DET KONGELIGE
FINANSDEPARTEMENT

Royal Ministry of Finance

EFTA Surveillance Authority
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Notification of the Norwegian special tax system for shipping

1. INTRODUCTION

In accordance with article 1 (3) of protocol 3 to the Surveillance and Court Agreement the Ministry of Finance hereby notifies to the EFTA Surveillance Authority the Norwegian special tax system for shipping.

The impending notification implies a continuation of the existing shipping tax system, which was approved by the Authority in its decision of 3 December 2008 (755/08/COL).

In the view of the Ministry, the notified measure constitutes state aid within the meaning of Article 61(1) of the EEA Agreement; cf. part II Section 1 of the Authority's decision 755/08/COL.

The legal basis for the compatibility of the notified measure is Article 61(3)(c) of the EEA Agreement (aid to facilitate the development of certain economic activities or of certain economic areas may be considered compatible with the functioning of the EEA Agreement where such aid does not adversely affect trading conditions to an extent contrary to the common interest) together with the Authority's Guidelines on State Aid to Maritime Transport (the Maritime Guidelines).

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The original Norwegian special tax system for shipping was approved by the Authority 1 July 1998, cf. decision 164/98/COL. The scheme offered eligible companies a postponed taxation of profits derived from operation of vessels, until untaxed income was distributed to shareholders, or the company exited the special tax system. To ensure that all exempted income was taxed on distribution or exit, the companies had to establish a special account of retained taxed income.

The Authority approved considerable amendments to the scheme, including transitional measures, on 3 December 2008, cf. decision 755/08/COL. The previous system of postponed tax was replaced by an exemption system, corresponding to the special tax regimes for shipping in other European countries, i.e. shipping income was tax exempt on a permanent basis. The changes were made on the background that the previous Norwegian shipping tax scheme of 1996 was not adequate in order to ensure new shipping investments in Norway, and new investments were largely placed in low-tax regimes for shipping in other countries.

By its decisions 755/08/COL, 181/09/COL and 407/10/COL, the Authority has approved transitional measures of 2007, 2009 and 2010, concerning the settlement of deferred taxation from the shipping tax system prior to 2007. Further amendments to the special tax system have been approved on 31 March 2009 (181/09/COL), 7 July 2010 (292/10/COL), 27 October 2010 (407/10/COL), 10 September 2014 (322/14/COL) and 26 November 2014 (519/14/COL). No amendments have been made to the tax scheme subsequent to the amendment approved by the Authority on 26 November 2014 (519/14/COL).

Although the current model of the scheme is not of limited duration, the Norwegian authorities were committed to re-notify the scheme after ten years. In its decision of 11 November 2016 (201/16/COL) the Authority approved a six month prolongation of the current special tax system, until 30 June 2017.

The special provisions on taxation of shipping companies are found in sections 8-10 to 8-20 of the Norwegian Tax Act ("Lov 26. mars 1999 nr. 14 om skatt av formue og inntekt") and in provisions set out in regulations issued by the Ministry of Finance ("Forskrift til utfylling og gjennomføring mv. av skatteloven av 26. mars 1999 nr. 14" sections 8-11, 8-13, 8-15 and 8-16).

The special tax scheme will benefit eligible undertakings carrying out eligible activities as defined in Sections 4 – 7 below.

The scheme is optional for qualifying companies. The choice of entering or leaving the scheme is made by a claim in the tax return for the fiscal year in question. However, as described under section 10.2 below, undertakings that opt for the special tax regime commit to remain under the regime for a minimum period of ten years. The decision to

opt for the scheme is made collectively at a company group level, cf. section 10.3. Companies and groups that opt out of the system are taxed under the standard company tax rules.

2. OBJECTIVE OF THE AID

The objective of the aid is to ensure the competitiveness of the Norwegian shipping industry. The shipping industry and the maritime know-how are important for the economy and employment in Norway, in particular in many local communities along the Norwegian coast. Norway represents one of the world's largest shipping fleets and the world's second largest offshore service fleet.

The special tax scheme of 2007 has ensured the competitiveness of the Norwegian tax framework, while remaining in line with other European tax regimes for shipping. Since 2007, the net tonnage within Norwegian shipping tax scheme has increased. The development of the net tonnage is shown in attachment 1 to this letter. As of 2015, there were about 1500 vessels taxed under the Norwegian Special tax system for shipping.

In the view of the Ministry of Finance, the objective of the notified measure is in line with the Maritime Guidelines. In its decision 755/08/COL Part II Section 3, the Authority stated:

'Under Article 61(3)(c) of the EEA Agreement, aid to facilitate the development of certain economic activities or of certain economic areas may be considered compatible with the functioning of the EEA Agreement where such aid does not adversely affect trading conditions to an extent contrary to the common interest. The Authority considers Article 61(3)(c) of the EEA Agreement together with the Maritime Guidelines to form the legal basis for assessing the compatibility of the notified measures.

These Guidelines at section 1.2.(c) Paragraph 4 allow the EFTA States to support the maritime transport industry; 'maritime industries are inextricably linked to maritime transport. This association is a strong argument in favour of positive measures whose aim it is to maintain a fleet dependent on EEA shipping. Since maritime transport is one of the links in the chain of transport in general and in the chain of the maritime industries in particular, measures seeking to maintain the competitiveness of the European fleet have also repercussions on investments on land and maritime-related industries and on the contribution of maritime transport to the economy of the EEA as a whole, and to jobs in general'.

The Authority has already approved the prior Norwegian Tonnage Tax scheme. The European Commission has a long standing case practice in this area."

The Norwegian authorities consider the abovementioned statement to be a valid assessment of the present situation concerning the shipping sector of the EEA.

The maritime industry is currently among Norway's most global, innovative and forward-looking industries. In order for the industry to continue its positive development, framework conditions are essential.

A competitive shipping tax regime is an important part of the Government's maritime strategy.[1] In the strategy, the Government states that:

> *"The Government will ensure that Norway continues to be a leading maritime nation with a large fleet registered in Norway. In order to maintain and further develop the maritime industry, it is important to ensure a considerable and competitive fleet under*
>
> *Norwegian flag. The Government will continue the shipping tax regime, strengthen the net wage scheme, and ease the trade area limitations for NIS vessels."*

The Norwegian tax scheme for shipping companies contributes to the preserving of Norway as a leading maritime nation. Shipping companies are often described as the core of the maritime sector. The Norwegian shipping industry is an integrated and important part of the European maritime sector, and an important driving force for the development of innovative and sustainable transport solutions at sea. Consequently, the competitiveness of the Norwegian shipping industry implies ring effects for the functioning of the European maritime sector and the further development towards more effective and sustainable operation. A competitive and strong Norwegian shipping industry is therefore important from both a Norwegian and a European perspective.

More than 200 Norwegian shipping companies, counting approximately 1800 ships in foreign trade, make up the core of the Norwegian maritime sector. According to a report by Erik W. Jakobsen, the shipping companies generate close to 60 percent of the Norwegian maritime sectors share of the Norwegian GDP.[2]

The Norwegian maritime offshore fleet has since 2004 experienced a considerable growth. This is illustrated by a growth in the number of employees, from 7 600 in 2004 to more than 19 000 in 2014, and its contribution to Norway's GDP increased from NOK 10 billion to NOK 45 billion during the same years.[3] The offshore fleet has expanded from 361 vessels in 2004 to 604 in October 2016.[4]

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[1] The Maritime Strategy is summarised in the document *Maritime Opportunities – Blue Growth for a Green Future* published by the Norwegian Ministry of Trade, Industry and Fisheries on 29 May 2015. The document can be found at the following internet address: https://www.regjeringen.no/contentassets/05c0e04689cf4fc895398bf8814ab04c/summary_maritime-opportunities_the-governments-maritime-strategy.pdf

[2] http://web.bi.no/forskning/papers.nsf/0/bde96fcd8d205914c12578a800420bdf/$FILE/2011-05-jakobsen.pdf

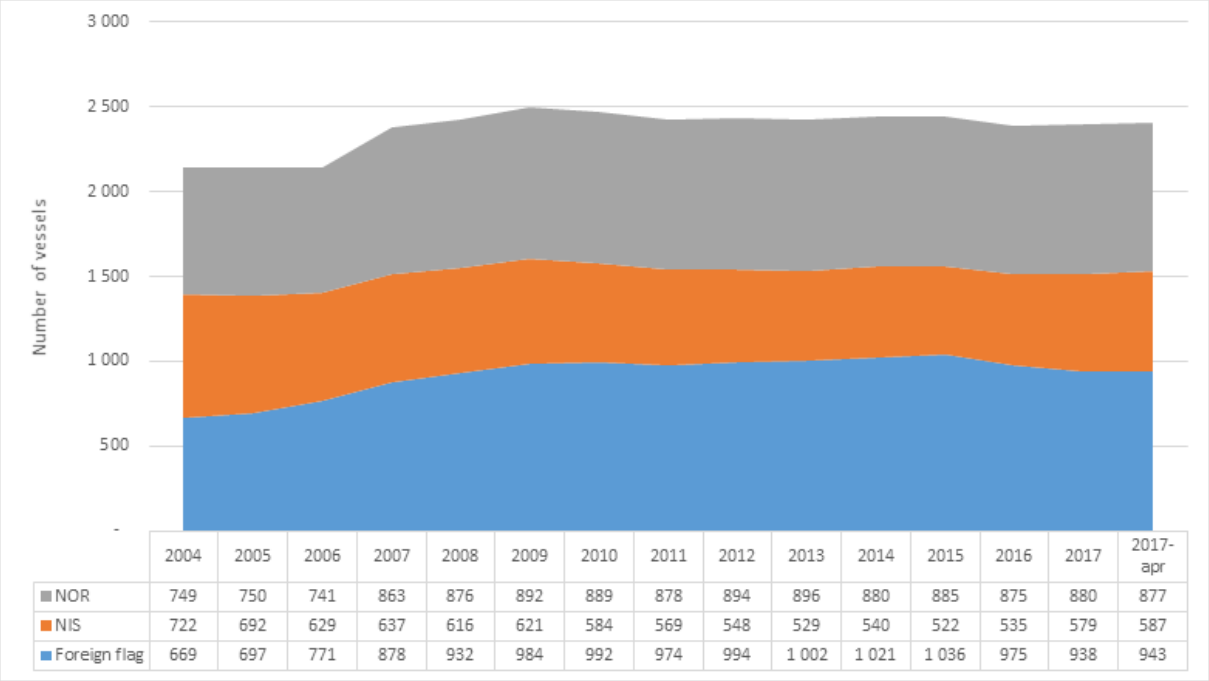
[3] Source: *I krevende farvann* issued by the Norwegian Shipowners Association in March 2015

[4] Source: The Norwegian Shipowners' Association.

Over the last three years the market conditions for offshore vessels has however deteriorated considerably in terms of activity and market rates. The number of offshore vessels taken out of operation (lay-up) is growing, and as of October 2016, more than 110 Norwegian controlled offshore vessels were laid up.

While the number of NOR registered vessels has remained stable over the last years, the number of NIS registered vessels has until recently been in steady decline and represented in 2015 only about 20 percent of the total Norwegian controlled fleet – down from about 35 percent ten years earlier.[5] The number of NIS vessels improved significantly in 2016 and 2017, following the liberalisation of NIS trade area restrictions, and reached 589 vessels as of 30 April 2017.

Overview of the development in number of vessels (2004 – 1.4.2017):[6]



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2017-apr
NOR	749	750	741	863	876	892	889	878	894	896	880	885	875	880	877
NIS	722	692	629	637	616	621	584	569	548	529	540	522	535	579	587
Foreign flag	669	697	771	878	932	984	992	974	994	1 002	1 021	1 036	975	938	943

[5] The Norwegian ship registers encompasses the Norwegian International Ship Register (NIS) and our domestic register, the Norwegian Ordinary Ship Register (NOR).
[6] Source: The Norwegian Shipowners Association, the Norwegian Maritime Authority and Statistics Norway

Overview of the development in number of vessels within the special tax scheme (2007-2015):[7]

Year	Vessels in total	Chartered in
2007	709	No verified data
2008	963	151
2009	1152	155
2010	1200	125
2011	1419	346
2012	1422	277
2013	1452	252
2014	1484	231
2015	1523	246

An expressed objective for the Norwegian Government is to preserve the country's position as a leading maritime nation. Among other things, this objective is based on the vital influence the industry has in many coastal communities, and the importance of maintaining and developing practical maritime knowledge and competence. The shipping tax scheme has proven an important element in this respect.

