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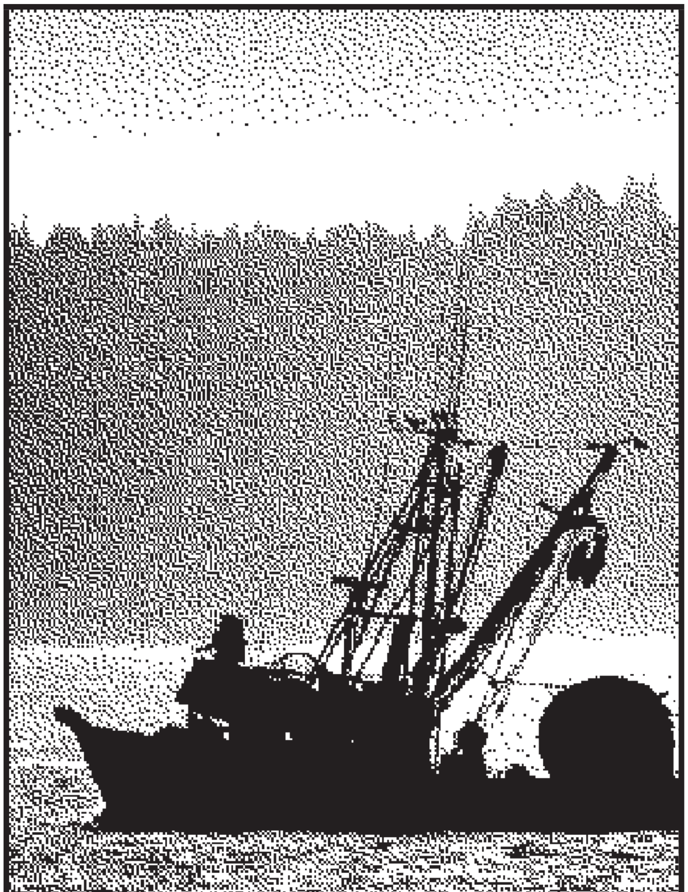
Capital Construction Fund for Commercial Fishermen



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Introduction

This publication discusses the Capital Construction Fund (CCF). The CCF is a special investment program administered by the National Marine Fisheries Service (NMFS) and the Internal Revenue Service (IRS). This program allows fishermen to defer paying income tax on certain income they invest in a CCF account and later use to acquire, build, or rebuild fishing vessels.

This publication does not discuss all the tax rules that may apply to your fishing trade or business. For general information about the federal tax laws that apply to individuals, including commercial fishermen, who file Schedule C or C-EZ, see Publication 334, Tax Guide for Small Business. If your trade or business is a partnership or corporation, see Publication 541, Partnerships, or Publication 542, Corporations.

Comments and suggestions. We welcome your comments about this publication and your suggestions for future editions.

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Capital Construction Fund

The following sections discuss CCF accounts and the types of bookkeeping accounts you must maintain when you invest in a CCF account. They also discuss the income tax treatment of CCF deposits, earnings, and withdrawals.

CCF Accounts

This section explains who can open a CCF account and how to use the account to defer income tax.

Opening a CCF account. If you are a U.S. citizen and you own or lease one or more eligible vessels (defined later), you can open a CCF account. However, before you open your CCF account, you must enter into an agreement with the Secretary of Commerce through the NMFS. This agreement will establish the following.

- Agreement vessels. Eligible vessels named in the agreement that will be the basis for the deferral of income tax.
- Planned use of withdrawals. Use of CCF funds to acquire, build, or rebuild a vessel.
- CCF depository. Where your CCF funds will be held.

You can request an application kit or get additional information from NMFS at the following address.

NOAA/NMFS, Financial Services Division, F/MB5
Capital Construction Fund Program
1315 East-West Highway
Silver Spring, MD 20910-3282

You can obtain information on the Capital Construction Fund Program at the following website: *www.nmfs.noaa.gov/mb/financial_services/ccf.htm*.

You can call NMFS to request an application kit or get additional information at (301) 713-2393 (ext. 204). Their fax number is (301) 713-1939.

Eligible vessels. There are two types of vessels that may be considered eligible, those weighing 5 tons or more and those weighing less than 5 tons. For each type, certain requirements must be met.

Vessel weighing 5 tons or more. To be considered eligible, the vessel must meet all the following requirements.

- Be built or rebuilt in the United States.
- Be documented under the laws of the United States.
- Be used commercially in the fisheries of the United States.
- Be operated in the foreign or domestic commerce of the United States.

