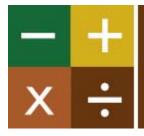


# MERCHANT MARINE CAPITAL CONSTRUCTION FUND

- Tax Benefits
- Deposit Limits
- Withdrawals Qualified vs. Nonqualified
- Accounting for CCF Funds
- R&D Credits
- Case Study



#### Tax Benefits of CCF Contributions

- Amounts deposited into the CCF are deductible from taxable income
- Investment earnings on deposits are generally excluded from income
- Deposits and investment earnings on deposits generate tax deferrals and accumulation of funds for up to 25 years per CCF program agreement
- For C Corporations only, CCF deposits and investment earnings are still subject to Alternative Minimum Tax (AMT), which is a parallel, federal tax structure designed to ensure that taxpayers with substantial income do not avoid tax liability through the excessive use of exclusions, deductions and **CREDITS**. AMT, which is calculated as 20% of AMTI for corporations, may be a factor when determining the amount of the CCF contribution for some businesses.
  - The amount of the AMT would become a Minimum Tax Credit (MTC) Carryover for use in future years. MTC would offset regular tax when the nonqualified distribution occurs.

#### **CCF Contribution Limits**

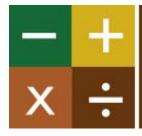


- Contributions may not exceed the following:
  - Taxable income from the operation of the agreement vessels
  - Depreciation on the agreement vessels allowable as a deduction
  - Net proceeds from the sale or disposition of an agreement vessel
  - Receipts from the investment or reinvestment of the fund assets



## Withdrawals – Qualified vs. Nonqualified

- Qualified withdrawals do not generate taxable income
  - "Qualified withdrawals" are withdrawals made from the CCF for the acquisition, construction or repair of a qualified vessel
- Nonqualified withdrawals generate taxable income, which are taxed at the highest marginal tax rate plus interest on the tax calculated from the date of the original deposit to the date withdrawn
  - "Nonqualified withdrawals" are withdrawals from the CCF that is not for a qualified purpose. Deemed nonqualified withdrawals are required for deposits that remain 25 years after initially deposited



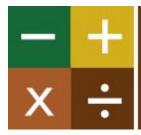
#### Accounting for CCF

- An annual audit of the fund is required though the scope and cost are not nearly as much as full financial statement audit for the business itself.
- The fund must maintain three accounts:
  - Capital account consists of amounts attributed to the depreciation allowable on agreement vessels, proceeds from the sale, disposition, insurance or indemnity of agreement vessels other than gain excluded by reason of insurance or indemnity proceeds being deposited in the fund and tax-exempt interest.
  - Capital gain account consists of gains on capital assets held more than six months for which the taxpayer receives insurance or indemnity proceeds and earnings on those proceeds, reduced by losses on fund capital assets held for more than six months.
  - Ordinary income account consists of income from operating agreement vessels, insurance or indemnity capital gains on assets held six months or less, reduced by capital losses on assets held six months or less, taxable interest and other ordinary income, ordinary income realized on insurance or indemnity proceeds or earnings thereon, and excluded dividends otherwise eligible for the dividends-received deduction that are not included in the capital account.

#### **R&D** Credits



- Many businesses, who qualify for inclusion in the CCF Program, may also qualify for a Research and Development Tax Credit (R&D)
- R&D Tax Credits are government sponsored benefits that provides income tax credits for companies conducting R&D in the U.S. Any company that designs, develops, or improves products, processes, techniques, etc. may be eligible.
- The R&D Credit is not a deduction but a credit against taxes owed/paid.
- The amount of the R&D Credit is 20% of qualified expenses.
- Similar to CCF Contribution, R&D Credits do not reduce AMT but unused R&D Credits do carryforward.
- It is important to consider the interaction of R&D Credits and CCF Contributions in a given year in order to assure the most benefit based on Contribution amounts.
- R&D Credit Studies generally cost approximately 35% of the credit calculated.



