

SHOULD YOU INCORPORATE YOUR BUSINESS?

If you own a small business in Florida, chances are you started out with a little office or shop, a vehicle, some supplies and a lot of hard work. You probably didn't think much about how you should structure your ownership of the business. After all, it was tough enough just getting started. If this sounds like you, then you are doing business as a "sole proprietorship," which has definite legal consequences. Is it the right structure for you?

In selecting the appropriate structure for a small business, two primary factors to consider are tax rates and potential liability. There are a number of different business structures available in Florida, including sole proprietorship, corporation, general partnership, limited partnership, limited liability limited partnership, and limited liability company. Each has different attributes, but in the small business category the sole proprietorship and corporation are most common.

Let's look at the first factor. As a sole proprietor in Florida you are taxed by the federal government as an individual and pay no state income tax. If your business were structured as a corporation, the assets of the business (including income) would belong to the corporation, which would pay both federal and state income tax. You would be the sole shareholder, entitled to dividends representing income remaining after taxes and expenses, and would have to pay federal income tax on your dividends. Doesn't sound like a good deal, does it? What makes it a good deal is that you may qualify as a "Subchapter S" corporation. This refers to a section of the U.S. Internal Revenue Code which allows qualifying corporations to be exempt from taxation. Instead, all income, gains, losses, deductions and credits are passed through to you, as the shareholder, and reported on your individual tax return, just like a sole proprietor. So why bother setting up a corporation? That brings us to the second factor.

As a sole proprietor, you are personally liable for all debts and obligations of your business. As you would expect, these include bills owed to your suppliers and other creditors. More importantly, they also include damages payable to parties who may be injured as a result of your business activities. To a certain extent you can limit your exposure for these damages by obtaining liability insurance, but remember that you are personally responsible for any shortfalls in insurance. This means that your non-business assets are at risk, subject to the protections afforded by Florida's Constitution (which exempts only your homestead and a limited amount of personal property from forced sale for the payment of your debts). If your business were incorporated, only the corporation would be liable for these obligations. As a shareholder, you would be insulated from liability for the corporation's debts and your only potential loss would be the amount invested in the business.

In order to decide whether the corporation or any other structure is the right one for your business, you should meet with an attorney who can assess your needs in the context of the particular business you operate. Most attorneys will incorporate a business for a flat fee, plus costs such as governmental filing fees. The typical incorporation will consist of filing Articles of Incorporation with the state and a Subchapter S election with the IRS, preparation of corporate

bylaws and organizational minutes, issuance of corporate stock and furnishing a corporate records book.

A word to the wise.... Once you've decided to incorporate your business, make sure you keep up the corporate formalities, including paying the state's annual fee, keeping appropriate records, advertising in the corporate name and signing contracts with your corporate title. Failure to actually conduct your business like a corporation can result in a court deciding that your corporation is just a sham, and can expose you to the personal liability you wanted to avoid.

Word count: 644