Vessel weighing less than 5 tons. A small vessel, weighing at least 2 net tons but less than 5 net tons, must meet all the following requirements to be considered eligible.

- Be built or rebuilt in the United States.
- Be owned by a U.S. citizen.
- Have a home port in the United States.
- Be used commercially in the fisheries of the United States.

Deferring tax on CCF deposits and earnings. You can use a CCF account to defer income tax by taking the following actions.

- Making deposits to your CCF account from taxable income.
- Excluding from income deposits assigned to certain accounts (discussed later).
- Making withdrawals from your CCF account when you acquire, build, or rebuild fishing vessels.
- Reducing the basis of fishing vessels you acquire, build, or rebuild to recapture amounts previously excluded from tax.

TIP

Reporting requirements. *Beginning with the tax year in which you establish your agreement, you must report annual deposit and withdrawal activity to the NMFS on NOAA Form 34-82. This form is due within 30 days after you file your federal income tax return even if no deposits or withdrawals are made. For more information, contact the NMFS at the address or phone number given earlier.*

Types of Accounts You Must Maintain Within a CCF

This section discusses the three types of bookkeeping accounts you must maintain when you invest in a CCF account. Your total CCF deposits and earnings for any given year are limited to the amount attributed to these three accounts for that year.

Capital account. The capital account consists primarily of amounts attributable to the following items.

1. Allowable depreciation deductions for agreement vessels.

2. Any nontaxable return of capital from either (a) or (b), below.

   a. The sale or other disposition of agreement vessels.

   b. Insurance or indemnity proceeds attributable to agreement vessels.

3. Any tax-exempt interest earned on state or local bonds in your CCF account.

Capital gain account. The capital gain account consists of amounts attributable to the following items reduced by any capital losses from assets held in your CCF account for more than 6 months.

1. Any capital gain from either of the following sources.

   a. The sale or other disposition of agreement vessels held for more than 6 months.

   b. Insurance or indemnity proceeds attributable to agreement vessels held for more than 6 months.

2. Any capital gain from assets held in your CCF account for more than 6 months.

Ordinary income account. The ordinary income account consists of amounts attributable to the following items.

1. Any earnings (without regard to the carryback of any net operating or net capital loss) from the operation of agreement vessels in the fisheries of the United States or in the foreign or domestic commerce of the United States.

2. Any capital gain from the following sources reduced by any capital losses from assets held in your CCF account for 6 months or less.

   a. The sale or other disposition of agreement vessels held for 6 months or less.

   b. Insurance or indemnity proceeds attributable to agreement vessels held for 6 months or less.

   c. Any capital gain from assets held in your CCF account for 6 months or less.

3. Any ordinary income (such as depreciation recapture) from either of the following sources.

   a. The sale or other disposition of agreement vessels.

   b. Insurance or indemnity proceeds attributable to agreement vessels.

4. Any interest (not including tax-exempt interest from state and local bonds), most dividends, and other ordinary income earned on the assets in your CCF account.

Tax Treatment of CCF Deposits

This section explains the tax treatment of income used as the basis for CCF deposits.

Capital gains. Do not report any transaction that produces a capital gain if you deposit the net proceeds into your CCF account. This treatment applies to either of the following transactions.

- The sale or other disposition of an agreement vessel.
- The receipt of insurance or indemnity proceeds attributable to an agreement vessel.

Depreciation recapture. Do not report any transaction that produces depreciation recapture if you deposit the net proceeds into your CCF account. This treatment applies to either of the following transactions.

- The sale or other disposition of an agreement vessel.
- The receipt of insurance or indemnity proceeds attributable to an agreement vessel.

Earnings from operations. Report earnings from the operation of agreement vessels on your Schedule C or C-EZ (Form 1040) even if you deposit part of these earnings into your CCF account. You subtract any part of the earnings you deposited into your CCF account from the amount you would otherwise enter as taxable income on Form 1040, line 43 (for 2005). Next to line 43, write “CCF” and the amount of the deposits. Do not deduct these CCF deposits on Schedule C or C-EZ (Form 1040).

CAUTION *If you deposit earnings from operations into your CCF account and you must complete other forms such as Form 6251,* Alternative Minimum Tax (Individuals), *or a worksheet for Schedule D (Form 1040), you will need to make an extra computation. When the other form instructs you to use the amount from Form 1040, line 41 (for 2005), do not use that amount. Instead, add Form 1040, lines 42 and 43 (for 2005), and use that amount.*

Self-employment tax. You must use your net profit or loss from your fishing business to figure your self-employment tax. Do **not** reduce your net profit or loss by any earnings from operations you deposit into your CCF account.