The existing state aid guidelines have contributed to growth, profit and employment in the European and Norwegian shipping industries. The Norwegian shipping tax scheme is intended to support the Norwegian maritime competiveness, and as such the shipping industry in the EEA as a whole, with the aim of:

- maintaining and improving maritime know-how and protecting and promoting employment for EEA seafarers;
- improving a safe, efficient, secure and environment friendly maritime transport;
- encouraging the flagging or re-flagging to the Norwegian Ordinary Ship Register (NOR) and the Norwegian International Ship Register (NIS);
- contributing to the consolidation of the Norwegian maritime sector, while maintaining an overall competitive fleet.

3. DURATION OF THE SCHEME

The measure is notified for a period as from 1 July 2017 through the income year of 2026. The inclusion of windmill farm vessels in the scheme (see section 5.6) is notified for the period as from 1 January 2017 through the income year of 2026. Although the special tax system for shipping companies is not of limited duration according to the Norwegian Tax Act, the Norwegian authorities will re-notify the scheme after ten years.[8]

[7] Source: The Central Tax Office for Large Enterprises

[8] In its decision of 11 November 2016 (201/16/COL) the Authority approved a six month prolongation of, the national special tax system for shipping in its current form, until 30 June 2017.

4. ELIGIBLE UNDERTAKINGS

The shipping tax scheme system is open for private and public limited companies formed under Norwegian law. This comprises "Aksjeselskap" (AS) and "almennaksjeselskap" (ASA).

Companies similar to Norwegian limited companies that are resident in another EEA state, and that only carry out qualifying shipping activities taxable in Norway, are also eligible for the special tax system. The activity restriction for companies resident in another EEA state is in line with the general system of ring fencing in the Norwegian shipping tax scheme.

To prevent spill over to non-shipping activities, companies within the special tax system (Norwegian or EEA-based) are only allowed to carry out activities that fall under the tax exemption, and can only own assets that are necessary to exercise these activities. Mixed companies carrying out both qualifying activities and other activities are not eligible under the scheme.

In order to be eligible for the scheme, a company has to either own a ship qualifying under the scheme or own shares or interests in limited companies, partnerships or Norwegian controlled foreign companies, which own such ships. Companies under the Special tax system may not own non-shipping related assets – including real estate. Companies are allowed to own financial assets. However, profits derived from financial assets are subject to standard company taxation.

Companies and groups that opt for the system have to include all their eligible vessels in the shipping tax regime.

Qualifying assets can be held through limited companies, partnerships, limited partnerships (Norwegian or foreign) and controlled foreign companies based in low tax countries (CFCs). Shipping income derived by limited companies under the special tax system through such companies may be taxed under the special tax system. The minimum ownership share is 3 percent. This means that small shipowning enterprises have the opportunity to take part in shipping projects through lesser ownership shares. At the same time, the minimum share ensures that the scheme only benefits genuine shipowners. In addition, administrative considerations concerning control of compliance call for a minimum share.

5. VESSELS AND OTHER ASSETS UNDER THE SCHEME

5.1 General remarks

The definition of allowable vessels in the Norwegian tax scheme for shipping is not framed as an exhaustive list of allowable types of vessels. Rather, the terms "transport ship" ("skip i fart") and "support vessel in petroleum activities" ("hjelpefartøy i petroleumsvirksomhet") are used in the Tax Act to define the scope of the scheme.

One reason for choosing this system, rather than providing an exhaustive list of allowable vessels in the legislation, is that a list would easily be outdated and new vessels that in fact perform transport activities under similar competitive conditions as the vessel types already included in the list, would fall outside the scheme.

The scope of both criteria ("transport ship" and "support vessel in petroleum activities") are interpreted by the tax authorities in their application of the rules. In regulations issued by the Ministry of Finance, some vessel types are exempt from the term "transport ship".[9] These vessel types are:

- ships in domestic traffic smaller than 100 gross registered tons;
- ferries in scheduled traffic between Norwegian ports where the distance between the first and last port is less than 300 nautical miles;
- ships operating mainly in Norwegian inland waterways;
- ships conducting stationary activities (e.g. in ports) or other activities where the sailed distance is less than 30 nautical miles (applies only to domestic traffic);
- vessels which are not self-propelled, unless the vessel is operated in connection with a self-propelled vessel;
- receiving boats, and vessels used as working platform;
- pleasure crafts, and
- fishing boats.

According to the tax authorities' administrative guidelines, the exemption mentioned under item four above (exemption for ships conducting stationary activities or other activities where the sailed distance is less than 30 nautical miles) applies only when more than 50 percent of the ships' activities during the course of a given year consist of stationary activities or other activities where the sailed distance is less than 30 nautical miles.

Vessels transporting goods and passengers overseas qualify for the current special tax system without regard to the abovementioned limitations.

Vessels that are not self-propelled do not qualify for the scheme unless the vessel is operated in connection with a self-propelled vessel. Further, vessels that are not self-propelled and operate mainly in Norwegian inland waterways do not qualify. Theoretically, under the current tax scheme, vessels that are not self-propelled and operate mainly in foreign inland waterways may be eligible for the scheme. Currently there are no such vessels within the scheme. The Ministry intends to propose an amendment to the Tax Act, excluding vessels that are not self-propelled and operate mainly in foreign inland waterways. Consequently, barges that are not self-propelled will be eligible for the new special tax scheme only if they are seagoing.

[9] Cf. section 8-11-1in the Ministry's supplementary regulations to the Tax Act (forskrift 19. november 1999 nr. 1158 til utfylling og gjennomføring mv. av skatteloven av 26. mars 1999 nr. 14).

In addition support vessels in petroleum activities qualify for the scheme, see section 5.4 below.

Turning to other allowed assets under the scheme, companies can only own assets that are necessary to exercise strategic and commercial management, daily technical operations and maintenance, and other allowable secondary activities, cf. section 6.2 below. However, companies are not allowed to own real property.

In addition, Companies are allowed to own financial assets. However, profits derived from financial assets are not tax exempt, but subject to ordinary taxation. Financial assets can only be held in the form of cash, claims and bank deposits, shares quoted on a stock exchange, and options carrying a right to buy or sell such assets.

5.2 Transport ships

All vessels under this category are engaged in transport activities that constitutes "maritime transport". When assessing the eligibility of a new specific vessel type, the tax authorities will investigate thoroughly whether maritime transport truly is the substantial activity of the vessel. The tax authorities will examine the vessel's operation concrete and in detail.

In administrative practise by the tax authorities, the term "transport ship" has been interpreted to include the following vessel types:

I. Passenger ships. The vessels are transporting passengers, i.e. the activity constitutes "maritime transport". Examples:
    i. Ferries
    ii. Cruise vessels
II. Ships transporting liquid and dry cargo. The vessels are transporting cargo, i.e. the activity constitutes "maritime transport". Examples:
    i. Bulk carriers
    ii. Tankers
    iii. Container ships
    iv. Car carriers
    v. Ro-ro carriers
    vi. Refrigerated cargo vessels
    vii. Chemical tankers
    viii. Shuttle tankers
    ix. Live fish carriers (well boats)
II. Cable laying vessels for high-voltage cables and data communication cables (with ROV[10]). The vessels are in motion during a substantial part of the assignment, i.e. performing transport and therefore qualifying for aid as "maritime transport"

[10] Remotely operated underwater vehicles, controlled from the cable laying vessels. The ROV performs tasks in the form of digging and covering pipe-laying trenches etc.

III. Tugboats not used in petroleum activities. At least 50 per cent of the towage activity effectively carried out by a tug during a given year must constitute maritime transport. The activity qualify as maritime transport according to the Maritime Guidelines section 3.1
IV. Seagoing barges being towed by another vessel. The notified measure does not include vessels that are not self-propelled and operate mainly in inland waterways (see section 5.1).
V. Barges used in transport of dredged material. (See section 5.3 for an elaboration on dredging and transport of dredged material.)
VI. Windfarm service vessels used in transportation assignments and therefore qualifying for aid as "maritime transport":[11]
    i. Vessels transporting and unloading parts to windmills at sea, but not taking part in construction, maintenance etc.
    ii. Installation support vessels for windmill farms (ISVs). ISVs supports the connection of cables to windmills at sea. The vessels are used for transporting crew and equipment to wind mill farms and between windmills
    iii. Vessels used for transport and grouting of concrete to wind turbine foundations
VII. Seismic vessels not engaged in petroleum activities. The vessels are in motion during the seismic survey and the activity therefore constitutes "maritime transport"
VIII. Rock-dumping vessels not engaged in petroleum activities. The vessels are transporting rocks to offshore installations and unloading the rocks to the seabed.

In addition to the abovementioned categories, Norwegian authorities notify an expansion of the scheme to windmill farm vessels, see Section 5.6 below.

5.3 Dredging activities

According to the Maritime Guidelines, dredging activities should not be eligible for tax relief. However, tax relief may be applied to those dredgers whose activity consists in "maritime transport" – that is, the transport at deep sea of extracted materials – for more than 50 percent of their annual operational time and only in respect of such transport activities.[12] As opposed to this, any dredging activity will make a vessel unqualified for the Norwegian scheme.[13] Transport of dredged material, including loading (by mud hose) of such material on to a transport vessel, is considered maritime transport in the real sense of the word, and does therefore qualify as an activity under the scheme.

[11] The notified measures also includes other types of windmill farm vessels, cf. section 5.6.
[12] Cf. the Maritime Guidelines section 3.1 paragraph 28.
[13] This is clearly stated in the preparatory works, cf. Ot.prp. nr. 92 (2003-2004) section 11.4.5.2.

5.4 Support vessels in petroleum activities

Support vessels in petroleum activities are eligible for aid under the special tax system for shipping. The activities constitute either maritime transport as such or maritime transport by analogy. The vessels employ qualified seafarers and transport equipment used for various offshore purposes. All vessel types listed below operate under the same competitive and technical conditions as vessels involved in transportation of goods and passengers at sea.

In its decision-making, the European Commission has established a practice including support vessel activities as eligible for aid under the maritime transport guidelines, when these vessels operate under the same competitive and technical conditions as vessels involved in the transportation of goods and passengers by sea. Reference is made to the maritime-aid case practice, as inter alia referred to in the Commission decision 1 April 2015 in SA.37912 (2013/N) – Croatia paragraph 84, where the Commission stated that:

> *"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 practice, the Commission has no objections against including such types of vessels in the scheme."*

In decision 13 April 2015, SA.38085 (2013/N) – Italy, the Commission in paragraph 54 found that activities sharing "a sufficient number of characteristics comparable with maritime transport" could be included by analogy, "provided that the market where they operate is open to international competition and there is a high risk of de-flagging and relocation". Considering vessels that provide rescue at sea and marine assistance on the high seas, the Commission in paragraph 55 finds that these vessels 1) "require qualified seafarers, with qualifications comparable to those working on board traditional maritime transport vessels" and 2) "are obliged to undergo technical and safety controls comparable to those of vessels dedicated to maritime transport".

In our view, vessels used in the petroleum service sector require the same level of qualification for seafarers and faces the same risk of relocation of on-shore activities. Fierce competition at an international market calls for inclusion of such vessels under the special tax scheme, in order to achieve the goals set out in the Maritime Guidelines. As a consequence, support vessels in the offshore sector are notified as qualifying vessels under the scheme.

