FOREIGNER'S TAX GUIDE TO STARTING A BUSINESS IN FLORIDA

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Establishing a business in Florida starts with proper planning, and the sooner you begin, the better. The Foreigner's Tax Guide to Starting a Business in Florida provides information on various state and federal requirements you need to know.

Setting up a business is a complex process. Many legal, regulatory and tax considerations enter into these requirements; however, only tax-related considerations are discussed in this booklet.

This document provides a basic overview of the tax issues, but is no substitute for experienced professional advice. Consult your professional advisors, or contact Kaufman, Rossin & Co. at 305.858.5600.

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Why should I consider investing in Florida?

Florida is one of the most international U.S. states and has become one of the most desirable places in the country to conduct business. With its strategic location at the crossroads of the Americas, Florida is a major global hub for trade and investment, import and export, high technology, banking and insurance, travel and tourism, recreation, communications, healthcare and education.

- **As the fourth most populous state with a workforce of more than 9 million, Florida's workforce is one of the most diverse in the nation, both culturally and linguistically. Over 3.2 million residents were born outside the United States, and many Floridians speak one or more of over 90 languages.**
- **The cost of doing business in Florida is very competitive: land, labor and capital are all more affordable than in California, New York or Texas.**
- **Florida's pro-business tax structure gives entrepreneurs advantages from the start, with limited taxes and no personal income tax.**
- **The State of Florida is dedicated to stimulating growth by providing assistance and incentives to a variety of high-wage, high value-added industries.**

What are my tax advantages to investing in Florida?

Florida has a pro-business tax climate that provides advantages for virtually every type of business. The state has many Free Trade Zones and Bonded Warehouses. Generally, you'll find:

- **NO state personal income tax (constitutionally guaranteed)**
- **NO business income tax on limited partnerships or subchapter S-corporations**
- **NO corporate franchise tax on capital stock**
- **NO state-level property tax assessed**
- **NO property tax on business inventories**
- **NO property tax on goods-in-transit for up to 180 days**
- **NO sales and use tax on goods manufactured or produced in Florida for export outside the state**
- **NO sales tax on purchases of raw materials incorporated into a final product for resale, including non-reusable containers or packaging**
- **NO sales/use tax on co-generation of electricity**
- **NO sales/use tax on the purchase or lease of manufacturing equipment for a new or expanding business**

- **NO sales/use tax on the purchase of parts and labor to repair manufacturing equipment**
- **NO sales/use tax on the purchase of electrical utilities used in a manufacturing process**
- **NO sales tax on the purchase of equipment and building materials for use in enterprise zones and sales/use tax or corporate income tax credits for jobs created in enterprise zones**

How should I structure my business to minimize my taxes?

Business activity may be conducted through a variety of organizational structures. The business structure you choose will impact your personal tax liability, as well as the amount of federal tax you and your company will pay.

Often, legal, immigration and tax considerations enter into choosing an organizational structure; however, only tax considerations are discussed in this booklet.

The most common forms of business are the sole proprietorship, partnership, corporation and limited liability company.

- **<u>Sole Proprietorships</u> – A sole proprietor is an unincorporated business that is owned by one individual. It is the simplest form of business organization to start and maintain. The business has no existence apart from you, the owner. Its liabilities are your personal liabilities. You undertake the risks of the business for all assets owned, whether or not used in the business. You include income and expenses of the business on your personal tax return; generally, in Florida sole proprietorships are not required to file tax returns.**

- **<u>Partnerships</u> – A partnership is the relationship existing between two or more persons who join to carry on a trade or business. Each person contributes money, property, labor, or skill, and expects to share in the profits and losses of the business.**

  A partnership must file an annual information return to report the income, deductions, gains, losses, etc., from its operations, but it does not pay income tax. Instead, it "passes through" any profits or losses to its partners. Each partner includes his or her share of the partnership's income or loss on his or her tax return.

  Generally, in Florida partnerships are not required to file information returns unless there is a corporate partner.

- **<u>Corporations</u> – In forming a corporation, prospective shareholders exchange money, property, or both, for the corporation's capital stock. A corporation**

generally takes the same deductions as a sole proprietorship to figure its taxable income. A corporation can also take special deductions.

The profit of a corporation is taxed to the corporation when earned, and then is taxed to the shareholders when distributed as dividends. However, shareholders cannot deduct any loss of the corporation.

- **<u>S corporations</u> – An eligible domestic corporation can avoid double taxation (once to the corporation and again to the shareholders) by electing to be treated as an S corporation. Generally, an S corporation is exempt from federal income tax other than tax on certain capital gains and passive income. Establishing an eligible domestic corporation can be difficult to achieve for non-U.S. persons.**

  On their tax returns, the S corporations shareholders include their share of the corporation's separately stated items of income, deduction, loss, and credit, and their share of non-separately stated income or loss.

