Manufacturing

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HOLBROOK & MANTER, CPAs
PROFESSIONAL SERVICES FIRM

IC-DISCs create tax incentives for exporters

Emerging technologies and markets make worldwide trade more accessible and attractive than ever. What's often overlooked is a tax incentive for companies to think globally: the Interest Charge-Domestic International Sales Corporation ("IC-DISC"). IC-DISCs were designed to provide a valuable tax break for exporters of US sourced goods and services.

Currently, IC-DISCs can provide up to a 20 percent tax advantage on qualifying export income. And, IC-DISCs are not difficult to set up and maintain. If you export U.S.-made products, you should give an IC-DISC serious consideration.

IC-DISCs are essentially a "special purpose corporation" whose principal purpose avails exporters a statutorily mandated tax incentive by (1) not taxing the IC-DISC (2) allowing the related exporter to deduct its IC-DISC payments and (3) taxing IC-DISC owners at a 15% rate on distributions.

The tax savings/incentive can equal 20% if the exporter pays federal income taxes at the 35% and its deductible payments to the IC-DISC are distributed to its owners who are taxed at a 15%. Obviously if tax changes affect the relationship between corporate rates and individual dividend rates this incentive may reduce or disappear.

IC-DISC Requirements

An IC-DISC is not required to (a) perform services, (b) hire employees or (c) have any tangible assets. But IC-DISCs must maintain their own financial and accounting records, and must file a federal tax return.

The export company can be a C Corporation, S Corporation, LLC or partnership, and the IC-DISC shareholders can be individuals, corporations, trusts or a combination. But IC-DISCs can only be C Corporations.

At least 95 percent of the IC-DISC's income and assets must be related to export activity, and the exported product must be comprised of at least 50 percent U.S. content. There is an exception for architects and engineers who work on projects that will be constructed outside the U.S.
The other IC-DISC requirements include:

- It must be approved by the Internal Revenue Service. The paperwork must be filed within 90 days of the start of the tax year.

- It must be incorporated in one of the 50 states or the District of Columbia, which means the IC-DISC, might have to pay state income tax on the commissions it receives from the export company.
- It must have only one class of stock with a par value of at least $2,500.

Operating as an IC-DISC

Once the IC-DISC has been created and IRS approved, the export company can begin to see financial benefits, but not before.
The export company pays a commission to the IC-DISC equal to no more than the greatest of: (i) 4 percent of the gross receipts from all qualified export sales, (ii) 50 percent of net income from all qualified export sales or (iii) a commission acceptable under traditional related party pricing rules.

Other considerations

It is worth noting that the shareholders of the IC-DISC do not need to match the shareholders of the parent company. In certain estate-planning circumstances, it can be helpful to structure ownership of the IC-DISC different from the parent company.

IC-DISC shareholders are able to defer tax on commissions by paying a small interest charge at the T-bill rate, which recently has been less than 1 percent.

As with any tax incentive, there are complex regulations that you must always be aware of. But at its core, IC-DISC is a valuable boost for American companies that wish to compete on a global stage.

To learn more about IC-DISC and how it could be applied to your business, contact Stephen C. Smith or your Holbrook & Manter representative. We have facilitated tax savings for a number of growth-minded clients.