When assessing the eligibility of a new specific offshore vessel type, the tax authorities looks into the function of the vessel, and assesses what category the vessel belongs to, out of four categories:

1. Support vessels other than entrepreneur vessels
2. Entrepreneur vessels
3. Mobile installations
4. Fixed installations

According to the Tax Act, categories 1 and 2 are eligible for the special tax scheme. However, vessels in category 2 are disallowed as far as the owner company is using them in operations on the Norwegian continental shelf.

Following a revision of the maritime guidelines in 2004, vessel types in category 3 are as from 2006 no longer eligible for the special tax scheme. Therefore, the term "support vessels in petroleum activities" does not include assets that are used in functions that are a part the core activities of oil and gas extraction. In effect, this excludes mobile installations namely drilling rigs, production ships, accommodation platforms etc. from the shipping tax scheme. Beyond that, the term "support vessels in petroleum activities" covers vessels in all types of support functions in the oil and gas extraction.

Vessel types in category 4 are not eligible for the special tax scheme.

In administrative practise by the tax authorities, the term "support vessel in petroleum activities" has been interpreted to include these vessel types:

I. Supply ships. Qualifies both as "transport ship" and "support vessel in petroleum activities"
    i. Ships constructed for the supply of provisions and equipment to and from petroleum offshore installations
    ii. FSVs (Fast Supply Vessels). Combined crew and provisions transport vessels in traffic to and from petroleum offshore installations
II. Seismic vessels in petroleum activities
III. Anchor Handling Tug Supply (AHTS) vessels in petroleum activities. The vessels are handling anchors and towing offshore petroleum platforms, barges and production ships
IV. Tugboats used in petroleum activities. Such vessels qualify for the special tax system as "support vessels in petroleum activities". The limitations set out in the Maritime Guidelines section 3.1 for tugboats in "maritime transport" (cf. section 2.2 III) are therefore not relevant for these vessel types
V. Emergency response and rescue vessels, diving vessels, fire vessels etc. in petroleum activities
VI. Pipe laying vessels in petroleum activities
VII. Lifting vessels in petroleum activities

VIII. Subsea vessels in petroleum activities, including IMR (Inspection, Maintenance and Repair) vessels. The vessels are specially designed for deep ocean operations
IX. Well intervention vessels
X. Rock-dumping vessels in petroleum activities (cf. section 5.2 VIII)
XI. Supply ships used as connecting links between production ships (FPSOs) and tankers
XII. Multipurpose vessels, performing two or more of the tasks described under item I-XI

The abovementioned support vessels are engaged in maritime transport activities and/or share characteristics with, and under the same competitive and technical conditions as vessels involved in maritime transport. The vessels are therefore considered qualifying vessels under the notified aid scheme. As far as their activities are not covered by the definition of "maritime transport" they should be considered eligible to be included in the scope of scheme by analogy.

5.5 Laid up, vessels under repair and ship building contracts

Laid up vessels and vessels under repair qualify if the vessel type in question qualifies for the scheme as such. Further, shipbuilding contracts concerning qualifying vessels are accepted as qualifying assets.

Laid up vessels and vessels under repair are vessels that are temporary without employment, due to market conditions or necessary repairing, respectively. Such vessels are not generating current earnings, but are kept within the special tax system. A forced removal of such vessels from the tax scheme during the lay-up/repair period would mean an administrative burden on the ship owners and the tax administration. Further, re-entry into the scheme may trigger taxation of capital gains, making further activity within the scheme less attractive. This would be contrary to the purpose of the special tax system. Lay ups and repairs are part of business within the ship owner industry, and there is no reason to exclude laid up vessels and vessels under repair from the scheme.

Ship building contracts concerning newbuildings are allowed within the scheme. The newbulidings may be replacing vessels, adding to the fleet, or the company may be recently established and contracting vessels in order to initiate shipping activities. In all cases, the contracting is an integrated part of the shipping activity. Further, entry into the special tax system after the completion of a vessel may trigger taxation of capital gains, making it less attractive to enter the scheme.

5.6 Expansion of the special tax scheme for shipping as from 2017 – inclusion of windmill farm vessels

According to the current administrative practice, vessels involved in activity in connection with construction, maintenance, repair and disassembly of windmills at sea,

may be eligible for the special tax scheme only to the extent that the vessels are used in transportation assignments ("maritime transport"). More specifically, vessels used directly in installation activities have not been accepted for special shipping tax. Vessels used in transport and placement of windmill parts however will be approved, provided that the placement of the windmills can be considered as unloading of the vessel, and thereby a natural part of the transport assignment. Other activities are not consistent with the notion of «maritime transport», and have so far not been considered eligible under the scheme.

It follows from section 5.2 VI above that the tax authorities have so far only approved the following windmill farm vessel types:

- Vessels transporting and unloading parts to windmills at sea, but not taking part in construction, maintenance etc.
- Installation support vessels for windmill farms (ISVs). ISVs supports the connection of cables to windmills at sea. The vessels are used for transporting crew and equipment to wind mill farms and between windmills
- Vessels used for transport and grouting of concrete to wind turbine foundations

A number of advanced vessels constructed for use in the oil service sector are laid up due to the current downturn of activity within the petroleum industry. Because of the limitations concerning vessels types allowed within the special tax scheme, it is not possible to make use of these vessels for the purpose of construction, maintenance etc. on windmill farms at sea while still being taxed under the scheme. The reason is that current scheme only covers support vessels in petroleum activities, not support vessels in other activities.

On 20 December 2016, the Norwegian Tax Act was amended in order to make vessels involved in activity in connection with construction, maintenance, repair and disassembly of windmills at sea eligible for the shipping tax scheme, even when they are not used in transportation assignments.

This amendment clarifies that the treatment of windmill farm vessels under the special tax system for shipping. At the same time, it is clear that by this amendment, the scheme will be expanded to vessels not literally comprised by the definition of maritime transport in the Authority's state aid guidelines.

The amendment was adopted by Parliament on 20 December 2016, but its entry into force was postponed, pending a final decision by the EFTA Surveillance Authority.[14] In this letter, the Ministry notifies the expansion of the scheme with effect as from the taxation period of 2017, i.e. as from 1 January 2017.

[14] The decision on when to implement the amendment has been delegated to the Ministry of Finance.

The expansion means that vessels that are engaged in activities in the form of construction, maintenance, repair and disassembly of windmills at sea will be eligible for the scheme. This includes vessels providing extra capacity at the offshore construction/repair/maintenance/disassembly site. The extra capacity vessels are used for temporary accommodation of crew during the mission, as workshop facilities and/or storage of spare parts, tools etc.

The tax scheme will not be available to windmill farm vessels operating in Norwegian internal waters or territorial waters.[15] The reasoning behind this limitation is that foreign companies performing activities on windmill farms in Norwegian internal waters or territorial waters will be liable to tax in Norway. Consequently, Norwegian companies performing such activities in internal or territorial waters should also be liable to tax.

Windmill farms at sea is already a significant industry in Europe. It represents a large potential for decarbonising and safeguarding energy production, and gives a competitive edge for European companies.

In some cases, issues concerning biodiversity, fisheries and ship transport may restrict the development of offshore wind power near the shores. In the years to come, the need for a specialised support fleet is likely to increase. Reduced activity within the petroleum sector reinforces offshore wind power as an attractive business area for companies with vessels, crew and knowledge connected to the petroleum offshore service sector. In a survey made by the Norwegian Shipowners' Association, about 90 percent of the offshore service providers stated that offshore wind power provides interesting business opportunities.[16]

In the same way as support vessels in petroleum activities, windmill farm vessels operate under similar competitive and technical conditions as vessels involved in the transportation of goods and passengers by sea. They do require the same level of qualification for seafarers and faces the same risk of relocation of on-shore activities. Fierce competition at an international market calls for inclusion of such vessels under the special tax scheme, in order to achieve the goals set out in the Maritime Guidelines. Activities involving windmill farm vessels should therefore be eligible for aid under the maritime transport guidelines.

Norwegian authorities believe that the proposed rule complies with the standstill obligation and has incentive effect. Although the rule was adopted by Parliament on 20 December 2016, its entry into force is made conditional upon approval from the Authority. After the Authority adopts its decision, the new rule, if approved, will enter into force by way of decision by the Ministry of Finance.

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[15] The Norwegian territorial waters are extending 12 nautical miles from the sea boundary ("grunnlinjen").
[16] Cf. attachment 13 to this letter - Memo of 31 March 2017 by the Norwegian Shipowners' Association.

The inclusion of the windmill farm vessels was announced on 6 October 2017 in connection with the National Budget for 2018.[17] The measure received attention both from advisors and the industry.[18] Based on inter alia enquiries and initiatives made during the past three years, it is our impression that the windmill farm vessel segment is very concerned with the matter.

When the new rules enter into force, they will have retroactive effect as from of 1 January 2017. Once approved, the standstill-obligation does not in principle prevent a measure from being fully adopted, also in respect of a period predating the Authority's decision.[19]

Although the new rules will have retroactive effect as from the 1 January 2017, Norwegian authorities argue that the measure has incentive effect also for activities initiated between 1 January 2017 and the date the new rule comes into force. The reason for this is that it is only fair to assume that the industry, as of 1 January 2017, has adjusted its activities taking the new rule into consideration, in accordance with the information provided by the authorities.

In support of our view, we wish to point to the Authority's decision 150/16/COL regarding amendment to the Norwegian Tax Act concerning charges in the depreciation rules for wind power plants.[20] That decision confirms that the fact that a state postpones the entry into force of a measure in order to comply with the standstill obligation does not prevent that same measure from having incentive effect where the industry was informed of the new rule and presumably acted in accordance with it.[21]

The information that new tax rules for windmill vessels were adopted, has been readily available to the industry since the day the new rules were passed in Parliament. From that day on, it was known that the new rules would apply as from 1 January 2017, regardless of when the entry into force of the rules. On this background, Norwegian authorities assume that the industry has acted on these premises. In particular, business decisions have most likely been adopted built on the assumption that these new rules will apply to them. Consequently, the rules has induced the investment in the named activities leading the investors in this sector to change or modify their behaviour.

On this background, Norwegian authorities argue that the proposed measure both complies with the standstill obligation and has incentive effect.

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[17] http://www.statsbudsjettet.no/Statsbudsjettet-2017/Statsbudsjettet-fra-A-til-A/Vindmollefartoyer/#artikkel
[18] See for example the article "Viktige tiltak i krevende tider" published by the Norwegian Shipowners' Association: https://www.rederi.no/aktuelt/2016/viktige-tiltak-i-krevende-tider/
[19] See to this effect C-384/07 in particular para. 25-26.
[20] Case 79160, Document No 80 4573.
[21] See chapter 2.3.4 of the decision to this effect.

6. QUALIFIED ACTIVITIES – ANCILLIARY ACTIVITIES

6.1 Principal activities

Qualifying activities are ownership, leasing and operation of ships whether directly owned or chartered in. The notified scheme includes some restrictions on chartering in and chartering out activities, cf. section 7 below.

Capital gains on the sale of assets used in connection with qualifying shipping activities are included in the profits that are tax exempt.

Although Section 3.1 Paragraph 10 of the Maritime Guidelines shows that the Authority has found it appropriate to extend the possibility of tax relief to ship management companies, ship management companies are not eligible under the Norwegian special tax system. However, strategic and commercial management, including daily technical operations and maintenance of ships, is allowed for the purpose of the special tax system for shipping companies. There is no general strategic management requirement in the Norwegian tax system for shipping, i.e. it is not required that vessels under the scheme be strategically and commercially managed from Norway (or from the EEA). For companies chartering out parts of the fleet on bareboat terms, the notified scheme implies that strategic management of all vessels chartered out on bareboat terms must be carried out from the EEA area, cf. section 7.2 below.

Companies within the special tax system are entitled to have employees of their own. Under the previous tax system (pre 2007), only ownership, leasing and operation of ships were allowed activities. Thus, all services had to be performed by companies outside the special tax system. Under the 2007 scheme, a company can perform strategic and commercial management, including daily technical operations and maintenance for vessels owned or chartered in by the company itself and vessels owned or chartered in by associated limited companies, associated partnerships, associated controlled foreign companies and shipping pool companies (where the company is one of the joint venturers).

