

Foreign Investment in the United States

Establishing a business in the U.S. by a foreign corporation can be a fairly smooth operation with the right guidance and support. There are steps to take in forming, operating and growing a business in the U.S. in addition to gaining approval from various governmental agencies impacting everything from commerce to the environment, at both the federal and state level. New York state is often the target for many international businesses looking for the right U.S. entry point. With ten offices across the state, including New York City, Harris Beach can serve foreign business interests here and throughout the country.

This guide includes many of the key legal issues to consider when deciding to invest in a U.S. location, whether it is a new business or the geographic expansion of an existing company.



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CONSIDER NEW YORK STATE AS A POINT OF ENTRY

New York State Foreign 2016 Investment

First Year Expenditures			
Total	U.S. Businesses Acquired	U.S. Businesses Established	U.S. Businesses Expanded
\$30,450,000	29,204	1,224	22

Source: U.S. Bureau of Economic Analysis

As the headquarters of 94 of the world's Fortune 500 companies, the most of any state, New York is a prime location for foreign companies to open a business. Major industries in NYS include clean technology, education, financial services, information and nanotechnology, and life sciences and biotechnology. The state offers assistance and financial incentives through Empire State Development to attract foreign businesses.

Services include:

- Identification of potential sites and real estate availabilities.
- Demographic, wage, tax and utility cost data.
- Access to New York's incentive programs such as financing, tax credits, and training assistance.
- Information about quality of life in communities under evaluation.
- Networking with local government officials and private business people.
- Expedited assistance with the procurement of state permits, charters, etc.
- Project coordination and facilitation through a network of regional and foreign offices.

STAKING YOUR GROUND IN THE U.S.

In the U.S., legal business entities are formed at the state level, not the federal level, and the following are the most common types of business entities:

Sole Proprietorships

- A single individual owns and operates the business.
- The proprietor is personally responsible for all liabilities of the business, is entitled to all the income from it and pays individual income taxes on that income.
- There are no governmental fees to establish a proprietorship.

Partnerships

- A partnership is an association of individuals or other entities to operate a business.
- While not required, most partnerships operate under a written partnership agreement that describes the responsibilities and benefits to each partner.
- The partners of a general partnership are responsible for the actions of the partnership and are taxed individually on the income of the partnership.
- Although there are usually no stated costs to establish a partnership (there may be filing and publication fees associated with a limited partnership), legal counsel should be consulted regarding preparation of a partnership agreement and the necessity to register the partnership with state or local authorities.
- Most states permit a special arrangement called “Limited Partnerships” – in these partnerships, limited partners do not have personal responsibility for the debts and obligations of the partnership. There must, however, be at least one general partner who is not protected by limited liability.

Corporations

- The incorporated business is a distinct entity from its owners, the “stockholders” or “shareholders,” who are *not* personally liable for the debts and actions of the corporation.
- This is the most formal means of conducting business and is preferred by foreign companies doing business in the U.S. because of U.S. tax law and insulation from legal claims.
- Corporations, which are “incorporated” under state law by filing a Certificate or Articles of Incorporation with the proper state agency, can exist perpetually.
- Corporations operate under the general direction of a Board of Directors, which establishes the policies under which the officers conduct daily corporate business.
- There are no restrictions on ownership of corporations. A U.S. corporation may be a subsidiary that is wholly-owned by foreign persons or a foreign company, and there is no citizenship or residency limitation on directors or management.
- Except for certain regulated industries, there are few minimum capital requirements, and a corporation may have only one shareholder.
- Unless the corporation is a publicly traded company, it is customary to have a shareholders’ agreement governing the relationship among the shareholders, much like a partnership agreement.
- Each state has an established fee schedule for the incorporation of a corporation.
- Accounting records should be formalized.
- There are no statutory audit requirements unless the corporation’s stock is publicly traded.

