

SPOTT, LUCEY & WALL, INC.

CRISTA M. LUCEY (415) 217-6902
CHARLOTTE R. WALL (415) 217-6903
RUSSELL T. MANSKY (415) 217-6906
MING P. FANG (415) 217-6909
LI ZHANG (415) 217-6907

CERTIFIED PUBLIC ACCOUNTANTS
601 MONTGOMERY STREET
SUITE 777
SAN FRANCISCO, CA 94111-2610

IRINA A. BENDA (415) 217-6943
MICHELLE PIGNATARO (415) 217-6905
DEVAN FRIDAY (415) 217-6944
JAMESON LLOYD (415) 217-6904
KRYSTLE Y. CHOW (415) 217-6942

Steps to set up an office or presence in the US:

1. **Meet with a US immigration attorney.** You will need to explain your intentions of bringing any non-US citizens to the US. A non-US citizen can work in the US only with a valid work permit. The more common permits are the L “intercompany transfer” or the E “treaty investor” visa for employees of the foreign company. The visa selected will have an impact on what kind of a company presence is to be set up and how it will be capitalized. The B1/B2 visa or the “visa waiver” visa for business travelers is only valid if the employee is paid by an employer outside the US (this is an immigration rule for sourcing - not to be confused with the US federal or state income tax sourcing rules). A visa waiver individual is restricted to attending US seminars, investigating investments and perhaps making a sales presentation. They are not authorized to perform services like computer programming, problem solving at a customer site, etc. without a valid work permit. Immigration counsel will explain these rules in more detail.
2. **Meet with a business attorney** (usually not the same person as the immigration attorney but often immigration attorneys can set up a corporation).
 - i. Have the attorney set up a US domestic corporation.
 1. The corporation should be set up where the company intends to have its headquarters.
 - a. If you use a Delaware company, have the attorney register the company to do business where the headquarters is.
 - b. Note that forms need to be filed in each jurisdiction.
 - c. Be careful not to authorize and issue too many shares if you set up a Delaware corporation – the annual fees can get large (small is about \$35).
 - d. Have the attorney explain the differences in a Delaware corporation and a corporation in the state your headquarters will be operating from.
 - e. Please note that you can very easily reorganize tax free from one state to another.
 2. Do not set up a “Limited Liability Company.” This type of entity is a “permanent establishment” for US federal purposes and a branch for state tax purposes causing the foreign parent corporation to be taxable in the US and states.
 3. The officers, directors and shareholders do not need to be US citizens or residents. Some states have some restrictions for certain types of businesses.
 4. Capitalizing the company:
 - a. Issue all the shares to the foreign parent company.

- b. A non-citizen not resident in the US is taxable on US located assets if they die (a death tax) to the extent the assets exceed \$60,000. Ownership of the US company through a foreign parent company avoids this issue.
 - c. The US / Foreign parent company's country income tax treaty provides very favorable withholding rates to a subsidiary on dividends compared to a non-US individual.
 - d. We recommend you consider capitalizing the company with about 3 months of working capital (one operating cycle) (rent, salaries, office supplies, etc.). This should be discussed with legal counsel and immigration counsel.
 - e. We recommend a shareholder loan to finance the long term assets secured by the assets for asset protection of the foreign parent.
 - f. We recommend a working capital revolving loan to finance receivables, etc.
- ii. You will need to get a US federal identification number for the company.
 - 1. Ask them to put zero for the employees on the form. This avoids correspondence with the US IRS.
 - 2. Ask them to use a US address for all tax correspondence so that it can be dealt with promptly. You can use care of our address for this purpose if you decide to engage our firm.
 - iii. You will need to file a report with the US Department of Commerce.
 - 1. See <https://www.bea.gov/surveys/fdiusurv.htm> for the forms to use.
 - 2. Typically, a small company would use the BE-605 indicating – an exemption from the monthly, quarterly and annual filing requirements.
 - 3. A small company would then only report every five years.
 - 4. The form is due 30 days after the quarter of the foreign investment.
 - 5. Penalty for failing to file is \$25,000.
 - iv. The company will need a transfer pricing agreement between the US company and the foreign parent setting forth how the various goods and services will be priced and paid for. We recommend that the foreign parent's accountants work with the company to pick these "arm's length" prices then have US legal counsel review the agreement for compliance with US contract law. The company needs "adequate contemporaneous documentation" for the price it picks for these intercompany/related party transactions.
 - v. Ask legal counsel about registering the company in any city or local municipality for business licenses, etc.
 - 1. For example see <http://www.sfbizinfo.org/> for San Francisco. San Francisco City will want an annual license fee and a tax based on San Francisco payroll.