#### Case Study - Assumptions

- Business is a "C" Corporation for Case Study I & II. Case Study III is an S Corporation
- Taxable income before Investment Income & Income Tax Expense = \$3,250,000
- For simplicity, all income earned, CCF contributions and taxes occur on January 1<sup>st</sup> of each year
- Business is located in AL
- Maximum Tax Rate Federal = 34%, AL = 6.5%
- CCF Contribution per Year = \$2,500,000
- Rate of Return on all Invested dollars = 8%
- Business qualifies for R&D Credit with \$1,000,000 in eligible expenses (Case Study II Only)

#### Case Study I



Ye	ear	Ta	exable Income CCF Contribution		Investment with Income Tax Expense	Ca	t CCF Contribu ash Available r Investment		n Investment Income				Total Investment alance, net of tax	
	1	\$	5,000,000	\$	-	\$ (1,844,770)	\$	3,155,230	\$	252,418	\$	(93,131)	\$	3,314,518
	2	\$	5,000,000	\$	-	\$ (1,844,770)	\$	3,155,230	\$	517,580	\$	(190,963)	\$	6,796,364
:	3	\$	5,000,000	\$	-	\$ (1,844,770)	\$	3,155,230	\$	796,128	\$	(293,734)	\$	10,453,987
	4	\$	5,000,000	\$	-	\$ (1,844,770)	\$	3,155,230	\$	1,088,737	\$	(401,694)	\$	14,296,261
!	5	\$	5,000,000	\$	-	\$ (1,844,770)	\$	3,155,230	\$	1,396,119	\$	(515,104)	\$	18,332,506
									To	tal Tax	\$ 1	10,718,476		

Ye	ear	Taxable Income	CCF Contribution	Investment w Income Tax Expense	ith CCF Contribut Non-CCF Cash Available for Investment	In	Non-CCF vestment Income	x on Non-CCF Investment Income	Non-CCF Investment alance, net of tax	F Investment Income	ax on CCF nvestment Income	CCF Investment Balance	Total Investment Balance, net of tax		nimum Tax redit C/O
:	1	\$ 5,000,000	\$ 2,500,000	\$ (1,109,027)	\$ 1,383,080	\$	110,646	\$ (49,084)	\$ 1,444,642	\$ 200,000	\$ (7,893)	\$ 2,700,000	\$ 4,144,642	\$	188,385
:	2	\$ 5,000,000	\$ 2,500,000	\$ (1,109,027)	\$ 1,374,556	\$	225,536	\$ (100,050)	\$ 2,944,684	\$ 416,000	\$ (16,417)	\$ 5,616,000	\$ 8,560,684	\$	392,505
:	3	\$ 5,000,000	\$ 2,500,000	\$ (1,109,027)	\$ 1,365,349	\$	344,803	\$ (152,958)	\$ 4,501,877	\$ 649,280	\$ (25,624)	\$ 8,765,280	\$ 13,267,157	\$	612,955
	4	\$ 5,000,000	\$ 2,500,000	\$ (1,109,027)	\$ 1,355,406	\$	468,583	\$ (207,868)	\$ 6,117,998	\$ 901,222	\$ (35,567)	\$ 12,166,502	\$ 18,284,500	\$	851,040
!	5	\$ 5,000,000	\$ 2,500,000	\$ (1,109,027)	\$ 1,344,668	\$	597,013	\$ (264,842)	\$ 7,794,838	\$ 1,173,320	\$ (46,305)	\$ 15,839,823	\$ 23,634,660	\$ 1	,108,173
							l Tax Deferral	6,327,830 4,390,646							