*Expenditures
by foreign
direct investors to
acquire, establish,
or expand U.S.
businesses totaled
\$373.4 billion
in 2016.*

Source:
U.S. Department of Commerce,
Bureau of Economic Analysis

Limited Liability Companies

- The limited liability company (often called “LLC”) is a relatively newer form of entity that provides limited liability for owners (called “members”), like that of a traditional corporation, but provides significantly more structural flexibility.
- As is the case in partnerships, LLCs do not pay taxes and the tax consequences flow through to the owners, or members, unless the LLC elects to be taxed as a corporation.

- LLCs are formed by filing organizational documents with the appropriate state.
- Operating Agreements or LLC Agreements define the rights and powers of the LLCs members and designate the management of the LLC. These documents are the equivalent of a partnership agreement, corporate bylaws or shareholder agreements.

Branches

- A foreign company may operate a branch, perhaps a simple sales office, in any state.
- The company would be subject to state laws and would have to be registered as a “foreign corporation” in most states, subject to the usual corporate laws and state and federal income taxes.
- As a branch operation, the liabilities of the branch are the responsibility of the corporate owner.
- For reasons associated with liability exposure, as well as adverse tax consequences, branches have become unpopular.

Joint Ventures

- A foreign company may form a joint venture with a company in the U.S. for a specific purpose for a particular length of time.
- The joint venture may be operated as a partnership, limited partnership, corporation or LLC and will be taxed accordingly.
- A Joint Venture Agreement should clearly describe the relationship between the parties and their respective responsibilities and should provide especially detailed provisions on the resolution of disputes.

By industry, 2016 foreign expenditures for new direct U.S. investment were distributed widely. Expenditures in manufacturing, \$129.4 billion, accounted for more than one-third of total expenditures, the largest share among major industries. Within manufacturing, expenditures were largest in chemicals (\$64.7 billion). There were also notable expenditures in professional, scientific, and technical services (\$59.1 billion) and in finance and insurance (\$47.9 billion).

Source:
U.S. Department of Commerce,
Bureau of Economic Analysis

Mergers and Acquisitions

- A foreign company may want to conduct business in the U.S. by acquiring or merging with an existing business (the target company).
- An acquisition is typically accomplished by: buying the target's stock for cash or by giving the acquiring company securities in exchange; acquiring the target's assets for cash or for the acquiring company's securities; or merging the target with another company owned by the foreign investor.
- States have specific rules regulating mergers and other takeovers.
- The use of stock (or other securities) in these transactions brings the federal and state securities laws into play and could require approval by the Securities and Exchange Commission or state securities regulators.
- Certain larger mergers and acquisitions (including the formation of joint ventures) are required to file "pre-merger" notifications and observe waiting periods.
- The Committee on Foreign Investment in the United States (CFIUS) has the power to review and possibly modify or prohibit a merger or acquisition if the transaction might pose a threat to national security.

TAX PLANNING

In deciding how to do business in the U.S., it is very important for businesses to understand U.S. tax laws and how they will impact income tax filings in the U.S. and one's home country, both at the organization and individual levels.

Under U.S. tax law, a non-resident—whether an individual or a corporation—is subject to U.S. federal tax if they have income that is effectively connected with the conduct of a trade or business within the U.S. The level of activity required for a trade or business is relatively low. It is important to recognize when you start to have business connections in the U.S. because you may be subject to U.S. tax or U.S. filing requirements. For example, employees traveling on a regular basis to the U.S. to perform service calls may be deemed to be carrying on U.S. trade or business.

If you have income that is effectively connected with a U.S. trade or business, you may be able to seek relief from U.S. federal tax due to relief provided under an applicable tax treaty. The U.S. has in place bilateral tax treaties with numerous countries. Those treaties typically cover various categories of income, although the categories vary from treaty to treaty. In order to obtain treaty benefits, it is necessary to satisfy the conditions of the residency article of the treaty as well as certain other requirements. In general, a person is treated as a resident of the country in which the individual is subject to tax by reason of domicile, residence or citizenship. A corporation generally is treated as a resident in the country in which it is subject to tax by reason of its place of incorporation or similar criteria. The U.S. treaty network includes treaties with most European countries and other major trading partners, including Mexico, Canada, Japan, China and Australia.

