the EEA.

to taxes on income and on capital¹³, Estonia has an unlimited right to tax profits earned by tax resident companies from international transport. As the Estonian authorities explained, if Estonia has no right to tax profits derived by a company from international transport, there is no need to apply the Tonnage Tax Scheme, either.

- (33) In the case of *ship operators*, pursuant to subsection 52¹ (3) of the Draft Income Tax Act, a tax resident company may apply the Tonnage Tax Scheme to income from international transport of goods or passengers by sea, not including scheduled passenger transport¹⁴ in the EEA, if it meets the following cumulative requirements:
- i. it has assumed responsibility for managing the maritime safety and technical service of a ship meeting the conditions provided for in clause 13(5)(1) of the Draft Income Tax Act and has a corresponding certificate;
 - ii. the strategic, commercial and technical management decisions related to the operation of the ship are made in Estonia;
 - iii. decisions related to management of the vessels' crew are made in a European Economic Area Contracting State;
 - iv. it is not an undertaking in difficulty within the meaning of Guidelines on State aid for rescuing and restructuring non-financial undertakings in difficulty established by the European Commission;
 - v. it has not failed to perform the obligation to repay the State aid declared illegal and incompatible with the internal market on the basis of the decision of the European Commission.
- (34) In the case of *ship management companies*, subject to subsection 52¹ (13) of the Draft Income Tax Act, the conditions to be imposed on ship managers to be allowed to apply the Tonnage Tax Scheme are the following:
- i. the ship is used for international maritime transport of goods or passengers and for activities directly related thereto (ancillary activities), not including ships providing scheduled passenger transport services in the European Economic Area;
 - ii. the gross tonnage of the vessels is at least 500;
 - iii. all vessels and crews managed must comply with international standards and requirements arising from the law of the European Union related to maritime security and safety, training and certification of seafarers, environmental conservation and working conditions on a ship;

¹³ Model Tax Convention on Income and on Capital: Condensed Version 2017, <http://www.oecd.org/ctp/treaties/model-tax-convention-on-income-and-on-capital-condensed-version-20745419.htm>

¹⁴ Estonia clarified that "scheduled services" include regular services, ie regular voyages according to a published timetable.

- iv. at least 60% of the gross tonnage of ships included in the calculation of the tonnage scheme used by the company must be registered under an EEA flag;
 - v. it is not an undertaking in difficulty within the meaning of Guidelines on State aid for rescuing and restructuring non-financial undertakings in difficulty established by the European Commission;
 - vi. it has not failed to perform the obligation to repay the State aid declared illegal and incompatible with the internal market on the basis of the decision of the European Commission
- (35) In addition, *ship management companies* wishing to apply the Tonnage Tax Scheme must also meet the following conditions:
- i. in case of crew management, the service provider makes management decisions in Estonia and fully adheres to and applies all the requirements of the Maritime Labour Convention of the International Labour Organization;
 - ii. in case of technical management, the service provider makes management decisions in Estonia, assumes responsibility for managing the maritime safety and technical service of the ship and has a corresponding certificate;
 - iii. the service provider has at least one crew manager and four other employees to manage crews of up to ten ships; the service provider has at least two crew managers and eight other employees to manage crews of more than ten ships;
 - iv. the service provider has at least one technical manager and four other employees to manage crews of up to ten ships; the service provider has at least two technical managers and eight other employees to manage crews of more than ten ships;
 - v. at least 51% of the employees are citizens of a EEA Contracting State.

2.6.1.2. *Eligible activities*

- (36) The Tonnage Tax Scheme is only applicable in relation to eligible activities, which are exhaustively listed in the Draft Act. The tax base for any other activities is calculated in accordance with the general corporate income tax rules. Eligible activities comprise the core activity of maritime transport as well as ancillary activities. Non-eligible activities are not listed in the Draft Act as the scheme can only be applied to eligible activities listed in the law and these lists are closed lists.
- (37) Core maritime activities comprise:
- Transport of passengers or goods for a fee;
 - Granting cabins for use for a fee;
 - Sale of food and drinks for immediate consumption on board;
 - Granting a vessel for use for a fee on the basis of a charter party except chartering out on the basis of a bareboat-charter party.

- (38) Ancillary activities comprise:
- provision of services or sale of goods, usually on passenger ships, provided that these activities are directly related to the transport of passengers by sea;
 - salvage;
 - loading, unloading and securing of cargo, if these activities are carried out by crew members of the ship of the tax resident company. In this regard, the Estonian authorities confirmed that such activities are deemed ancillary only if they are not rendered to third parties, even if such third parties are belonging to the same group of the companies with the tax resident company (for instance companies operating within the port area). In addition, the Estonian authorities confirmed that if these activities are rendered to third parties, the revenues from these activities will be taxed under regular taxation and the Tonnage Tax Scheme will not apply; finally, revenues coming from these activities are subject to the control mechanism explained at recital (124);
 - granting containers or other tanks for use for a fee;
 - granting a space on board for use for a fee to a seller of products or a provider or services;
 - granting an advertising space on board for use for a fee;
 - mediation of sightseeing during a voyage to a passenger on a ship, provided that the passenger's cabin remains in his/her use.
- (39) The Estonian authorities confirmed that the Tonnage Tax Scheme will be applied to revenues from ancillary activities (activities directly related to international transport of goods and passengers by sea) provided that such income does not exceed 50% of the total eligible income of eligible vessels. The Estonian authorities explained that the relevant sections of the Draft Act clarify that income received from ancillary activities is taxed on the basis of the Tonnage Tax Scheme if it does not exceed 50% of the income received from the activities of international transport of goods and passengers by sea of an eligible vessel.

2.6.1.3. *Eligible vessels*

- (40) Generally, vessels operating maritime transport activities are eligible to benefit from the Tonnage Tax Scheme. The Estonian authorities submitted that the situation with Estonian passenger shipping is currently sufficiently good, consisting at present of 18 over 500 GT Estonian-flagged passenger vessels. For this reason, according to a decision by the Estonian Government, vessels providing scheduled passenger services in the European Economic Area are not allowed to participate in the Tonnage Tax scheme (and in the Seafarer Scheme). The Estonian authorities thus clarified that the scheme will only be applicable to the following vessels:

- i. vessels used for international¹⁵ maritime transport of goods or passengers and for ancillary activities directly related thereto, not including vessels providing scheduled passenger service in the European Economic Area and vessels sailing mainly between Estonian ports; and
 - ii. vessels whose gross tonnage is at least 500 GT¹⁶; and
 - iii. vessels flying the flag of an EEA Contracting State (save for the applicable limitations in terms of EEA flag-share (see recitals (101) to (107)).
- (41) In addition, vessels have to meet the standards set out in international conventions. This requirement is stipulated in the provision of the eligible ship operators and eligible ship management companies (clauses 52¹ (3)1) and 52¹ (13)3) of the Draft Income Tax Act).
- (42) Also eligible under the Tonnage Tax Scheme are activities carried out on towage and dredging vessels, provided that 50% of the annual operations of the vessels' activities constitute maritime transport and only in respect of such transport activities.

