

ESTABLISHING A BUSINESS LEGAL ISSUES IN THE UNITED STATES

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As you prepare to launch your Australian business in the United States, you will discover that the process can be very straightforward and efficient. A corporate attorney can assist you with the steps below to set up a wholly owned subsidiary of your Australian company, and the Australian company will become the 'Parent'.

FORM OF CORPORATION

Corporation

Corporations are the most common form of company that limits its investors' liability; they are most attractive to outside investors. In fact, US Venture Capitalists (VCs) are only able to invest in C Corps (not LLCs).

A Corporation is a separate taxable entity. As such, its earnings or losses are taxed at both the entity level and, to the extent any distributions are made, at the stockholder level.

Limited Liability Company (LLC) is simpler to operate from a corporate governance perspective than a C Corp. An LLC can be taxed as a partnership (taxed only at the investor level) or as a corporation.

Note: Please see the Taxation fact sheet in terms of the tax issues tied to selecting an entity.

STATE OF INCORPORATION

Delaware is the state of choice for many international companies to incorporate in because most US public companies are Delaware registered companies, US venture capitalists will only invest in Delaware companies, and Delaware has the most sophisticated and company-friendly corporate laws in the United States. A company incorporated in Delaware may be physically located in any US state and will be qualified to do business in the state where it is headquartered. More information on [incorporating in Delaware](#) is available from its website.

Australian companies that are not seeking venture capital funding and that intend to do business in one US state may choose to incorporate in the state where it locates its US headquarters. For example, see [California](#) and [New York](#).

ESTABLISH THE US SUBSIDIARY (THE 'SUB')

Establish your company with the following documents.



Australian Government

Australian Trade and Investment Commission



Corporation

A corp requires a Certificate of Incorporation filed in the applicable state, bylaws, and an initial written action by written consent of the board, and stock purchase agreement.

C corps can be established in less than a week if Delaware is selected; filing costs in each state vary, but are less than US\$1000.

LLC

An LLC requires filing a Certificate of Formation in the applicable state and that more than one member (LLC investor) enter into an LLC Operating Agreement.

Note: It is not necessary that any investor, officer or director of a Corp or an LLC reside in the US or hold a US passport.

HIRE YOUR US TEAM

This could include a board of directors, management team, advisors, employees and consultants.

Offer letters

US employment law starts out with the fundamental concept of employment 'at will', which means that you or your employee can decide to terminate the relationship at any time for any reason, so long as the US sub does not discriminate (please also see the Employment Practices fact sheet).

Confidential information and invention assignment agreements

For any tech or life science start-up these agreements, by which your employees or consultants agree to keep your information confidential and confirm your company has all the rights in the intellectual property employees and consultants work on, are essential to ensure that your US sub protects its confidential information and intellectual property.

Director and officer indemnification agreements

It is customary (but not required) for members of a US board of directors to receive a Director and Officer Indemnification Agreement to protect them. In the case of a US sub, this agreement would become more relevant at the time of a 'flip up' (see below).

COMMERCIAL AGREEMENTS AND IP LICENSES

US subs of Australian companies will have the opportunity to establish relationships with US customers and vendors, all of which will require carefully negotiated commercial agreements or intellectual property licenses. Your corporate attorney should be able to review the commercial or license agreements you use in Australia and revise them so they are enforceable under the law of the state where you are established or located.

MERGERS AND ACQUISITIONS

As your US business grows, you may decide to acquire other businesses by buying their assets or their stock (the method of acquisition is typically determined based on the tax outcome). Alternatively, you may decide to sell the US sub, or the Australian parent together with the US sub, to a US buyer.

See the buyer acquisition case study on the next page.

FLIP UPS

If you intend to raise money from US angels (individuals who are early investors) or US VCs you will need to enter into a flip up transaction. A flip up occurs when the US sub issues shares to the shareholders of the Australian parent in exchange for the Australian shareholders' shares in the Australian parent. The US sub becomes the new parent and the Australian parent becomes the wholly owned subsidiary. This permits a US investor to invest in a US (Delaware)

CASE STUDY – US buyer acquisition of Australian parent

Challenge

A Sydney mobile advertising company ('MobileAd'), with a successful Silicon Valley based Delaware subsidiary was approached by a large privately held US company: the US buyer proposed that MobileAd first go through a 'Flip Up' (see below) before the acquisition proceeded.

Action

The US based management team and its corporate counsel were tasked with convincing the US buyer, which had only acquired US companies in the past, that acquiring an Australian company would be fairly streamlined and would not delay the closing.

Outcome

Although initially reluctant to assume responsibility for a company governed by the laws of a foreign jurisdiction, MobileAd's team was successful in showing the buyer that Australia's sophisticated corporate laws and the fact that Australia and the United States both are founded on common law tradition would make a flip up unnecessary.

Take Away

US strategic buyers may be open to acquiring an Australian Parent and its US sub even though US VCs will require a flip up before investment.

company that holds all of the intellectual property in its Australian subsidiary.

RAISING FUNDS FROM ANGELS

Convertible debt or equity

A newly 'flipped up' US parent of an Australian sub can raise funds from US angels by issuing convertible debt or convertible equity to the angels (typically under US\$500,000).

Convertible debt issuances

Convertible debt issuances are a relatively inexpensive way to raise funds (through a typically simple convertible note). The company issues debt that converts to equity at the time a venture capitalist agrees to invest a designated amount at a specific valuation. Convertible debt issuances have the advantage of avoiding any further valuation of the company until the company is valued by a VC.

Convertible equity certificate issuances

Convertible equity certificate issuances are similar to convertible debt but represent a promise to issue equity in the future without burdening the company with debt.

RAISING VENTURE CAPITAL FUNDS

Assuming the US Parent has issued only common stock to the Australian investors during the flip up, the first issuance of preferred stock by your company will be to VCs and will provide the VCs with greater rights, preferences and privileges than the common stock. These rights typically include rights to receive proceeds in any liquidation event before the holders of common stock, dividends, anti-dilution rights and protective provisions allowing the preferred investors rights to make certain decisions about the company independent of the holders of common stock.

STOCK OPTION PLANS

Your new US parent is able to establish a stock option plan as a means to incentivise its employees and consultants (including members of the board of directors). This would customarily be one of the first steps it takes after flip up in order take advantage of the lowest valuation of the company in the US.

Among start-up companies, the vesting schedule for employees is customarily a four year vesting period: employees will vest (have the right to purchase shares in the company at a price determined at the time the options are granted) at a rate of 25 per cent of their option shares after their first year of service (called a one year 'cliff'), after which they will vest 1/48th each month in their option shares, with the possibility of accelerating that vesting schedule at the time their company is acquired.

Initial Public Offerings (IPOs)

IPOs are the ultimate liquidity event for a US company (and the end goal for US VCs if a sale of the company is not more lucrative).

DISCLAIMER

While care has been taken to ensure the information in this document is accurate, the Commonwealth of Australia represented by the Australian Trade and Investment Commission does not provide warranty or accept liability for any loss arising from reliance on such information.

Prepared by Montgomery Pacific
LLP www.montgomerypacific.com

Kathy Woeber Gardner, Partner
San Francisco, CA

Kathy@MontgomeryPacific.com