In choosing a structure in which to conduct business in the U.S., it is important to consider the tax consequences of that choice. For example, although limited liability companies have proliferated in the U.S. due to its pass-through taxation for U.S. tax purposes, some countries may treat limited liability companies as non-resident corporations.

Foreign companies with activities in the U.S. must also be concerned about state-level taxes. There are no uniform rules among the states as to whether tax liabilities are imposed, and state taxes can sometimes be due even when no U.S. federal tax obligations exist. In addition, sales and other state and local taxes must be considered.

Most states will impose tax using a “nexus” standard, dependent upon whether a foreign taxpayer has some connection to the state. For example, a U.S. subsidiary of a foreign company may have to file tax returns in a state where such distribution center is located, if it creates nexus to the state. States apply apportionment factors to tax a portion of a foreign company’s income.

The bottom line is that companies with business operations in the U.S. could be liable for a variety of taxes and there are a number of considerations to make in order to determine how best to structure and operate the business in a tax-efficient manner.

MITIGATING RISKS

While there is no requirement to be a U.S. citizen or even a resident, foreign companies face most of the same risks for establishing and running a business on American soil as do U.S. citizens. There are inherent risks in any business operation which can be minimized or avoided by adhering to protocols. Our attorneys can help assess custom needs based on individual businesses, and the first priority is to create a legal risk management plan. There are a few topline considerations for all businesses to keep in mind.

Regulatory Compliance

- There are strict guidelines for compliance with requirements of anti-money laundering laws and with the mandates of anti-bribery laws.
- The Treasury Department's Office of Foreign Assets Control regulates the delivery of products and services (whether by conventional means or via e-commerce) in compliance with embargo and trade restraint rules.
- Products and goods must meet U.S. safety guidelines mandated by requirements of legislation, such as the Consumer Product Safety Act and the Bioterrorism Act, as well as registration with federal entities such as the U.S. Food and Drug Administration.
- Compliance with antitrust laws impacts several areas of distribution and marketing, including the price-setting for resale through distributors, the limitation of distributor sales territories and set requirements for product supply.
- Security offerings in the U.S. are regulated by federal and state security laws.

Cybersecurity

- Cybersecurity is becoming an increasing concern for businesses operating in the U.S. It has become a focal point at both the federal and state level. The Federal Trade Commission has jurisdiction over businesses that hold consumer data and is bringing actions against those companies when the organization either fails to meet its promised level of confidentiality or is negligent in its protection of customers' private data. In addition, nearly every state has data privacy laws which set forth data protection requirements and obligate businesses to notify individuals when certain types of private information have been breached.

- Beyond these general tenets, there are a number of cybersecurity standards which are industry-specific and which are also regulated at both the federal and state level. For instance, in the financial sector, the Gramm-Leach-Bliley Act is a federal law mandating certain cybersecurity protections. New York state has additional regulations at 22 NYCRR 500 in which the state's Department of Financial Services establishes a set of cybersecurity standards with provisions for auditing and penalties for non-compliance.
- There are a number of contractual cybersecurity standards which may impact businesses operating in the U.S. For example, companies that accept credit cards will need to comply with rules established by the payment card industry. Further, many companies regulated by certain cybersecurity regulation require their vendors to comply with the same rules.
- Businesses operating in the U.S. must still be cognizant of the cybersecurity laws of other nations' states. For instance, the European Union's GDPR protects the data privacy of its citizens regardless of where the data is hosted and the penalties for violators are quite steep. This is true even if the organization does no business in the EU or has no presence in that jurisdiction but holds data relevant to EU citizens.

RUNNING OF THE OPERATION

The running of the U.S. operation includes everything from the protection of the intellectual property to the type of labor hired to produce the product or service.