Currency hedging instruments connected to qualifying shipping activities are, for taxation purposes, treated in the same way as shipping revenues, i.e. a profit is tax exempted and a loss is not tax deductible, cf. the Authority decision 292/10/COL.

Eligible undertakings may generate income as a result of joint and several liability for employer obligations under Norwegian law. For taxation purposes, such income is treated in the same way as shipping revenues, that is, any profits are exempted from ordinary corporate tax whereas any losses are not tax deductible, cf. the Authority decision 322/14/COL.

6.2 Ancillary activities

A number of ancillary activities are within the scope of the shipping tax regime as notified by the Ministry of Finance namely:

- loading and unloading of goods;
- temporary storage of goods at, or near the harbour, pending further transport;
- transport of goods and persons in the port area;
- embarking and disembarking of persons;
- sale of goods and services for consumption on board;
- leasing out of containers;
- operation of ticket offices and passenger terminals;
- hiring out of conference rooms, and
- door-to-door transport for the maritime leg of the transport only (i.e. joint transport that consists of sea transport by a qualifying vessel, and inland/air transport, when the inland/air transport is carried out by an independent contractor).

As mentioned above, a company can perform strategic and commercial management, including technical operations and daily maintenance, for its own vessels, and vessels in associated companies, partnerships, CFCs and shipping pool companies (where the company is one of the joint venturers), regardless of whether the associated company is taxed under the special tax system. Other secondary activities can only be performed for the company's own vessels, and vessels in affiliated companies taxed under the special tax system.

Temporary storage of goods, at or near the harbour, is an integrated part of maritime transport services. In connection with the loading or unloading of goods that are being transported by a shipping company's vessels, it can be necessary and practical to place the cargo temporary at the harbour or at a storage nearby, pending further transport. This activity is closely linked to and carried out in connection with maritime transport, and should therefore be considered eligible for state aid according to the Maritime Guidelines.

Door-to-door-transport is a joint transport that consists of sea transport by a qualifying vessel and inland/air transport, when the inland/air transport is carried out by a third party contractor. The transport agreement with the third-party contractor has to be made on normal market conditions, and the remuneration that the protractor receives for the inland/air transport is subject to corporate taxation. The Ministry considers door-to-door-transport to be integral to and inherent in the overall transport service provided by shipping companies. The ability for shipowners to offer integrated transport contracts, although not taking part in inland/air transport activities themselves, is important in order to be competitive in the maritime transport market.

The European Commission has approved door-to-door-transport in the Danish special tax system[22]

To ensure that the scope of the special tax system is limited to genuine maritime transport, ancillary activities will benefit from the tax exemption only insofar as they are closely connected to the transport services that are subject to the scheme.[23]

According to the Commission decision of 18 December 2015 (SA.33828), concerning shipping taxation in Greece, paragraph 127, "core revenues" of beneficiaries of the Greek special tax system should always cover more than 50 per cent of the vessel's total (core and ancillary) gross revenues.[24]

In the Norwegian special tax system for shipping, the only non-core ancillary activities allowed under the shipping tax scheme are 1) income from sale of services for consumption on board and 2) hiring out of conference rooms. Our understanding is that the remaining ancillary activities allowed in the Norwegian special tax system listed above fall within the category "core revenue", as defined by the Commission in its decision of 18 December 2015, paragraph 126-127.

Although it is not an explicit requirement in the Norwegian special tax system for shipping, that such core revenues should cover more than 50 per cent of a vessel's total (core and ancillary) gross revenues, it is unlikely that the core revenues will be less than 50 per cent of gross revenues, owing to the fact that ancillary activities will benefit from the tax exemption only insofar as they are closely connected to the transport services. This criterion in effect excludes the revenue intensive non-core activities. In our view and based on practical experience, the possibility that gross revenues from sale of services for consumption on board and/or hiring out of conference rooms could amount to 50 per cent of a vessel's total (core and ancillary) gross revenues is only theoretical. In light of the closely connected criterion, Norwegian authorities believe that a requirement that non-core revenue cannot cover more than 50 per cent of gross revenues is not needed in the Norwegian system in order to ensure that the main revenue originates from core shipping activities.

Compliance with the "closely connected"-requirement is ensured by the tax office. In the same way as for other requirements concerning the special tax scheme, the requirement may be subject to subsequent tax controls by the tax office. We refer to the description of the control and sanction measures in section 11 below.

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[22] Cf. the European Commission's decision C (2002) 931 dated 12 March 2002 section 2.10.4.

[23] Cf. section 8-13-1 b) and c) of the Ministry's supplementary regulations to the Tax Act (forskrift 19. november 1999 nr. 1158 til utfylling og gjennomføring mv. av skatteloven av 26. mars 1999 nr. 14).

[24] We assume that although the Commision in the same desicion, paragraph 134, uses the term "ancilliary activities" when adressing bareboat chartering out, income from bareboat chartering out is not to be included in "non-core revenue" for the purpose of a cap on such revenue.

7. CHARTERING IN AND OUT

7.1 General remarks

The current Norwegian special tax scheme does not contain restrictions with respect to allowing income related to the chartering in or out of vessels. Chartering activities have been an integrated part of the special tax system since it was established in 1996, as approved by the Authority in 1998 and 2008.

The Norwegian shipping industry engages in diversified operations worldwide, where all the various forms of chartering (rental of ships) are being used. Chartering in and out of vessels provides operating flexibility for the companies, and enables them to meet market changes and respond adequately to secure their position also by using the various forms of chartering of vessels.

In our view, state aid to chartering activities contributes to the achievement of the maritime guidelines objectives in the Norwegian maritime sector. Chartering of vessels, whether it is on time charter, voyage charter or bareboat terms, is an integrated part of the operation of a shipping company's fleet. For this reason, the activity is allowed without restrictions in the current Norwegian special tax scheme.

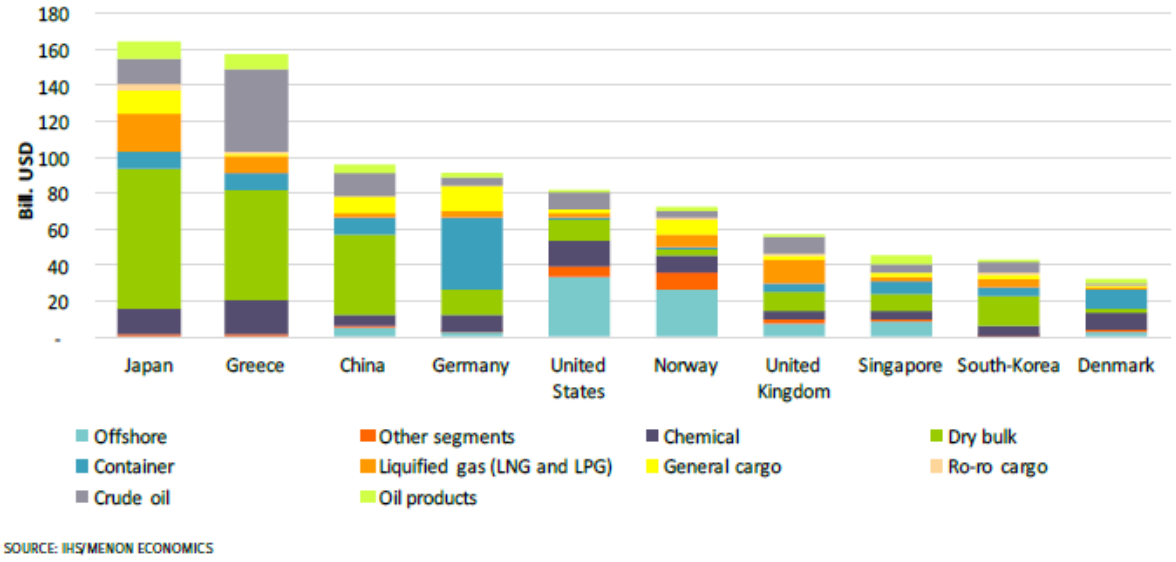
For the reasons explained below, Norwegian authorities hereby notify a scheme with certain limitations on chartering out on bareboat terms and chartering in on time charter/voyage charter terms. We believe that the system proposed continues to meet the needs of the industry to use these forms of activity where necessary, and ensures that only companies actually involved in maritime activity are taxed within the shipping tax scheme.

7.2 Bareboat chartering out

In its most simplistic form, bareboat chartering can be defined as the rental of a vessel only, from a ship-owning company to an operator. For the pupose of the notified scheme, bareboat chartering is defined as the chartering out of vessels without crew. Chartering on bareboat terms is a contract form used in all shipping segments, but it is particularly common in the offshore segment. Bareboat chartering out allows shipping companies to meet the regulatory and commercial needs and requirements in diverse international markets worldwide.

The Norwegian shipping sector differs substantially from the shipping sectors of other countries. The Norwegian offshore fleet is the second largest (second only to United States) and most modern offshore fleet in the world. Unlike the shipping sectors of other countries (USA excluded) the Norwegian maritime sector is dominated by offshore service vessels.

The figure below shows the market value of the top 10 merchant fleets of the world by segments as of 2015.[25]



SOURCE: IHS/MENON ECONOMICS

The Norwegian mobile offshore industry earns a large part of its income from activities connected to foreign continental shelves. Important markets include the North Sea, Australia, West Africa, Brazil, Indonesia, Malaysia, the Mexico Gulf and Canada.

Although the vessels involved in the named activities, may in some cases be chartered out on contracts that include bareboat terms and in some cases are registered in local ship registers (cf. section 9 below), the Norwegian content is overall substantial. The spill over effects contributes to the Norwegian maritime sector. For example, it will often be the case that a Norwegian owned ship operating in foreign waters is designed, built, financed, classified and insured by Norwegian enterprises.

The Norwegian content in the operation and management of vessels varies according to the individual contracts, and is ultimately controlled by local content requirements. The local hiring obligation may necessitate the signing of multiple contacts with the same contracting party. The vessel is charted out on bareboat terms, ensuring the shipowner predictability for a given period. Contracts concerning technical and crew management etc. are signed separately, and can be adapted to the varying local content requirements and the customers' needs.

The Norwegian maritime sector is within a number of segments a strong, global force. It is among the world's most innovative maritime sectors and a driving force in technological development. The petroleum service segment increasingly dominates the sector. The activity takes place worldwide, with contributions from the knowledge-

[25] The figure is published in the report "Maritime Outlook 2016" by the Norwegian Shipowners' Association.

based Norwegian maritime sector. Norwegian shipping companies are a driving force in the development of new environmental technology.

In the Norwegian context, bareboat chartering out arrangements adds to the commodity and service flows within the Norwegian and European shipping sector and makes positive contributions to the achievement of the aims of the Maritime Guidelines.

In particular, the Norwegian maritime sectors' efforts in the offshore segment abroad rely heavily on suppliers in the Norwegian maritime supply industry. The fleet is highly specialised and technologically advanced. The contract value of an offshore service vessel may be multiple times the value of for example a bulk carrier. Although the market situation in the offshore sector has been challenging for some time, there are still Norwegian offshore vessels under construction in Norwegian shipyards.

Largely, Norwegian suppliers carry out the development of the vessels. An illustration of this is included in the Norwegian Shipowners' Association publication "Norwegian offshore shipping companies – local value creation, global success" (see attachment 2). The illustration on page 24 of the report lists the 94 different Norwegian equipment suppliers involved in the construction of the AHTS vessel "Normand Prosper", owned by the Norwegian shipping company Solstad Offshore.

Case practise by the Commission concerning the Commission's Maritime Guidelines are mainly accommodated to countries with a less significant offshore fleet which for the large part does not operate in the same markets and does not face the same local content requirements. The special tax schemes of those countries, which are mainly targeted at traditional shipping, are clearly different from the Norwegian special tax scheme.