  Generally, in Florida S corporations are not required to file information returns.

- **<u>Limited liability Company</u> – A limited liability company (LLC) is an entity formed under state law by filing articles of organization as an LLC. None of the members of the LLC are liable for its debts.**

  An LLC may be classified for federal income tax purposes as either a partnership, a corporation, or a disregarded entity.

Do non-resident aliens and foreign corporations need to file and pay taxes?

A non-resident alien and foreign corporation are generally taxed in the same manner as a U.S. citizen or domestic corporation on all income that is "effectively connected" with the conduct of a trade or business in the United States. If any U.S. source income received by a non-resident alien or foreign corporation is not effectively connected with a U.S. trade or business, then it will be taxed at a flat 30-percent rate, or lower treaty rate. A flat 30-percent tax rate or lower treaty amounts or rates will also apply to the profits (and certain interest amounts) of a U.S. branch of a foreign corporation that are remitted to the foreign corporation during the tax year.
A non-resident alien foreign corporation who engages in trade or business in the United States at any time during the tax year or who has taxable income must generally file an income tax return. For a non-resident alien, Form 1040NR is used for this purpose. For a foreign corporation, Form 1120F is used for this purpose. The returns are due on or before the 15th day of the 6th month following the close of the tax year (generally June 15 for calendar year taxpayers).

What is a federal tax payer identification number and do I need one?

The United States taxes the worldwide income of U.S. Citizens, resident aliens and domestic corporations, without regard to whether the income arose from a transaction or activity originating outside its geographic borders. U.S. Citizens, resident aliens and domestic corporations must have a taxpayer identification number so the IRS can process your returns.

The three most common kinds of taxpayer identification numbers are the social security number (SSN), individual taxpayer identification number (ITIN) and the employer identification number (EIN).

- **A SSN is issued to individuals by the Social Security Administration (File Form SS-5)**
- **A ITIN is issued to nonresident or resident aliens who do not have and are not eligible to get an SSN (File Form W-7, W-8 or W-9)**
- **An EIN is issued to individuals (sole proprietors), partnerships, corporation and other entities by the IRS (File Form SS-4, W-8 or W-9)**

You must include your taxpayer identification number (SSN, ITIN or EIN) on all returns and other documents you send to the IRS. You must also furnish your number to other persons who use your identification number on any returns or documents they send to the IRS.

What is a tax year?

You must figure your taxable income and file an income tax return based on an annual accounting period called a tax year. A tax year is usually 12 consecutive months. Depending on the tax entity, there are two kinds of tax years.

1. **Calendar tax year. A calendar tax year is 12 consecutive months beginning January 1 and ending December 31.**
2. **Fiscal tax year. A fiscal tax year is 12 consecutive months ending on the last day of any month except December. A 52-53 week tax year is a fiscal tax year that varies from 52 to 53 weeks but does not have to end on the last day of a month.**

A corporation may adopt either a calendar tax year or a fiscal tax year by filing the first income tax return using that tax year. Thereafter, you continue to use that tax year unless you get IRS approval to change it. Generally any entity other than a corporation must use a calendar year.

What are accounting methods?

An accounting method is a set of rules used to determine when and how income and expenses are reported. You choose an accounting method for your business you file your first income tax return. The two accounting methods listed below are most commonly used.

1. **Cash method. Under the cash method, you report income in the tax year you receive it. You usually deduct or capitalize the expenses in the tax year you pay them.**
2. **Accrual method. Under an accrual method, you generally report income in the tax year you earn it, even though you may receive payment in a later year. You deduct or capitalize expenses in the tax year you incur them, whether or not you pay them that year.**

Typically businesses with inventory must use the accrual method. However, many small businesses qualify to use the cash method.

What Federal business taxes do I need to pay?

The form of business you operate determines what taxes you must pay and how you pay them. The following are the four general kinds of business taxes.

- **Income tax – All businesses except partnerships, S corporations and sole proprietorships must file an annual income tax return. Partnerships and S Corporations file an information return. The federal income tax is a pay-as-you-go tax. You must pay the tax as you earn or receive income during the year. An employee usually has income tax withheld from his or her pay.**

- **Self-employment tax – Self employment (SE) tax is a social security and Medicare tax primarily for individuals who work for themselves. Your payments of SE tax contribute to your coverage under the social security system. You coverage provides you with retirement benefits, disability benefits, survivor benefits, and hospital insurance (Medicare) benefits.**

- **Employment taxes – This section discusses the employment taxes you must and the forms you must file to report them. Employment taxes include the following:**

  i. **<u>Federal income, social security and Medicare taxes</u> – You generally must withhold federal income tax from your employee's wages. Social security and Medicare taxes pay for benefits that workers and their families receive under the Federal Insurance Contributions Act (FICA).**

