Dissertation Title
The European and Greek Shipping Taxation

Vasiliki-Aikaterini Andrioti
Student ID: 1104150002
Supervisor Professor: Dr. George Matsos

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PREFACE

The shipping industry plays an important role in the national economy of almost all countries. OECD States are trying to reinforce their merchant fleet and attract the relevant land based activities under their jurisdiction by applying tax incentives. Through this paper, it will be shown that OECD States have to reconsider the tax incentives already applied for achieving a friendlier taxation policy. The first part of this work will be dedicated to the main principles that govern the taxation of international shipping, the OECD approach on shipping taxation and the expansion of open registries that offer to ship owners a series of tax advantages that traditional maritime nations fail to provide. On the second part of this work, a description of the different systems of shipping taxation will be made with main emphasis on the scheme of tonnage taxation which is also applied by the Greek State. In chapter 3 of this work, special emphasis will be given on the fiscal aid measures which are permitted by the 2004 Maritime Transport Guidelines and the Commissions’ responses to recent cases in which particular problems arise regarding the interpretation and scope of application of these Guidelines. Finally, special interest will be given on the evaluation of the Greek tonnage regime by the European Commission and its conformity with the maritime Guidelines (chapter 4). This special interest on the Greek scheme is explained by the leading role of Greek ship owners in the European shipping industry. In addition to this, current Greek financial crisis raised Commission’s concerns regarding the protection of the integrity of the euro area. The Commission supervises the actions of Greek authorities at all levels and especially those which contribute to the return of Greece to financial stability. A strong merchant fleet can ensure the return of Greece to financial stability and its economic growth.

For the completion of this dissertation, special thanks are owed to my supervisor Mr Matsos, for his invaluable guidance, support and supervision throughout my dissertation’s progress. I really appreciate the opportunity he offered me to cooperate with him and focus on the most important parts of this dissertation by omitting all the unnecessary background information.
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INTRODUCTION

The massive migration of EU vessels to third countries is explained by the friendly taxation policy offered to them. In reaction to this migration, many European countries have implemented various kinds of tax schemes and incentives to achieve the re-flagging of EU vessels. The most effective tax scheme to combat the migration of EU vessels to these friendlier shipping tax regimes (Flags of Convenience) is the tonnage tax scheme. This scheme has constantly being judged by the European Commission for its conformity with EU State Aid rules in a number of cases. The 2004 Maritime Guidelines provide special guidance to the Commission’s evaluation of prohibited state aid measures taken by the Member States. In 2015, the Commission brought its allegations against the Greek authorities regarding the conformity of the Greek shipping tonnage tax scheme with the state aid rules.
1 THE MAIN PRINCIPLES OF TAXATION IN INTERNATIONAL SHIPPING

Shipping is a business characterized by a high degree of mobility because it can be operated in any State and the activities of shipping companies are taking place in many countries.¹ The application of regular tax principles is impossible in international shipping² because the business of a shipping company can be taxed in any of those jurisdictions³.

Today, the “real place of effective management” constitutes the rule for the taxation of profits derived from the operation of international shipping. This rule was progressively recognized as the most appropriate method for the taxation of shipping profits in spite of the initial refusal of EU countries to apply it⁴. It was incorporated in 1927 and 1928 draft bilateral Conventions until 1963 when it was finally introduced in article 8 of the OECD Model Convention⁵. According to this article, the country where the place of effective management is situated retains exclusively the right to tax the profits derived from the operation of international shipping. Residence is not used as a tax allocation criterion⁶ because the activities of shipping enterprises are carried out in many countries in which permanent establishments are often installed⁷. The consecutive stops of a ship during its voyage in a large number of countries makes the proper attribution of profits owned by these permanent establishments really difficult⁸. Another unpleasant consequence of allocating profits to the various permanent establishments would be fragmented taxation⁹. As it

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¹ Steven Suarez, “The taxation of Mobile Activities” [2010] BIFD, p.45-46
² Steven Suarez, “The taxation of Mobile Activities” [2010] BIFD, p.46
³ Dale Pinto, “Exclusive Source or Residence-Based Taxation- Is a New and Simpler World Tax Order Possible?” [2007] BIFD, p.279
⁷ Klaus Vogel, Double taxation Conventions: a commentary to the OECD, -UN-US model conventions for the avoidance of double taxation of income and capital with particular reference to German treaty practice( Kluwer Law and Taxation Publishers 1997), p.482
⁸ Klaus Vogel, Double taxation Conventions: a commentary to the OECD, -UN-US model conventions for the avoidance of double taxation of income and capital with particular reference to German treaty practice( Kluwer Law and Taxation Publishers 1997), p.482
has correctly been stated “if it was obligatory to pay taxes in all countries the ships cross, no profit would be left for the companies which would probably sell their vessels”\(^\text{10}\).

Therefore, the principle of permanent establishment contained in the Article 7 of OECD Model Convention cannot be used for the taxation of international shipping and the States where the shipping activities are exercised do not have a right to tax them even if the enterprise holds a permanent establishment in their territory. Thus, the right of taxing shipping profits derived from the international activity of a shipping enterprise belongs exclusively to the place of effective management of the shipping enterprise.

\[\text{1.1 Place of effective management versus place of residence}\]

The priority of the State of effective management over the State of residence is justified by the fact that if it was otherwise, exclusive taxation might rest with a State which harboured no more than the enterprise’s registered seat, while the entire business of the shipping company was handled outside of that State\(^\text{11}\). Moreover, the priority over the residence State is dictated by anti-treaty shopping reasons\(^\text{12}\). More specifically, if a company was taxed according to where it has its registered seat, it would be possible for it to transfer its seat in a State with low taxation while maintaining its real activities in another State\(^\text{13}\). Therefore, difficulties would be created regarding the certification of the place of effective management in jurisdictions with inefficient and insufficient transparency guarantees. Furthermore, there is a high risk of non-taxation in case the place of effective management is

\[\text{\textsuperscript{10} G.Maisto, “The history of article 8 of the OECD Model Treaty on Taxation of shipping and Air Transport”, [2003] Intertax \(p. 239\)}\]

\[\text{\textsuperscript{11} Ekkehart Reimer, Alexander Rust, Klaus Vogel on Double Taxation Conventions, Wolters Kluwer law\& Business 2015, p.549}\]

\[\text{\textsuperscript{12} Klaus Vogel, Double taxation Conventions: a commentary to the OECD, -UN-US model conventions for the avoidance of double taxation of income and capital with particular reference to German treaty practice( Kluwer Law and Taxation Publishers 1997),p.482}\]

\[\text{\textsuperscript{13} Klaus Vogel, Double taxation Conventions: a commentary to the OECD, -UN-US model conventions for the avoidance of double taxation of income and capital with particular reference to German treaty practice( Kluwer Law and Taxation Publishers 1997) ,p.484}\]
situated in a place other than that of the State of residence. There is the risk that the enterprise will not be taxed at all if both the place of effective management does not allow the taxation of shipping profits and article 8 does not authorize the State of residence to tax them.