TIP ***Partnerships and S corporations.*** *The deduction for partnership earnings from operations deposited into a CCF account is separately stated on Schedule K (Form 1065), line 13d, and allocated to the partners on Schedule K-1 (Form 1065), box 13 (for 2005). The deduction for S corporation earnings deposited into a CCF account is separately stated on Schedule K (Form 1120S), line 12d, and allocated to the shareholders on Schedule K-1 (Form 1120S), box 12 (for 2005).*

Tax Treatment of CCF Earnings

This section explains the tax treatment of the earnings from the assets in your CCF account when the earnings are redeposited or left in your account. However, if you choose to withdraw the earnings in the year earned, you must generally pay income tax on them.

Capital gains. Do not report any capital gains from the sale of capital assets held in your CCF account. This includes capital gain distributions reported to you on Form 1099-DIV or a substitute statement. However, you should attach a statement to your tax return to list the payers and the amounts and to identify the capital gains as “CCF account earnings.”

Interest and dividends. Do not report any ordinary income (such as interest and dividends) you earn on the assets in your CCF account. However, you should attach a statement to your return to list the payers and the amounts and to identify them as “CCF account earnings.”

If you are required to file Schedule B (Form 1040), you can add these earnings to the list of payers and amounts on line 1 or line 5 and identify them as “CCF earnings.” Then, subtract the same amounts from the list and identify them as “CCF deposits.”

Tax-exempt interest. Do not report tax-exempt interest from state or local bonds you held in your CCF account. You are not required to report this interest on Form 1040, line 8b.

Tax Treatment of CCF Withdrawals

This section discusses the tax treatment of amounts you withdraw from your CCF account during the year.

Qualified Withdrawals

A qualified withdrawal from a CCF account is one that is approved by NMFS for either of the following uses.

- Acquiring, building, or rebuilding qualified vessels (defined next).
- Making principal payments on the mortgage of a qualified vessel.
- NMFS will not approve amounts withdrawn to purchase nets not continuously attached to the vessel, such as seine nets, gill set-nets, and gill drift-nets.
- NMFS will approve amounts withdrawn to purchase trawl nets.

Qualified vessel. This is any vessel that meets all of the following requirements.

- The vessel was built or rebuilt in the United States.
- The vessel is documented under the laws of the United States.
- The person maintaining the CCF account agrees with the Secretary of Commerce that the vessel will be operated in United States foreign trade, Great Lakes trade, noncontiguous domestic trade, or the fisheries of the United States.

How to determine the source of qualified withdrawals. When you make a qualified withdrawal, the amount is treated as being withdrawn in the following order from the accounts listed below.

1. The capital account.
2. The capital gain account.
3. The ordinary income account.

Excluding qualified withdrawals from tax. Do not report on your income tax return any qualified withdrawals from your CCF account.

! CAUTION *Reduce the depreciable basis of fishing vessels you acquire, build, or rebuild when you make a qualified withdrawal from either the capital gain or the ordinary income account.*

Nonqualified Withdrawals

A nonqualified withdrawal from a CCF account is generally any withdrawal that is not a qualified withdrawal. Qualified withdrawals are defined under *Qualified Withdrawals,* earlier.

Examples. Examples of nonqualified withdrawals include the following amounts from either the ordinary income account or the capital gain account.

- Amounts remaining in a CCF account upon termination of your agreement with NMFS.
- Amounts you withdraw and use to make principal payments on the mortgage of a vessel if the basis of that vessel and the bases of other vessels you own have already been reduced to zero.

- Amounts determined by the IRS to cause your CCF account balance to exceed the amount appropriate to meet your planned use of withdrawals. You will generally be given 3 years to revise your plans to cover this excess balance.
- Amounts you leave in your account for more than 25 years. There is a graduated schedule under which the percentage applied to determine the amount of the nonqualified withdrawal increases from 20% in the 26th year to 100% in the 30th year.

How to determine the source of nonqualified withdrawals. When you make a nonqualified withdrawal from your CCF account, the amount is treated as being withdrawn in the following order from the accounts listed below.