2.6.1.4. Eligible revenue for each eligible vessel

- (43) Revenues eligible for the calculation of the tax base under the Tonnage Tax Scheme are in principle revenues coming from international transport of goods or passengers by sea (core maritime transport activities, see recital (37) above).
- (44) However, revenues considered ancillary to the core maritime transport activities (see recital (38) above) can also benefit from the Tonnage Tax Scheme up to a maximum of 50% of the total eligible income generated by maritime transport activities for each eligible vessel.
- (45) The Tonnage Tax Scheme will be also applied to ship management's income provided that such income was derived from the provision of crew management or technical management.

2.6.2. Time and voyage charter-in

- (46) Time and voyage charterers are shipping companies which rent vessels with crew from other ship owners to satisfy the needs of their own clients. Under tonnage tax schemes, maritime transport activities carried out with chartered-in vessels (i.e. vessels rented from other ship owners) with crew are eligible under certain conditions, namely if they fulfil the same requirements as the vessels owned and managed by the ship-owner.
- (47) According to subsection 52¹(4) of the Draft Income Tax Act, at least 25% of the gross tonnage of the vessels included in the calculation of the Tonnage Tax Scheme has to be owned and operated by the ship operator. Thus, the gross tonnage of chartered-in vessels with crew (time and/or voyage) used by the company may not

¹⁵ For maritime transport to be considered international according to the Draft Act, see fn[12].

¹⁶ The reason for the restriction of the gross tonnage for the ships below 500GT is driven from the fact that international conventions and regulations apply fully to ships from 500GT.

exceed 75% of the gross tonnage of the ships included in the calculation of the tonnage scheme. In addition, at least 60% of the gross tonnage of the ships included in the calculation of the tonnage scheme used by a tax resident company must be registered under an EEA flag.

2.6.3. *Bareboat charter-out*

- (48) The Estonian authorities clarified that chartering out a ship on the basis of a bareboat charter party as other than intra-group transaction is considered an eligible activity only if the following conditions are met:
- a. the reason for chartering out is the excess capacity of the tonnage of a ship temporarily not used in business by the tax resident company due to other reasons than purchasing or chartering a ship for the purpose of chartering it out; and
 - b. the ship is chartered out for no longer than three years; and
 - c. the chartering out does not exceed 50% of the gross tonnage of vessels used by the tax resident company and included in the calculation of the tonnage scheme.
- (49) The Estonian authorities added that as only up to 50% of the tonnage taxed fleet can be bareboat chartered-out, the remaining percentage will in any case be operated by the tonnage tax beneficiary.

2.6.4. *Level of tonnage tax*

- (50) The tax to be paid under the Tonnage Tax scheme is based on the amount of net tonnes operated (subsection 52¹(19) of the Draft Income Tax Act). The income amount subject to tax under the Tonnage Tax scheme is calculated as the product of the net tonnage of the ship used by the company implementing the Tonnage Tax Scheme and the corresponding tax base ratios as follows:
- Up to 1,000 net tonnes: EUR 0.84 daily tax base for each 100 net tonnes,
 - Between 1,001 and 10,000 net tonnes: EUR 0.62 daily tax base for each 100 net tonnes,
 - Between 10,001 and 25,000 net tonnes: EUR 0.40 daily tax base for each 100 net tonnes,
 - Above 25,000 net tonnes: EUR 0.20 daily tax base for each 100 net tonnes.
- (51) According to subsection 52¹(20) of the Draft Income Tax Act the tax base ratios set out above are applied depending on the age of the ship as follows:
- i. 50% for ships not older than five years;
 - ii. 75% for ships older than five years but not older than ten years; and
 - iii. 100% for ships that are older than ten years.

Applying the abovementioned tax rates, all vessels covered that are available to the company will be considered based on calendar days.

2.6.5. Flag link requirements

- (52) Under the Tonnage Tax Scheme (subsection 52¹(4)2) of the Draft Income Tax Act), at least 60% of the gross tonnage of the vessels that a company wants to include in the Tonnage Tax Scheme must be registered under the flag of one or more EEA Contracting State(s). The same requirements apply for ship management companies providing crew and/or technical management. For dredging and towage vessels, such flag-share requirement is increased to 100%.

2.7. Seafarer Scheme

- (53) The aim of the Seafarer Scheme is to reduce fiscal and other costs and burdens of EEA shipping companies and seafarers towards levels in line with world norms. The special regime is aimed at stimulating the development of the sector by attracting more vessels under Estonian flag and therefore providing more sea-going positions to European seafarers. All measures are envisaged to maintain and improve EEA maritime know-how.
- (54) As a result of the envisaged Seafarer Scheme, the following treatment will be foreseen for eligible employers/seafarers (see also table 1, recital (6)):
- The social tax paid by the employer will be set at 20% instead of 33% and only on a tax base of up to 750-euro, instead of on the actual earnings;
 - The personal income tax rate for seafarers working on ships covered by the special tax treatment will be of 0% (for both resident and non-resident seafarers), instead of 20% on earnings; and
 - The unemployment insurance premiums' rates will remain the same, at 2,4% (0,8% of which for the employer and 1,6% of which for the employee), but the valid tax rates will be paid on the tax base, i.e. up to 750 euros per month worked, instead of the actual earnings;¹⁷ and
 - The funded pension contribution rates will also remain the same, at 2%, but the valid tax rates will also be paid on the tax base, i.e. up to 750 euros per month worked, instead of the actual earnings.

The following table summarizes the estimated aid amounts following the new regime:

Table 5: summary of estimated aid amounts (Seafarer Scheme)

Seafarer Scheme: aid amounts calculation ¹⁸	2020	2021	2022	2023	2024	2025

¹⁷ Resident seafarers from third countries will be exempted from unemployment insurance premiums as they have no possibility of receiving unemployment insurance benefits.