The principle of the place of effective management can apply only if the shipping enterprise has its residence in one of the contracting States. In case it has its residence in another State then both the Contracting States are obliged to tax it according to their tax law. Therefore, a shipping enterprise should be very careful when it is examining where to establish and take into account all the previously mentioned things. The suitability of a jurisdiction for having a shipping business on its territory is determined by the double Taxation Conventions it has concluded with other countries. Enterprises which are taxable in a regime that provides zero or minimal taxation to a shipping business may be doubled taxed for their activities if a double taxation Convention does not exist with their State of residence.

1.2 The scope of Article 8 OECD

Pursuant to article 3 paragraph e of OECD Model Convention, the term international traffic includes “any transport by a ship operated by an enterprise that has its place of effective management in a Contracting State, except when the ship is operated solely between places in the other contracting State”.

There is difficulty in defining the scope of Article 8. In the Commentary of article 8, it is mentioned that not only profits from the carriage of passengers or cargo are covered by article

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14 Ekkehart Reimer, Alexander Rust, Klaus Vogel on Double Taxation Conventions, Wolters Kluwer law & Business 2015, p.549
15 Ekkehart Reimer, Alexander Rust, Klaus Vogel on Double Taxation Conventions, Wolters Kluwer law & Business 2015, p.549
16 Klaus Vogel, Double taxation Conventions: a commentary to the OECD, -UN-US model conventions for the avoidance of double taxation of income and capital with particular reference to German treaty practice (Kluwer Law and Taxation Publishers 1997), p.489
17 “Hong Kong Tax Competitiveness Series: The shipping Industry” (KPMG 2007).p.7
18 “Hong Kong Tax Competitiveness Series: The shipping Industry” (KPMG 2007).p.7
8 but other types of income that are closely linked to the carriage activity as well\textsuperscript{20}. Income derived from shipping activities other than in international traffic is governed by article 7 OECD Model Convention and source State is obliged to tax in that case\textsuperscript{21}. If an enterprise is activated both in international traffic and in inland traffic its profits will be taxed in the following way\textsuperscript{22}: The ones from international traffic will be taxed pursuant to article 8 and the others according to article 7. Articles 10 and 11 of the OECD Model Convention are applied for the taxation of an enterprise’s income derived from dividends and interest\textsuperscript{23}. Furthermore, income from dividend distributions made by the shipping enterprises falls within the scope of article 10\textsuperscript{24}. Regarding income which derives from the leasing of a ship, the following distinction should be made: If the leasing of a ship is on a charter fully equipped basis then it is governed by article 8 of the OECD Model Convention whereas if it is on a bareboat basis it is regarded as royalties and article 12 applies. However, article 8 can still apply in case of income derived from the leasing of a ship in a bareboat basis if the bareboat charter lease constitutes an insignificant part of the shipping enterprise’s income\textsuperscript{25}.

Some countries deviate from the rules of the OECD Model Convention and this has led to complex court decisions. The Mediterranean Co case illustrates the negative consequences


\textsuperscript{21} Klaus Vogel, Double taxation Conventions: a commentary to the OECD, -UN-US model conventions for the avoidance of double taxation of income and capital with particular reference to German treaty practice( Kluwer Law and Taxation Publishers 1997), p.483

\textsuperscript{22} Klaus Vogel, Double taxation Conventions: a commentary to the OECD, -UN-US model conventions for the avoidance of double taxation of income and capital with particular reference to German treaty practice( Kluwer Law and Taxation Publishers 1997), p.487

\textsuperscript{23} Klaus Vogel, Double taxation Conventions: a commentary to the OECD, -UN-US model conventions for the avoidance of double taxation of income and capital with particular reference to German treaty practice( Kluwer Law and Taxation Publishers 1997), p.487

\textsuperscript{24} Klaus Vogel, Double taxation Conventions: a commentary to the OECD, -UN-US model conventions for the avoidance of double taxation of income and capital with particular reference to German treaty practice( Kluwer Law and Taxation Publishers 1997), p.487

\textsuperscript{25} Klaus Vogel, Double taxation Conventions: a commentary to the OECD, -UN-US model conventions for the avoidance of double taxation of income and capital with particular reference to German treaty practice( Kluwer Law and Taxation Publishers 1997), p.487-488
of the failure of the courts to apply the OECD Model rules\textsuperscript{26}.

1.3 Ship Registration and Flags of Convenience

Ship registration is the act by which a ship is attributed the nationality of the jurisdiction to which the ship has been documented\textsuperscript{27}. In this way, a state confers its flag upon the ship and imposes responsibilities on the ship owner. States are allowed to determine the conditions according to which a ship can be registered in their records and gain their nationality\textsuperscript{28}. Ship owners usually register their ships in the most liberal registries known as Flags of Convenience.

There is not a uniform definition of the term “Flags of Convenience” or “open registers”\textsuperscript{29}. Many have attempted to define it like the International Transport Worker’s Federation\textsuperscript{30}. The only thing in common of these different definitions is that in the case of “Flags of Convenience” there is not a genuine link with the States of their registry\textsuperscript{31}. Nowadays, the International Transport Worker’s Federation decides what is and what isn’t a Flag of Convenience by using the “Rochdale criteria 1970” written by a British Committee\textsuperscript{32}. These criteria which are common to all Flags of Convenience are the following\textsuperscript{33}:

- Registration, ownership and control of the vessels is allowed to non-residents.
- The owner can enter and exit the ship records easily.
- The corporate tax rates are low or non-existent.
- The flag State cannot supervise the ship’s compliance with international shipping standards.
- The crew of the ship is permitted to be non-nationals.
- The size of merchant fleet is not proportionate to the needs of the flag State. Only tonnage fees are earned by the flag State.