#### Case Study II



Year	Taxable Income	CCF Contribution	Income Tax Expense	Non-CCF Cash Available for Investment		Ta In	vith CCF Col ex on Non- CCF evestment Income	Inv	ution with lon-CCF vestment nce, net of tax	Ir	Credit CCF ovestment Income	In	ax on CCF evestment Income	CCF Investment Balance	Total Investment Balance, net of tax	Minimum Tax Credit C/O	&D Credit Carryover
1	\$ 5,000,000	\$ 2,500,000	\$ (1,127,973)	\$ 1,364,134	\$ 109,131	\$	(49,239)	\$ 1	1,424,026	\$	200,000	\$	(7,893)	\$ 2,700,000	\$ 4,124,026	\$ 421,369	\$ 100,000
2	\$ 5,000,000	\$ 2,500,000	\$ (1,127,973)	\$ 1,355,610	\$ 222,371	\$	(100,331)	\$ 2	2,901,675	\$	416,000	\$	(16,417)	\$ 5,616,000	\$ 8,517,675	\$ 842,738	\$ 200,000
3	\$ 5,000,000	\$ 2,500,000	\$ (1,127,973)	\$ 1,346,403	\$ 339,846	\$	(153,335)	\$ 4	4,434,590	\$	649,280	\$	(25,624)	\$ 8,765,280	\$ 13,199,870	\$ 1,264,107	\$ 300,000
4	\$ 5,000,000	\$ 2,500,000	\$ (1,127,973)	\$ 1,336,460	\$ 461,684	\$	(208,307)	\$ 6	6,024,427	\$	901,222	\$	(35,567)	\$ 12,166,502	\$ 18,190,929	\$ 1,685,476	\$ 400,000
5	\$ 5,000,000	\$ 2,500,000	\$ (1,127,973)	\$ 1,325,722	\$ 588,012	\$	(265,305)	\$ 7	7,672,856	\$	1,173,320	\$	(46,305)	\$ 15,839,823	\$ 23,512,679	\$ 2,106,845	\$ 500,000
					Total Tax	\$	6,424,274										

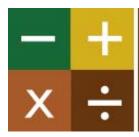
	Investment with CCF Contribution with R&D Credit - electing the reduced Credit																
Year	Taxable Income	CCF Contribution	Income Tax Expense	Non-CCF Cash Available for Investment	Non-CCF Investmer Income	t	Tax on Non- CCF Investment Income		Non-CCF investment ilance, net of tax		CCF nvestment Income		ax on CCF nvestment Income	CCF Investment Balance	Total Investment Balance, net of tax	Minimum Tax Credit C/O	&D Credit arryover
1	\$ 5,000,000	\$ 2,500,000	\$ (1,103,758)	\$ 1,388,349	\$ 111,0	58 \$	(49,037)	\$	1,450,380	\$	200,000	\$	(7,893)	\$ 2,700,000	\$ 4,150,380	\$ 435,000	\$ 65,000
2	\$ 5,000,000	\$ 2,500,000	\$ (1,103,758)	\$ 1,379,825	\$ 226,4	16 \$	(99,964)	\$	2,956,657	\$	416,000	\$	(16,417)	\$ 5,616,000	\$ 8,572,657	\$ 870,000	\$ 130,000
3	\$ 5,000,000	\$ 2,500,000	\$ (1,103,758)	\$ 1,370,618	\$ 346,1	32 \$	(152,840)	\$	4,520,617	\$	649,280	\$	(25,624)	\$ 8,765,280	\$ 13,285,897	\$ 1,305,000	\$ 195,000
4	\$ 5,000,000	\$ 2,500,000	\$ (1,103,758)	\$ 1,360,675	\$ 470,50	)3 \$	(207,729)	\$	6,144,067	\$	901,222	\$	(35,567)	\$ 12,166,502	\$ 18,310,569	\$ 1,740,000	\$ 260,000
5	\$ 5,000,000	\$ 2,500,000	\$ (1,103,758)	\$ 1,349,937	\$ 599,5	20 \$	(264,690)	\$	7,828,834	\$	1,173,320	\$	(46,305)	\$ 15,839,823	\$ 23,668,657	\$ 2,175,000	\$ 325,000
					Total Tax Tax Deferra		6,300,943 123,332										