¹⁸ Explanatory note from the Estonian authorities: the number of crew members is derived from the number of ships in the register: based on this assumption, at the end of 2020 there will be 18 new ships in the register and thus 234 seafarers (consisting of seafarers from both EE, EEA and third countries); the number of months worked in a year was estimated in 8; the average net salary per month was based on

Estimated number of ships	18	36	90	162	216	288
Number of crewmembers (Registers I+II)	234	468	1 170	2 106	2 808	3 168
Average net salary (EUR)	2,883	2,969	3,059	3,150	3,245	3,342
Tax base under the special tax regime (EUR)	750	750	750	750	750	750
Taxes payable under the new regime (EUR)	286,978	573,955	1,434.888	2,582.798	3,443.731	3,885.235
Taxes payable under ordinary tax treatment (forgone fiscal revenues) (EUR)	3,991.705	8,222.913	21,174.000	39,256.597	53,912.393	62,648.965
Amount of aid (EUR)	3,704.728	7,648.958	19,739.112	36,673.798	50,468.662	58,763.730
Aid intensity	93%	93%	93%	93%	94%	94%

2.7.1. Scope of the scheme

- (55) According to the Estonian authorities, the incentives granted on the basis of the special seafarer workforce tax treatment are applicable only to subjects eligible for the special tax treatment, i.e. seafarers and employers whose seafarers work on eligible vessels. In addition, the Seafarer Scheme can be applied only if the vessels are used for international transport of goods or passengers or activities directly related thereto, as described above in recitals (40) to (42).
- (56) Employment income from seafarers working on board vessels used for activities other than eligible maritime transport activities and ancillary activities will be subject to regular personal income taxation and social security contributions.

the current system (in 2020 it will be 2883 euros), and grows within years; the tax base is that of 750 euros a month as set out by the new legislation.

2.7.1.1. Scope of the exemption from income tax

- (57) The remuneration earned in this capacity by Community seafarers working on vessels eligible for the special workforce treatment will be subject to a 0% income taxation.

2.7.1.2. Scope of the partial exemptions from social security contributions

- (58) Community seafarers working on the vessels eligible for the special workforce treatment will be entitled to social security protection at reduced contributions rates compared to the general contributions rates (see recitals (6) and (54)).

3. ASSESSMENT OF THE MEASURES

3.1. Tonnage Tax Scheme

3.1.1. Existence of aid

- (59) According to Article 107(1) 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".
- (60) It follows that, in order for a measure to be qualified as State aid within the meaning of Article 107(1) TFEU, the following four cumulative conditions have to be met:
- It has to be imputable to the Member State and granted out of State resources.
 - It has to confer an economic advantage on undertakings.
 - The advantage has to be selective.
 - The measure has to distort or threaten to distort competition and affect trade between Member States.
- (61) In this respect, the Commission first of all notes that Estonia accepts the State aid qualification under Article 107(1) TFEU of the notified measure.
- (62) Furthermore, the Tonnage Tax Scheme will provide companies commercially active in the field of maritime transport with the possibility to opt for an advantageous taxation compared to all other companies taxable in Estonia. Therefore, the Commission considers that Estonia will forego fiscal revenue and that, therefore, the Tonnage Tax Scheme involves State resources. Moreover, since the measure is implemented through national legislation, it is imputable to Estonia. Also, the measure exonerates the commercially active companies concerned from a fiscal levy which they normally would have to pay and, thus, involves an advantage.
- (63) Moreover, the measure is selective since (i) companies normally have to pay corporate income tax (reference framework), (ii) the Tonnage Tax Scheme is

specifically applicable to companies / activities in the maritime transport sector (derogation from reference framework) and (iii) there is no justification apparent or invoked by Estonia by the nature or general scheme of the fiscal reference framework. Finally, in view of other possible means of transport and the global scale of maritime transport, the Tonnage Tax Scheme is liable to distort competition and affect trade within the liberalised European shipping market.

- (64) It follows that the measure involves State aid in the sense of Article 107(1) TFEU.

3.1.2. Legality of the aid

- (65) The Commission takes note of the commitment of the Estonian authorities to respect the standstill obligation laid down in Article 108(3) TFEU and not to enforce the regime until the Commission adopts a decision authorising the notified measures.

3.1.3. Compatibility of the aid

- (66) Pursuant to Article 107(3)(c) TFEU, aid to facilitate the development of certain economic activities or of certain economic areas may be considered compatible with the common market, where such aid does not adversely affect trading conditions to an extent contrary to the common interest.

- (67) The Commission has issued guidelines for the application of Article 107(3)(c) TFEU with regard to State aid to maritime transport ("Maritime Guidelines"). The Commission has also issued a Communication providing guidance on State aid to shipmanagement companies ("Shipmanagement Communication").¹⁹ Aid in favour of the maritime sector must therefore be examined in the light of these texts.

- (68) The Commission considers that the Tonnage Tax Scheme is in line with the Maritime Guidelines, the Shipmanagement Communication and the Commission's decisional practice. This conclusion is based on the following findings:

3.1.3.1. Objectives of the scheme

- (69) According to their chapter 2.2, the Maritime Guidelines are intended to clarify what State aid schemes may be introduced in order to support the Union maritime interest, with the aim of: improving a safe, efficient, secure and environmental friendly maritime transport, encouraging the flagging or re-flagging to Member States' registers, contributing to the consolidation of the maritime cluster established in the Member States while maintaining an overall competitive fleet on world markets, maintaining and improving maritime know-how and protecting and promoting employment for European seafarers, and contributing to the promotion of new services in the field of short sea shipping following the White Paper on Community transport policy.

- (70) The Commission notes that the objectives of the Tonnage Tax Scheme as described in section 2.3 above are in line with the objectives as described in the Maritime Guidelines. The Tonnage Tax Scheme aims at guaranteeing economic conditions

¹⁹ Communication from the Commission providing guidance on State aid to shipmanagement companies, OJ C 132, 11.6.2009, p. 6-9.

in order to maintain the competitiveness of the European shipping sector, attract investments and achieve economic growth, increase the EEA's maritime fleet and create skilled maritime employment in the EEA.

- (71) The compatibility condition described in recital (69) above is therefore fulfilled.

3.1.3.2. *Scope*

Eligible undertakings

- (72) As explained in section 2.6.1. above, any tax resident company that incurs an income tax obligation in Estonia will have the option, as an alternative to the ordinary procedure for taxation of income derived from international transport of goods and passengers by sea, to choose the Tonnage Tax Scheme.
- (73) The Commission notes that the conditions laid down in Section 3.1 of the Maritime Guidelines are fulfilled, both in case of ship owning companies and ship managers. The Commission also notes that, with regard to crew managers, all of the additional requirements set out in the Shipmanagement Communication, in sections 6.1 and 6.2, are fulfilled. In particular, Estonia has ratified and applies both the Convention of the International Maritime Organization on the Standards of Training, Certification and Watchkeeping for Seafarers (STCW) and the Maritime Labour Convention (MLC) of the International Labour Organization. These conventions are also implemented into national law. The MLC is also implemented by the Estonian Seafarers Employment Act.