\textsuperscript{26} IN: ITAT(Mum), 6 Nov.2012, Assistant Director of Income Tax( International taxation) v. Mediterranean Shipping Co, found on IBFD tax treaty case law news

\textsuperscript{27} Richard Coles, Edward Watt, Ship Registration, law and practice( Lloyd’s Shipping law library, 2\textsuperscript{nd} ed.2009), p.7

\textsuperscript{28} Richard Coles, Edward Watt, Ship Registration, law and practice( Lloyd’s Shipping Law library, 2\textsuperscript{nd} ed.2009), p.13


\textsuperscript{32} A.K. Febin, “Evolution of the Flag of Convenience”, National University of Advanced Legal Studies, Cochin, India, December 2007

\textsuperscript{33} A.K. Febin, “Evolution of the Flag of Convenience”, National University of Advanced Legal Studies, Cochin, India, December 2007
The ship owners move their fleet to these open registers which offer many tax advantages such as lower operating costs, no crew requirements and less regulatory control. Another advantage is that it is very difficult to ascertain the beneficial ownership of the vessel. The community merchant fleet has been reduced because ship owners elect to register their vessels in third countries and take advantage of the merits which are offered to them. More information regarding the way this scheme works and its impact on the ship owner’s decision on which flag to choose can be found in the article of Peter Marlow and Kyriaki Mitroussi, “Shipping Taxation: perspectives and impact on flag of choice”, in the book of Richard Coles, Edward Watt, Ship Registration, law and Practice and in the UNCTAD “Maritime Law Review 2012”.

2 SYSTEMS OF SHIPPING TAXATION

The corporation tax system is used for the taxation of a company’s annual profits. According to the corporation tax system, the calculation of tax is made by a multiplication of profits with a specific rate which is fixed by tax code. The traditional corporate tax system diverges from other favourable tax systems which intervene in the way that profits are calculated. These favourable tax regimes are the following:

- Tax incentives specifically for shipping business within the framework of a corporate tax system.
- Favourable tax regimes which do not offer any exemption for the shipping profits but they provide a low effective tax rate.

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39 “choosing a profitable course around the globe, corporate taxation of the global shipping industry” (Pricewaterhousecoopers 2010)
• European tonnage tax regimes where the calculation of tax is based on the tonnage of a vessel.

• Greek tonnage tax regime.

2.1 Tax incentives within a corporate tax system

Many countries apply different tax incentives which reduce the tax burden\(^\text{40}\). The application of the tax incentives narrows the tax base on which tax is calculated or provides a complete tax exemption\(^\text{41}\). The application of these incentives results in an effective tax rate according to which the enterprise is finally taxed\(^\text{42}\). The effective tax rate is affected by the type of corporate tax system\(^\text{43}\). Under the classical system, both the company and its shareholders are taxed for their profits\(^\text{44}\). The second system is the imputation system under which the tax that the company pays is attributed to the shareholders by way of a tax credit so as the tax that has to be paid on a distribution is reduced\(^\text{45}\). The third system is the split rate one under which the profits that a company keeps are taxed more than the ones which are paid out as dividends\(^\text{46}\).

The profitability and the allowances of a shipping enterprise are important factors for the effectiveness of this system\(^\text{47}\). The higher the profits and the allowances of a shipping enterprise are, the more the benefits of this regime will be. Overall, this system is complex and uncertain regarding the tax planning of a company because of the constant

\(^\text{40}\) Pricewaterhousecoopers, p. 26

\(^\text{41}\) Pricewaterhousecoopers, p. 26


\(^\text{44}\) Peter Marlow and kyriaki Mitroussi, “Shipping Taxation: perspectives and impact on flag of choice”[2011] Int.J.Shipping and Transport Logistics, p.308


changes that the tax corporation system faces\textsuperscript{48}. Nowadays, this system is not used by many countries. Some of the countries that continue to apply this system are Panama, Hong Kong, Canary Islands, France and China\textsuperscript{49}. Panama which is the biggest registry in the world\textsuperscript{50} applies a statutory tax rate of 25\%\textsuperscript{51}. Moreover, vessels registered under the Panamanian flag are not taxed in case the income comes from international maritime commerce\textsuperscript{52}.

2.2 Favourable tax systems

Antigua and Barbuda are a clear example of countries which apply favourable tax regimes\textsuperscript{53}. These countries do not offer the previously mentioned tax incentives but their tax rates are very low\textsuperscript{54}. The companies which are registered in Antigua and Barbuda as International Business Corporations enjoy a tax exemption for fifty years\textsuperscript{55}. This tax exemption presupposes that the International Business Corporations does business with companies which do not reside in Antigua and Barbuda\textsuperscript{56}. Similarly, in Barbados if a company is registered as an International Business Corporation, the corporate tax rates are very low (0.25\% to 2.5\%)\textsuperscript{57}. In Bermuda if the company is registered as an exempted one then it is not obliged to pay any income tax on profit, capital gains or personal income\textsuperscript{58}.

