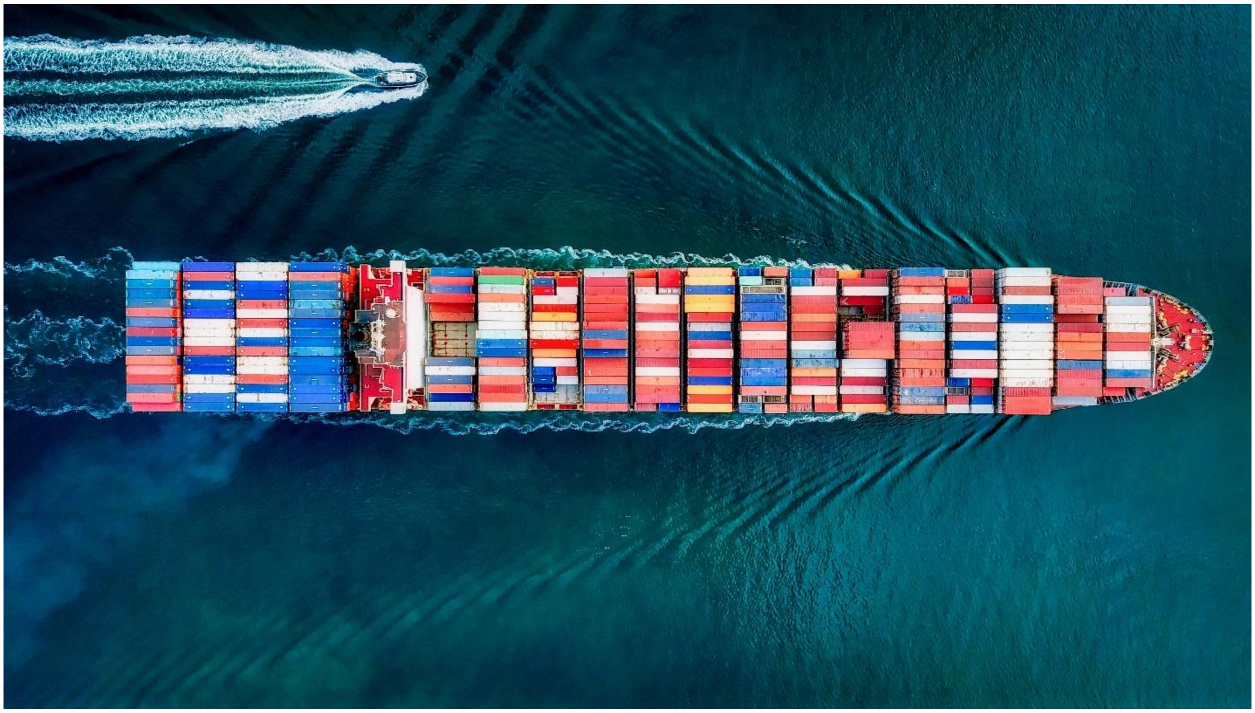
THE INTERNATIONAL
PROPELLER CLUB
of the United States

An international business network dedicated
to the promotion of the maritime industry,
commerce and global trade.

Governmental financial support for vessel operations



Governments around the world enact policies to promote the registration of vessels in their country.

The U.S. Department of Defense depends upon the U.S.-flag merchant marine to provide strategic sealift capabilities in support of DoD operations. During Operations Enduring Freedom and Iraqi Freedom, U.S.-flag commercial vessels transported 63% of all military cargoes that were transported to Iraq and Afghanistan.

The country in which a vessel is registered is known as the "flag-state" of the vessel. When an owner is making the decision regarding which country to flag a vessel there are 3 cost factors that they typically consider:

- Capital cost (the cost to build the ship)
- Tax costs (typically the corporate taxes that will be paid on the earnings derived from the vessel).
- Operating costs (the cost to employ personnel, insurance, etc.)

