

HOW THE SECTION 883 EXEMPTION WORKS

Under IRC section 883, the United States grants a blanket exemption from all income taxes for international ship-owners and operators, including incidental land-based activities conducted as part of international shipping activity, if a majority of the ultimate owners of the business are “resident” in countries that grant a reciprocal exemption from income tax for U.S. companies engaged in international shipping. The blanket exemption (statutory exemption) exempts foreign companies from tax on income effectively connected with a U.S. trade or business, directly or through an agent, as well as the branch profits tax. The statutory exemption applies to both the freight tax and the normal U.S. corporate income tax regime. To claim this exemption, two tests must be met:

- The vessel-owning/-operating company must be incorporated in a qualifying jurisdiction; and
- Its ownership must be traced and documented through all intermediate structures to qualified persons appropriately resident in qualifying countries.

The “if you don’t tax us, we won’t tax you” policy underlying this exclusion is meant to encourage free trade. Unfortunately, compliance and interpretative restrictions still act as impediments to this goal. □