Companies within the Norwegian shipping tax scheme servicing the oil, gas and renewable industries at sea will usually separate the vessel ownership and operational activities in order to be competitive in the operating state. In the markets where these companies operate, being able to offer vessels on bareboat terms is very often a prerequisite when bidding for contracts on foreign continental shelves, i.a. due to regulatory requirements with respect to staffing of vessels etc. set by the host state.

In a number of jurisdictions, local manning requirements apply to vessels operating on the continental shelf. The specific rules on what positions on board that must be manned locally vary according to i.a. the vessel type and the duration of the vessel's assignment.

In practice, local companies that know the market and are known to potential employees often need to undertake hiring of local crew necessary to fulfil the local content requirements. In countries typically demanding local content, the labour

market concerning resident employees is often tight. This is the case in for example Brazil and Australia. Norwegian enterprises within the offshore services segment are heavily engaged in operations on the Brazilian and Australian continental shelves.

Norwegian authorities are aware only of a few Norwegian ship-owners that have been able to set up their own local subsidiaries, carrying out recruiting services for the enterprise. This is a viable option only in cases where the size and duration of the operations in the country in question, makes it possible to undertake such an investment. In other cases, the shipowners must rely on existing local companies that are able provide for the recruitment of crew. The Norwegian offshore service sector is characterised by a number of smaller enterprises with few vessels. These will often lack the resources to undertaking such long-term investments. For such enterprises, the only option in order to compete on certain foreign markets is to charter out on bareboat terms, leaving the task of recruiting local employees to local companies.

To substantiate this line of argumentation, Norwegian authorities refer to Attachment 3 to this letter. The attachment is a memo dated 10 April 2013 by the Brazilian law firm KINCAID to the Norwegian Shipowners' Association, describing the obligation to hire a certain proportion of Brazilian employees on foreign vessels and the challenges this imposes on the Norwegian offshore service segment. The memo demonstrates that the rules can be complex and difficult to meet without assistance from a local company.

Another country in which local content requirements may render it necessary to charter out vessels on bareboat terms is Canada. A case study prepared by Center for Energy Economics describes local content requirements in North Atlantic Canada. (See attachment 4.) The study shows that both local management and local employment may be necessary in order for vessels to operate offshore in the provinces of Newfoundland and Nova Scotia.

Incidentally, the study also refers to local content requirements in the non-EEA jurisdictions of Nigeria, Brazil and Australia, cf. page 6 and 7 of the study.

Chartering out of vessels on bareboat terms is both common and necessary arrangements. In many cases, operating a vessel on bareboat terms is also a contractual requirement set by the oil or renewable contracting parties.

There may also be other commercial reasons why a shipping company would prefer bareboat chartering out, for instance when providing ships to a charterer for operation in territories where the risk related to crew cost and availability, cost and timely access to ship repairs and maintenance, spare parts and other necessities for running the ship, is considered unacceptable. These are important factors when assessing the commercial risks involved for instance with providing transportation services to charterers operating in some countries. Many shipping companies have experienced difficulties in managing an efficient technical operation of ships in some territories.

In their Master Thesis, Thomas Vikenes and Carl-Emil Kjølås Johannessen describe challenges connected to technical management of vessels in Brazil.[26] These challenges implies that shipping companies need to establish a substantial level of activity in Brazil in order to carry out technical management by their own. For companies not able to perform such activities, technical management services must be contracted to local management companies or other third parties. Restrictions on this possibility will affect the smaller shipping companies the most because they are unable to establish the necessary level of activity in order to carry out technical management themselves.

Offshore enterprises applying bareboat chartering out as a part of their maritime operations contribute significantly to the maintaining of a strong and knowledge-based Norwegian maritime sector. As far as the Ministry is aware, no other EEA country is in a comparable situation to the Norwegian maritime sector in relation to the significance of bareboat chartering out activities.

On a general note, it should also be stressed that bareboat chartering out involves and requires certain types of maritime competencies and know how, and is not an entirely passive activity. The ship owner remains, for instance, responsible for structural maintenance, inspection by class, insurance and modifications to the ship imposed by new rules for safety and environment. The owner also has a direct economic interest in the market value of the ship, which is a direct function of the freight market. Many contracts are therefore not "clear-cut" bareboat contracts but retain responsibility for certain tasks, for example technical management with the shipowning company.

In many cases, the charter will take elements from both the time- and bareboat-charter formats when the responsibilities are distributed between the parties. The rights and obligations between the parties are negotiated as part of the contract. This means that it is often not possible to define a negotiated charter contract as either a clear cut time or bareboat charter. It may also be that for commercial reasons even under a typical time charter contract, the shipowners may opt not to provide crewing and other technical ship management services themselves, but rather to contract these services from an independent, professional third party supplier who can provide such services on more competitive terms. In some cases, the chartering is essential when a newly established shipping company with a narrow capital basis needs extra tonnage to realise its ambitions.

Flexibility concerning bareboat chartering is of great importance also in some technically advanced sub-segments of the Norwegian deep-sea fleet, including gas tankers, chemical tankers and ro-ro carriers (car ships). In individual cases within the sub-segments, chartering out on bareboat terms out may be the commercially relevant

[26] See attachment 5 on page 65 et seq.

form of chartering out. Safe for the general trends described above it is difficult to point out certain universal reasons behind the commercial practises in the market.

For all segments, a commercial decision to apply bareboat terms may be founded on one or more of the following reasons connected to staffing of the vessel in question (the list is not exhaustive):

- Local legislation requires local crew not available (in sufficient number) to the shipping company
- The customer has special demands concerning the crew, and such demands cannot be met by the shipping company itself
- The charterer wishes to employ its available crew on board the vessel
- The contracting parties wishes to engage a third-party crew manning company that also handles reporting obligations, tax payments etc.
- One of the contracting parties has an ownership interest in a crew manning company, and therefore wishes to engage that company

In our view, bareboat arrangements allow the ownership of vessels to be retained in Norway, and thereby contributes to the aims of the Maritime Guidelines. In addition, the connection to Norwegian maritime sector makes it likely that a substantial part of land-based activities characterized by advanced and knowledge-based technology will be carried out in Norway. Further, even if the charterer is located outside of the Norway, the ship owner or a third party located within Norway or the EEA may carry out some management services. The crew may also be fully or partly European.

On this background it must be concluded that in a Norwegian context, bareboat chartering out arrangements adds to the commodity and service flows within the Norwegian and European shipping sector and makes positive contributions to the achievement of the aims of the Maritime Guidelines..

Looking at the facts, a survey (2012) in the Norwegian shipping industry indicates that bareboat chartering takes place in all ship segments, but more frequently for the offshore companies.[27] The share of bareboat chartering out is on average 36 per cent, and bareboat rental takes place in approximately 25 per cent of the shipping companies. To our knowledge, the normal case is that only a smaller percentage of the company's total tonnage is chartered out on bareboat terms. That means that very few companies have a fleet of bareboat chartered out vessels only.

The Ministry acknowledges that certain limitations on bareboat chartering out would contribute to ensuring that core shipping activities remain the main activity of companies taxed under the special tax scheme. In particular, a limitation would exclude

[27] The survey is referred to in a letter from the Norwegian Shipowners' Association to the Ministry of Finance of 12 October 2016 (see attachment 6 to this letter).

pure ship lessors from the scheme. In its decision of 18 December 2015 in the Greek tonnage tax case (SA.33828), the Commission stipulated that no more than 50 percent of a company's fleet should be chartered out on bareboat terms.[28] In line with the practice of the Commission, Norwegian authorities plan to introduce a new restriction on bareboat chartering out whereby such activity should not exceed 50 percent of the company's fleet during an income year.

The limitation mentioned do not apply to intra-group bareboat contracts. The limitation on bareboat chartering out should be measured on a yearly basis, but counting the tonnage chartered out for each day of the year. Further, there should be an option to measure the bareboat chartered out share of the total tonnage over a period of four years, in order to avoid unmerited exclusions from the special tax scheme in situations where the share is in excess of the maximum share for a short term period. The share of tonnage chartered out on bareboat terms will be measured on a company group level. This is due to the fact that shipping enterprises are often organised as company groups with special purpose companies owning one vessel each.

In addition to the overall cap, the Commission has further required that the chartering out on bareboat terms must be related to temporary excess capacity and limited to a period of 3 years. Furthermore, the excess capacity must not be acquired specifically for chartering out purposes. In the following, Norwegian authorities will explain that other additional requirements are better suited to achieve the objectives in the Maritime Guidelines in the Norwegian context.

The Ministry is concerned that the three additional requirements set out in the Commissions practice in relation to maritime sectors which are different from the Norwegian, would prevent the achievement of the goals of the Maritime Guidelines within the specific context of the Norwegian maritime sector. As we have pointed out, the Norwegian offshore vessel segment offers services on a market where bareboat chartering out contracts are regular and necessary arrangements, sometimes required by regulatory requirements. These activities are therefore a part of regular business operations, and not limited to situations of temporary excess capacity for a limited period. Regardless of the specific design of a 3-year limitation, the limitation may prevent Norwegian shipping companies from operating on a number of foreign continental shelves as they operate in markets where bareboat is a necessary, permanent arrangement and where the normal contract period required by the customer may be longer than 3 years. Further, as bareboat chartering out is necessary in order to operate in some territories, the vessels in question are in some cases acquired specifically in order to engage in such operations.

The additional restrictions on bareboat chartering out set out in the practice of the Commission, will severely constraint the possibility to enter into commercially viable

[28] Cf. section 4.2.1.2 of the Commission decision.

agreements. As mentioned above, Norwegian offshore service sector is characterized by the presence of small enterprises with few vessels. This distinctive feature of the Norwegian maritime industry makes it particularly difficult to meet rigid requirements concerning temporary excess capacity, time limits and acquiring purposes.

Our view is therefore that the achievement of the goals set out in the Maritime Guidelines is best served by allowing a certain share of bareboat chartering out activity, not limited to temporary excess capacity. Further, vessels acquired specifically for chartering out purposes should be allowed under the special tax scheme.

In the offshore sector, bareboat chartering out contracts are usually of a duration of between 3 and 5 years, often with an option to extend the charter period (up to 3 years). It follows from this that a 3 year limitation relating either to the specific vessel or the company itself would in effect prevent bareboat chartering out and consequently operations in several jurisdictions outside the EEA. Reviewing the information Norwegian authorities possess at this point, we have reason to believe that the Norwegian offshore sector is in a particular situation compared to other EEA countries in this regard as it is particularly big and particularly active in such territories. Consequently, Norwegian authorities notify an alternative additional limitation to the effect that bareboat chartering contracts must not exceed a contract period of 5 years, with a possibility to extend the contract for up to 3 years. A 5+3 year limitation correspond with common practice concerning contract periods in the offshore service sector. We believe that this limitation is better suited to achieve the objectives of the Maritime Guidelines while also taking into account the characteristics of the Norwegian fleet.

Furthermore, Norwegian authorities suggest another additional requirement to the effect that strategic management of all vessels chartered out on bareboat terms must be carried out in the EEA. This excludes pure ship lessors from the special tax system and ensures an even closer connection to the EEA maritime sector where companies are engaged in activities requiring them to charter out on bareboat terms.

The strategic management is the higher management of the company, such as carried out by the CEO and the Board. It includes the determination of plans, budgets and guidelines for its operations together with the financial management of the company, such as the signing of agreements for purchase / sale of ships, long-term charters, various cooperation agreements, financing agreements, loan agreements, pledge agreements and insurance contracts. Thereby, the strategic management is strongly connected to maritime operations and contribute significantly to the knowledge-based maritime sector with the EEA.

Although the petroleum sector is a good example to illustrate the needs in the Norwegian sector, Norwegian authorities observe that the flexibility concerning bareboat chartering is present also in sub-segments of the Norwegian fleet. The legal

and market conditions is varying and continually changing. It is therefore difficult to foresee and regulate exactly what type of vessels and which market segments that meet the challenges described above and consequently have the commercial need to charter out on bareboat terms under the prescribed conditions. In general, different types of vessels should be treated in the same way. The requirements notified by Norway will therefore apply to all sub-segments of the Norwegian shipping sector.