\textsuperscript{48} Peter Marlow and kyriaki Mitroussi, “Shipping Taxation: perspectives and impact on flag of choice”\textsuperscript{[2011]} Int.J.Shipping and Transport Logistics ,p.312
\textsuperscript{49} Pricewaterhousecoopers , p. 26
\textsuperscript{50} UNCTAD “Maritime Transport Review 2012”
\textsuperscript{51} Pricewaterhousecoopers , p. 27
\textsuperscript{52} Pricewaterhousecoopers , p. 27
\textsuperscript{53} Pricewaterhousecoopers , p. 29
\textsuperscript{54} Pricewaterhousecoopers , p. 29
\textsuperscript{55} Pricewaterhousecoopers , p. 29
\textsuperscript{56} Pricewaterhousecoopers , p. 29
\textsuperscript{57} Pricewaterhousecoopers , p. 29
\textsuperscript{58} Pricewaterhousecoopers , p. 29
2.3 European tonnage tax regimes

Tonnage taxation is characterized by the principle that the calculation of tax payable is based on the tonnage of vessels instead of the real accounting profits from the exploitation of a vessel\textsuperscript{59}. The very low effective tax rate which is less than 1\% makes the application tonnage tax regimes attractive for many countries\textsuperscript{60}. The basic characteristics of the tonnage tax regimes are the following\textsuperscript{61}:

- Regarding the qualifying activities, it must be stated that the tonnage tax regime covers only specific shipping activities such as those which are related to the international transport of goods and persons by sea. Some other activities which can qualify for a tonnage tax regime are towage, dredging and cable laying activities.

- The existence of a ‘lock-in-period’ in most tonnage tax regimes. The ‘lock-in period’ obliges an enterprise which enters the tonnage tax system to remain to this system for a certain time, usually of ten years. The aim of this requirement is to prevent taxpayers from switching regimes when they face losses. Tonnage tax regimes require a certain percentage of ownership regarding the vessel. This degree of ownership is not the same in all tonnage tax regimes. There is also a requirement for a certain degree of management activities that a company must undertake in its country of residence.

- Capital gains on the sale of vessels and equipment are excluded from ordinary taxation. If an enterprise leaves the scheme before the expiration of the ‘lock-in period’, exit taxes are imposed on it.

- There must be a flag link between the flag a vessel is flying and the place of residence of the company that has the ownership of the vessel. However, there are many exemptions. According to the 1997 Maritime Guidelines, the flag link requirement is not required when the strategic and commercial management of a vessel is taking place within Europe.

\textsuperscript{59} Pricewaterhousecoopers, p. 8
\textsuperscript{60} Pricewaterhousecoopers, p. 8
\textsuperscript{61} Pricewaterhousecoopers, p. 8-9
There are two tonnage tax models: The Dutch model and the Greek model which will be described right after the Dutch model.

The Dutch Model which was introduced in 1996 is applied by Belgium, Bulgaria, Denmark, Finland, France, Germany, India, Ireland, Italy, Japan, Republic of Korea (South Korea), the Netherlands, the Netherlands Antilles, Norway, Poland, South Africa, Spain, Sweden, the UK, and the USA. Under this model, the taxable operating profit of a vessel is based on the net tonnage of the vessels instead of the actual operating profits. This profit is then subject to the ordinary corporate income tax rates. Moreover, regular taxation rules apply on the shipping company and its non-qualifying shipping income. A vessel must operate in international traffic at sea in order to qualify for this scheme. Dredging and towing activities can qualify only if more than 50% of these activities are exercised at sea. Ship management activities may also qualify for the tonnage tax regime. Generally, both legal entities and individuals can qualify for this scheme but in some countries such as France and Italy only legal entities can enter it. Finally, capital gains are not subject to corporate taxation.

The priority of the tonnage tax system over the ordinary corporation tax system is evident. This system is characterized by simplicity, certainty and transparency. Its tax provisions are easy to understand and this leads to lower administrative costs. Moreover, the avoidance of tax evasion is achieved by the predefinition of tax costs for each fiscal year and this creates tax certainty. This system is also characterized by a high degree of transparency because the different tax levels of each state are available to the ship owners who can make a comparison and decide where to register their vessels. One disadvantage of the tonnage tax regime is that tax costs are increased when the enterprise incurs losses in a fiscal year. However, this disadvantage is outweighed by the previously mentioned advantages.

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62 Pricewaterhousecoopers, p. 10
63 Pricewaterhousecoopers, p. 10
64 Pricewaterhousecoopers, p. 10
65 Pricewaterhousecoopers, p. 10
66 Pricewaterhousecoopers, p. 14
67 Pricewaterhousecoopers, p. 14
68 Pricewaterhousecoopers, p. 14
69 Pricewaterhousecoopers, p. 16
70 Pricewaterhousecoopers, p. 22
2.4 Greek tonnage Tax Regime

The Greek Model which was introduced in 1957 is followed by Cyprus and Malta\(^72\). However, these countries apply different methods for the calculation of the taxable profit\(^73\). The Greek tonnage tax applies to all ships which fly a Greek flag\(^74\). Furthermore, it applies to ships which fly a foreign flag and are doing ship management activities in Greece which comply with certain criteria\(^75\). According to Article 3 Law 27/1975, the taxation of vessels is divided into two categories. The type of vessels which are included in Category A are those which relate to international shipping such as engine-propelled cargo ships, tankers, freighters, passenger ships and floating drilling platforms for the exploitation of oil\(^76\). This category enjoys constitutional protection\(^77\). In this category the size and the age of the vessel are used for the calculation of tonnage tax (Article 6 of Law 27/1975)\(^78\). Tax rates are increasing by 4% each year since 2007\(^79\). Very low tax rates apply when the age of the vessels is less than 5 years and the tonnage of the ship is big\(^80\). Vessels such as engine-driven ships and sailing ships are included in Category B\(^81\). The taxation of these vessels is done according to Article 12 paragraph 1 Law 27/1975 and is different from that applied to vessels in category A. The calculation of tax rates in this case is based on the gross tonnage of the vessel\(^82\).
The Greek tonnage tax differentiates from the Dutch tonnage tax regarding the calculation of a deemed profit which is not based on the registered tonnage of the vessel. Subsequently, this profit is subject to ordinary corporation tax. The activity of the ship is subject to taxation according to the Greek tonnage Model. Another difference regards the reduction of annual tax when the ship is not active for a period which exceeds the two months in two tax years. The reduction of the tax is done proportionally to the period of the year that the vessel was not active. The voluntary nature of the Greek tonnage tax is another element which differentiates it from the Dutch tonnage tax. More specifically, ship owners are obliged to be taxed under the Greek tonnage tax and cannot opt for the application of the ordinary corporate tax.

