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STRATEGY

Why Expat Entrepreneurs Shouldn't Incorporate Businesses Overseas

Don't make the mistake of incorporating your business overseas until you've read the four reasons you shouldn't.

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Today every business can be global; you can set up a website and sell products and services to anyone, anywhere. The increase in global mobility leads to some interesting questions, including, "Where should I incorporate?"

This question is tougher for US citizens and expat entrepreneurs than for those of most other countries because the US tax code is borderless, meaning US citizens are taxed by the IRS regardless of where they are located. Under the Tax Cuts & Jobs Act, the businesses owned by US citizens are now taxed irrespective of location, too. This makes the prospect of incorporating overseas significantly less attractive for US expat entrepreneurs.

So, why won't incorporating your business overseas save most expat entrepreneurs money?

1. Filing taxes and understanding the subtleties of a tax code in a foreign language can be a nightmare.

Not all of the popular countries for incorporation are English speaking countries -- take Hong Kong as an example. Trying to learn the rules, correspond with the local revenue department, and complete the required forms online can be extremely difficult and time-consuming. Even if the forms are translated, the translation may not be 100% clear. This can lead to mistakes or the need to consult with local tax experts which can be expensive.

2. The new Global Intangible Low Tax Income tax, or "GILTI tax," is an added complication.

Under this provision, corporate profits for Controlled Foreign Companies are deemed "GILTI" if they exceed a 10 percent return on depreciable, tangible assets owned by the company. These profits will be taxed in the US at the individual's tax rate, even if they are not distributed. What does this mean for business owners? A more complex US reporting requirement, plus you may not be able to defer taxes on your overseas corporate profits!

3. Overseas merchant discount rates can be very high.

Most US businesses will pay a merchant discount rate (the fee you pay to process credit cards) of about 2.9 percent plus $0.30. However, this can be more expensive overseas. Processing in Hong Kong will cost at least $3.9 percent plus $0.30.

If your customers are overseas, the price increases to 4.4 percent plus a fixed fee based on the currency received. Other countries have even higher starting merchant discount rates such as 5.4 percent in Belize, the Cayman Islands, and Panama. Losing an extra 2.5 percent of top-line revenue can have a big impact on your bottom line!

4. Hidden fees are everywhere.

Incorporating your business overseas can lead to all sorts of other fees, such as:

- Foreign exchange fees when moving money or paying people (about $50 per wire plus foreign exchange fees).
- Higher incorporation fees; for example, Belize's fee is $1,500, Cayman's $3,745, and Hong Kong's $2,875. Compare these to the cost to start a US LLC or C Corp which can be as little as $200.
- Annual Audit Fees, Annual Incorporation Fees, Registered Agent services, and more. These are all extra costs and filing burdens you may encounter if you incorporate overseas.

New expat entrepreneurs get excited about the idea of "corporate formation," and they spend a lot of time thinking about what type of corporate structure and where to incorporate. However, that time and energy would be better spent on perfecting their business product or service.

The time, money, and hassle are multiplied if you try to incorporate overseas. There is a chance you may save a bit of money on taxes (if you manage to not fall afoul of the international tax rules), but you will most certainly spend an excess of time, energy, and money dealing with tax rules.

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