On this background and acknowledging the necessity of the exclusion of pure ship lessors, the Ministry notifies a rule allowing that revenues from bareboat activity can be subject to the Norwegian special tax system for shipping under the following conditions:

- The activity must not exceed 50 per cent of the company group's fleet within the special tax system during the income year. There should also be an option to measure the bareboat chartered out fleet over a period of four years.
- For companies chartering out parts of the fleet on bareboat terms, strategic management of all vessels chartered out on bareboat terms must be carried out from the EEA area.
- Bareboat chartering contracts must not exceed a contract period of 5 years, with a possibility to extend the contract for up to 3 years.
- Intra-group bareboat chartering out is allowed unconditionally.

As mentioned above, in many cases, the charter will take elements from both the time and bareboat charter formats when the responsibilities, rights and obligations between the parties are negotiated.

For the purpose of the notified limitation on bareboat chartering out, bareboat chartering is defined as the chartering out of vessels without crew. However, when assessing chartering contracts, the tax authorities will have to examine the details of the contract agreements in order to asess whether they should be considered as being bareboat contracts.

Different forms of contract agreements used i.a. in Brazil, implies that vessels are being chartered out on bareboat terms from a ship-owning Norwegian company to an unrelated party. However, in some cases the shipping enterprise carries out the staffing of the vessel through a local affiliate (a subsidiary company). In those cases, the other contracting party in reality receives the same service as under a time charter contract (chartering of a vessel with crew). The Ministry would like to clarify that it does not intend to apply the abovementioned limitations on bareboat chartering out to chartering agreements of the said type. In our view, these agreements although formally entered into as bareboat chartering agreements in reality deliver a time-charter service to the customer. In line with the aim of the Maritime guidelines, we assume that the decisive factor should be that the enterprise is carrying out the staffing within the group.

7.3 Chartering in on bareboat terms

We refer to the remarks made under sections 7.1 and 7.4. Chartering in provides both commercial and operational flexibility. State aid to companies chartering in on bareboat terms does serve the aim of preservation of maritime know-how within the EEA. The reasoning behind restrictions on chartering in on voyage charter/time charter terms cannot be extended to companies chartering in on bareboat terms where the company operates the ship, and is responsible for the crew and technical management. It is the Ministry's understanding that chartering in on bareboat terms, i.e. to rent vessels without a crew provided by the charterer, is eligible for state aid according to practice by the Commission.[29]

7.4 Voyage charter/time charter

As stated in section 7.1, chartering of vessels, including chartering in on time charter and voyage charter, is considered a fully integrated part of the operation of a shipping company. Customer demands can vary significantly over short periods and shipowners have to be able to respond adequately and in a flexible manner. Time and voyage chartering is one of the key mechanisms at their disposal. Indeed, by chartering a vessel, the commercial/operational control is given to the charterer for an agreed period, while leaving ownership and management of the vessel in the hands of the shipowner. The latter generally retains the operating costs (i.e. the crew, maintenance and repair) and the charterer covers all voyage related costs (i.e. bunkers, port charges, etc.) as well as cargo-handling costs.

A number of reasons make chartering in attractive to a company. Firstly, it provides a certain degree of operating flexibility. Time chartering can range from a term of years to weeks or days. It is used to respond to a surge in demand or, conversely, to return the vessels swiftly should the demand weaken. It therefore allows shipowners to accommodate their customers' needs optimally. This is particularly useful in periods when markets are volatile. Moreover, companies may decide that in a specific economic environment, it is more convenient to pay a stable monthly hire rather than raise the considerable capital to buy another vessel. Buying vessels is often not an attractive alternative, and new buildings are long-term investments, normally with a delivery period of two to three years. Finally, companies may find they have different business strengths – some focus on owning assets, whilst others have a less capital-intensive strategy and focus on operating chartered in assets. Many smaller shipowners do not have the market knowledge or an organisation to conclude business with the end user, and instead choose to time charter the vessels out to ship operators.

Norwegian ship owners and ship operators have over the past decades a proven record of accomplishment of excellent management and operational abilities, and, thus, high-

[29] See for instance the commission decision of 25 February 2009 in case C 2/08 concerning the Irish tonnage tax, paragraph 6.

level employment and skills have been developed and maintained by chartering tonnage into Norwegian companies.

On this background, the Ministry finds that over the whole, companies chartering in on time charter and voyage charter contributes to the preservation of maritime know-how in the EEA. We are however, aware that according to several decisions by the Commission, a limitation on the chartering in of non-EEA flagged vessels on time charter or voyage charter terms may be appropriate in order to ensure that the beneficiaries of aid through a shipping tax scheme do not lose their know-how in terms of crew management and technical management. In Case N 563/01, approved on 12 March 2002, concerning Danish tonnage tax, a ratio of owned to time chartered ships of 1:4 was approved. This opinion seems to be confirmed by the Commission's decision in case N 171/2004 concerning the Danish tonnage tax (cf. paragraph 30) and the decision of 13 April 2015 concerning the Italian tonnage tax (cf. paragraph 62).

Further, in its decision of 25 February 2009 in case N 572/07 concerning the Irish tonnage tax, the Commission approved a ratio of owned to time chartered ships of 1:10 provided that each of the chartered-in vessels is registered in a Community or EEA maritime register or the crew management and technical management of the chartered-in vessel are carried out on the territory of the Community or the EEA.

The Ministry notify a limitation to 90 per cent on the chartering in of non-EEA flagged vessels on time charter or voyage charter terms. This would be in line with the Maritime Guidelines and contribute to the achievement of their aim. Considering the Norwegian maritime sector, a 90 per cent limitation would be suitable in order maintain needed flexibility for companies within the special tax scheme.

Any limitations on chartering in will be measured on a yearly basis, but counting the tonnage chartered out for each day of the year. The share of tonnage chartered in will be measured on a company group level.

For the purpose of the notified scheme, time charter and voyage charter are defined as the chartering in of vessels with crew. When assessing chartering in contracts, the tax authorities will have to examine the concrete details of the contract agreements in order to assess whether they should be considered as being time charter or voyage charter contracts.

8. CALCULATION OF TAX

The special tax system for shipping companies system is an exemption system, in which no ordinary corporate tax is imposed on profits derived from eligible activities. Instead, ship owners are obliged to pay a tonnage tax calculated by reference to each of the vessels a participating company operates. The tonnage tax rates vary with the net tonnage of the vessel.

The tonnage tax is calculated by reference to the net tonnage of each of the vessels a participating company operates at the following rates per day:

- no tax for the first 1000 net tons, thereafter,
- NOK 18 per 1000 net tons from 1001 to 10 000 net tons, thereafter
- NOK 12 per 1000 net tons from 10 001 to 25 000 net tons, thereafter
- NOK 6 per 1000 net tons above 25 000 net tons.

The rates above do not correspond to the mode of calculation used to determine a virtual profit to which corporate tax rates will be applied but to the tax which will effectively be paid by the shipping companies. The tonnage tax rate is directly fixed by the Norwegian authorities and is not linked to the corporate taxation system. The tonnage tax is payable irrespective of the company's actual profits or losses.

In its approval of the Norwegian special tax system for shipping of 2007 (755/08/COL) the Authority referred to Section 3.1 Paragraph 18 of the Maritime Guidelines, in which it is inter alia stated:

"In order to keep the present equitable balance, the EC Commission stipulated that it will only approve schemes giving rise to a tax-load for the same tonnage fairly in line with the schemes already approved.

(…)

The Authority will likewise seek to keep an equitable balance in line with already approved systems."

The Authority considered that the tonnage tax rates applicable in Norway kept an equitable balance in line with the tonnage tax regimes in other EEA States. As it appears from the table below, the level of taxation for Norwegian companies is on the whole higher than the rates the Commission has approved for i.a. Cyprus[30] and Croatia.[31] [32]

Net Tonnage					
	0-1000	1001-10000	1001-25000	25001-40000	>40000
Norway	0 €	72.65 € Per 100 NT	48.44 € Per 100 NT	24.22 € Per 100 NT	24.22 € Per 100 NT
Croatia	36.38 € Per 100 NT	30.99 € Per 100 NT	20.21 € Per 100 NT	12.80 € Per 100 NT	7.41 € Per 100 NT
Cyprus	36.07 € Per 100 NT	30.73 € Per 100 NT	20,04 € Per 100 NT	12,69 € Per 100 NT	7,35 € Per 100 NT

The tonnage tax is differentiated within the special tax system for shipping based on a set of pre-defined environmental criteria; cf. the Authority decision 519/14/COL. Based

[30] Commission decision of 24.3.2010 in N 37/2010, Cyprus.
[31] Commission decision of 1.4.2015 in SA.37912 (2013/N) - Croatia
[32] The calculations are based on average exchange rates November 2016 – April 2017 sourced from Eurostat.

on an environmental rating of a ship within the scheme, the shipping company can obtain a reduction of the standard tonnage tax pursuant to the Norwegian Tax Act Section 8-16[33] and the Ministry's supplementary regulations to the Tax Act Section 8-16 Part B[34].

The environmental rating of a ship is carried out as follows: Pursuant to the Norwegian Regulation on Environmental Declaration, shipping companies may submit a voluntary environmental declaration to the Norwegian Maritime Authority, by using the standard Form for Calculation of the Environmental Factor. The Form for Calculation of the Environmental Factor is issued by the Maritime Authority and sets out the criteria used for determining the environmental rating of a ship.

Based on the environmental declaration, the ship will receive an environmental rating on a scale from 1 to 10. Depending on the environmental rating of the ship, the standard tonnage tax may be reduced by up to 25 percent.

The differentiated reduction of the tonnage tax based on the environmental rating of the ship is calculated as follows:

Environmental rating	Tonnage tax reduction
Up to 1	2.5%
1 to 2	5.0%
2 to 3	7.5%
3 to 4	10.0%
4 to 5	12.5%
5 to 6	15.0%
6 to 7	17.5%
7 to 8	20.0%
8 to 9	22.5%
9 to 10	25.0%

The tonnage tax reduction aims at providing an incentive for shipping companies under the scheme to make use of more environmentally sound ships in terms of both technology and operation. The reduction of the tonnage tax aims at rewarding companies for exceeding the mandatory requirements when it comes to environmental performance of their ships.

The total amount of tonnage tax accrued and the total amount of environmental reduction for the income years 2011 – 2015 was as follows:

[33] The Norwegian Tax Act of 26.3.1999 No 14 («*Lov av 26. mars 1999 nr. 14 om skatt av formue og inntekt*»)
[34] Forskrift 19. november 1999 nr. 1158 til utfylling og gjennomføring mv. av skatteloven av 26. mars 1999 nr. 14.

Year	2011	2012	2013	2014	2015
Tonnage Tax (MNOK)[1]	36	39	43	48	45
Environmental reduction (NOK)	215.033	312.197	375.404	445.553	425.645
Number of companies that obtained reduction	29	32	34	29	18

[1] Not including environmental reduction

In the view of the Ministry of Finance, the tonnage tax rates within the special tax system for Shipping, including the differentiated reduction of the tonnage tax, should be held compatible with the EEA Agreement, cf. Article 61(3)(c) of the Agreement and the Maritime Guidelines Section 3.1 Paragraph 17 – 18 and Section 5.

9. FLAG REQUIREMENT

According to Section 3.1 Paragraph 7 of the Maritime Guidelines tax relief schemes should, as a rule, require a link with an EEA flag. However, Section 3.1 Paragraph 8 of the Guidelines supports the view that aid may be exceptionally granted where a fleet also comprises vessels registered outside the EEA:

"Before aid is exceptionally granted (or confirmed) to fleets which also comprise vessels flying other flags, EEA States should ensure that beneficiary companies commit themselves to increasing or at least maintaining under the flag of one of the EEA States the share of tonnage that they will be operating under such flags when these Guidelines become applicable. Whenever a company controls ship operating companies within the meaning of the Seventh Council Directive 83/349/EEC18 (Article 1), incorporated as point 4 of Annex XXII to the EEA Agreement, the above mentioned tonnage share requirement will have to apply to the parent company and subsidiary companies taken together on a consolidated basis. Should a company (or group) fail to respect that requirement, the relevant EEA State should not grant further tax relief with respect to additional non-EEA flagged vessels operated by that company, unless the EEA-flagged share of the global tonnage eligible for tax relief in that EEA State has not decreased on average during the reporting period referred to in the next Paragraph. The EFTA State must inform the Authority of the application of the derogation. The EEA-tonnage share requirement set out in this Paragraph does not apply to undertakings operating at least 60% of their tonnage under a EEA flag."