The payment of the tonnage tax results in the exhaustion of any other tax liability of the ship owner regarding the income which derives from the operation of the ship. The same applies to the shareholders or partners of a shipping company who are discharged from any tax liability. Furthermore, the distributions of intermediate holding companies are not subject to any tax liability up to the beneficial owner. The exemption also covers capital gains which arise out of the sale of vessels. According to Article 2 of Law 27/1975, only income which derives from the operation of the ship is exempted from income tax and not other commercial activities. Income which derives from the exploitation-chartering of the ship does not qualify for tonnage tax. There is an exemption though for chartering activities which can be subject to tonnage tax under the Law 89/1967.

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83 Pricewaterhousecoopers, p. 15
85 Pricewaterhousecoopers, p. 10
88 Pricewaterhousecoopers, p. 15
The type of profits which qualify for tonnage tax are mainly those related to the transportation of cargo and passengers\(^92\) and those deriving from activities such as lease payments, advertisement and casinos\(^93\). Capital gains which derive from the shares of a shipping company are subject to ordinary taxation according to the Opinion 432/2000 of the Greek legal council\(^94\). Finally, the transfer of shares of a shipping company is not subject to donation and heritage tax\(^95\).

### 3 FISCAL AID IN MARITIME TRANSPORT

The Member States and the Community decided to use the instrument of State Aid in order to encourage the re-flagging of EU owned vessels which had been registered under non-EU flags.

In maritime transport, state aid which takes the form of operating aid is exceptionally allowed under certain conditions. Operating aid aims to counterbalance the more favourable fiscal conditions enjoyed by non-EU companies\(^96\). Moreover, it seeks to counter the massive flagging out of EU vessels to third countries and mostly Flags of Convenience.

According to Article 107 paragraph 1 of TFEU state aid is *any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the provision of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market*.”

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A fiscal measure falls within the scope of Article 107(1) TFEU when its effects are equivalent to subsidies which distort competition. The compatibility of a tax measure with the State aid rules is determined by its effects and not its nature or the public authority’s policy intentions. For a tax measure to be regarded as State aid the following requirements must be fulfilled:

- A tax advantage such as a tax exemption or reduction must be provided on the beneficiaries which reduces partially or fully the enterprise’s tax burden.
- The tax advantage must be granted by a Member State or through State resources. There must be a direct link between the tax revenue and the aid measure financed by that revenue.
- Competition distortions through tax advantages which affect trade between Member States. Not only selective advantages can cause a distortion of competition but also general ones which lead to wider competition distortions. The main purpose of the State aid rules is to prevent such competition distortions between Member States. This is justified by the fact that State aid rules are included in the TFEU where competition matters are regulated. Distortions of competition are often justified by the non-harmonised tax environment and the allocation of taxing powers theory. The problem is to distinguish which cases fall within the scope of the allocation of taxing powers theory and are considered as allowed distortions of competition and which do not and are allowed to be applied.

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regarded as forbidden distortions of competition\textsuperscript{104}. However, the Commission and the Court of justice consider the distortion of competition criterion as always given and have not make such a distinction between allowed and forbidden distortions of competition. The selectivity criterion which will be described below is not an adequate criterion for the establishment of a distortion of competition\textsuperscript{105}. Thus, emphasis should be shifted from selectivity to competition distortion because the non-harmonised environment of taxation includes also non-prohibited competition distortions\textsuperscript{106}.

- The tax advantage must be selective. The scope of fiscal aid is restricted to the financial result of the tax advantage\textsuperscript{107}. The measure must favour selectively certain types of activities or the production of specific products. It must be stated that not only selective tax advantages are incompatible with the EU competition rules but also the general ones. It is not logical for a major distortion of competition which includes a minor distortion to be compatible with competition rules and the minor one incompatible\textsuperscript{108}. This is explained by the fact that both arise out of the same cause and the minor is part of the major distortion\textsuperscript{109}.

Tonnage tax which applies in a particular sector (the maritime transport), may also be considered state aid because a fixed amount of tax is paid irrespective of whether the company makes high or low profits or even suffers losses\textsuperscript{110}. According to the

\begin{footnotesize}
\textsuperscript{104} George Matsos, “ Systematic Misconceptions of State Aid Law in the area of Taxation”, ESTAL , vol.13, No.3, p. 498, 2014
\textsuperscript{105} George Matsos, “ Systematic Misconceptions of State Aid Law in the area of Taxation”, ESTAL , vol.13, No.3, p. 493, 2014
\textsuperscript{107} George Matsos, “ Systematic Misconceptions of State Aid Law in the area of Taxation”, ESTAL , vol.13, No.3, p. 491, 2014
\end{footnotesize}
Commission’s assessment, if the special forms of taxation result in less tax being paid in relation to the normal tax on corporate profits then they are considered to be state aid.\textsuperscript{111}

A fiscal measure may be exempted from the prohibition of Article 107(1) TFEU. According to Article 107 (3) TFEU operating aid is allowed for the development of economic areas when such aid does not affect trading conditions to an extent contrary to the common interest.\textsuperscript{112} It is also allowed for the reduction of environmental taxes and in maritime transport.\textsuperscript{113} The aid offered must be necessary, proportional and in the community’s interest.\textsuperscript{114} It has been found that when operating aid aims to mitigate the costs of an enterprise which derive from its day-to-day management activities then it does not fall in the scope of Article 107(3) TFEU.\textsuperscript{115} Moreover, payments which improve the situation of an undertaking without promoting any of the conditions in Article 107(3) are not allowed.\textsuperscript{116}

According to Article 108(1) TFEU the European Commission is the sole competent authority to review the compatibility of fiscal measures with State aid rules.\textsuperscript{117} If member States fail to notify the potential state aid measure to the European Commission then a new tax is imposed pursuant to Article 108(3).\textsuperscript{118}

\begin{footnotesize}
\begin{enumerate}
\item Phedon Nicolaides, “Fiscal Aid for Maritime Transport” in Antonios M. Antapases, Lia I. Athanasiou, Erik Rosaeg (eds), \textit{Competition and regulation and shipping related Industries} (Martimus Nijhoff Publishers 2009), p. 228
\item Phedon Nicolaides, “Fiscal Aid for Maritime Transport” in Antonios M. Antapases, Lia I. Athanasiou, Erik Rosaeg (eds), \textit{Competition and regulation and shipping related Industries} (Martimus Nijhoff Publishers 2009), p. 228
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\item George Matsos, “Systematic Misconceptions of State Aid Law in the area of Taxation”, \textit{ESTAL}, vol. 13, No. 3, p. 495, 2014
\end{enumerate}
\end{footnotesize}
3.1 The 2004 Maritime Guidelines

The 2004 Guidelines on State aid have a similar context with the previous 1997 Guidelines. Some of their objectives are the preservation of the maritime know-how, the development of maritime skills, the improvement of maritime safety and employment conditions both at sea and on shore\textsuperscript{119}.