Eligible vessels

- (74) The vessels eligible under the Tonnage Tax Scheme are described in section 2.6.1.3., recitals (40) et ss.
- (75) Only genuine maritime transport activities are eligible for aid under the Maritime Guidelines. Maritime transport is defined as the transport of goods and persons by sea between ports, as well as between a port and an offshore installation/structure²⁰. Activities which are not maritime transport, such as the activities carried out by fishing boats, exploitation of construction sites, and inland transport of containers, are not eligible.
- (76) The Commission notes that, as explained in section 2.6.1.3., vessels eligible to benefit from the Tonnage Tax Scheme are vessels operating maritime transport activities.

Eligibility of towage and dredging vessels

- (77) In line with the Maritime Guidelines, activities carried out on towing vessels are only eligible to benefit from the Tonnage Tax scheme provided that 50% or more of the annual operations of the vessel's activities constitute maritime transport and only in respect of such transport activities. Eligible tugboats and dredgers are only those registered in an EU/EEA State, with a gross tonnage of at least 500 GT and providing their activities outside a port and outside the territorial sea of Estonia.

²⁰ Cf. section 2 of the Maritime Guidelines – Scope and general objectives of the revised State aid guidelines.

Moreover, separate accounting for maritime transport activities and non-eligible other activities is required.

- (78) The Commission notes that such conditions are also respected, as explained in section 2.6.1.3., recital (42).

Conclusion

- (79) The vessels considered eligible by Estonia for the Tonnage Tax Scheme are also considered eligible by the Commission. The Tonnage Tax Scheme thus is in line with the Maritime Guidelines, the Shipmanagement Communication and the Commission's case practice in this respect.

Eligible revenue for each eligible vessel

- (80) The Commission's decision-making practice distinguishes between:
- Core revenues from maritime transport activities: core revenues are revenues from ticket sales or fees for cargo transportation and, in case of passenger transportation, letting of cabins in the context of maritime voyage and sale of food and drinks for immediate consumption on board. These revenues are directly eligible for a tonnage taxation scheme.
 - Non-core (ancillary) revenues (e.g. advertisements in vessels) from maritime activities: Ancillary revenues are other types of revenues which are frequently provided on board (especially in passenger transport) and which do not threaten to excessively distort competition with land-based providers, who are taxed according to the general rules of taxation. Examples of ancillary services would be the rental of advertising billboards on-board; the sale of goods and the provision of services customarily offered on passenger ships, including spa, hairdresser services, gambling and other entertainment services; the renting out of ship premises to shop and services' operators, the intermediation in provision of local excursions, etc. These revenues are eligible only insofar as they do not exceed 50% of the total gross eligible revenues from the operation of a given vessel. In addition, land-based services, such as local excursions or road part transportation included in the overall service package must be bought-in either from unrelated companies or at arm's length price from the same group's entities, which are subject to usual income taxation.
 - Contracts non-customary and unrelated to maritime transport: such as acquisition of cars, livestock, property, are ineligible revenues (neither as core nor as ancillary revenues).
- (81) The Commission agrees that the notified scheme, which exhaustively lists core and ancillary activities, is in line with the requirements listed above. The Commission also agrees that, in the light of the exhaustive lists provided by the Estonian authorities, the activities listed in recital (37) would correspond to typical genuine core maritime transport activities, and the activities listed in recital (38) would correspond to typical ancillary activities.
- (82) Moreover, in relation to these requirements, the Commission notes that, as explained above in section 2.6.1.4., only revenue generated by maritime transport activities (core revenues) and revenues derived from activities ancillary to maritime transport (non-core revenues), only up to a maximum of 50% of the total income

generated by maritime transport activities of each eligible ship, can benefit from the Tonnage Tax Scheme.

3.1.3.3. *Ring-fencing measures*

- (83) In order to enable the individual monitoring of revenues, expenses and losses from eligible and non-eligible activities and vessels, the companies opting for the Tonnage Tax Scheme are required to separate accounts accordingly.
- (84) The Commission notes that in accordance with Section 16 of the Accounting Act²¹ a requirement of separate accounting applies to companies' eligible and ineligible activities. As such, companies opting for the Tonnage Tax Scheme are required to organise their accounts in such a way as to enable separate accounting of eligible, ancillary and ineligible activities. Revenues from ineligible activities will be taxed under the ordinary procedure.
- (85) The Estonian authorities emphasized that, together with the Tonnage Tax Scheme, a set of ring-fencing measures will be put in force to limit abuses, namely:
- application of market conditions to the relations between tonnage taxed companies and other companies of the same group, as well as to the transactions inside the company between economic units that apply different taxing principles (transfer pricing);
 - the Tonnage Tax Scheme would be binding until the conditions for application of the Tonnage scheme are met, but no longer than the expiry of the decision of the European Commission authorising the grant of the State aid;
 - if the right to apply the Tonnage Tax Scheme has been lost, the taxpayer only has the right to re-apply the Tonnage Tax Scheme following the expiry of the decision authorizing the European Commission to grant appropriate State aid, provided that the Commission has granted new State aid authorization and that the conditions for the implementation of tonnage arrangements are met;
 - the taxpayer will not be able to treat part of their eligible ships under the Tonnage Tax Scheme and another part under the regular corporate income taxation ('all or nothing rule');
 - all of the eligible income and expenditures from eligible ships of the tonnage tax beneficiary would have to be covered by the Tonnage Tax Scheme.
- (86) Moreover, the Tonnage Tax Scheme was developed with a focus on other precautionary measures for companies where only a part of their activity meets the conditions for application of the Tonnage Tax Scheme, in order to prevent income taxable under regular taxation from being shifted to the Tonnage Tax Scheme (the so-called spill-over effect). Thus, measures for the application of principles for distribution of income and expenses related to the tonnage tax company's different type of activities were taken. Based on these measures, accounting must make it possible to distinguish which part of the income or expenses are related to an

²¹ Accounting Act (<https://www.riigiteataja.ee/en/eli/506112017002/consolide>)

operating activity based on a different taxation scheme (Section 16 of the Estonian Accounting Act).

- (87) Finally, the Estonian authorities committed to amend their Draft Act to reflect the Commission's practice on the 'all or nothing' clause for group of companies. In this regard, the Commission underlined that a group-level approach is required in the context of tonnage tax cases, so that if one entity within a group opts for the Tonnage Tax Scheme, all other eligible entities must do so. As a result, to avoid risks of circumvention, tonnage tax requirements should be calculated for all eligible entities of a group taken together rather than at a company-level.
- (88) The Tonnage Tax Scheme thus is considered in line with the Maritime Guidelines and the Commission's case practice in this respect.