     Social security tax pays for benefits under the old-age, survivors, and disability insurance part of FICA. Medicare tax pays for benefits under the hospital

insurance part of FICA. You withhold part of these taxes from your employee's wages and you pay a matching amount yourself.

ii. **<u>Federal Unemployment Tax</u> – The federal unemployment tax is part of the federal and state program under the Federal Unemployment Tax Act (FUTA) that pays unemployment compensation to workers who lose their jobs. You report and pay FUTA tax separately from social security and Medicare taxes and withheld income tax. (For more information, see – Do I need to pay taxes in Florida?)**

iii. **<u>Hiring Employees</u> – Have the employees you hire fill out Form I-9 and Form W-4. If your employees qualify for and want to receive advanced earned income credit payments, they must give you a completed Form W-5.**

1. **Form I-9 – You must verify that each new employee is legally eligible to work in the United States. Both you and the employee must complete the U.S. Citizenship and Immigration Services (USCIS) Form I-9, Employment Eligibility Verification.**
2. **Form W-4 – Each employee must fill out Form W-4, Employee's Withholding Allowance Certificate. You will use the filing status and withholding allowances shown on this form to figure the amount of income tax to withhold from your employee's wages.**
3. **Form W-5 – An eligible employee who has a qualifying child is entitled to receive advance earned income credit (EIC) payments with his or her pay during the year. To get these payments, the employee must give you a properly completed Form W-5, Earned Income Credit Advance Payment Certificate.**
4. **Form W-2 – After the calendar year is over, you must furnish copies of Form W-2, Wage and Tax Statement, to each employee to whom you paid wages during the year. You must also send copies to the Social Security Administration.**

iv. **Excise taxes – You will have to verify whether you may have to pay excise taxes if you do any of the following:**

- **Manufacture or sell certain products**
- **Operate certain kinds of businesses**
- **Use various kinds of equipment, facilities or products**
- **Receive payment for certain services**

What kind of business expenses can I deduct?

You can deduct business expenses on your income tax return. These are the current operating costs of running your business. To be deductible, a business expense must be both ordinary and necessary. An ordinary expense is one that is common and accepted in your field of business, trade or profession. A necessary expense is one that is helpful and appropriate for your business, trade or profession. An expense does not have to be indispensable to be considered necessary.

When can I deduct a business expense? When you deduct an expense depends on your accounting method.

1. **Cash method. Under the cash method of accounting, you generally deduct business expenses in the tax year you pay them.**

2. **Accrual method. Under an accrual method of accounting, you generally deduct business expenses when the all-events test has been met, given that all events have occurred that fix the fact of liability and the liability can be determined with reasonable accuracy, and economic performance has occurred.**

Do I need to pay taxes in Florida?

The location and type of business you operate determines the types of taxes you are subject to in Florida. The Florida Department of Revenue administers 32 taxes and fees, such as sales and use tax, discretionary sales tax, unemployment tax and corporate income tax.

- **Sales and use tax. Sales tax applies to the sale, rental, lease or license of goods, certain services and the lease of commercial real property in Florida, unless the transaction is exempt. If your business will have taxable transactions, you must register as a sales and use tax dealer before you begin conducting business in Florida. Dealers must collect sales tax at the time of each sale and pay the tax for each collection period to the Department of Revenue.**

- **Discretionary sales tax. Most Florida counties impose a discretionary sales surtax ("Surtax") that generally applies to transactions that are subject to sales and use tax. A dealer who sells or delivers taxable goods or taxable services into a county with a Surtax must collect the Surtax at the rate imposed in the county where the goods or services are delivered. On most transactions, the Surtax is limited in application to the first $5,000 of the sales price of the item sold or in the case of leased personal property, the first $5,000 of each lease payment. In the case of real property leases, the Surtax is not capped and therefore applies to the full amount of each lease payment.**

- **Unemployment tax. Unemployment compensation provides partial, temporary income to workers who lose their jobs through no fault of their own, and are able and available to work. The employer pays for the unemployment compensation through a tax administered by the Department of Revenue. Workers do not pay any part of the unemployment tax and employers must not make payroll deductions for this purpose. The employer's payments go into a reserve fund from which benefits are paid to eligible claimants. (For more information, see – What business taxes do I need to pay?)**

- **Corporate income tax. With the exception of S corporations, corporations and entities treated as corporations that do business, or earn or receive income in Florida, including out-of-state corporations, must file a Florida corporate income tax return unless exempt. You must file a return even if no tax is due.**

What type of records do I need to keep?