1. The ordinary income account.
2. The capital gain account.
3. The capital account.

Paying tax on nonqualified withdrawals. In general, nonqualified withdrawals are taxed separately from your other gross income and at the highest marginal tax rate in effect for the year of withdrawal. However, nonqualified withdrawals treated as made from the capital gain account are taxed at a rate that cannot exceed 15% for individuals and 34% for corporations.

TIP

Partnerships and S corporations. *Taxable nonqualified partnership withdrawals are separately stated on Schedule K (Form 1065), line 20c, and allocated to the partners on Schedule K-1 (Form 1065), box 20 (for 2005). Taxable nonqualified withdrawals by an S corporation are separately stated on Schedule K (Form 1120S), line 17d, and allocated to the shareholders on Schedule K-1 (Form 1120S), box 17.*

Interest. You must pay interest on the additional tax due to nonqualified withdrawals that are treated as made from either the ordinary income or the capital gain account. The interest period begins on the last date for paying tax for the year for which you deposited the amount you withdrew from your CCF account. The period ends on the last date for paying tax for the year in which you make the nonqualified withdrawal. The interest rate on the nonqualified withdrawal is simple interest. The rate is subject to change annually and is published in the Federal Register.

You also can call NMFS at (301) 713-2393 (ext. 204) to get the current interest rate.

Interest deduction. You can deduct the interest you pay on a nonqualified withdrawal as a trade or business expense.

Reporting the additional tax and interest. Attach a statement to your income tax return showing your computation of the tax and the interest on a nonqualified withdrawal. Include the tax and interest on Form 1040, line 63 (for 2005). To the left of line 63, write in the amount of tax and interest and "CCF."

Tax benefit rule. If any portion of your nonqualified withdrawal is properly attributable to contributions (not earnings on the contributions) you made to the CCF account that did not reduce your tax liability for any tax year prior to the withdrawal year, the following tax treatment applies.

1. The part that did not reduce your tax liability for any year prior to the withdrawal year is not taxed.
2. That part is allowed as a net operating loss deduction.

More Information

This section briefly discussed the CCF program. For more detailed information, see the following legislative authorities.

- Section 607 of the Merchant Marine Act of 1936, as amended (46 U.S.C. 1177).
- Chapter 2, Part 259 of title 50 of the Code of Federal Regulations (50 C.F.R., Part 259).
- Subchapter A, Part 3 of title 26 of the Code of Federal Regulations (26 C.F.R., Part 3).
- Section 7518 of the Internal Revenue Code (IRC 7518).

The application kit you can obtain from NMFS at the address or phone number given earlier may contain copies of some of these sources of additional information. Also, see their web page at *www.nmfs.noaa.gov/mb/financial_services/ccf.htm*.

How To Get Tax Help

You can get help with unresolved tax issues, order free publications and forms, ask tax questions, and get information from the IRS in several ways. By selecting the method that is best for you, you will have quick and easy access to tax help.

Contacting your Taxpayer Advocate. If you have attempted to deal with an IRS problem unsuccessfully, you should contact your Taxpayer Advocate.

The Taxpayer Advocate independently represents your interests and concerns within the IRS by protecting your rights and resolving problems that have not been fixed through normal channels. While Taxpayer Advocates cannot change the tax law or make a technical tax decision, they can clear up problems that resulted from previous contacts and ensure that your case is given a complete and impartial review.

To contact your Taxpayer Advocate:

- Call the Taxpayer Advocate toll free at 1-877-777-4778,
- Call, write, or fax the Taxpayer Advocate office in your area,
- Call 1-800-829-4059 if you are a TTY/TDD user, or
- Visit *www.irs.gov/advocate*.

For more information, see Publication 1546, How To Get Help With Unresolved Tax Problems (now available in Chinese, Korean, Russian, and Vietnamese, in addition to English and Spanish).

Free tax services. To find out what services are available, get Publication 910, IRS Guide to Free Tax Services. It contains a list of free tax publications and an index of tax topics. It also describes other free tax information services, including tax education and assistance programs and a list of TeleTax topics.

Internet. You can access the IRS website 24 hours a day, 7 days a week, at *www.irs.gov* to:

- *E-file* your return. Find out about commercial tax preparation and *e-file* services available free to eligible taxpayers.
- Check the status of your refund. Click on *Where's My Refund.* Be sure to wait at least 6 weeks from the date you filed your return (3 weeks if you filed electronically). Have your tax return available because you will need to know your social security number, your filing status, and the exact whole dollar amount of your refund.
- Download forms, instructions, and publications.
- Order IRS products online.
- Research your tax questions online.
- Search publications online by topic or keyword.
- View Internal Revenue Bulletins (IRBs) published in the last few years.
- Figure your withholding allowances using our Form W-4 calculator.
- Sign up to receive local and national tax news by email.
- Get information on starting and operating a small business.