3.1.3.4. *Time and voyage charter-in*

- (89) Time and voyage charterers (as described in section 2.6.2. above) are providers of maritime transport services and are normally covered by the Maritime Guidelines. However, such companies may only benefit from tonnage taxation if they contribute to an objective of the Maritime Guidelines, notably the development of the EEA flag or the preservation of EU know-how or a combination of the two.
- (90) This is the case if one of the following conditions is fulfilled: (i) in addition to time/voyage chartered vessels equipped and manned by other companies, the tonnage tax beneficiary has in its fleet also vessels for which it ensures crew and technical management and provided such vessels constitute at least 20% of the total tonnage taxed fleet; or (ii) the share of the vessels that are both non-EEA and time/voyage chartered does not exceed 75% of the beneficiary's fleet under tonnage tax, or (iii) at least 25% of the beneficiary's entire fleet is EEA-flagged. In all mentioned cases, the beneficiary stays under the separate obligation to maintain/increase the share of EEA-flagged tonnage of its own fleet (owned vessels or chartered in on a bareboat basis).
- (91) Based on clause 52^l(4)1) of the Draft Income Tax Act, in order to implement the Tonnage Tax Scheme, at least 25% of the gross tonnage of the ships included in the calculation of the Tonnage Tax Scheme in use by the ship operator must be in the ownership of, or in use on the basis of a bareboat charter agreement, by the ship operator. In addition, time and voyage chartered-in vessels must also comply with the 60% flag-link requirement (see recital (52)) to apply the Tonnage Tax Scheme.

Conclusion

- (92) The Tonnage Tax Scheme thus is in line with the Maritime Guidelines and the Commission's case practice in this respect.

3.1.3.5. *Bareboat charter-out (BBO)*

- (93) In principle, BBO is not a maritime transport activity, but rather a leasing activity, as the main risk for the transport rests with the lessee and not the lessor. Unfair competition to the detriment of genuine leasing companies which do not benefit from tonnage tax but which come under the normal corporate tax has to be avoided. Therefore, BBO activities may only be allowed for tonnage tax to address a situation of temporary (maximum 3 years) overcapacity.

- (94) In order to be eligible for tonnage taxation, the Commission has considered in its decision practice that:
- bareboat chartering out contracts must be restricted to a maximum period of three years;
 - temporary excess capacity must be related to the beneficiary's own shipping services, i.e. excess capacity specifically acquired (bought or chartered) for chartering-out purposes is ineligible for tonnage taxation; and
 - at least 50% of the tonnage taxed fleet must still be operated by the tonnage tax beneficiary. EEA intra-group BBO transactions are eligible without any limitations.
- (95) Intra-group bareboat charter activities are always eligible without restrictions, since the beneficiary as a group performs maritime transport through an intra-group leasing structure.
- (96) In the present case, as evidenced at recitals (48) and (49) above, the Commission notes that based on subsection 52¹(10) of the Draft Income Tax Act, bareboat charter-out activities are eligible subject to the three above-mentioned conditions.

Conclusion

- (97) The Tonnage Tax Scheme thus is in line with the Maritime Guidelines and the Commission's case practice in this respect.

3.1.3.6. Level of Tonnage Tax

- (98) According to section 3.1 of the Maritime Guidelines "*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 following table below provides an overview of tonnage tax base ratios in schemes previously approved by the Commission and the Estonian Tonnage Tax Scheme.

Table 6: Tonnage tax rates in schemes previously approved by the Commission and the Estonian Tonnage Tax Scheme.

Tonnage	Taxation base under tonnage tax regimes per 100 net tonnes per day in euro														
(Net tonnes)	NL	DE	DK	UK	ES	IRL	FIN	FR	BE	SL	PL	LT	IT	PT	EE
Up to 1,000	0.91	0.92	0.94	0.97	0.9	1	1.38	0.93	0.9	0.9	0.5	0.93	0.9	0.75	0.84
1,001 –10,000	0.67	0.69	0.67	0.73	0.7	0.75	1.03	0.71	0.7	0.67	0.35	0.67	0.7	0.6	0.62
10,001 –25,000	0.46	0.46	0.4	0.48	0.4	0.5	0.69	0.47	0.4	0.4	0.2	0.43	0.4	0.4	0.40
25,001 –40,000	0.23	0.23	0.27	0.24	0.2	0.25	0.57	0.24	0.2	0.2	0.1	0.27	0.2	0.2	0.20
40,001 –50,000	0.23	0.23	0.27	0.24	0.2	0.25	0.57	0.24	0.05	0.2	0.1	0.27	0.2	0.2	0.20
Over 50,000	0.05	0.23	0.27	0.24	0.2	0.25	0.57	0.24	0.05	0.2	0.1	0.27	0.2	0.2	0.20

Conclusion

- (100) Based on the tax loads and tonnage tax base ratios as described above (for details see above section 2.6.4), the Commission observes that the tax loads and the envisaged tax rates are fairly in line with tonnage tax schemes previously approved by the Commission. The Tonnage Tax Scheme thus is in line with the Maritime Guidelines and the Commission's case practice in this respect.

3.1.3.7. *Flag link requirements and national flagging restrictions*

- (101) In line with chapter 3.1 of the Maritime Guidelines, beneficiaries must have a certain share of their fleet under EU/EEA flags. If the share of EEA-flagged vessels of the entrant's fleet is above 60%, there is no obligation for the beneficiary, as long as the share remains above 60%. If this share is less than 60%, beneficiaries must in principle at least maintain or increase the share, and if the tonnage share falls below this level no further tax relief for additional non-Community flagged vessels may be granted. National flagging restrictions according to which the benefits of the scheme are restricted to a certain level of national flagging (and not EEA flagging) infringe internal market rules in a manner indissolubly linked to the assessment of the compatibility of that aid measure.²² Therefore, such national flagging restrictions cannot be approved.
- (102) The Commission notes that, pursuant to Section 52¹(4)2) of the Draft Income Tax Act, the Tonnage Tax Scheme covers vessels irrespective of their flag operated by companies subject to taxation in Estonia. However, the Estonian authorities confirmed that the Tonnage Tax Scheme requires that companies benefitting from it have at least 60% of their gross tonnage under EEA flags.
- (103) In addition, the Estonian authorities confirmed that the Tonnage Tax Scheme does not discriminate between EEA flags. The Tonnage Tax Scheme is not restricted to national flagged vessels and it is open to all EEA flags (i.e. to all EEA-flagged vessels).
- (104) The Tonnage Tax Scheme is thus in line with the Maritime Guidelines and the Commission's decisional practice in this respect.