- **Why keep records? Everyone in business must keep records. Good records will help you do the following:**
    1. **Monitor the progress of your business**
    2. **Prepare your financial statements**
    3. **Identify source of receipts**
    4. **Keep track of deductible expenses**
    5. **Prepare your tax returns**
    6. **Support items reported on tax returns**

- **What kinds of records should I keep? The business you are in affects the type of records you need to keep for federal tax purposes. Except in a few cases, the law does not require any specific kind of records. You can choose any recordkeeping system suited to your business that clearly shows your income and expenses. For instance, organize them by year and type of income or expense.**

  <u>Gross receipts.</u> Gross receipts are the income you receive from your business. You should keep supporting documents that show the amounts and sources of your gross receipts. For sales made outside the state of Florida, you must retain a bill of lading documenting the out-of-state sale.

  <u>Purchases.</u> Purchases are the items you buy and resell to customers. If you are a manufacturer or producer, this includes the cost of all raw materials or parts purchased for manufacture into finished products. Your supporting documents show the amount paid and that the amount was for purchases.

Expenses. **Expenses are the costs you incur (other than purchases) to carry on your business. Your supporting documents should show the amount paid and that the amount was for a business expense.**

Assets. **Assets are the property, such as machinery and furniture you own and use in your business. You must keep records to verify certain information about your business assets. You need records to figure the annual depreciation and gain or loss when you sell the assets.**

- **How should I keep my records? You should set up a recordkeeping system using an accounting method that clearly shows your income for your tax year. Your recordkeeping system should include a summary of your business transactions. This summary is ordinarily made in your books (for example, accounting journals and ledgers). Your books must show your gross income, as well as your deductions and credits.**

  There are computer software packages you can use for recordkeeping. These can be purchased in many retail stores. These packages are very helpful and relatively easy to use.

- **How long should I keep my records? You must keep your records as long as they may be needed for the administration of any provision of the Internal Revenue Code. Generally, this means you must keep records that support an item of income or deduction on a return until the period of limitations for that return runs out. The period of limitations is the period of time in which you can amend your return to claim a credit or refund, or the IRS can assess additional tax.**

  Employment tax records. **If you have employees, you must keep all employment tax records for at least 4 years after the date the tax becomes due or is paid, whichever is later.**

  Assets. **Keeps records relating to property until the period of limitations expires for the year in which you dispose of the property in a taxable disposition. You must keep these records to figure any depreciation, amortization, or depletion deduction, and to figure you basis for computing gain or loss when you sell or otherwise dispose of property.**

  Records for non-tax purposes. **When your records are no longer needed for tax purposes, do not discard them until you check to see if you have to keep them longer for other purposes. For example, your insurance company or creditors may require you to keep them longer than the IRS does.**

  Best practices for record retention are found in Exhibit 1, on page 15.

What are the penalties for not filing returns or paying my taxes?

The law provides penalties for not filing returns or paying taxes, as required. Criminal penalties may be imposed for willful failure to file, tax evasion, or making a false statement.

- **Failure to file tax returns. If you do not file your tax return by the due date, you may have to pay a penalty. The penalty is based on the tax not paid by the due date.**
- **Failure to pay tax. If you do not pay your taxes by the due date, you will have to pay a penalty for each month, or part of a month, that your taxes are not paid.**
- **Failure to withhold, deposit or pay taxes. If you do not withhold income, social security, or Medicare taxes from employees, or if you withhold taxes but do not deposit them or pay them to the IRS, you may be subject to a penalty of the unpaid tax, plus interest. You may also be subject to penalties if you deposit the taxes late.**
- **Failure to follow information reporting requirements. A penalty applies if you do not file information returns or do not furnish a required statement to a payee by the due date, if you do not include all required information, or if you report incorrect information.**

Exhibit 1: Recommended Document Retention Time Periods[1]

Type of Record	Retention Period
Copies of tax returns as filed	7 years after liquidation of entity
Tax and legal correspondence	7 years after liquidation of entity
Audit reports	7 years after liquidation of entity
General ledger and journals	7 years after liquidation of entity
Financial statements	7 years after liquidation of entity
Contracts and leases	7 years after liquidation of entity
Real estate records	7 years after liquidation of entity
Corporate stock records and minutes	7 years after liquidation of entity
Bank statements and deposit slips	6 years
Sales records and journals	6 years
Other records relating to revenue	6 years
Employee expense reports	6 years
Travel and entertainment expenses records	6 years
Canceled checks	3 years
Paid vendor invoices	3 years
Employee payroll expense records	3 years
Inventory records	3 years [2]
Depreciation schedules	tax life of asset plus 3 years
Other capital asset records	tax life of asset plus 3 years
Other records relating to expenses	3 years
Partnership agreement and amendments	permanently
Operating agreement and amendments (LLC)	permanently

[1]This table contains recommended document retention periods based on federal requirements. These recommendations should work for Florida tax purposes as well. Also, it may be necessary to retain some records longer because of nontax reasons. For example, insurance policies, leases, real estate closing statements, and employee payroll records might need to be kept longer than needed for IRS purposes. Taxpayers should consult with their attorneys about how long to retain legal documents.

[2]Longer if you use LIFO.

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