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Tax Incentive Can Save Exporters Cash

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GUEST COLUMNIST

Many CPAs and owners of businesses that export are missing the boat on one of the most powerful tax incentives available for exporters. The IC-DISC, a little known and underutilized tax incentive, holds the key to providing owners significant tax savings on the profits from export sales.

Exporters have only one alternate tax savings incentive at their disposal: the Interest Charge-Domestic International Sales Corporation, also known as IC-DISC. With the current 15 percent tax rate on corporate dividends, companies that export property or provide services outside the United States should seriously consider the tax savings and advantages the IC-DISC can provide.

What's The Benefit?

To determine if you can benefit from an IC-DISC structure, you must be able to answer yes to the following questions:

1. Does your company sell or lease export property or provide services that are related in or are subsidiary to any exchange of property outside the United States?
2. Is your company profitable for tax purposes?
3. Is your company closely held?

If your answer is "yes" to each of the questions, then your federal income tax on a portion of your export profits can be reduced significantly. To take advantage, a "paper" corporation needs to be set up.

First, let's explain what constitutes export property. Although exporters often think export property must be new, the export property can be used equipment, scrap metal or produce.

The key is that the property must be grown, produced or extracted in the United States by an entity other than the IC-DISC. In most circumstances, the manufacturing (or operating company) owners will establish the IC-DISC for their benefit. The export property must be held for sale, lease or rental in the ordinary course of business for direct use or consumption outside the United States. Property can also satisfy this destination test if it is sold to a customer in the United States provided the property does not undergo further manufacturing prior to export and is shipped to its foreign destination within one year.

The IC-DISC Benefit

The IRS allows exporters a commission deduction (deductible against 35 percent income) payable to the IC-DISC. The owners of the IC-DISC will report this income as dividends (taxed at 15 percent) when the money is distributed.

The structure allows owners the opportunity to convert regular income taxed at 35 percent into dividend income taxed at 15 percent. There are special provisions which allow for a one year deferral of income to individual IC-DISC shareholders on income attributable to $10 million or less of export receipts.

The commission income of the IC-DISC is calculated using one of the two following methods, whichever is greater: 4 percent of qualified export receipts or 50 percent of combined taxable income from export sales.

In summary, the IC-DISC structure is the only remaining tax incentive available for exporters. Yet, it is underutilized, which means those businesses that could take advantage of these benefits are paying more tax than is necessary.

As tax season approaches and new business years begin it makes good business sense to review all your costs including minimizing your tax burden. ■

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