3.1.3.8. *Flag entry level*

- (105) The objective of the Maritime Guidelines is to enhance the competitiveness of the European shipping sector and the EU/EEA flag. The Commission therefore considers desirable that Member States introduce an entry floor as regards the EU/EEA flag link for shipping companies entering the Tonnage Tax scheme.
- (106) The Estonian authorities confirmed that the Tonnage Tax Scheme requires that companies have at least 60% of the gross tonnage of the ships flying the flag of an EEA Contracting State.
- (107) In light of the above, the Commission concludes that the flag entry level requirement is fulfilled.

²² See judgment in Case C-598/17 *A-Fonds* EU:C:2019:352.

3.1.3.9. *Aid cumulation /Aid ceiling*

- (108) In line with Chapter 11 of the Maritime aid Guidelines, a reduction to zero of taxation and social charges of seafarers and a reduction of corporate taxation of shipping activities such as described in section 3.1.3.6, recital (100), is the maximum level of aid which may be permitted.
- (109) The Estonian authorities confirmed that the companies liable under the Tonnage Tax Scheme do not qualify for any other tax benefits or incentives that are similar to those provided by the regime. In particular, the prohibition of accumulation of benefits with other benefits is monitored in the context of the reporting obligations of the companies, and checks by the Estonian Maritime Administration are carried out on a risk-based selection so that companies receiving aid comply with all the conditions of the special tax treatment. If such conditions are not met, the undertaking loses the right to use the special tax treatment.
- (110) The Tonnage Tax Scheme thus is in line with the Maritime Guidelines and the Commission's decisional practice in this respect.

3.1.3.10. *Preferential fiscal treatment of capital gains and dividends related to shares in shipping companies as well as maritime intermediaries.*

- (111) As set out in section 3.1 of the Maritime Guidelines the fiscal advantages must be restricted to shipping activities and normal tax levels should be preserved for the remuneration of shareholders and directors. Therefore, income related to dividends paid by shipping companies and capital gains arising from the sale of shares in shipping companies do not constitute income arising from shipping activities, but rather income arising for the shareholders from their investment activities. There is no compatibility basis which would justify preferential tax treatment of income from such investment activities.
- (112) As regards capital gains, the Estonian authorities submitted that there is no special regulation for capital gains in Estonia. The Estonian authorities confirmed that capital gains arising from the sale of shares in shipping companies are treated in the same way as gains arising from the sale of shares in any other company.
- (113) As regards dividends and other profit distributions, the Estonian authorities confirmed that no preferential treatment is offered to shareholders of shipping companies and maritime intermediaries compared to shareholders of companies falling under the normal tax system. Dividends and other profit distributions received from a tax resident company are treated in the same way, regardless of whether the company applied the Tonnage Tax Scheme or whether its profits fell under the standard corporate income tax system in Estonia.
- (114) In this regard, the Estonian authorities further explained the standard corporate income taxation system in Estonia, which has a unique nature since it only taxes distributed profits. The Estonian authorities also further explained the Estonian dividends' taxation system at the level of shareholders, where a distinction is made between individuals (natural persons), legal persons, foreign and non-foreign entities.

- (115) Based on the explanations provided by the Estonian authorities, it appears that the Estonian standard corporate taxation system is, although only taxing distributed profits, not to be considered as a withholding tax, as the tax burden is on the distributing company. The Estonian standard corporate income tax system, as a general rule, does not foresee any additional taxation at the level of the recipients of dividends and/or other profit distributions. As a result, these recipients are not liable to bear any further tax burden upon receipt of dividends, if corporate tax is paid at the level of the distributing company. The envisaged Tonnage Tax Scheme would not alter this general rule. As such, shareholders in shipping companies subject to tonnage taxation in Estonia would be treated, when receiving dividends, as shareholders in any other company operating in other economic sectors in Estonia, i.e. they would not be subject to dividend tax.
- (116) However, under the standard corporate income tax system there is an exception to this general rule in cases where the distributed profits are lower or equal to the average distributed profits in the three previous years.²³ In those circumstances, the (natural person) recipient of the distributed profits is subject to a dividend tax of 7% over the profits withheld by the company distributing the profits. The rationale of this rule is, as explained by the Estonian authorities, to prevent the distortion of the neutrality of taxation of various types of income at the level of a natural person.²⁴ To ensure that shareholders in shipping companies which opt for the Tonnage Tax Scheme would not benefit from a tax relief which they would not have under the standard corporate income tax system, the Estonian authorities have committed to amend their law to ensure equal tax treatment of shareholders in the same circumstances whereby these shareholders would be subject to the above-mentioned 7% tax, irrespective of whether a shipping company opt for the Tonnage Tax Scheme or remains subject of the normal corporate tax system. Therefore, shareholders in shipping companies meeting the conditions for the application of the 7% dividend tax will be subject to the same rules as shareholders in any other company, even if these shipping companies will opt for the Tonnage Tax Scheme.
- (117) Considering the above, the Commission concludes that the Tonnage Tax Scheme does not provide for preferential fiscal treatment of capital gains and dividends and, therefore, is in compliance with the Maritime Guidelines and the Commission's decisional practice in this respect.

3.1.3.11. *Tax liabilities when opting-in to the Tonnage tax scheme*

- (118) When opting-in to the Tonnage Tax Scheme tax liabilities have to be settled or they would constitute a separate State aid measure which would be acceptable only within the limits of the aid ceiling fixed in the Maritime Guidelines.
- (119) The Estonian authorities confirmed that the Draft Act ensures clarity of tax calculation when switching from a tax regime to another. A tax resident company wishing to switch to the Tonnage Tax Scheme is obliged to declare all circumstances affecting the amount of the tax liability specified in §§ 49–52 of the

²³ Section 50(1) of the Estonian Income Tax Act.

²⁴ In fact, in circumstances foreseen by Section 50(1) of the Estonian Income Tax Act, tax resident distributing companies are subject to a lower 14% income tax rate, as foreseen by Section 4(5) of the Income Tax Act.

Draft Income Tax Act, including the amount of the profit which is taxable on the basis of those sections and the taxation of which is deferred until the distribution of profits, as well as the amount of income taxed pursuant to section 52⁷ under the Tonnage Tax scheme.

- (120) The Estonian authorities also confirmed that all potential or hidden tax liabilities linked to the depreciation of a ship (or other asset) are settled before entry in the Tonnage Tax Scheme and repaid to the State. For instance, if a ship enters the Tonnage Tax Scheme from an economic unit whose profit is taxed under standard taxation to an economic unit whose income is taxed under the Tonnage Tax Scheme, all potential tax liabilities will be settled before entry in the Tonnage Tax Scheme.
- (121) In light of the above, the Commission considers The Tonnage Tax Scheme is thus in line with the Maritime Guidelines and the Commission's decisional practice in this respect.

