

BRIEFING

SPANISH TAX LEASE: BACK ON TREND
THE EU COMMISSION'S DECISION AGAINST
THE "OLD" SYSTEM IS ANNULLED

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THE "OLD" SPANISH TAX
LEASE FOUND TO BE
COMPATIBLE WITH EU
COMPETITION RULES

THE STATE OF SPAIN AND
OTHERS APPEALED THE EU
COMMISSION'S 2013
DECISION DECLARING
THAT THE "OLD" TAX LEASE
CONSTITUTED AN ILLEGAL
STATE AID.

THIS HAS NOW BEEN
ANNULLED BY THE
GENERAL COURT OF THE
EU.

THIS IS EXTREMELY
POSITIVE NEWS FOR THE
SPANISH SHIP FINANCE
MARKET WHEN VIEWED
ALONGSIDE THE DECISION
OF DECEMBER 2014
WHICH DISMISSED AN
APPEAL OF THE
NETHERLANDS' MARITIME
TECHNOLOGY
ASSOCIATION AGAINST
THE NEW TAX LEASE.



The commencement of formal proceedings in 2011 by the EU Commission (the "Commission") against the – in today's market – so-called "old" Spanish tax lease threw cold water on the Spanish domestic ship finance industry. Following several complaints from the shipbuilding sectors in other Member States, the Commission challenged certain Spanish tax and financial regimes, which allegedly distorted competition in the shipbuilding sector. The proceedings ended on 17 July 2013, when the Commission adopted a Decision, relating to state aid (the "Decision")¹, which the General Court of the European Union ("GCEU") has now annulled.

According to the Commission, the "old" Spanish Tax Lease ("STL") combined five different individual – yet related – tax measures in order to generate a tax benefit, in particular:

- i. **an accelerated tax depreciation** of leased assets: Spanish law allowed for an accelerated amortization of leased assets, whereby the rent paid under qualifying finance leases would be deductible, within certain limits;
- ii. **a discretionary application** of early depreciation of leased assets: in principle, the accelerated depreciation of the leased asset would start on the date on which the asset is delivered and is operational. However, the Ministry for Economic Affairs and Finance could, upon formal request by the lessee, determine an earlier starting date for depreciation, under certain conditions;

¹ Decision 2014/200/EU relating to the state aid S.A. 21233 C/11 (ex NN/11, ex CP 137/06).

“IN THE DECISION THE COMMISSION CONCLUDED THAT THE [“OLD” SPANISH TAX LEASE] ... CONSTITUTED STATE AID TO THE EIGs AND THEIR INVESTORS, AND WERE PARTIALLY INCOMPATIBLE WITH THE INTERNAL MARKET.”

- iii. **the specific tax transparent regime of economic interest groupings (“EIGs”):** even though EIGs have their own legal status and personality different from its members, from a tax perspective, they are “transparent” with respect to them, resulting in “the possibility to pass on the substantial losses incurred by the EIG through early and accelerated depreciation”.
- iv. **the tonnage tax regime (“TT”)** and, more precisely, the treatment of capital gains in the context of the transfer of vessels to the TT system: according to the Commission, in the context of the STL, the taxation arising from the sale of vessels within the TT system was avoided due to certain features of the law whereby such vessels were deemed to be new, not used.
- v. **article 50 para. 3 of the Spanish Corporate Income Tax Regulation:** In the case of the STL, the Commission observed that the EIGs could “leave the normal corporate income taxation system to join the TT system without either settling the hidden tax liability resulting from the early and accelerated depreciation immediately on entry into the TT system or subsequently when the vessel is sold or dismantled”, as an exception to the general ring-fencing rules set out in the Corporate Income Tax law.

In the Decision the Commission concluded that the above (most particularly the early depreciation of leased assets, the application of TT to non-eligible companies, vessels or activities and the measures resulting from the above-mentioned article 50 para. 3 of the Corporate Income Tax Regulation) constituted state aid to the EIGs and their investors, and were partially incompatible with the internal market. The Commission ordered the recovery of the aid only from the investors having benefitted from the advantages at issue.

The appeal and the main discussion at stake

The Decision was appealed before the GCEU on the basis of four arguments, the first and most fundamental being the violation of Article 107.1 of the Treaty for the Functioning of the European Union (“TFEU”). The other three were invoked as fall-back arguments should the GCEU consider the existence of a state aid. In essence, the appeal argued that the Commission violated several EU general principles of law: equal treatment, the protection of legitimate expectations and legal certainty.

“IN ESSENCE, THE APPEAL ARGUED THAT THE COMMISSION VIOLATED SEVERAL EU GENERAL PRINCIPLES OF LAW...”

However, after examining the first argument, the GCEU stated that since the Decision incurred in several errors and a lack of motivation in relation to the qualification of the measures as state aid in light of the provisions of Article 107.1 of the TFEU, the rest of the arguments did not need to be examined.

In particular, the GCEU concluded that, in the absence of an economic advantage in favour of the EIGs (in essence due to their tax transparency regime), the Commission wrongly assessed that EIGs had benefitted from state aid, when in fact the investors were those taking advantage of the tax and other economic advantages which resulted from the STL.

According to the GCEU, the Commission was also wrong to declare that there was a selective advantage and, therefore, state aid in favour of the EIGs and investors. Any operator taxable in Spain could benefit from the tax advantages resulting from the STL. Finally, the GCEU further questioned the underlying reasoning for concluding

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that the three measures at stake were likely to distort competition and affect trade between Member States.

In conclusion, on 17 December 2015 the GCEU decided to annul the Decision and hold the Commission liable for its costs and those of the parties appealing. In any event, it should be noted that the Court’s decision is subject to appeal before the EU Court of Justice within two months of its formal notification.

Effects on the Spanish market

This is extremely positive news for the Spanish ship finance market. The years 2014 and 2015 have seen an increase of transactions governed by the rules of the new Spanish tax lease, which replaced the “old” one, but coupled with a prudent approach by Spanish investors hit by the effects of the Decision and that of shipowners and their financiers. Rumour has it that in light of this ruling, several arranging banks will step back into the market, currently dominated by two entities.

The good news should be considered alongside the decision of the GCEU of 9 December 2014, whereby the Court dismissed the appeal (case T-140/13) filed by the Netherlands Maritime Technology Association against the Commission’s decision concluding that the new Spanish tax lease did not constitute State aid.

Overall and so far, a promising 2016 ahead for the Spanish ship finance market.

CONTACTS

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