According to these Guidelines, some types of aid which are considered to be compatible with the Common Market are the following\textsuperscript{120}:

- Reduced or zero corporation tax.
- Aid for towing and dredging at sea if more than 50\% of these activities per year take place at sea.
- Tax relief for the ship owners’ gains from the operation of EU-flagged vessels. Tax relief may also be provided for the entire fleet of EU-based ship owners under certain conditions.
- Non-taxation of profits deriving from the sale of ships for a number of years.
- Tonnage tax.
- Tax relief for ship management companies which provide both technical and crewing management and are responsible for the operation of vessel.
- Reductions in social insurance contributions and in the seafarers’ income taxes.

Generally, the 2004 Maritime Guidelines provide stricter rules on the application of fiscal aid measures and emphasize the importance of tonnage taxation for the maintenance of the EU fleet\textsuperscript{121}. These Guidelines better arranged issues such as the kind of vessels which qualify for tonnage tax by including tugboats and dredgers under certain conditions which were previously mentioned. Moreover, the flag link requirement was softened through a

\textsuperscript{119} Michael Sanchez Rydelski, “The EC State Aid Regime: Distortive Effects of State Aid on Competition and Trade” (Cameron May Ltd 2006), p.405


requirement to register new capacities under an EU flag under certain circumstances\textsuperscript{122}. This requirement applies to a limited number of companies whose share is already below 60 per cent\textsuperscript{123}. Also, the total share under community flags of vessels tax-livable in the Member state concerned must have decreased over the last three years\textsuperscript{124}. Finally, the 2004 Guidelines were supposed to be reviewed but on October 2 of the year 2013, it was confirmed by the European Commission that they will remain the same.

### 3.2 PROBLEMATIC ISSUES IN THE GUIDELINES

Despite the fact that the 2004 Guidelines have evolved over the years by crystallizing a number of new issues which arose in state aid cases, their implementation is still problematic. There is still difficulty in interpreting their scope of application. The cases that will be presented below highlight such interpretation problems by the European Commission.

#### 3.2.1 RING-FENCING MEASURES

The European Commission usually invites Member States to take measures to ensure that fiscal advantages should be restricted to shipping activities only\textsuperscript{125}. The measures could be\textsuperscript{126}: 1) to verify intra-group transactions based on the arm’s length principle 2) to separate accounting and proper allocate revenues between eligible and non-eligible activities 3) the all-or nothing option( if one entity of the group opts for the tonnage tax then the whole group should opt for the tonnage tax). In the Danish case C 5/2007\textsuperscript{127}, the Commission emphasized the importance of those measures and did not authorize the removal of the monitoring of commercial transactions between entities which are subject to tonnage tax and those which do not. The European Commission found the measure taken by the Danish authorities detrimental to other Member

\textsuperscript{122} Michael Sanchez Rydelski, “The EC State Aid Regime: Distortive Effects of State Aid on Competition and Trade” (Cameron May Ltd 2006), p.406

\textsuperscript{123} Michael Sanchez Rydelski, “The EC State Aid Regime: Distortive Effects of State Aid on Competition and Trade”(Cameron May Ltd 2006), p.406

\textsuperscript{124} Michael Sanchez Rydelski, “The EC State Aid Regime: Distortive Effects of State Aid on Competition and Trade”(Cameron May Ltd 2006), p.406

\textsuperscript{125} Phedon Nicolaides, “Fiscal Aid for Maritime Transport” in Antonios M.Antapases, Lia I.Athanasiou, Erik Rosaeg(eds), Competition and regulation and shipping related Industries( Martimus Nijhoff Publishers 2009),p.233

\textsuperscript{126} Phedon Nicolaides, “Fiscal Aid for Maritime Transport” in Antonios M.Antapases, Lia I.Athanasiou, Erik Rosaeg(eds), Competition and regulation and shipping related Industries( Martimus Nijhoff Publishers 2009), p.233

\textsuperscript{127} paras. 23-29 of the Decision
states’ tax systems. The measure would create an unjustified distortion of competition between companies which had foreign affiliates and others which did not.

Regarding the all-or nothing option, in case N 93/2006 of Poland, the Commission stressed that companies should stay in the tonnage tax scheme for 10 years and rejected the minimum of 5 years that Poland wanted to adopt. The commission adopted the minimum of 10 years because it found it consistent with the existing tonnage tax schemes and did not want vessels and ship owners operating in different Member State registers to be treated unequally.

In case of Finland, the Commission found the reformulated rules on the issue of group subsidies in a situation of a company under tonnage tax regime to be in line with the ring-fencing principles as set in the Maritime guidelines. More specifically, the Commission agreed with the decision of Finland that subsidies between groups of companies would not be subject to tonnage tax.

### 3.2.2 CHARTERING OF VESSELS

Although chartering of vessels is not covered by the Maritime Guidelines, the Commission’s practice has established some rules. In case C 58/2007, Denmark proposed raising the proportion of owned tonnage to chartered-in tonnage to 1:10. The Commission had doubts because of its former decisions where it had mentioned that any additional capacities exceeding the threshold of 1:4 should be taxed under normal corporation tax. The Commission also rejected the proposal of Denmark to include management fees derived from the management of vessels of third parties in tonnage tax by using the same reasoning about the exceeding threshold. Another similar case is that of Ireland (C 2/08) in which Ireland wanted the requirement that not more than 75% of

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128 paras. 40-41 and 115 of the Decision


130 para. 36 of the Decision


eligible could be chartered in to be excluded from its legislation\textsuperscript{133}. The Commission stressed that “even though the guidelines do not mention any limits for the inclusion of time chartered ships under tonnage tax schemes, in its decision making practice the Commission has authorised schemes where companies with a ratio of 1:3 or 1:4 owned to time chartered ships were eligible to tonnage tax. The exception of the 1:4 ratio as compared to the initial 1:3 ratio in Decision No 563/2001/EC concerning the initial approval of the Danish tonnage Tax was justified on the basis of an in depth market analysis\textsuperscript{134}.” Another remark of the Commission is that the principle of fiscal competition with other Member States had not been invaded and that the fully exclusion of the time charter limit could violate the common interest principle pursuant to Article 107 (3) (c) TFEU\textsuperscript{135}.