3.1.3.12. *Duration & evaluation*

- (122) According to relevant case-law, aid schemes cannot be approved as compatible under Article 107(3) TFEU for an unlimited duration.²⁵ Schemes must be subject to a regular review of their effectiveness and impact.
- (123) The Tonnage Tax Scheme will remain in force for six years. The present Decision is directly applicable in the Estonian national law and is valid until 30 June 2026 (see recital (26)).
- (124) Pursuant to section 12 of the Maritime Guidelines, the Commission further notes that an evaluation of the regime has to be carried out after three years starting from the date when aid was granted.
- (125) In this regard, Estonia has indicated that it will undertake to put in place, within one year of the entry into force of the Draft Act, an appropriate control mechanism, by which it regularly verifies, at least ex post and on a sample basis, that all compatibility conditions are met, and to impose sanctions in case of fraud.

3.1.3.13. *Conclusion (on compatibility)*

- (126) Based on the foregoing, the Commission considers that the Tonnage Tax Scheme fulfils all the necessary criteria under the Maritime Guidelines and its decisional practice. Therefore, the Commission concludes that the Tonnage Tax Scheme is a State aid measure compatible with the internal market pursuant to Article 107(3)(c) TFEU.

3.2. **Seafarer Scheme**

3.2.1. *Existence of aid*

- (127) The Commission first of all notes that Estonia accepts the State aid qualification under Article 107(1) TFEU of the notified measure.

²⁵ Case C-67/09 P *Nuova Agricast*, EU:C:2010:607, para. 80.

- (128) The 0% income taxation and the partial reduction of social security contributions in respect of qualifying seafarers constitute foregone State revenue and thus involve State resources. Moreover, since the measures are implemented through national legislation, they are imputable to Estonia. The measures also grant a selective advantage to the shipping companies hiring these seafarers as they benefit from lower labour costs in comparison to companies not benefiting from the scheme (e.g. because not at least 60% of the net tonnage of their fleet flies the flag of a Member State of the EU/EEA) which would be otherwise comparable. For the same reasons as in the case of the Tonnage Tax Scheme, the Seafarer Scheme is also liable to distort competition and affect trade within the liberalised European shipping market.
- (129) It follows that the measures involve State aid in the sense of Article 107(1) TFEU.

3.2.2. Legality of the aid

- (130) The Commission takes note of the commitment of the Estonian authorities to respect the stand-still obligation laid down in Article 108(3) TFEU and not to approve the Draft Act until the Commission reaches a decision authorising the notified measure.

3.2.3. Compatibility

- (131) Pursuant to Article 107(3)(c) TFEU aid to facilitate the development of certain economic activities or of certain economic areas may be considered compatible with the common market, where such aid does not adversely affect trading conditions to an extent contrary to the common interest.
- (132) As outlined above, State aid in favour of the maritime sector must be examined in the light of the Maritime Guidelines.

3.2.3.1. Objectives of the scheme

- (133) The 2004 Maritime Guidelines provide that State aid schemes in relation to labour-related costs for seafarers may be introduced in order to support the Community maritime interest, in particular with the aim of:
- reducing fiscal and other costs and burdens borne by Community ship-owners and Community seafarers towards levels in line with world norms, directly stimulating the development of the maritime transport sector and employment, rather than providing general financial assistance,
 - encouraging the flagging or re-flagging to Member States' registers,
 - contributing to the consolidation of the maritime cluster established in the Member States while maintaining an overall competitive fleet on world markets,
 - maintaining and improving maritime know-how and protecting and promoting employment for European seafarers.
- (134) The Estonian authorities clarified that the new system is directed towards seafarers who do not have access to the Estonian social security system today. It was noted

that around 5000 Estonian seafarers have very limited access to the Estonian social security system nowadays, including no access to the State health insurance system, old age survivor pension scheme and unemployment scheme. In this regard, it is planned that the new system will bring additional vessels under the Estonian (and potentially other EEA) flag, and as Estonian and other EEA seafarers will start working on board those vessels they will gain access to the Estonian social security system.

- (135) In addition, the Estonian authorities underlined how the new system will improve the social security situation of both Estonian and other EEA seafarers²⁶. In particular, it was also noted that no internationally trading cargo vessels of 500 GT or more nor passenger vessels trading outside the EEA of 500 GT or more are under the Estonian flag today. Since there are no vessels under the Estonian flag today that would fall under the category of eligible vessels under the scheme, there are also no seafarers whose social security would be negatively affected. In fact, only the seafarers working on eligible vessels will be covered by the new social security scheme. Therefore, social security levels of those seafarers who are currently subject to the Estonian social security system will not be affected.
- (136) Finally, Estonia notes that MLC standards will be improved. For instance, standard A4.5.3 stipulates that each Member shall take steps according to its national circumstances to provide the complementary social security protection to all seafarers ordinarily resident in its territory. Estonia underlines that as a result of the reform social security will also be extended to non-resident seafarers. In addition, social security protection for seafarers will equal that of shore workers resident in the same territory, as required by the MLC.
- (137) In light of the above, the Commission notes that the objectives of the Seafarer Scheme as described above as well as in section 2.3 above are in line with the objectives as described in the Maritime Guidelines. The scheme aims at guaranteeing economic conditions in order to maintain the competitiveness of the European shipping sector, attract investments and achieve economic growth, increase the EEA's maritime fleet and create skilled maritime employment in the EEA.
- (138) The Seafarer Scheme thus is in line with the Maritime Guidelines and the Commission's decisional practice in this respect.

3.2.3.2. *Scope of the scheme*

- (139) Seafarer schemes in the sense of the Maritime Guidelines may concern either:
- reduced rates (or a (partial) reimbursement) of income tax for Community seafarers on board vessels registered in a Member State, and/or

²⁶ For instance, the Estonian authorities noted that as a result of the reform many Estonian seafarers will have the option to buy private health insurance for the time that they are not covered by the employer's health insurance (which normally terminates two months after the end of the employment contract).

- reduced rates (or a (partial) reimbursement) of contributions for the social protection of Community seafarers employed on board vessels registered in a Member State.
- (140) As described in section 2.7 above, the Seafarer Scheme comprises (i) a total exemption from the obligation to pay personal income tax, as well as (ii) a partial exemption in the sense of reduced rates from the obligation to pay contributions for social protection. These exemptions are in line with the requirements of the Maritime Guidelines.
- (141) The Seafarer Scheme thus is in line with the Maritime Guidelines and the Commission's decisional practice in this respect.

