Maritime UK

One voice for *shipping*, *ports* and maritime *business*

The success of the tonnage tax

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In the last 12 years the decline in the size of the UK merchant shipping industry has been dramatically reversed, with a growth in our merchant shipping fleet by up to six times.

Shipping now earns £1.5 million for the UK economy every hour of every day. It is also part of a much wider maritime services cluster in the UK, which contributes nearly £27 billion to the UK's GDP and supports around half a million British jobs.

During this time recruitment of professional seagoing officers has doubled – which is crucial also for the full range of other maritime activities in the UK, including our ports, manufacturing, business services in the City, government regulatory activity, and many more.

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All this has been made possible by the far-sighted and apolitical endorsement in this country of a tax regime for shipping, parallel to that developed in other EU countries, which enables high-cost fleets in Europe to compete on an equal basis with their industry competitors world-wide – the tonnage tax.

A 2011 study by Oxford Economics concluded that the implementation of the tonnage tax has delivered significant benefits to the UK economy. The study estimated that the shipping industry's contribution to UK GDP is around two to three times as large as it would otherwise have been, and that this additional activity supports around 70,000 extra jobs in the UK.

At a time of economic difficulty, when our island nation needs to trade its way back to prosperity, it is vital that we have a fiscal regime that is competitive with other maritime nations.

J. Stewart

Jim Stewart
Chairman, *Maritime UK*

What is the tonnage tax?

The tonnage tax is a ring-fenced regime allowing ship-operating companies to have their taxable profits from shipping activities determined at fixed rates, according to the carrying capacity (tonnage) of the ships in their fleet. These, rather than the actual profits, are then subject to corporation tax in the normal way, producing a low tax charge that is competitive in the international shipping markets. Introduced in 2000, this system reflects the norm in many other countries throughout the world and is explicitly approved under the EU's state aid policy.

> ***The UK regime is designed to nurture and protect UK talent***

Companies are required to elect into the regime for a 10-year period and may extend that election on a rolling annual basis. The UK regime is unusual in that companies are also subject to a specific commitment to train new recruits every year, designed to nurture and protect UK talent.

Tax regimes in other maritime nations

For most major trading economies across the globe, it is standard practice for their shipping companies to be subject to low- or nil-taxation regimes. Closer to home, such regimes are expressly authorised by the European Commission.

Tonnage tax is the most prevalent example. The primary model, introduced in 1996 by the Netherlands and adopted by the UK has since been implemented by Belgium, Bulgaria, Denmark, Finland, France, Germany, India, Ireland, Italy, Japan, Norway, Poland, South Africa, South Korea, Spain, Sweden, and the USA. An older 1957 model was applied in Greece, and has been followed by Cyprus and Malta. Almost all of the top 10 shipping nations, by owned fleet-size, operate tonnage tax regimes.

Many other nations also have specific shipping tax exemptions or incentives – including Hong Kong, the Philippines and Singapore.

What the tonnage tax does

The principal aim of this country's tonnage tax is to create a positive fiscal environment, both to keep shipping companies within the UK and to create an incentive for inward investors. This generates jobs, retains skills and contributes to economic growth. The 10-year minimum sign-up period ensures some longevity for this arrangement, which is in the mutual interest of both the companies and Government.

Eligibility for the tax is centred on the requirement for ships to be 'commercially and strategically managed' within the UK, regardless of where those ships are registered. This recognises it is the operation of the ship which creates the value.

How the tax came about

In its 1997 Annual Review, the Chamber of Shipping called for a more competitive tax environment to be established in the UK. In particular, it suggested the introduction of a tonnage-based tax regime for British companies.

Following this, a Shipping Working Group, including representatives from the industry, trade unions and Government departments, was established by the then Deputy Prime Minister, John Prescott, in March 1998. The group suggested that such a tax could underpin a renaissance of the UK shipping industry. The Government's response was published in December, in the form of a report titled British Shipping – Charting a New Course, and set out the policy and objectives for a new national maritime policy.

> ***'... a key ingredient of a package designed to allow UK shipping to achieve its full economic potential***

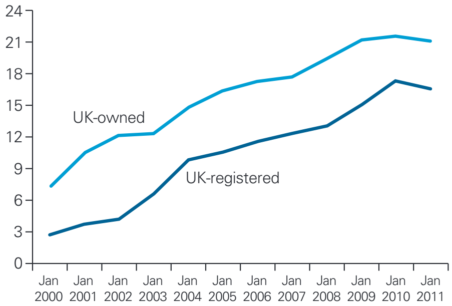
A similar conclusion was reached by an independent enquiry commissioned by the Chancellor of the Exchequer, and the Deputy Prime Minister announced the tax change on 12 August 1999. The following year, it was a key ingredient – along with major reforms to the Maritime and Coastguard Agency – of a package designed to reverse the decline in the UK merchant fleet and allow the UK shipping industry to achieve its full economic potential.

