

Taxation of Demurrage and Detention Damages

by Karl Berlin

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Introduction

Port delays have been a frequent issue in the shipping industry, and not only in recent times — even though disruptions such as the COVID-19 pandemic and the consequences of Brexit at U.K. ports have exacerbated the issue.

Because delays at ports are costly, demurrage and detention are two important concepts within the international maritime industry to spread the risk and cost of those delays. Demurrage and detention are charges under voyage charter parties with the purpose of encouraging the timely offloading of cargo, whether containers or bulk, and the timely redelivery of containers or vessels to the owners.

However, they apply in different situations and in different ways. And the taxation of demurrage and detention charges can be a contentious issue under applicable double tax treaties.

The introduction of the international shipping income and qualified ancillary international shipping income exclusions, and particularly the limitations on the latter vis-à-vis the former, adds another challenge.

The Concepts

Demurrage

Demurrage is an integral component of the laytime provisions within voyage charter parties (that is, contracts between a charterer and a shipowner for the hire of a ship or for carriage of goods or passengers) that operate under fixed laytime. A laytime provision in charter parties refers to the agreed period during which the charterer can load and unload cargo without incurring additional charges.

Just as with the rate agreed for transporting cargo (also known as freight) on a specific voyage, the negotiated demurrage amount reflects prevailing market conditions rather than the vessel's daily operational costs.

Demurrage serves as the compensation to which shipowners are entitled should charterers fail to load or discharge the vessel within the allotted laytime.

The interpretation of demurrage can vary across different jurisdictions. Under English law, failing to load or discharge the vessel within the allowed laytime constitutes a technical breach by the charterers. The consequence of this breach is demurrage, which is liquidated damages payable for detaining the vessel beyond the stipulated laytime. Because the charterer is already in breach by this time, otherwise applicable laytime exceptions do not apply once the vessel is on demurrage: A party in breach cannot benefit from its own breach.¹ Under Scandinavian law, demurrage doesn't seem to be a technical breach per se, but rather a contractual agreement determining an owner's right to compensation for the delay of the vessel in port.

¹ *Islamic Republic of Iran Shipping Lines v. Ierax Shipping Co.*, [1991] 1 Lloyd's Rep. 81, at 87.