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Tax Strategies for Global Business Growth

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Outline

- Introduction to International Tax
- Case Study
- Exporting
- Selling Through an Agent
- Employees in a Foreign Country
- Establishing a Foreign Entity

Introduction to International Tax

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- Foreign countries generally seek to expand their tax revenue base
- Nonvoting companies and individuals are easy targets
- Growing businesses seek to keep their costs low
- Long term costs can be well in excess of short term costs if decisions aren’t vetted with advisors
- US income tax treaties may provide some protection
- It’s important to be intentional, to think ahead and to obtain practical advice when considering growth in foreign markets

Case Study

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US Co is a US manufacturer of equipment established in 2002. US Co is responsible for the North American operations of its Parent. Parent distributes goods directly to customers that were existing prior to 2002 in North America and US Co provides customer service for those customers. See handout for timeline and activities that we will reference as we go through the remaining slides.

Exporting

When growing internationally, businesses often start with exporting in order to keep things simple. In fact businesses who export often don't consider themselves international businesses because they don't have any foreign entities. This often leads to businesses missing critical issues that could create current tax benefits or that may lead to higher compliance costs later.

Exporting

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Potential Risks & Opportunities:

- What are delivery terms?
  - Title transfer in US or foreign country
  - Sourcing of income for tax purposes

- Who is importer of record?
  - Customer, broker, contractor or US business
  - Foreign sales tax (VAT or GST)
  - Income tax implications

- Does the US company have a foreign bank account?
  - Foreign Account Tax Compliance Act (FATCA)
  - Foreign Bank Account Reporting (FBAR)

Exporting

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– Are you taking advantage of duty drawback?
  - Businesses that export goods that were imported or goods produced from raw materials that were imported may qualify
  - Generally brokers can help with recordkeeping needed for potential refund of import duties
– Have you considered an IC-DISC?
  - US manufactured goods that are exported
  - Must form a new legal entity to which commissions are paid
  - Federal tax rate reduction of 15 to 20% on commissions
  - Other issues must be considered (ex. State tax, reduction of other tax benefits, etc.)

Selling through an Agent

In order to keep costs low and avoid having a foreign employee, businesses often try to use agents outside the US. These contracts should always be reviewed by a local attorney. Foreign countries, like the US, want their citizens employed and may disagree with your classification as a contractor. Your current contractor may later be a whistleblower in order to obtain government benefits or to get back at you.

Selling through an Agent

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Potential Risks & Opportunities:

- Same risks and opportunities as exporting
- Do you have a contract?
  - Not having a contract is not an option even if your relationship is good
  - Be specific regarding terms of the arrangement and use local counsel
  - Income tax implications in treaty and non treaty countries
- Is the agent dependent or an employee?
  - Treaty exceptions to income tax protection
  - Sole practitioners
  - Limited or non-existent client base of the agent
- Does the agent take ownership of goods?
  - Sales based tax obligations rest with importer of goods
  - Personal property taxes may apply

Employees in a Foreign Country

As businesses look for more opportunities to grow overseas they often think about expanding their presence by either sending US employees abroad to provide services or hiring foreign employees. Customers begin to demand this local presence. The presence of US employees abroad or the hiring of local employees can both lead to a significant increase in the visibility of a business to tax authorities and these changes should be considered carefully.

Employees in a Foreign Country

Potential Risks & Opportunities:

– Same risks and opportunities as exporting
– Are your US employees working outside the US?
  - Salespersons or executives travelling abroad
  - Foreign payroll tax implications
  - Individual income tax in the foreign country
– Are your US employees providing services outside the US?
  - Withholding tax implications
  - Business and individual income tax implications
  - Foreign sales taxes may apply to services

Employees in a Foreign Country

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- What are US tax implications when you don’t have a local entity?
  - Federal and state foreign tax credits
  - Foreign fixed asset depreciation
- What are implications when hiring local employees?
  - Payroll tax filings will be required
  - Foreign bank accounts are more likely
  - Important to understand the labor laws
  - Mandatory benefits may be an issue

Establishing a Foreign Entity

The larger a foreign market becomes for a business the more likely the company eventually forms a local entity to keep the US company blocked from local taxation. There may also be customer or prospect requests for a more definitive local presence. Establishing foreign entities requires advice from both US and foreign advisors to ensure that globally you have a structure that is both tax efficient and most importantly allows for ease of doing business.

Establishing a Foreign Entity

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Potential Risks & Opportunities:

– Same risks and opportunities as exporting
– Did you have foreign and US advice in regard to the type of entity used?
    - Local investor requirements
    - Entity choice implications in the foreign country
    - Withholding taxes
    - Entity choice implications in the US
    - Choices available via US check the box elections
        - Flow through versus corporate entity
        - Cash flow needs
        - Direct versus indirect foreign tax credits
        - Future limitations of flow through entity choice
    - Ongoing operational issues to avoid US entity filing requirements

Establishing a Foreign Entity

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- Are you aware of US informational reporting requirements associated with forming a foreign entity?
  - Forms 5471, 8865 and 8858 related to ownership of foreign entities
  - Form FinCen 114 related to ownership of foreign financial assets
  - Penalties for nonfiling
- Have you considered transfer pricing?
  - Governmental concerns
  - Planning strategies