3.2.3 CABLE LAYING AND DREDGING ACTIVITIES

In case C 22/2007 of Denmark a problem arose regarding which type of activities the Maritime guidelines cover and whether cable layers and dredgers could be included as well. Commission’s view, which was in line with the ruling of the Court of Justice in case C-251/04(Greece v Commission) was that maritime transport covers only the straightforward carriage of goods or passengers by sea between a port and an off-shore installation and no other services such as towing which are incidental or ancillary to such carriage\textsuperscript{136}. However, the new definition of maritime transport in section 3.1 of the Guidelines appears to be at odds with the Commission’s view. In The Guidelines it is mentioned that “fiscal arrangements for companies (such as tonnage tax) may be applied to those dredgers whose activity consists in maritime transport for more than 50% of their annual operational time and only in respect of such transport activities”

and consequently these activities fall within the meaning of maritime transport\textsuperscript{137}. The Commission decided that cable-laying and dredging activities should be associated by analogy with maritime transport for the purpose of reducing labour-related costs\textsuperscript{138}. The Commission pointed out that there are similarities between cable-laying, dredging and maritime transport vessels such as the level of qualification for seafarers under the same labour-law and social framework, the risk of relocation of on-shore activities and the fact that all these are sea-going vessels which are obliged to undergo the same technical and safety controls\textsuperscript{139}.

In case C 93/2006 of Poland, the Commission stated that for both towage and dredging, the operational time of each tug or dredger (and not the revenue generated) was used to measure if the 50\% threshold is achieved\textsuperscript{140}. Furthermore, the Commission enumerated a list of ancillary activities such as the leasing and the use of containers which are covered by tonnage tax only if the tonnage tax companies provide them\textsuperscript{141}.

In case N37/2010 of Cyprus, the Commission also mentioned that tonnage tax covers a number of ancillary activities such as hotel, catering, entrainment and retailing activities provided that the shipping companies exercise them and they are useful for carrying out the main activities\textsuperscript{142}.

### 3.2.4 OTHER PROBLEMATIC ISSUES

In case of Finland (SA 30515-N448/2010), the Commission noted that even after the relaxation of the rules on the flag requirement, it would be obligatory for the beneficiaries to maintain at least 60\% of their tonnage registered in the EU\textsuperscript{143}. Moreover, it is possible for companies to charter in with crew 75 \%( whereas previously a 50\% was required) of tonnage and all their


\textsuperscript{138} para. 70 of the Decision

\textsuperscript{139} paras.66-69 of the Decision


\textsuperscript{142} para. 85 of the Decision

\textsuperscript{143} para. 24 of the Decision
income is covered by tonnage tax\textsuperscript{144}. Companies can also charter in with crew up to 80\% of tonnage in order to expand their operations for a short period\textsuperscript{145}. The Commission imposed a limitation with respect to ships chartered in with crew so that on shore activities which relate to vessels could be subject to tonnage tax more easily within the community\textsuperscript{146}. Furthermore, it is now possible for a shipping company within a group to choose to be taxed under the tonnage tax regime independently of the taxation regime applicable to other maritime transport companies of the same group\textsuperscript{147}. This is justified by the fact that the application of the tonnage tax regime to transportation revenues of such companies would place such companies in worse situation than under the normal corporate income taxation regime\textsuperscript{148}.

Another important issue that arose in the recent case of Malta (SA.33829/2012) concerns the taxation of gains deriving from the sale of ships and shares of maritime transport companies. The Commission considers that the exemption from income tax on income arising from capital gains\textsuperscript{149} and dividends\textsuperscript{150} from shares in companies, which derive their income from the maritime transport and are covered by the Commission guidelines, constitutes State aid. The Commission notes that such income does not arise from shipping activities but from investment activities\textsuperscript{151}. However, any economic activity requires an investment and thus shipping activities must be interpreted broadly so that the pure investment on shipping companies to be regarded as shipping income\textsuperscript{152}. The allegation that income tax exemption of capital gains and shares, related to shares in shipping companies, does constitute State aid is not in accordance with the nature of such income, which is income from the company’s activity\textsuperscript{153}. Another additional argument why such income is not considered State aid is that corporate tax systems take into consideration, when taxing dividends, the fact that corporate tax has already been paid for the distributed income\textsuperscript{154}.

\textsuperscript{144} para. 26 of the Decision
\textsuperscript{145} para. 26 of the Decision
\textsuperscript{146} para. 29 of the Decision
\textsuperscript{147} para. 35 of the Decision
\textsuperscript{148} para. 35 of the Decision
\textsuperscript{149} para. 92 of the Decision
\textsuperscript{150} para. 94 of the Decision
\textsuperscript{151} para. 92 of the Decision
\textsuperscript{152} George Matsos, “ Systematic Misconceptions of State Aid Law in the area of Taxation”, ESTAL , vol.13, No.3, p. 503, 2014
\textsuperscript{153} George Matsos, “ Systematic Misconceptions of State Aid Law in the area of Taxation”, ESTAL , vol.13, No.3, p. 504, 2014
\textsuperscript{154} George Matsos, “ Systematic Misconceptions of State Aid Law in the area of Taxation”, ESTAL , vol.13, No.3, p. 504, 2014
Overall, the previous mentioned cases showed how difficult is to extend the coverage of fiscal aid to ship management. It is not easy to distinguish ship managers who act as ship owners and those who do not. One solution would be to extend the same fiscal treatment to all income derived from the operation of a vessel\textsuperscript{155}. In this way, there will be no arbitrary distinction between eligible and non-eligible ship owning and ship managing activities\textsuperscript{156}.

