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The Hidden Costs of Expansion in the U.S.

Establishing a foreign subsidiary or legal entity is a traditional route for businesses building an overseas presence. While this method ensures compliance with local laws and regulations, it is an expensive and time-consuming process that puts a significant strain on management, hiring the right local partner, internal legal, HR, and financial resources that if not performed properly will result in delays, lost opportunities, and significant costs.

Businesses need to budget at least $15,000 to $20,000 to get a legal entity up and running in most overseas markets. However, the total costs associated with establishing an entity go far beyond the initial setup phase.

In addition to the initial capital investment, the average direct and indirect ongoing entity maintenance fees average at least $100,000.00 - $200,000.00 per year. This number changes drastically depending on which market you select, the number of employees hired, their required salaries and benefits, and additional factors including office space and legal address, local bank relationships, warehousing, regulatory licenses, filing intellectual property, trademark, and copyright protection, and other local business requirements.

Common Hidden Costs with Entity Establishment

Creating and maintaining a legal entity requires a long-term financial commitment. If an organization selects this global expansion route, it must have a manageable budget in place. Companies need knowledgeable internal teams with adequate bandwidth to respond to opportunities and keep up with changing laws and regulations before establishing an entity in your chosen market.

Before a Company decides to establish a foreign entity it is advisable to select a local partner during the start-up phase. Here are a few hidden costs to consider throughout the initial start-up phase while running an overseas entity:

I. Registered Office Address

Most countries require a physical registered office address to establish an entity and receive Federal and State Tax ID. Depending on exchange rates, market demand, and the size of space a business needs, average real estate or office space prices in a target market might be more expensive compared to the firm's HQ location regardless of the remote working environment due to the Covid-19 pandemic.

In addition to purchasing space, companies need to provide technology such as phones, computers, software, and other sales and marketing materials local staff or consultants require to manage their overseas operations successfully, which if not coordinated well with local staff or local partner can create major operational mistakes and added expense.

II. Resident Director Requirement

Another requirement to establish an entity and receive a tax ID is hiring a Resident Director who may be represented by your local partner. This Resident Director is any local employee or consultant who is acting as your local partner and may also act as a legal representative for a company. This person signs paperwork for a business in the new market and goes to court in the event of any legal issues with proper internal controls to ensure approval from the management or holding company.

Companies must factor in the salary or consulting fee for this person or the fees for hiring a third-party local partner to act as the Resident Director.

III. Ongoing Administrative Costs

On average, it takes 160 hours to properly research and complete the necessary tasks to set up a foreign subsidiary —but that is just the beginning of the required time and legal cost.

There are both direct and indirect administrative costs that companies are responsible for throughout the lifetime of their entity.

Direct costs include everything legally required to keep an subsidiary compliant in the foreign market, such as;

- Yearly tax filings
- Monthly social security payments
- Running payroll
- Other necessary payments that are specific to that market

Indirect costs include the time and resources required to train internal legal, finance, business development, sales and marketing, operations teams to manage their tasks in a new country e compliant to avoid running afoul with the company which may affect the holding company directly and indirectly. Many companies have little to no experience with the local laws and regulations in their target market. Educating internal teams and keeping them up-to-date with changing legislation is an additional cost that firms must consider which are significantly reduced by having a local partner.

IV. Entity Teardown Fees

If a business chooses to leave a country where they have a legal entity, they must go through a lengthy process to officially tear it down. Dissolving an entity typically takes 3 times longer and costs 3 times more than the amount required to establish the entity.

This process is complex, and the dissolution costs and time commitments vary drastically from country to country. However, many costs come from completing necessary closing responsibilities, such as end-of-year compliance tasks, paying annual taxes, fulfilling severance requirements for employees, legal and much more.

In general, it is more expensive and time-consuming for companies in heavily regulated industries (such as banking), higher annual revenues, and a significant headcount to dissolve an entity.

V. Opportunity Costs

Setting up a foreign entity is time-consuming, and time lost in this extensive process leads to missed revenue opportunities. On average, it takes up to 4 to 6 months or more to establish an entity and begin operating in a new country. Companies must consider what they could lose during this time, such as revenue, or competition gaining traction in a market, taking away valuable customers.

Essential Considerations Before Establishing an Entity

Since entity establishment is a long, complicated, and expensive process, a natural question arises: How do I know if my company must establish an entity overseas or if I can seek other global expansion options?

Here are three important considerations that help businesses decide whether or not entity establishment is a viable option for them:

I. Companies That Must Hold Fixed Assets

If a firm is in the real estate or manufacturing industry, it must hold fixed assets, meaning most countries require an entity. If your business is within these industries, entity establishment is your only global expansion option.

II. Companies with an Extensive Budget

Setting up an subsidiary costs between $15,000 and $20,000 depending on the country, and around $150,000 - 200,000 per year to maintain, and this number changes based on a variety of factors. Establishing a subsidiary option is only suitable for companies that are ready to make a financial investment ideally with a local partner that may reduce those cost and mitigate many risks and obstacles during the start-up phase.

III. Companies Hiring a High Headcount

An organization that has a high headcount in one country with no legal entity raises concern with the government, as this indicates that a firm is potentially using misclassified foreign independent contractors.

Many countries charge severe financial and legal penalties for independent contractor misuse. Establishing an entity and legally hiring these workers as full-time employees is the most cost-effective way to ensure compliance with local laws and regulations.

Strategic Local Partner: A Cost-Effective and Flexible Option

Entity establishment of the subsidiary is a traditional global expansion method, but it is not a realistic choice for many firms looking for a more flexible alternative. The good news is that entity setup is no longer the only compliant option.

Companies that want to test foreign markets quickly, with less risk and a lower financial commitment, must partner with a Local Partner with strategic relationships including financing for the company to access to grow properly.

The benefits of Global Hills Group as a Strategic Local Partner:

I. Smaller Financial Commitment

Entity establishment is expensive and has many surprise costs along the way. Global Hills Group is 60% or more cost-effective compared to setting up a foreign subsidiary, and there are no additional costs associated with hiring permanent staff or entering other geographical locations within the country.

II. Quicker Setup Time

On average, it takes up to 4 – 6 months or more to establish an entity overseas. Global Hills Group enables companies to get up and running in as few as 3-4 days, which is ideal for short-term projects with tight deadlines or for time-sensitive global initiatives.

III. Flexibility to Test New Markets

Global Hills Group is an ideal option for companies looking to test a new market and determine if there is product-market fit customers and arrange financing including investments during the initial growth of the company.

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Learn More About What Global Hills Group can do for your Company

While entity establishment is a good option for companies, it is not the only way to compliantly enter foreign markets. Global Hills Group offers a multi-faceted approach for being a Strategic Local Partner to companies seeking to test their global expansion ambitions.

For more information about how Global Hills Group is a quicker and more cost-effective solution for your company's global expansion, contact:

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