- vi. You will need these documents for the accountants:
 1. Articles of Incorporation stamped by the Secretary of State
 2. Minutes of the first meeting
 3. Copy of the Department of Commerce Report
 4. Copy of the IRS letter assigning the identification number.
 5. Copies of relevant contracts, loans, etc.
3. **Open a US bank account –**
- a. If you have a relationship with a bank in foreign parent that has an affiliate in the US, ask your foreign parent banker for a referral – that will make the process easier.
 - b. The banker will need
 - i. The Articles of Incorporation stamped by the Secretary of State
 - ii. The letter from the IRS with the identification number.
 - iii. Identification of the officers.
 - iv. Allow a lot of time for this step – since 9/11 the US banking system has new laws about “know your customer” which makes them cautious when opening bank accounts for anyone. They have the power to freeze any account they consider suspicious.
4. **Accounting and bookkeeping -**
- a. The US has no mandatory auditing requirements for privately held companies. The only report you will be required to file is the tax returns (income, sales, property, information, etc.).
 - b. Select a fiscal year -We recommend you use a year other than the same year of the foreign parent company. Say the foreign parent is on a calendar year, then we would recommend a June 30 year end. This allows for tax efficiency when transferring goods and services income and deduction between the companies.
 - i. If the company is providing advice and consent (i.e. consulting) it is mandated to use the calendar year.
 - c. Select an accounting method – cash or accrual
 - i. Cash is normal and preferred (again, an office manager doing the routine bookkeeping understands cash accounting).
 - ii. Cash cannot be used if global gross income for the entire affiliated group is more than \$5 million.
 - iii. Cash method generally cannot be used if there are inventories.
 - d. Buy a bookkeeping program – we recommend QuickBooks (we have no financial interest in Intuit Corporation).
 - i. It is one of the top rated programs.
 - ii. The program is widely used it is easy to hire an office manager for the routine bookkeeping tasks rather than hire an expensive bookkeeper.
 - iii. Buy the US version.
 - iv. You can easily transfer the data files by email to the accountants or other parties for reporting.
 - v. It is full featured – see <http://quickbooks.intuit.com/>
 - e. Design a chart of accounts – use the same chart of accounts the foreign parent company uses.
 - f. Consider having the foreign parent company bookkeeping staff keep the books for the US company.

- (i) There is no rule requiring the books and records to be kept in the US – they just need to be presented to the US tax authorities if they ask for them.
- g. In the US it is common to use a contract bookkeeper for monthly reporting rather than a Certified Public Accounting firm. CPA firms have expensive overhead and the contract bookkeepers are substantially less expensive.

5. Transferring employees

- a. Contact us prior to transferring any employees so we can make recommendations on how the contract might be structured for tax efficiency.

6. Hire an income tax return preparer for tax compliance.

- a. The most important consideration is to keep the *foreign parent company* out of the US and state tax nets.
 - i. If the US company is a “dependent agent” of the foreign parent company (i.e. the transfer pricing arrangement does not allow for sufficient profits) it could create a “permanent establishment” under the treaty.
 - ii. If the officers of the foreign parent come to the US and execute contracts on behalf of the foreign parent the foreign parent could be engaged in a US business.
 - iii. If the foreign parent has assets in the US (i.e. it leases property to the US subsidiary) it could have a permanent establishment and nexus in the US and states.
 - iv. Other – discuss with us any other transactions with the US or states for consideration.
 - v. If the foreign parent has a permanent establishment it is liable for filing federal income tax returns and paying US taxes.
 - vi. If the foreign parent has “nexus” for state purposes:
 - 1. It is liable for state income taxes usually on a basis of allocating global net taxable income computed on a state accounting basis and allocated to the state based on a formula of these items in the state compared to the world: payroll, property and sales.
 - 2. If the foreign parent is selling tangible personal property to customers in the state it could be liable for collecting state sales taxes (similar to the VAT).
- b. The corporation needs to file US federal returns each year and a year must end on the last day of the month and the year cannot be more than 12 months. For example, if the company is set up on July 1 the year cannot end later than the following June 30.
- c. The corporation would file form 1120
 - i. see Publication 542 for corporations at <http://www.irs.gov/pub/irs-pdf/p542.pdf>
 - ii. The income tax returns should take into account:
 - 1. The treaty between the US and foreign parent. For example the German Treaty provides:
 - a. Interest is not subject to US withholding tax (generally 30%) but may be limited under the “income stripping rules.”
 - b. Royalties are not subject to US withholding tax.
 - c. Dividends are subject to withholding tax at this time but there is a protocol pending to eliminate withholding.

- d. Other
 - 2. If a California corporation – consider making water’s edge election.
 - d. The corporation would attach form 5472 to report related party transactions – see <http://www.irs.gov/pub/irs-pdf/f5472.pdf>
 - e. The corporation would file state income tax returns – see <http://www.spottlucywall-cpas.com/links.html> for a complete list of links to all the state income tax forms. State taxes vary – California is 8.84% with a minimum tax of \$800.
 - f. The corporation would file form 1042 to report any payments of US sourced income to foreign persons – see IRS Publication 515 for more about that at: <http://www.irs.gov/pub/irs-pdf/p515.pdf> and form 1099 to US persons.
 - g. We would recommend the US corporation hire a payroll processing company – two publicly traded companies in this business are ADP and Paychex.
 - i. These providers can also collect the worker’s compensation insurance.
 - ii. These providers can direct deposit to the employee’s account so you can manage payroll virtually.
 - iii. We recommend you give the provider full power of attorney to make all tax deposits and file all forms. The penalties for late filing or payment can be substantially more than an entire year of fees to the service provider.
 - iv. These providers can offer other services such as management of fringe benefits – see IRS Publication 15-B for a list of fringe benefits at <http://www.irs.gov/pub/irs-pdf/p15b.pdf>
 - v. We recommend you have the payroll provider register the company for US payroll processing with the state you will be operating in.
 - vi. The US and foreign parent may have an agreement on Social Security – see http://www.ssa.gov/international/Agreement_Pamphlets/foreign_parenty.html for a copy of the agreement.
 - 1. This would be used if a foreign parent employee desired to stay on the foreign parent Social system.
- 7. Other**
- a. Please contact us for a complimentary introductory meeting at any time in this process. We will go over all the above as applicable as well as items that come to our attention that are specific to your situation.
 - b. Please feel free to send an email to Info@SpottLuceyWall-CPAs.com if you have any questions.

Please contact us if you have any questions.

Spott, Lucey & Wall Certified Public Accountants