

By PwC Deutschland | 23. Januar 2013

# No tax on off-balance sheet intangibles on change to tonnage tax

**The Supreme Tax Court has held that the hidden reserve calculation on the change to tonnage tax (shipping lines) cannot include those intangibles that could not be taken up under the accounting rules prudently applied.**

The German tonnage tax system allows shipping lines to determine their taxable income from the operations of their ships in international waterways on an almost invariably favourable formula based on the number of days at sea and the net register tonnage (a measure of a merchant ship's available space for passengers and cargo – 1 NRT = 2.83 m<sup>3</sup>) of the ship. The option is exercised by ship at ten-yearly intervals, the first opportunity being the year in which the ship is put into service. On election for tonnage tax, the untaxed reserves accumulated in previous periods through the accretion in value of capital and other assets are established in a register comparing the book and market values of each item at the close of the immediately preceding business year. These reserves are then released to taxable income on disposal of the asset to which they relate, on withdrawal of that asset from international operations, or on election to return to regular taxation on the results of the vessel concerned.

A shipping line ordered a vessel from a shipyard in the USA for a fixed price for delivery in December, some 17 months later. The price was to be paid in instalments based on progress in construction. As things turned out, the ship was not completed until the following January, at which time the shipping line took possession and started the process of registration, fitting out and working up. At this stage, the line applied for approval to tax the ship's operations by "tonnage" (NRT). On approval, it drew up its register of hidden reserves (consisting entirely of exchange gains on its US \$ prepayments, but offset by the losses on the corresponding liabilities). Some years later, the tax auditors noticed that the hidden reserve register made no mention of the rise in ship prices between the date the ship was ordered and the date the line took possession. In their view, the vessel acquired was worth more than the amount paid for it and this accretion in value should have been reflected in the schedule as an "order value".

The Supreme Tax Court has now held that the shipping line could not have taken up an "order value", as such an asset had not, and could have, been capitalised in the accounts prior to delivery of the ship. Rather, it was a contingent asset from unfinished business. If it could not be accounted for, it could not have a book value (the tax office claimed the book value was nil), which could not therefore be compared with a current market value. Accordingly, no hidden reserve could be registered.

The tax office then tried another tack by claiming the value of the prepayments had risen beyond their nominal amount. The thinking seems to have been, the ship had been almost completely paid for by the end of the year of valuation, so that in effect the line was about to receive a vessel of greater value than the nominal amount of cash paid. The court, however, did not examine the substance of this argument, saying merely that the value of the prepayments was no longer open to dispute. Each item on the hidden reserve register was separate from the others and thus fell under its own statute bar. The passage of time since the register was drawn up meant that only those items still open could now be attacked in court. The tax office had based its case on an "order value" which in the event proved to be a non-existent asset. Since this was the only item still in dispute, the tax office no longer had a case.

Supreme Tax Court judgment IV R 47/09 of November 29, 2012, published on January 23, 2013

## Schlagwörter

tonnage tax