The Norwegian special tax system requires a link with the flag of one of the EEA States. However, fleets which comprise vessels flying other flags are also eligible provided that the beneficiary companies commit themselves to increase or at least maintain the share of the tonnage operated under the flag of one of the EEA States. The EEA tonnage

share requirement does not apply to undertakings operating at least 60 percent of their tonnage under an EEA flag, or if the EEA flagged share of the total tonnage eligible for tax relief in Norway has not decreased on average during the previous year. For companies within the scheme that prepare consolidated accounts, cf. the Seventh Council Directive 83/349/EEC, the flag requirement applies to the companies as a group.[35]

Tugboats and barges used for transportation of matter from dredging activities are required to be EEA-flagged. (Vessels performing any amount of actual dredging activities are not allowed within the special tax system; cf. Section 3.1 Paragraph 15 – 16 of the Maritime Guidelines and Section 5.3 above.)

The companies within the special tax system are obliged to report to the tax authorities all relevant information concerning their EEA registered tonnage share every year in connection with the tax return. According to the Tax Assessment Act, the tax authorities may request further detailed information and documentation concerning the tonnage and registration of vessels.

Compliance with the "increase or at least maintain" requirement is controlled by the tax office. In the same way as for other requirements concerning the special tax scheme, the flag requirement may be subject to subsequent tax controls by the tax office. The tax authorities will exclude from the special tax system companies that do not meet the flag requirement.
For more detailed description of the control and sanction process we refer to section 11 below.

The Ministry of Finance is of the opinion that the flag requirement as described above complies with the Maritime Guidelines to Section 3.1 Paragraphs 7 – 9.

"(…) recipients must provide the EFTA State concerned with proof that all the conditions for the derogation from the flag link have been fulfilled during the period. Furthermore, evidence must be provided that, in the case of the beneficiary fleet, the tonnage share requirement laid down in the previous Paragraph has been observed and that each vessel of that fleet complies with the relevant international and EEA standards, including those relating to security, safety, environmental performance and on-board working conditions. Should recipients fail to provide such evidence, they will not be allowed to continue to benefit from the tax scheme."

Both the Norwegian International Ship Register (NIS) and the Norwegian Ordinary Ship Register (NOR) qualify as EEA registers as regards the flag requirement. At the same time, there is no requirement to register ships in the Norwegian register in order

[35] A company group may consist of more than one chain of companies within the shipping tax scheme. Each chain will be consolidated separately for the purpose of the flag requirement.

to be eligible under the scheme. Consequently, a company can fulfil the flag requirements by registering in other EEA-registers. This is in line with the Maritime Guidelines Section 2.2 Paragraph 2, in which it is stated that aid schemes should not be conducted at the expense of other EEA States' economies.

The Ministry would like to stress that contrary to the NIS register, the Norwegian shipping tax regime does not maintain trade area limitations. The shipping tax scheme does not exclude vessels in traffic between Norwegian and foreign ports (or between foreign ports). In accordance with the objective of the scheme, it is oriented towards international shipping exposed to world market competition (including traffic connected to petroleum activities on the continental shelf). Some limitations have therefore been made concerning domestic traffic, cf. Section 5.2 above.

Ship-owners are at the outset free to choose the country of registration. Decisions on registration are mainly dependent on the quality and service level of the marine authorities, cost of crew and other framework conditions. Special legal requirements on a national level may also affect the choice of register. The growth of international commercial ship registers has made the marine authorities exposed to competition.

The Norwegian authorities have adopted various incentives to choose the Norwegian flag. These supplement the special tax scheme for shipping. To give a full picture, Norwegian authorities believes it is necessary to give an overview of the system of measures.

The Norwegian International Ship register was established in 1987 as a Norwegian alternative to foreign open registers. The main distinction between the NOR and NIS register, is the possibility for vessels in NIS to employ foreign crew on their domestic wage conditions. This involves that NIS vessels generally have lower operational costs. On the other hand, vessels in NIS have limited access to perform trade in Norway (trade area limitations).

The tax refund scheme for seafarers on Norwegian flagged vessels has since 1993 been developed in order to maintain and develop Norwegian/EEA maritime competencies and practical maritime know how. The Norwegian tax refund scheme has over time developed into an important policy instrument for preserving Norway's position as a leading maritime nation. The scheme is an important element in making the Norwegian ship registers attractive and competitive.

In its maritime strategy the Government has listed a number of measures aimed at making the Norwegian shipping registers more competitive (page 21).[36] These measures are:

[36] See footnote 1.

- a limited softening of the trade area limitations for NIS registered vessels in short sea shipping
- a limited softening of the trade area limitations for NIS registered international ferries
- a limited softening of the trade area limitations for NIS registered construction vessels
- a strengthening of the NOR register's competitiveness, among other things by removing the limitfor maximum refunds in the tax refund scheme for employing seafarers for NOR vessels in short sea shipping and international ferries, as well as for the coastal route Bergen–Kirkenes
- the establishment of a special tax refund scheme adapted to NIS, replacing the current reimbursement scheme. It will give tax refund from the first seafarer. At the same time it will be required that training positions are linked to the scheme
- the establishment of special tax refund schemes with a tax refund level similar to the current NOR scheme for NIS-registered passenger vessels in international traffic and construction vessels in NIS.
- the inclusion of sailing vessels above 498 gross tonnes mainly engaged in education in a tax
- refund scheme corresponding to the coastal route Bergen–Kirkenes.
- a proposition of regulatory changes so that vessels registered in the Norwegian International
- Ship Register (NIS) can carry cargo and passengers between ports at Svalbard as well as between Svalbard and the mainland.

With exemption of a change of the trade area limitation for NIS registered international ferries and the support scheme for these ferries, all these measures are implemented.

Against this background, the Norwegian maritime authorities are focused on customer orientation, effectiveness and expertise. The Maritime Directorate (Sjøfartsdirektoratet) works nationally and internationally on marketing in particular the Norwegian International register as a quality register. This work was also emphasised in the Martime Strategy (chapter 3.3) and the Maritime Directorate is well under way with digitalisation and simplification of their services. In a recent publication, the Maritime Directorate has recently issued a publication (see attachment 14) that describes the implications and advantages of using the NIS register.

Norwegian expertise and innovation strength influences international standards, through i.a. the International Maritime Organisation (IMO). The basis of national and international regulations involving safety for ships, protection of the environment and working and living conditions for seafarers is a series of international conventions agreed at the IMO and the International Labour Organisation (ILO). International conventions and standards that regulate shipping are important in order to avoid inefficiencies through technical barriers to trade and a “race to the bottom” in terms of safety, environmental and social standards. The implementation and control of these

rules are conducted by the flag states and port states including the various Port State Control Mechanisms (Paris MoU, Tokyo MoU and US Coast Guard etc.). In practical terms these mechanisms implies that the international rules are enforced for all vessels regardless of flag.

The flag requirement in the Norwegian special tax scheme was implemented in 2005, subsequent to amendments of the Maritime Guidelines. To our knowledge, the implementation of the flag requirement varies between EEA countries.

A beneficiary company may enter the Norwegian special tax scheme for shipping without any EEA-flagged vessels. There is no general minimum share of EEA-flagged vessels that has to be met by all beneficiary companies. These features of the Norwegian special tax scheme should be seen in light of specific considerations in the Norwegian maritime sector, which in our opinion, lead to the conclusion that a "no-zero entry" requirement should not be applied in the Norwegian scheme. Norway has a unique offshore fleet, concerning both its size and operation, compared to other EEA states for whom the requirement of "no zero entry" has been applied.[37] In particular, Norwegian enterprises within the offshore services segment are engaged in operations inter alia on continental shelves outside Australia, Africa, Asia and South America. Activities on continental shelves are typically considered part of the domestic regime where local content provisions may apply. These limitations set the conditions for any foreign participation. In some cases, registration of vessels in the country of operation is a prerequisite in order to perform activities in such waters. Although these vessels may be a mix of chartered out and non-chartered out vessels (cf. section 7.2 above), the registration prerequisite may be applicable to all vessels. Companies in the Norwegian maritime sector have encountered local requirements in a number of countries , set as prerequisite for foreign vessels to operate its waters. We have also seen examples where a local flag is not a legal condition, but implies preferential treatment.

As an example, in Brazil a local content requirement, including preferential treatment of Brazilian registered vessels, implies challenges for foreign ship-owners. A report prepared by the Brazilian Association of Norwegian Shipowners (ABRAN) in November 2016 serves to illustrate the challenges connected to local content demands (see attachment 7).

According to Brazilian legislation, non-Brazilian flagged oil service vessels may have their operations terminated to the advantage of Brazilian flag owners. In order to operate in Brazilian waters, foreign-flagged vessels must have their authorisation renewed annually. However, the renewal can be 'blocked' by a Brazilian flagged vessel of the same category. The Brazilian flagged vessel may then take over the employment contract.

[37] For a description of the Norwegian maritime sector, with emphasis on the importance of the offshore segment, see section 7 above.

In fact, a number of Norwegian ship-owners have had their contracts cancelled. The blocking procedure means that EEA flag owners are losing out to ship-owners with Brazilian registered vessels (see attachment 8, 9 and 10).

On this background, Norwegian ship-owning companies are in practice compelled to register vessels in Brazil, in order to maintain and develop their operations on the Brazilian continental shelf. Registration of vessels in the Brazilian ship register strengthens the ship-owners position and possibilities on the Brazilian market.

Effects of local content requirements and preference of Brazilian flag vessels are discussed in the abovementioned ABRAN report, see for example page 21 of the report (the last page) on which it is stated that companies are reflagging their vessels to the Brazilian REB register, to overcome such challenges.

As mentioned, the local flag requirement implies that Norwegian ship-owners have an incitement to opt for Brazilian registration of their vessels in order to maintain and expand their operation on the Brazilian continental shelf. This can be illustrated by attachment 11 to this letter, which is an excerpt of a presentation made by the Norwegian shipping company DOF ASA in September 2016. The presentation shows that DOF has built a number of vessels in Brazil, and that these vessels are under Brazilian flag.

In the United States, the U.S. Customs and Border Protection, Department of Homeland Security, has submitted a notice on proposed modification and revocation of ruling letters relating to application of the Jones Act.[38] If carried through, the proposed changes will mean that a number of offshore service vessels must register under the US flag in order to operate on the continental shelf of USA.

The Brazil and US cases serves as examples of the general need when operating in several jurisdictions, for flexibility concerning registration of vessels. In light of the markets where the Norwegian fleet operates, it seems that a non-zero rule would prevent commercially viable activities.

In particular, a distinctive feature of the Norwegian offshore service sector is the presence of small enterprises (company groups) with few vessels. For longer or shorter periods, operations may be limited to continental shelves where registration of vessels in the country of operation is required. Registration of one or more vessels in an EEA register may therefore not be a viable an option for these enterprises. A minimum EEA share requirement could prevent small companies in particular, from taking part in operations on certain continental shelves while remaining within the special tax system. A rule disfavouring small companies is in itself undesirable and a flagging-out of these

[38] Cf. attachment 12 to this letter. The Jones Act regulates maritime activity in US waters. The act already imposes considerable requirements concerning, shipbuilding, registering, ownership and staffing of vessels in coastwise trade within the United States.

companies would be a considerable drawback for the knowledge-based activities of the Norwegian offshore service segment.

