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NEWSLETTER

THE NEW TONNAGE TAX: A PORTUGUESE GEOSTRATEGIC ASSERTION

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IBFD Tax Correspondent Angola, Mozambique and East-Timor, 2013, 2014, 2015, 2016, 2017, 2018

SUMMARY

Following the publication of Decree-Law no. 92/2018, a new legal framework aimed at maritime shipping and merchant fleets has been introduced. With the goal of reinforcing the competitiveness of the Portuguese flag across the seas, it is established a new special regime for the computation of the taxable income based on the vessels’ tonnage (tonnage tax), as well as a special tax and contributory regime for the seafarers. The legal changes are supplemented with a revamped and simplified registration for ships and vessels.



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I. INTRODUCTION

A new tonnage tax system was recently introduced in Portugal by Decree-Law no. 92/2018, of November 13th, following the legislative authorization granted by Law no. 42/2018, of August 9th.

The enactment of the tonnage tax scheme as the intention of contributing to the international competitiveness of the Portuguese merchant fleet and to preserve Portugal's economic growth.

In order to create this new regime, the Ministry of Sea first conducted a *benchmarking* study on the various tonnage tax regimes of the different countries in the European Union. The study has proved and demonstrated that the main and critical factors contributing to the success of ship registers are the tax regime applicable to the Merchant Navy's activity, as well as the social protection regime applicable to the crew.

In this context, the aforementioned Decree-Law establishes:

- a special regime for the computation the taxable income, based on the tonnage of vessels;
- a specific tax and contributive regime for the maritime activity;
- a simplified registry of vessels and ships.

The tonnage tax regime was also previously controlled and approved by the European Commission in the context of the State Aid (decision of 6th April of 2018 SA.48929).

II. TONNAGE TAX

The tonnage tax scheme is an optional method for determining the applicable taxable income derived from ships and vessels registered as well as both strategically and commercially managed in the European Union (EU) or the European Economic Area (EEA). The tonnage tax allows the Portuguese ship-owners to compute their taxable income on the basis of the net tonnage of the

vessels, i.e. based on the size of the maritime fleet. Hence, it deviates from the principle of taxation based on the companies' actual profit.

III. CALCULATION OF TAXABLE INCOME

When the net tonnage exceeds 1,000 net tonnes, the amount of taxable income of taxable entities subject to Portuguese Corporate Income Tax (IRC) may be calculated by applying each level to a vessel's net tonnes covered by such level, according to the following table:

NET TONNAGE	DAILY TAXABLE INCOME FOR EACH 100 NET TONNES
Up to 1,000 net tonnes	€ 0,75
Between 1,001 and 10,000 net tonnes	€ 0,60
Between 10,001 and 25,000 net tonnes	€ 0,40
More than 25,001 net tonnes	€ 0,20

Further taxable income reductions are granted according to the description above for start-ups of the maritime

industry, with said reductions being 50% and 25% in the first two active years. Reductions of 10% to 20% also apply for vessels with capacity exceeding 50,000 net tonnes, provided that they meet certain environmental requirements.

Other legally foreseen deductions to the taxable income are not applicable. Expenses or losses incurred by the taxpayer relating to activities or vessels not covered by the regime may yet be deducted.

IV. CORPORATE INCOME TAX APPLICABLE

The general rates of the Corporate Income Tax (IRC) are applicable, namely 21% in mainland Portugal and Madeira island and 16,8% in Azores Archipelagos.

Therefore, without prejudice to the applicability of other provisions stated in the Madeira International Business Center, to entities subject to Madeira's special tax regime, the tax rate of 5% there foreseen is not applicable to the

income voluntarily submitted to the *tonnage tax* scheme.

Moreover, the *tonnage tax* scheme does not affect the imposition of autonomous taxation (the taxation of certain expenses) foreseen in the Corporate Income Tax Code.

V. TAX AND CONTRIBUTORY REGIME

SEAFARERS' PERSONAL INCOME TAX (IRS)

With regard to the fiscal and contributory benefits applicable to seafarers of vessels eligible for the tonnage tax scheme, it is also noteworthy that the new scheme exempts the seafarers from paying personal income tax (IRS), insofar as they are on board for at least 90 days during the tax year.

SEAFARERS' SOCIAL SECURITY

The new scheme also enables the contribution payment of the social security (*Segurança Social, SS*) at reduced rates, more precisely 6%, where

4.1% are charged to the employers and 1.9% to the employees.