The impact of UK tonnage tax

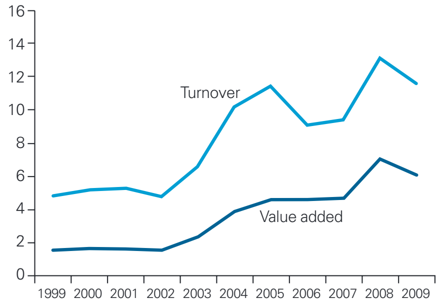
In the last quarter of the 20th century, both the UK fleet and the number of seafarers were in long-term decline.

Since 2000, there has been remarkable growth of shipowners and operators within our shores. The UK-owned fleet has grown by almost three times, and the UK-registered fleet – albeit from a very low base – has grown by more than six times.

UK-owned and UK-registered fleets 2000-2011 (Dead Weight Tonnes)



Shipping industry's contribution to GDP (£bn)



This turnaround is of major benefit to the UK economy. The shipping industry's contribution to GDP in terms of turnover and value added has risen steadily over the last decade. The most recent figures from the Office of National Statistics suggest shipping's gross revenue in 2011 stood at a massive £12.9 billion.

In a 2011 report, Oxford Economics estimated that the shipping industry's contribution to UK GDP is around two to three times as large as it would otherwise have been, and that the additional activity supports around 70,000 extra jobs in the UK.

The 10-year training condition has been another major benefit. The number of new entrant officer trainees has more than doubled since 2000. Department for Transport figures showed 472 in 2001; for the 2011/12 academic year, this figure is 983 – the highest for at least 20 years. The growth in trainee officer recruitment has risen twice as quickly as the number of UK-based ships and, while tonnage tax companies are only obliged to provide training, the high success rates in securing permanent employment for UK trainees have been proven. An MCA survey of new officer trainees in the autumn of 2010, for example, found that 96 per cent of those asked had found work. Furthermore, a BIMCO study of the same year into global supply and demand of seafarers found an overall shortage of officers, suggesting the opportunities for work will continue.

If there had been no tonnage tax in this country, it is clear that the numbers of jobs at sea and ashore in the shipping sector would have continued to decline damagingly, with a consequent devastation of the professional skills base available to the UK's wider maritime cluster. In contrast, shipping has been a model of growth in recent years, with employment growth over the last five years averaging 10 per cent compared to the economy-wide average of 0.3 per cent.

Challenges

Despite the benefits reaped over the last 12 years, the tonnage tax and UK fleet continue to face challenges. The state of the market generally has created tough conditions that are expected to continue for some time. Hardships have been felt by all industries and shipping has not been exempt from that.

The mismatch between supply and demand of ships has created a key struggle, while other countries which saw the benefits of the UK tonnage tax have implemented their own tax incentives in an attempt to lure shipping companies away from our shores. Singapore, for example, was recently named as the most important shipping centre in the world and its influence is expected only to increase. The UK needs to ensure a stable and attractive regime to maintain its competitiveness.

The last few years also saw significant challenges resulting from misinterpretations by HMRC inspectors of some key tonnage tax requirements, particularly relating to eligibility for the regime. These created a damaging perception of the UK as a world maritime centre and a growing loss of confidence from many tonnage tax companies, causing investors to query the value of basing their businesses here. In the last year the Government has reasserted policy control,

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urgently revised its guidance to inspectors, and re-affirmed its support for the tonnage tax system for the future in warm terms.

Other potential challenges continue today in the form of the European Commission's current review of the EU's Maritime State Aid Guidelines, which have provided the justification for the UK's and other member states' tonnage tax regimes. These have been a major success in underpinning the EU's shipping industry, and it is critical that they should be re-affirmed by the review, subject only to a few specific clarifications. It will be important to maintain the pragmatic flexibility in the present guidelines, if they are to continue to be successful.

Looking forward

For the successes of the UK fleet to be sustained, a stable and competitive environment is vital, not least in fiscal and employment policy. The 10-year condition of tonnage tax means that shipping companies must be able to have confidence that the regime will not be modified during that period, without good cause and adequate notice – and that decisions in other policy areas will not reduce the attractiveness of basing shipping businesses in the UK and of training British seafarers.

As a ship's life can be anything from 25 years upwards, shipping companies adhere to long-term business plans. The attractiveness of basing strategic operations within the UK therefore depends on long-term fiscal incentives, coupled – crucially – with the flexibility for companies to be able to make commercial decisions without restrictions in such areas as flagging and crewing. Our key competitors do not make these impositions. For the UK to do otherwise could spark its downfall.

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