### Case Study III - Passthrough (



Year	Taxable Income	CCF Contribution	Investment wi Income Tax Expense	th CCF Contribu Non-CCF Cash Available for Investment		Tax on Non- CCF Investment Income	Investment	CCF Investment Income	Tax on CCF Investment Income	CCF Investment Balance	Total Investment Balance, net of tax	Minimum Tax Credit C/O
1	\$ 5,000,000	\$ 2,500,000	\$ (922,385)	\$ 1,577,615	\$ 126,209	\$ (46,565	) \$ 1,657,259	\$ 200,000	\$ -	\$ 2,700,000	\$ 4,357,259	\$ -
2	\$ 5,000,000	\$ 2,500,000	\$ (922,385)	\$ 1,577,615	\$ 258,790	\$ (95,482	) \$ 3,398,182	\$ 416,000	\$ -	\$ 5,616,000	\$ 9,014,182	\$ -
3	\$ 5,000,000	\$ 2,500,000	\$ (922,385)	\$ 1,577,615	\$ 398,064	\$ (146,867	) \$ 5,226,994	\$ 649,280	\$ -	\$ 8,765,280	\$ 13,992,274	\$ -
4	\$ 5,000,000	\$ 2,500,000	\$ (922,385)	\$ 1,577,615	\$ 544,369	\$ (200,847	) \$ 7,148,130	\$ 901,222	\$ -	\$ 12,166,502	\$ 19,314,633	\$ -
5	\$ 5,000,000	\$ 2,500,000	\$ (922,385)	\$ 1,577,615	\$ 698,060	\$ (257,552	) \$ 9,166,253	\$ 1,173,320	\$ -	\$ 15,839,823	\$ 25,006,076	\$ -
					Total Tax	\$ 5,359,238	•					

Year	Taxable Income	CCF Contribution	Income Expen	nse /	Ion-CCF Cash Available for Investment	Inv	Investmon-CCF estment ncome	Ta	with CCF Co ax on Non- CCF nvestment Income	In	bution with Non-CCF westment ance, net of tax	In	D Credit CCF ovestment Income	In	ax on CCF vestment Income	Inv	CCF estment alance	Total Investment Balance, net of tax	Minimum Tax Credit C/O	R&D Cred Carryove	
1	\$ 5,000,000	\$ 2,500,000	\$ (859	9,280) \$	1,640,720	\$	131,258	\$	(45,115)	\$	1,726,863	\$	200,000	\$	-	\$ 2	,700,000	\$ 4,426,863	\$ -	\$ •	-
2	\$ 5,000,000	\$ 2,500,000	\$ (859	9,280) \$	1,640,720	\$	269,407	\$	(92,598)	\$	3,544,391	\$	416,000	\$	-	\$ 5	,616,000	\$ 9,160,391	\$ -	\$ ;	-
3	\$ 5,000,000	\$ 2,500,000	\$ (859	9,280) \$	1,640,720	\$	414,809	\$	(142,575)	\$	5,457,345	\$	649,280	\$	-	\$ 8	,765,280	\$ 14,222,625	\$ -	\$ ;	-
4	\$ 5,000,000	\$ 2,500,000	\$ (859	9,280) \$	1,640,720	\$	567,845	\$	(195,175)	\$	7,470,735	\$	901,222	\$	-	\$ 12	2,166,502	\$ 19,637,238	\$ -	\$ ;	-
5	\$ 5,000,000	\$ 2,500,000	\$ (859	9,280) \$	1,640,720	\$	728,916	\$	(250,537)	\$	9,589,834	\$	1,173,320	\$	-	\$ 15	5,839,823	\$ 25,429,657	\$ -	\$ ;	-
						Total	Тах	\$	5,022,400												



#### Case Study - Summary

Description	Type of Corp	Total Tax	Total Net Investment	MTC C/O	R&D Credit Carryover
Investment without CCF Contribution & No R&D Credit	С	\$ 10,718,476	\$ 18,332,506	\$ -	\$ -
Investment with CCF Contribution & No R&D Credit	С	\$ 6,327,830	\$ 23,634,660	\$ 1,108,173	\$ -
Investment with CCF Contribution & with R&D Credit	С	\$ 6,424,274	\$ 23,512,679	\$ 2,106,845	\$ 500,000
Investment with CCF Contribution & with R&D Credit (reduced)	С	\$ 6,300,943	\$ 23,668,657	\$ 2,175,000	\$ 325,000
Investment with CCF Contribution & No R&D Credit	S	\$ 5,359,238	\$ 25,006,076	\$ -	\$ -
Investment with CCF Contribution & with R&D Credit	S	\$ 5,022,400	\$ 25,429,657	\$ -	\$ -