VI. COVERED ENTITIES

Corporate income taxpayers as well as tax residents in Portugal, i.e., with head office or management in Portugal, who mainly conduct commercial activities related to maritime transportation of people or cargo, may request that the new *tonnage tax* scheme applies to them.

VII. ECONOMIC SUBSTANCE REQUIREMENTS

The application of the tonnage tax scheme is subject to certain legal requirements:

LOCATION OF STRATEGIC AND COMMERCIAL MANAGEMENT

The beneficiary companies are required to be strategically and commercially managed from a country that is a member of the EU or the EEA.

VESSEL HOLDERS

If the beneficiaries are vessel holders, at least 60% of the net tonnage of their fleet

is required to be registered under the flag of the location in question.

VESSEL CHARTERERS

If, on the other hand, the beneficiaries are vessel charterers, the net tonnage is required to be less than 75% of the total fleet of the owner.

SEAFARERS' ORIGIN

At least 50% of the seafarers (workers) are required to be nationals from the EU, the EEA or Portuguese-speaking Countries.

VIII. COVERED AND EXCLUDED MARITIME ACTIVITIES

COVERED ACTIVITIES

The beneficiary companies are also required to carry out certain activities. These consist of maritime transport of persons and goods, namely the transport as such, the sale of goods for consumption onboard as well as the supply of services directly related with the transport.

Covered are also the activities of research vessels, support of offshore activities, and

towage and dredging are covered, provided that, among other things, 50% of the annual operations constitute maritime transport.

(EXPLICITLY) EXCLUDED ACTIVITIES

The tonnage tax scheme generally excludes the activities not covered by the scheme, but it also explicitly excludes, namely, the following activities:

- i. regular passenger transport activities, unless carried out in Madeira and the Azores;
- ii. activities the object of which is not the transport of goods or passengers, such as fishing;
- iii. provision of services consisting of loading, unloading, piloting, and towing to third parties;
- iv. museum activities, feasibility studies, exploration and extraction of natural resources, and marine conservation;
- v. permanently anchored vessels; and
- vi. leisure, recreational, educational, or social activities.

IX. COVERED REVENUES

The new tonnage tax scheme applies to:

- i. core revenues derived from maritime transport activities (goods and passengers);
- ii. ancillary revenues strictly related to shipping activities, which have been limited to maximum of 50% of each eligible vessel's operating revenues; and
- iii. revenues derived from towage and dredging.

X. OPTING INTO THE TAX REGIME

The option for the regime may be exercised via Internet at the 'Portuguese Tax Portal' either i) when activity is initiated or ii) until of the end of the tax period in which the taxable persons intend to initiate the *tonnage tax* scheme's application.

The taxable persons who intend that the regime produce its effects on or after 1st of January of 2018 (i.e. retroactively), shall express such intention during Q1 2019.

The optional scheme shall apply for a five-year minimum period. However, a transitory regime is foreseen, which reduces the period to merely three years in case the option for the regime is exercised until the end of the taxable period beginning on or after January 1st, 2020.

XI. TAX REGIME'S DURATION

The optional scheme can be applied to tax periods beginning on or after January 1st, 2018, and remains in force for ten years, i.e. until 2028, with a conditional renewal by the European Commission in the context of Fiscal State Aid.

The Community guidelines on State aid to maritime transport issued by the European Commission were updated for the last time in 2017. Therefore, the eventual evolution of the European Commission's position may be, gradually, assessed by the future decisions related to the tonnage tax regimes in force in other European jurisdictions.

XII. VESSEL REGISTRATION

Furthering the Decree-Law of the Vessels and Maritime National System (“SNEM”), the new registry scheme implements procedures concerning ship registry and it digitalizes every associated act by running the entire procedure electronically.

The new registry scheme is distinct and will coexist with the International Shipping Register of Madeira (“MAR”).

XIII. CONCLUSION

The maritime areas of sovereignty and jurisdiction originated by the continental coast and thirteen Atlantic islands determine Portugal’s deep relationship with the sea.

The fact that 53% of the EU’s external trade takes place in the waters under Portuguese jurisdiction underlines the importance of the tonnage tax scheme. In addition, approximately 60% to 70% of all Portuguese external trade and national import occurs by sea.

Taking into account that Portugal has the 11th largest area of jurisdictional water in the world, and one of the most confluent places of maritime traffic in the world, maritime activities play a strategic role in the creation of vital economic synergies for the country.

From this point of view, the tonnage tax scheme may represent a crucial step in order to promote and develop the desired growth of the Portuguese maritime-port sector.

Lisbon, December 6th, 2018

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