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I. FORMS OF BUSINESS ORGANIZATIONS

U.S. Corporation

A corporation with limited liability is the form of organization most common in the US. Many of the procedures and requirements are similar to those relating to the formation of companies in the UK, except that the US Corporation is subject to the specific corporate law requirements of the state in which it is incorporated. Thus, for example, a US corporation incorporated in New York may have certain restrictions placed on it by New York corporate law, which will not be relevant for a Florida corporation.

In fact, the state known for its most liberal company law requirements is Delaware, and even though a US corporation may be conducting business activities in, for example, New York, and therefore be subject to tax in that state, it may be incorporated as a Delaware corporation to obtain the greatest flexibility with respect to future changes in its charter. The charter, or articles of incorporation, contains the objects and other provisions relating to the corporation, and must be filed with the Secretary of State in the state selected.

A Branch of Foreign Corporation

A foreign corporation may itself establish a branch within the US to conduct its business activities even though most foreign corporations choose to form subsidiary companies for many non-tax reasons. Most countries have the ability to subject foreign corporations to domestic taxation if they form a branch, open an office or employ staff, or otherwise conduct business activities which enables the taxing administration to assess the foreign corporation as though it had a deemed permanent establishment.

The US has the concept of taxable income “effectively connected” with a US source, and if a foreign corporation has “effectively connected” income, then the foreign corporation will be subject to US tax on such income the same way as US domestic corporation. Moreover, if 25% or more of a foreign corporation’s gross income is effectively connected income, then any dividends paid by the foreign corporation to a non-US resident will be subject to US withholding tax unless an applicable tax treaty provides otherwise.

The income of a foreign corporation that is not effectively connected with a U.S. trade or business or attributable to foreign corporation’s permanent establishment in the United States is subject to the 30% (or lower rate under an applicable treaty) rate.

Partnership

General and limited partnerships may be formed, normally by means of a written partnership agreement, which is usually registered under state law. For legal purposes, a partnership is defined as an association of two or more persons formed to carry on a business for profit as co-owners. As defined for U.S. tax law, a partnership includes a syndicate, pool, joint venture or other unincorporated organization by which any business is conducted – and which is not, for federal income tax purposes, a corporation, trust or estate. Each state and the District of Columbia has its own laws governing the formation and operation of partnerships.

Partnerships are treated as conduits for U.S. income tax purposes, and each partner recognizes a proportionate share of income, loss and credit, whether or not it is distributed to the partners. Partnerships allow for much flexibility for allocation of profits and losses, as well as distributions.

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Any partnership engaged in a trade or business in the United States that has foreign partners must withhold U.S. tax on the foreign partner's distributive share of business income.

Limited Liability Company

Limited liability companies are a relatively new but increasingly popular phenomenon in the US. The LLC is usually defined from a US legal perspective as a company – statutorily authorized in certain US states – that is characterized by limited liability, management by members or managers, and limitations on ownership transfer. As a legal entity, the LLC is able to own property in its own name, incur debts and other liabilities, enter into contracts, and initiate judicial proceedings. The LLC is a relatively new business form in the US that allows members flexibility to manage the entity's internal affairs; in fact, most state statutes permit LLC members to participate in the entity's management without sacrificing their limited liability protection. As with other legal entities, state (not federal) law governs the creation of an LLC. A multi-member LLC is treated as partnership for US federal tax purposes unless it elects to be taxed as a corporation.

LLCs become very appealing to foreign investors who are concerned with the cost of taxation at the corporate level and the litigious nature of American society.

II. TAXATION

1. Income taxation

- Under the current law, Federal corporate tax rates on income and net capital gains are 25-35%. The 28-39.6% rates will become effective in tax years beginning after 2010 unless Congress takes legislative action.
- The income (such as dividends, interest and royalties) of a foreign corporation that is not effectively connected with a U.S. trade or business or a permanent establishment in case of a treaty country resident corporation, is taxed at a rate of 30% (or lower rate under an applicable treaty).
- The states and some municipalities (e.g., New York City) generally impose corporate income tax at rates varying between 1% and approximately 12%. These taxes are levied on US and foreign corporations conducting business activities in the particular state so that, for example, a Delaware corporation with an office in New York will pay New York state taxes as well as any Delaware taxes payable as a result of business operations in Delaware. The calculation of the state tax is generally based on the taxable income declared for federal tax purposes, subject to minor adjustments.

2. Sales taxes

- Sales taxes are imposed at state and local levels as opposed to the federal level in respect of products and certain services sold within the United States. In this respect, it differs from a value added tax system in that it is a consumer tax which is only levied once at the point of consumption, as opposed to throughout a chain of transactions leading to final consumption. The applicable rates of taxes vary from state to state at rates of between 3% and 7%, with exemption generally given for food and medical products (for example the rate of sales tax in California is currently 7%). Moreover, sales taxes are not levied on intangible property, e.g. royalties regarding copyrights, as compared to the VAT system in EU countries.

3. Social security taxes

- Social security taxes will need to be paid by resident individuals working within the US by both employer and employee at the rate of 6.2% on the first \$106,800 of salary, plus a "Medicare" tax, again payable by employer and employee at 1.45% of salary. However, under any of the totalization agreements entered into by the US,

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foreign nationals will not need to pay social security taxes in the US if they are transferred temporarily to the US for a period of less than five years, provided they remain subject to social security tax in their home country (not all totalization agreements have the five-year rule). Moreover, they would still be entitled to benefits within the US, provided that ultimately the foreign national has contributed to the social security system for at least 18 months in the US.



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