On this background, the Ministry of Finance notifies a flag requirement similar to the requirement as described in the EFTA Surveillance Authority's decision of 3 December 2008 on the notification of amendments to the Norwegian Special tax system for Shipping. This means that companies and groups must commit themselves to increase or at least maintain under the flag of one of the EEA States the share of the tonnage that they would operate under such flags. A company may enter the scheme without any EEA-flagged vessels. The EEA tonnage share requirement does not apply to undertakings operating at least 60 per cent of their tonnage under an EEA flag, or if the EEA flagged share of the total tonnage eligible for tax relief in Norway has not decreased on average during the previous year.

10. RING FENCING MEASURES

According to the Maritime Guidelines Section 3 Paragraph 19 the fiscal advantages must be restricted to shipping activities and spill-over into non-shipping activities must be prevented.

The Norwegian Special tax system applies only to qualifying ships carrying on qualifying activities. To prevent spill-over to non-shipping activities, companies within the special tax system are only allowed to carry out tax exempted activities, and own assets that are necessary to exercise these activities (except for financial assets).
In order to ensure that the special tax system only benefits eligible activities, the ring-fencing measures described under sections 10.1 to 10.8 below have been put in place.

A company within the shipping tax scheme may own financial assets as well as shipping related assets. Profits derived from financial assets are not tax exempt, but subject to ordinary taxation. Interest costs are partially deductible. The deductible part of the interest costs corresponds to the proportion of the aggregate capital of the company that consists of financial capital. For example, if 10 per cent of the aggregate capital of the company consists of financial assets, and 90 per cent of the aggregate capital consists of non-financial assets, 10 per cent of the interest costs will be deductible. The remaining 90 per cent of the interest costs are regarded as shipping-related interest costs, and therefore not deductible.

10.1 Taxation of hidden reserves upon entry into the scheme

Profits derived from shipping activities outside the special tax system, including gains on assets, are subject to taxation upon entry into the special tax system. The income settlement means that latent capital gains (hidden tax liabilities) on vessels and other non-financial assets will be taxed when a company enters the scheme. The taxable income is calculated as the difference between the market value and the tax value of the company (excluding financial assets). Consequently, capital gains related to previously over-depreciated ships entering the special tax system are not covered by the

Norwegian shipping tax scheme. On the contrary, such gains are assessed and taxed upon entry into the scheme.

All non-financial hidden reserves and losses will be a part of the income settlement, increasing or reducing the calculated entry income. Financial assets is not subject to a settlement, because such income is taxed both within and outside the special tax system

The Norwegian scheme does not allow a postponement of the taxation of gains when a company enters the scheme. In its Decision of 13 April 2015 in case SA.38085A concerning the Italian tax scheme for shipping, the Commission approved that taxation of gains may be postponed until the vessel in question is actually sold. In the Norwegian scheme, the income is assessed immediately. However, the income may be entered into the "profit and loss account" of the company.[39] The income cannot be set off against tonnage tax or financial losses within the scheme.

10.2 Lock-in period

The scheme provides for a lock-in period, i.e. undertakings that opt for the tonnage tax regime commit to remain under the favourable tax regime for a minimum period of ten years. A company exiting the scheme before the expiry of the ten year period will not be allowed to re-enter the regime before the expiry of the ten year period.

To the knowledge of the Ministry, in other European special tax regimes for shipping there is usually a ten year lock-in/lock-out period. The consequences of exiting the regimes before the expiration of the lock-in period vary, but as a rule an exit is without effect on profits which have arisen while the company has been within the special tax system

10.3 All-or-nothing rule

A company which is eligible for the special tax system and belonging to a group of companies, in which some companies have opted for the special tax system, is obliged to opt for the tonnage tax system. In other words, the decision to opt for the special tax system is made collectively at the level of the group.

10.4 Rule against thick capitalisation

The special tax system contains a provision aiming to prevent all capitalisation not producing deductible costs being attributable to non-eligible activities. As interest payments have a tax value for a company within the scheme only to the extent that they offset taxable financial income, the scheme involves an incentive for such companies to be “overcapitalised” and for debt and interest payments to be shifted to related

[39] The profit and loss account is kept for tax purposes. At least 20 per cent of the balance of the profit and loss account must be entered as income every year. The profit and loss account is a part of the ordinary company tax rules, i.e. the system of entering capital gains into the account does not imply a special advantage for companies within the shipping tax regime.

companies subject to ordinary taxation. To prevent shifting of interest payments, a minimum amount of debt for eligible companies is stipulated equal to 30 percent of the company's total capital. If a company has less debt than 30 percent, the difference between the actual debt and the minimum debt multiplied with a regulated interest rate, is treated as taxable income.

10.5 Tax neutral effect of group contributions

Companies within the special tax system are allowed to make group contributions to and receive group contributions from companies both within and outside the special tax system. However, a group contribution shall be tax neutral, i.e. a group contribution will not be deductible for the contributor and will not be treated as taxable income for the receiver.

10.6 Restrictions on group contributions subsequent to an exit from the scheme

The amended special tax regime can give companies incentives to opt into the regime for income years with a profit, and opt out for income years with a loss. This is because a profit will be tax-free within the regime, while a deficit will be tax deductible outside the regime. To counteract such adaptations, companies that exit the shipping tax system will not be entitled to receive group contributions for tax purposes in the exit year and the two following years.

10.7 The Arm's length principle

The general provision in Norwegian tax legislation that imposes an arm's length principle will apply to transactions between associated companies and persons. For example, normal market terms will apply for tax purposes where a transaction takes place within a group of companies, between a company benefiting from the shipping tax system and a company subject to the standard corporate tax.

10.8 Exit from the special tax system

Profits derived from shipping activities within the special tax system are tax exempted on a permanent basis. Thus, it is not necessary to settle profits upon exit, and companies are not required to keep an account of retained untaxed income.

However, to ensure that an increase in value of the company's assets within the special tax system will remain tax-free, and a decrease not tax deductible, new bases of depreciation on the assets will be calculated at the time of exit, equal to the market value.

As mentioned under section 10.1, all hidden reserves are settled upon entry into the scheme. The establishment of new tax values for assets at the time of exit prevents double taxation or double deduction of any hidden reserves or losses in the company prior to its entry into the scheme.

11. CONTROL AND SANCTION MEASURES

Compliance with the requirements of the special tax system is controlled by the tax office. In their tax return, companies within the special tax scheme reports on the various conditions required to be taxed within the scheme. Companies may also be subject to subsequent tax controls by the tax office.

Companies have to fulfil all requirements in order to be eligible for the special tax system. If a company no longer fulfils the necessary requirements, it has to revert to regular corporate taxation, regardless of whether the breach is done deliberately or not. The exit will have effect as from the income year in which the requirements were breached, i.e. all shipping profits derived in the year of exit will be subject to ordinary corporate taxation.

However, in order to avoid unmerited exclusions from the tax scheme, companies that have breached the requirements, have a two-month time limit to fulfil the requirements, running from the breach came into being. Fulfilling the requirements within the time limit allows the companies to stay within the special tax system. If the breach is insignificant or caused by circumstances outside the control of the company, the two-month time limit runs from the moment the company ought to have discovered the breach.

The tax authorities can extend the time limit, if the company proves that it will be particularly difficult to fulfil the requirement within the time limit. The tax authorities have taken a strict view on the application of this clause. The exception will not be applied in cases where a correction of the breach within two months is merely less convenient or more costly than a delayed correction.

If a requirement is breached again within three years from the last breach was corrected, no time limit to fulfil the requirements will apply, and the company has to revert to corporate taxation.

12. TRANSPARENCY

The transparency rule incorporated in Section 2.2 of the Guidelines on aid to maritime transport, stipulates that state aid should be granted in a transparent manner, so that companies and individuals are aware of their rights and obligations. As shown in the description above, the Norwegian special tax system for shipping meets the transparency criteria in Section 2.2 of the Guidelines.

The Tax Authorities will submit information on tax related state aid, including state aid through the Norwegian special tax system for shipping, to the National State Aid Register. Information concerning income tax aid schemes (including the special tax system for shipping) for the income year of 2016 will be reported by the taxpayers to the tax authorities during 2017, and subsequently submitted to the National State Aid Register.

The publication of information will comply with the transparency requirements. The implementation of the transparency requirement to the special tax scheme for shipping will be in accordance with the text incorporated in the General Block Exemption Regulation and across the recently revised state aid rules in relation to rapid deployment of broadband networks, state aid to promote risk finance investments, state aid to airports and airlines and regional state aid for 2014-2020.

13. NATIONAL LEGAL BASIS

The legal basis for the Special tax system for shipping companies is as follows:

I. The Tax Act (Lov 26. mars 1999 nr 14 om skatt av formue og inntekt (skatteloven)) sections 8-10 to 8-18 and section 8-20.

II. The tonnage tax rates are established in the parliamentary resolution on income and net wealth taxes (Stortingsvedtak om skatt av inntekt og formue mv.). For constitutional reasons the parliamentary resolution must be adopted ahead of every income year.

III. The Ministry has issued further provisions in sections 8-11, 8-13, 8-15, 8-16 and 8-20 of the Ministry's supplementary regulations to the Tax Act (forskrift 19. november 1999 nr. 1158 til utfylling og gjennomføring mv. av skatteloven av 26. mars 1999 nr. 14).

14. TRANSITIONAL PROVISIONS

The Ministry would like to point out that, participants should be given sufficient time to adjust to the new requirements contained in this notification. Otherwise, the risk of disturbances in the Norwegian shipping industry, including the risk of emigration of vessels and/or shipping companies to non-EEA jurisdictions, could be substantial. Both from a Norwegian and European perspective it is important that the Norwegian shipping industry, as an important driving force for the development of innovative and sustainable transport solutions in the European maritime sector, is given the opportunity to reorganize its operations without facing a risk of being excluded from the special tax scheme.

The notified limitation concerning bareboat chartering out may mean that some of the companies within the Norwegian special tax scheme for shipping will exit the scheme. However, some of the enterprises involved in bareboat chartering out may be able to restructure future contracts in order to meet the new limitations imposed. To encourage companies to adapt to the new requirements and continue their presence within the Norwegian shipping tax scheme, the limitations will only apply to new bareboat chartering out contracts. Tonnage chartered out on existing contracts

(including options to extend existing contracts for up to 3 years[40]) will not be included in the limitation. To prevent abuse and exclude pure ship lessors, this transitional rule will not apply to long-term contracts, i.e. contracts of a duration of more than 5 years. In the offshore sector, bareboat chartering out contracts are usually of duration of between 3 and 5 years.

As mentioned under section 7.4 above, the Ministry considers that a limitation to 90 per cent on the chartering in of non-EEA flagged vessels on time charter or voyage charter terms would be in line with the Maritime Guidelines and contribute to the achievement of their aim. However, the need for companies to adapt to a new chartering in limitation, and remain within the Norwegian shipping tax scheme, calls for a transitional rule. The limitation will therefore only be applied to new chartering in contracts.

15. AMOUNT OF AID

Based on average profits and taxes payed for the period 2012-2014, the Ministry of Finance has estimated the annual tax expenditure to NOK 200 million and the tax expenditure in total for the period 2017-2026 to NOK 1 900 million. The actual tax expenditure will depend on the development of profits within the shipping sector during the 10-year period.

16. CONCLUDING REMARKS

To the assessment of The Ministry of Finance, the notified measure constitutes state aid within the meaning of Article 61(1) of the EEA Agreement.

The Authority approved the Norwegian Shipping Tax scheme in 2008 (Decision 755/08/COL) with reference to the Maritime Guidelines Section 1.2.(c) Paragraph 4. It follows from the discussion above that the Ministry of Finance finds that the notified measure complies with the Maritime Guidelines and should be held compatible with the EEA Agreement Article 61(3)(c).

Yours sincerely,

Bjørn Berre
Deputy Director General

Hallvard Rue
Legal Adviser

[40] Cf. section 7.2.

This document has been signed electronically and it is therefore not signed by hand.

Enclosure