The international shipping market is generally a free market with little or no economic regulation. Therefore, vessel owners attempt to have the lowest cost in order to offer the most competitive rates. European countries and the United States have higher a higher cost of living than in many countries. Corporations based in these countries normally pay a higher tax rate than in underdeveloped countries. Mariners from developed countries are usually paid more than mariners from other countries due to the higher cost of living in their home country.

To make the financial decision to flag a ship in their country more attractive, many European countries and the United States offer financial incentives to decrease the cost differential between the cost of registering a ship in their country and the cost of registering the vessel in a so called “flag of convenience” country. The European Union has established financial limits on these promotional policies so that they will not disrupt the marketplace. This column will explain these maritime policies as they affect each of the 3 cost areas identified above.

Capital cost:

In general, vessel owners are free to purchase a ship built in any country they choose for the international trade. Therefore, they usually pick the country with the lowest price ship.

European Union: No restrictions on purchasing foreign-built ships for the international trade.

United States: The U.S. has allowed vessel owners to purchase foreign-built ships for the international trade since 1912. However, in 1936, Congress enacted the Construction Differential Subsidy (CDS) program to compensate vessel owners for the higher cost of building a ship in the United States if they chose to build one here. The CDS program was eliminated by President Ronald Reagan in 1981. Since that time, virtually all U.S.-flag vessels built for the foreign trade have been built in foreign shipyards.

Tax cost:

Most underdeveloped countries have a very low – or non-existent corporate tax rate for vessels registered in their country. To help make registering vessels in developed countries more financially attractive, some countries have enacted so called “tonnage taxes” as a way of decreasing the tax liability for owners of vessels registered in their country.

The mechanism for a tonnage tax is relatively simple: There is a formula that states that the income that is subject to taxation is based upon the tonnage of the vessel – not based on the revenues and profit made from the vessel operations. For example, the owner of a container ship that is 55,000 net tons may have a computed taxable income from that ship of $25,000 to which the corporate tax rate for that country is then applied.

European Union: The EU has allowed member countries countries to enact "tonnage tax" systems. The EU does review these tax rates and has approved them for countries such as Greece, …. (See this link for additional information regarding EU approved tonnage taxes.

United States: In 2004 the United States Congress enacted a "tonnage tax" system for U.S.-flag vessels engaged in international trade. The tonnage rates were modeled after the tonnage tax system used in Great Britain.

Operating costs:

Europe: In Europe, some countries, such as Great Britain and Norway do not require all of the ships personnel to be citizens of their country. In addition, some countries do not tax the income of mariners engaged on international voyages. Therefore, the owners can have a lower pay-scale that reflects that tax-break. European shipowners flag less than 60% of their tonnage in European countries. In January 2020, the European Commission approved 5 programs to support maritime shipping in Cyprus, Denmark, Estonia, Poland, and Sweden. These programs were comprise of tonnage tax programs and tax reductions for seafarers.

United States: There are approximately 80 U.S.-flag vessels engaged in international commerce.

In 1995 Congress enacted the Maritime Security Program (MSP) to pay U.S.-flag vessel owners for making their ships available to transport military supplies and personnel when needed. Most of the 60 ships in this program are containerships and Roll On/Roll Off ships. Congress recently reauthorized this program for a 10-year period. Vessel owners are currently paid $5 million per ship annually and this will increase to $5.3 million per ship per year in 2022. The $300 million that is appropriated for this program helps to pay for the increased operating costs of U.S.-flag vessels compared to their foreign-flag competition.

In addition, the United States cargo-preference program requires a percentage of cargoes bought with Federal funds to be transported on U.S.-flag ships. For military cargoes the requirement is 100% of the cargoes and for non-military cargoes the requirement is 50% of the cargoes must be transported on U.S.-flag vessels.

Regarding the taxation of U.S. mariners income, the United States does not exempt any of the income of mariners from U.S. taxation. In contrast, most other U.S.-citizens that work overseas do not have to pay U.S. income tax on their first $107,000 of income.

The IPCUS supports governmental measures designed to promote transportation of goods and passengers on ships registered in countries in which the vessels are owned.

For further information see:

[EC approval of maritime support schemes]

[Maritime Security Program]