Pillar Legal Tech Law Blog[1]
Where should I incorporate my foreign-owned U.S. subsidiary?

Foreign companies that want to establish a subsidiary in the U.S. should consider incorporating in the state where the subsidiary's primary operations will be concentrated.

This approach can help avoid additional filings and costs that arise from incorporating in one state while locating your U.S. headquarters in another. For instance, if a company incorporates in Delaware but establishes its main U.S. office in California, it must register as a "foreign" corporation in California and file tax returns in both jurisdictions, resulting in duplicate fees and administrative burden.

If I have operations across multiple U.S. states, what's the recommended incorporation strategy?

For companies operating across multiple U.S. states, the recommended approach is to establish one subsidiary in the state where you have the largest operational presence (typically measured by number of employees or scale of operations), and then register as a foreign corporation in other states where you conduct business.

When does "foreign qualification" apply?

Generally, foreign qualification is required in the following situations:

- Physical Presence. When your company maintains a physical presence in another state, such as operating an office, warehouse, or retail location.
- Employment Activities. When you hire employees in another state, its necessary to manage state payroll tax obligations, handle state unemployment insurance, maintain worker's compensation insurance, and meet other local employment regulations.
- Business Operations. When your company conducts significant business operations in another state, which includes regularly conducting business transactions, selling products or services to state residents, meeting state-specific revenue thresholds, and maintaining ongoing business relationships with local clients. For instance, in California, if your business has $600,000 or more in gross receipts from the state during the tax year, you are considered to be doing business

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in California and should register as a foreign corporation in California, even if you don't have a physical presence.

Would it be beneficial to incorporate a foreign-owned U.S. subsidiary in Delaware if we hope to attract U.S. investors?

The benefits of Delaware incorporation for attracting U.S. investors largely depend on your corporate structure and fundraising strategy.

Delaware is a popular choice for incorporation due to its well-established corporate legal system, including a specialized Court of Chancery with over 200 years of corporate case law. This extensive legal precedent provides consistency and predictability in court decisions. Its corporate statutes are regularly reviewed and updated by legal experts to keep pace with business and legal developments. Additionally, Delaware's widespread use ensures most corporate lawyers are familiar with its laws, and many standard legal templates, like the National Venture Capital Association Series A documents, are designed for Delaware corporations. Please find more information in our article "***Where should I incorporate my tech startup?***"

However, if your U.S. subsidiary is wholly owned by a foreign parent company and you plan to raise funds at the parent company level, these Delaware advantages are not relevant. Since the foreign parent company would be the primary investment vehicle rather than the U.S. subsidiary, and there is no risk of corporate disputes between the sole shareholder (the parent) and the subsidiary, the sophisticated corporate law framework of Delaware offers little benefit. It may be more practical to incorporate the subsidiary in the state where your primary U.S. operations are located to simplify administrative matters and reduce compliance costs.

Nevertheless, if you anticipate future structural changes such as spinning off the U.S. subsidiary or pursuing an exit strategy for the subsidiary alone, incorporating in Delaware could be advantageous. Delaware's corporate framework makes these transactions more straightforward and familiar to potential U.S. buyers or investors.

What else should I consider when deciding where to incorporate my U.S. subsidiary?

- Labor Union/Employment Law. Employment laws vary from state to state, particularly regarding labor unions and employee protections. If your subsidiary will employ a large workforce, it's important to consider the role of labor unions in the state, as this can impact your labor costs, operations, and potential union negotiations. States like Texas, Florida, and Arizona are "right-to-work" states, meaning employees are not required to join a union or pay union dues as a condition of employment. States like California, New York, and Illinois have strong union protections and may see more unionization efforts within their labor force.

- Specific Tax Advantages. Different states offer varying tax benefits and structures, which you might want to consider when incorporating your subsidiary. For instance, states like Wyoming, South Dakota, and Nevada are often chosen for their lack of state corporate income tax. Delaware and Texas are known for having relatively favorable franchise tax structures, while other states may impose higher rates or additional fees based on your company's revenue or capital.[2] States, like Oregon and New Hampshire, do not have a state-level sales tax, which could be a big benefit if your business relies on selling products to consumers. States like California, New York, and Georgia offer tax credits and incentives for companies in certain industries, such as technology, film, and renewable energy.

Each state has its own set of benefits and challenges, so a thorough analysis of your business needs can help make the right choice.

Should I consider establishing multiple U.S. subsidiaries if I operate different types of businesses?

You may consider establishing different subsidiaries if you want to isolate liabilities for different businesses. When operating multiple distinct business units, especially those with differing risk profiles, setting up separate subsidiaries can help protect each part of your business from liabilities arising in another. For example, if you operate both a manufacturing business and a retail business, keeping them as separate subsidiaries can help ensure that potential product liability issues in the manufacturing operation don't put the retail business's assets at risk. This structure also provides greater flexibility in terms of future business decisions, such as selling one business unit or bringing in investors for just one of the businesses.

By: Greg Pilarowski, Ziwei Zhu
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[2] You may find more information about state taxes here: https://www.northwestregisteredagent.com/maintain-a-business/state-tax-rates.