Labor and Employment

- Establishing hiring policies ensures employees work within terms set by the company. Contracts often apply to high-level executives, while hourly or salary employees work “at will.”
- The federal Immigration and Reform Act prohibits the hiring of foreign workers without the proper visas. There are several classifications of visas, designed to permit entry for foreign nationals training in the U.S.; nonimmigrant workers serving a specific time period; and other skilled workers who will not displace a U.S. worker.
- Specific safety conditions must be met through the federal Occupational Safety and Health Act (OSHA).

Intellectual Property Protection

- Trademarks and other company branding avoid infringement by securing U.S. trademark protection.
- First Class Contracts are critical to the protection of the business; its dealings with vendors and suppliers; and the avoidance of potential lawsuits.

Product Liability

- Manufacturers that sell in the U.S. are liable for any damages sustained as a result of negligence on the behalf of the manufacturer or the seller.
- U.S.-based insurance companies provide commercial or comprehensive general liability policies that provide fairly broad coverage for liability arising from commercial activities.
- Liability may also pertain to any breach of warranty.

Financing

There are a variety of types and sources of financing generally available to establish and finance U.S. operations, including economic development opportunities available through tax incentives, loans and grants. They include the following, each of which carries unique legal and tax implications:

- Debt financing
 - Asset-based loans
 - Term loans
 - Subordinated loans
 - Trade credit
- Public offerings and private placements of securities
- Venture capital and private equity
- Merger and acquisition transactions
- Government-backed loans and grants
- New Markets Tax Credits
- EB-5 Immigrant Investor Visa and Regional Center Program Financing
- Industrial development and exempt facility financings

By country of ultimate beneficial owner, a small number of countries accounted for most of the U.S. investment. The largest source country was Canada, with expenditures of \$58.5 billion. There were also substantial expenditures from the United Kingdom (\$54.5 billion), Ireland (\$35.4 billion), and Switzerland (\$34.9 billion). By region, about one-half of the new investment in 2016 was from Europe and nearly one-quarter was from the Asia and Pacific region.

Source:
U.S. Department of Commerce,
Bureau of Economic Analysis

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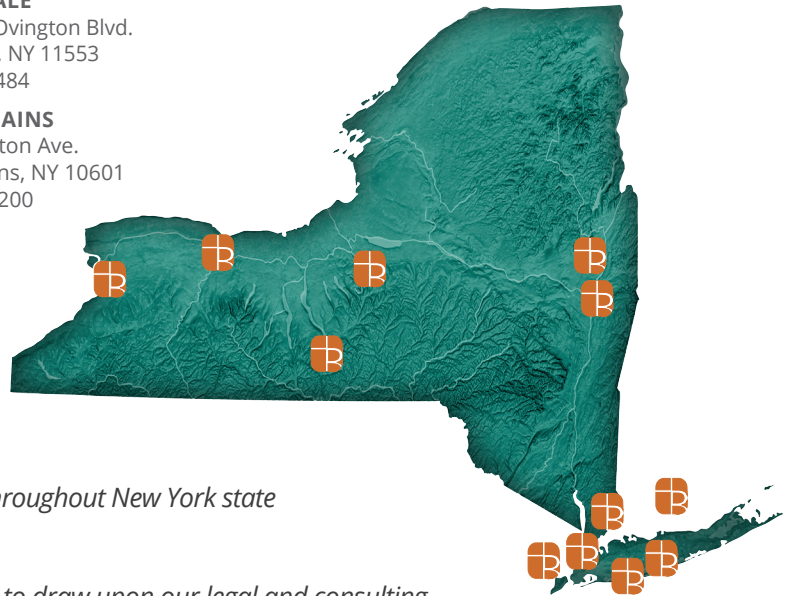
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Harris Beach has a strong office presence throughout New York state and our capabilities extend far beyond.

Our clients recognize the value in our ability to draw upon our legal and consulting resources from across the firm, whether their needs require regional, national or international solutions. Wherever we are needed, we mobilize our team to provide multi-disciplinary service through true engagement.

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