3.2.3.3. *Eligible seafarers – General rule*

- (142) Only Community seafarers, employed on board vessels registered in a Member State, are eligible to benefit from the Seafarer Scheme. Under the Maritime Guidelines, Community seafarers are defined as:
- *"Community / EEA citizens, in the case of seafarers working on board vessels (including ro-ro ferries) providing scheduled passenger services between ports of the Community,*
 - *all seafarers liable to taxation and/or social security contributions in a Member State, in all other cases."*
- (143) The Estonian authorities noted that as the special tax treatment does not apply to ships that provide scheduled passenger services in the EEA, there is no conflict with the rule that aid in the case of scheduled passenger vessels may be provided solely to Community seafarers if the passenger ship travels between Community ports.
- (144) The Estonian authorities therefore confirmed that only Community seafarers employed on board vessels registered in a Contracting State are eligible to benefit from the Seafarer Scheme. In this regard, in light of the exemption concerning scheduled passenger services in the EEA, by Community seafarers is meant "seafarers who are liable to taxation and/or social security contributions in a Contracting State".
- (145) The Commission therefore concludes that the Seafarer Scheme only applies to Community seafarers in the sense of the Maritime Guidelines.

3.2.3.4. *Eligible seafarers – Towage and dredging vessels / activities*

- (146) For the maritime part of towage and dredging (maritime transport of materials), Community seafarers are eligible to benefit from the Seafarer Scheme only if they are working on board seagoing self-propelled tugboats and dredgers, which are registered in a Member State, carrying out maritime transport at sea for at least 50% of their operational time.
- (147) The Estonian authorities confirmed that in order to apply the Seafarer Scheme at least 50% of the work time of dredgers and/or tugboats have to comprise maritime transport. In addition, the Seafarer Scheme is open to all EEA-flagged vessels also

in the case of vessels carrying out towage and dredging activities, and according to subsection 13(6) of the Draft Income Tax Act the ship must fly an EEA flag.

- (148) It follows that seafarers employed on towage and dredging vessels are eligible, provided that at least 50% of the annual operations of the vessel's activities constitute maritime transport.

3.2.3.5. *Eligible vessels*

- (149) Only genuine maritime transport activities are eligible for aid under the Maritime Guidelines (see above section 2.7.1.).
- (150) The Seafarer Scheme is only applicable to maritime transport, provided that it is international according to the Draft Income Tax Act. The Estonian authorities explained that for maritime transport to be considered as international, in case the ship provides scheduled passenger services, then 50% or more of the annual port of calls of the ship must be located outside the EEA; in case the ship does not provide scheduled passenger services, more than 50% of the voyages must take place as follows:
- i. between an Estonian port and foreign port;
 - ii. between an Estonian port and an installation outside of the territorial sea of Estonia;
 - iii. between ports of a foreign country or foreign countries; or
 - iv. between a foreign port and a facility located off the shore.

- (151) The 0% income taxation and the partial exemption from the contribution for social protection only apply to seafarers employed on eligible vessels which carry out international maritime transport activities. In addition, in the case of the Seafarer Scheme, pursuant to clause 13(5) 2) of the Draft Income Tax Act, vessels will have to fly an EEA flag. It follows that the eligible vessels under the Seafarer Scheme are in line with the requirements of the Maritime Guidelines.

3.2.3.6. *National flagging restrictions*

- (152) National flagging restrictions, according to which the benefits of the Seafarer Scheme are conditional on a certain level of national (and not EEA) flagging, infringe internal market rules.
- (153) Pursuant to clause 13(5)2) of the Draft Income Tax Act, as well as other provisions, the Estonian authorities confirmed that the Seafarer Scheme does not discriminate between EEA flags. For this reason, the Commission considers that there is no infringement of internal market rules and that the conditions of the Maritime Guidelines on EEA flagging are complied with.

3.2.3.7. *Aid cumulation / aid ceiling*

- (154) In line with Chapter 11 of the Maritime aid Guidelines, a reduction to zero of taxation and social charges of seafarers and a reduction of corporate taxation of

shipping activities such as described recital (100), is the maximum level of aid which may be permitted.

- (155) In the same way as for the Tonnage Tax Scheme, the Estonian authorities confirmed that companies opting for the Seafarer Scheme do not qualify for any other tax benefits or incentives that are similar to those provided by the regime and cannot obtain benefits exceeding the full exemption from taxes and contributions for social protection. The prohibition of accumulation with other benefits is monitored in the context of the reporting obligations of the companies and checks by the Estonian Maritime Administration are carried out on risk-based selection. Moreover, the Estonian authorities have committed to notify to the Commission any additional aid granted to beneficiaries of the Seafarer Scheme prior to implementation.
- (156) Therefore, the Commission concludes that the requirements relating to aid cumulation / aid ceiling are fulfilled.

3.2.3.8. *Duration and evaluation*

- (157) According to the case-law, aid schemes cannot be approved as compatible under Article 107(3) TFEU for an unlimited duration.²⁷ Schemes must be subject to a regular review of their effectiveness and impact.
- (158) The Seafarer Scheme will enter into force on 1 July 2020 and remain in force for six years, expiring on 30 June 2026. In addition, prolongation of the scheme will be subject to a new notification to the Commission.
- (159) The Commission notes that this duration is in line with previously approved State aid schemes in the maritime sector.
- (160) Pursuant to section 12 of the Maritime Guidelines, the Commission further notes that an evaluation of the regime has to be carried out after three years or as soon as 500 workers are registered as social security beneficiaries, whichever comes first. As described in recital (124) with regard to the Tonnage Tax Scheme, Estonia has indicated that it will undertake to put in place, within one year of the entry into force of the Draft Act, an appropriate control mechanism, by which it regularly verifies, at least ex post and on a sample basis, that all compatibility conditions are met, and to impose sanctions in case of fraud.

3.2.3.9. *Conclusion (on compatibility)*

- (161) Based on the foregoing, the Commission considers that the Seafarer Scheme fulfils all the necessary criteria under the Maritime Guidelines and its decisional practice. Therefore, the Commission concludes that the Seafarer Scheme constitutes a State aid measure compatible with the internal market pursuant to Article 107(3)(c) TFEU.

²⁷ Case C-67/09 P *Nuova Agricast* EU:C:2010:607, para. 80.

4. CONCLUSION

The Commission concludes that the Tonnage Tax and the Seafarer Scheme, as assessed above, constitute State aid pursuant to Article 107(1) TFEU which is compatible with the internal market pursuant to Article 107(3)(c) TFEU.

5. DECISION

The Commission has accordingly decided:

- not to raise objections to the aid on the grounds that it is compatible with the internal market pursuant to Article 107(3)(c) of the Treaty on the Functioning of the European Union.

The Commission notes that for reasons of urgency, Estonia exceptionally accepts the adoption and notification of the decision in English.

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Your request should be sent electronically to the following address:

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State Aid Greffe
B-1049 Brussels
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Yours faithfully,
For the Commission

Margrethe VESTAGER
Executive Vice-President