4 GREEK SHIPPING TAXATION AND EU LAW

Greek state’s provisions on the taxation of profits deriving from maritime transport do not comply with those of the OECD Model Convention. More specifically, for the allocation of these profits, the State of registry is used. Regarding the Greek tonnage tax, it must be stated that it falls within the scope of the OECD Model Convention. Pursuant to article 2 paragraph 1, the OECD Model Convention covers taxes on income and capital. According to paragraph 4 of this article, any tax which is similar in nature with the previously mentioned taxes is covered by the Convention. Greek tonnage tax must be regarded as identical to income tax and thus the OECD Model Convention applies\textsuperscript{157}.

The establishment of Law89/1967 contributed to the expansion of management activities in Greece. This law gives the possibility to foreign companies which own or charter vessels with a Greek of foreign flag to establish their management activities in the Greek State and not be subject to any form of taxation\textsuperscript{158}. This scheme gives the opportunity to ship owners to operate their companies in third countries while maintaining their management activities in Greece and

\textsuperscript{155} Phedon Nicolaides, “Fiscal Aid for Maritime Transport” in Antonios M.Antapases, Lia I.Athanasio, Erik Rosaeg(eds), \textit{Competition and regulation and shipping related Industries} (Martimus Nijhoff Publishers 2009).p.239


\textsuperscript{157} Georgios Matsos, “ Tonnage Tax and Tax Competition” in Antonios M.Antapases, Lia I.Athanasio, Erik Rosaeg(eds), \textit{Competition and regulation and shipping related Industries} (Martimus Nijhoff Publishers 2009) .p.282

take advantage of the profits deriving from these foreign incorporations without paying any tax in Greece.

In 2012 the Commission started the existing aid procedure concerning the Greek Law 27/1975 on the taxation of ships and in 2015 it invited Greece to better target its tonnage tax. More specifically, the Commission found that the Greek provisions do not comply with the EU state aid rules because they allow shareholders of shipping companies to take advantage of the favourable tax treatment which only maritime transport providers should enjoy. According to the Commission’s remarks, all maritime sector intermediaries and operators of ships, who are not engaged in shipping activities, should be excluded from the preferential tax treatment. Moreover, favourable tax treatment should not be given to insurance intermediaries and maritime brokers.

Generally, the Commission stressed that the Greek tonnage tax scheme is not well targeted and gives advantages to the shareholders of maritime transport companies as well as companies other than maritime shipping companies beyond what is allowed under the Maritime Guidelines. Therefore, the Commission found that it is necessary for Greek state to review which vessels are eligible for tonnage tax by excluding fishing vessels, port tugboats, and yachts rented out to tourists without a crew from the favourable tax regime. Operators of such vessels should be taxed according to the standard income tax. The Commission’s proposals do not concern the operation of bulk carrier and tanker vessels which can continue to enjoy a tonnage-based taxation instead of profit-based taxation under the condition that the operators of vessels keep the share of the fleet they have under EU flags.

If Greece agrees to the measures proposed by the European Commission, it would have to change its national rules with effect from 1 January 2019 at the latest.

According to Theodore Veniamis, president of the Union for Greek ship owners, the Commission’s concept is not sound. It does not take into consideration the fact that some of the advantages such as capital gains are granted to individuals only and not to shipping companies and thus cannot be assessed according State aid rules. A tax advantage to shareholders does not result in an indirect advantage to a company if anybody can invest in such an undertaking. The Commission should have showed how the shipping companies gain indirect advantages under the

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159 para. 181(e) of the Decision
160 para. 182(i) of the Decision
161 para. 182(a) of the Decision
162 Theodore E.Veniamis, “Executive Summary of the Union of Greek Ship owners to the EU Commission Decision for the Greek Tonnage Tax System” (Nafsgreen World Shipping news 2016)
“aid” scheme at issue. The Commission could have also used its discretion and the solid evidence submitted by the Greek government to declare the Greek regime compatible. When applying the Guidelines, the Commission has to deviate from them, in individual cases, by giving justifications which comply with the principle of equal treatment and do not constitute an infringement of the general principles of law. Last but not least, the Commission should not have only considered the general rules on taxation as a reference framework but also the constitutionally protected provision of Law 27/1975. It is not obvious that shipping companies and other companies in Greece are in a similar factual and legal situation according to the constitutionally protected provisions. Finally, the Commission has not adequately proved distortion of competition on the basis of the Guidelines because the casual link between the alleged advantage and the distortional result is remote.

CONCLUSION

The traditional maritime nations decided to combat the massive migration of EU vessels to third countries by developing favourable tax schemes such as the tonnage tax scheme. This scheme includes many tax advantages such as low tax rates and is characterized by transparency, simplicity and certainty. However, despite its advantages, it cannot compete effectively open registries or “Flags of Convenience” where ship owners are subject to low or even zero taxation.

State aid is granted to Member States to become competitive in the international maritime field. Some of the aims of State aid are the promotion of the use of EU flags, the prevention of flagging out and the maintenance of a Community fleet by reducing taxes. The Maritime Guidelines are used by the Commission to evaluate the compliance of their measures with EU state aid rules. However, according to EU law the taxing powers are reserved to the Member States which cannot be obliged to use one uniform set of rules on all subjects of each individual tax. The European Commission should not consider the variations in tax schemes as distortions of competition. When applying the Guidelines, the Commission should take into consideration that distortion of competition caused only by the fragmented allocation of taxing powers to the Member States cannot constitute prohibited State aid. Due to the diversity of shipping services between operators, the Commission should not just restate the accepted legal principles of the Guidelines but assess the measures on each individual case.

Finally, the evaluation of the Greek scheme showed that the European Commission’s decision was incompatible in some parts with the Maritime Guidelines. More specifically, business

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activities were treated differently with respect to their taxation and commercial operators of vessels were excluded from tonnage tax\textsuperscript{165}. Despite the inconsistencies of the Commission’s decision with the Maritime Guidelines, it is evident that the Greek State has to better target its tonnage tax system and make it more attractive for the establishment of management activities in its territory.

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