Phone. Many services are available by phone.

- *Ordering forms, instructions, and publications.* Call 1-800-829-3676 to order current-year forms, instructions, and publications and prior-year forms and instructions. You should receive your order within 10 days.
- *Asking tax questions.* Call the IRS with your tax questions at 1-800-829-1040.
- *Solving problems.* You can get face-to-face help solving tax problems every business day in IRS Taxpayer Assistance Centers. An employee can explain IRS letters, request adjustments to your account, or help you set up a payment plan. Call your local Taxpayer Assistance Center for an appointment. To find the number, go to *www.irs.gov/localcontacts* or look in the phone book under *United States Government, Internal Revenue Service.*
- *TTY/TDD equipment.* If you have access to TTY/TDD equipment, call 1-800-829-4059 to ask tax questions or to order forms and publications.
- *TeleTax topics.* Call 1-800-829-4477 and press 2 to listen to pre-recorded messages covering various tax topics.
- *Refund information.* If you would like to check the status of your refund, call 1-800-829-4477 and press 1 for automated refund information and follow the recorded instructions or call 1-800-829-1954. Be sure to wait at least 6 weeks from the date you filed your return (3 weeks if you filed electronically). Have your tax return available because you will need to know your social security number, your filing status, and the exact whole dollar amount of your refund.

Evaluating the quality of our telephone services. To ensure that IRS representatives give accurate, courteous, and professional answers, we use several methods to evaluate the quality of our telephone services. One method is for a second IRS representative to sometimes listen in on or record telephone calls. Another is to ask some callers to complete a short survey at the end of the call.

Walk-in. Many products and services are available on a walk-in basis.

- *Products.* You can walk in to many post offices, libraries, and IRS offices to pick up certain forms, instructions, and publications. Some IRS offices, libraries, grocery stores, copy centers, city and county government offices, credit unions, and office supply stores have a collection of products available to print from a CD-ROM or photocopy from reproducible proofs. Also, some IRS offices and libraries have the Internal Revenue Code, regulations, Internal Revenue Bulletins, and Cumulative Bulletins available for research purposes.

- *Services.* You can walk in to your local Taxpayer Assistance Center every business day for personal, face-to-face tax help. An employee can explain IRS letters, request adjustments to your account, or help you set up a payment plan. If you need to resolve a tax problem, have questions about how the tax law applies to your individual tax return, or you're more comfortable talking with someone in person, visit your local Taxpayer Assistance Center where you can spread out your records and talk with an IRS representative face-to-face. No appointment is necessary, but if you prefer, you can call your local Center and leave a message requesting an appointment to resolve a tax account issue. A representative will call you back within 2 business days to schedule an in-person appointment at your convenience. To find the number, go to *www.irs.gov/localcontacts* or look in the phone book under *United States Government, Internal Revenue Service.*

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- A CD that is released twice so you have the latest products. The first release ships in late December and the final release ships in late February.
- Current-year forms, instructions, and publications.
- Prior-year forms, instructions, and publications.
- Tax Map: an electronic research tool and finding aid.
- Tax law frequently asked questions (FAQs).
- Tax Topics from the IRS telephone response system.
- Fill-in, print, and save features for most tax forms.
- Internal Revenue Bulletins.
- Toll-free and email technical support.

Buy the CD-ROM from National Technical Information Service (NTIS) at *www.irs.gov/cdorders* for $25 (no handling fee) or call 1-877-233-6767 toll free to buy the CD-ROM for $25 (plus a $5 handling fee).

CD-ROM for small businesses. Publication 3207, Small Business Resource Guide CD-ROM, has a new look and enhanced navigation features. This CD includes:

- Helpful information, such as how to prepare a business plan, find financing for your business, and much more.
- All the business tax forms, instructions, and publications needed to successfully manage a business.
- Tax law changes.
- IRS Tax Map to help you find forms, instructions, and publications by searching on a keyword or topic.
- Web links to various government agencies, business associations, and IRS organizations.
- "Rate the Product" survey—your opportunity to suggest changes for future editions.

An updated version of this CD is available each year in early April. You can get a free copy by calling 1-800-829-3676 or by visiting *www.irs.gov/smallbiz*.