Legal entity rationalization

Optimizing your global organizational structure

The reality of global expansion

Companies are expanding to new territories at an ever-increasing rate, and global M&A activity is continuing to gain steam. However, with this wave of expansion comes an increased administrative and financial burden on international structures.

Mergers and acquisitions create the additional burden of multiple entities in countries, and countries with entities you no longer operate in. For each country, the legal entity must maintain constant monitoring to ensure it is always compliant from a legal and tax perspective. With ever-changing compliance requirements and regulations, each entity may take a different form, depending on what is best for the organization.

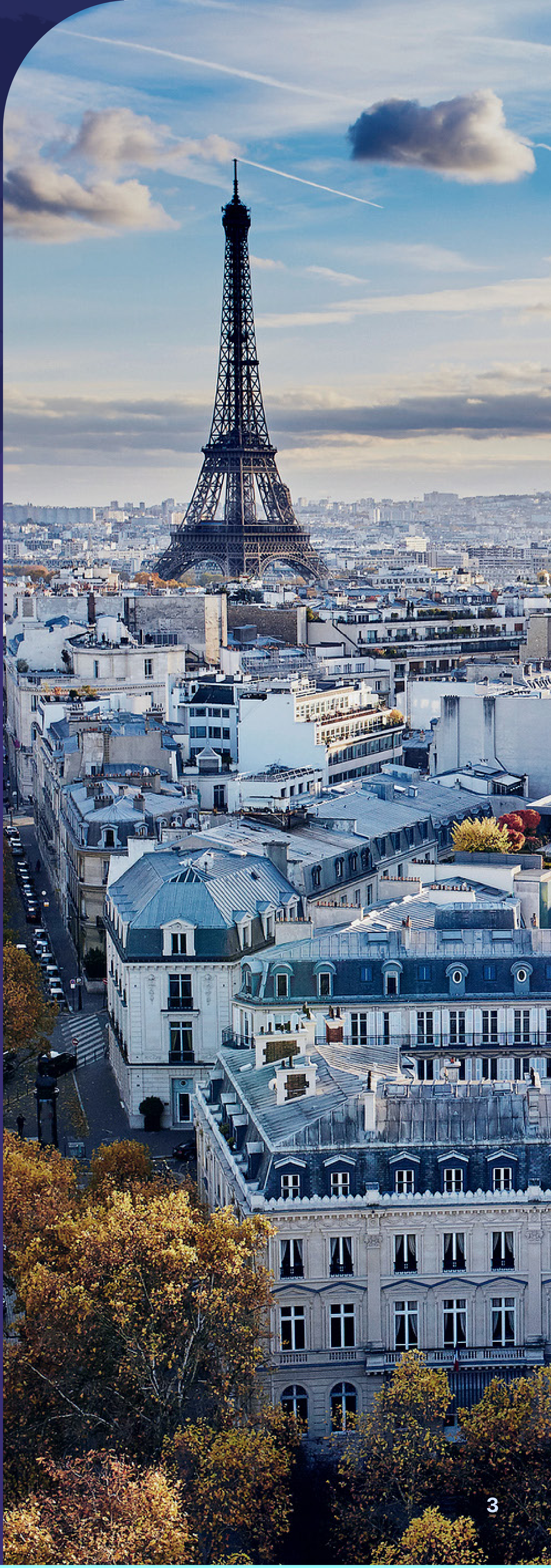
The more legal entities that exist, the greater the inherent risk due to the group structure. Experts in international subsidiary structures often recommend assessing these complex structures for potential legal entity rationalization on a consistent basis.

Understanding legal entity rationalization

With any legal entity rationalization, the focus is on reviewing your subsidiary structure to identify and resolve any conflicts and redundancies. This process creates a legal structure that is easier to manage and creates more effective international tax structures resulting in both cost and risk reductions.

It may also be called corporate simplification due to the reduction of legal entities. Typically, there are two ways to achieve legal entity rationalization. The first is to search for dormant entities to ensure a company is not spending unnecessary maintenance money. However, simply eliminating dormant entities does not usually result in large cost savings.

That is where some companies will take the second approach, which looks at the entire organizational structure to assess each entity. Whether you need an entity to support a small number of employees, or decide an employer of record solution might be more effective, rationalizing the structure by registering it as a foreign entity in the country is a must.



Why companies should consider legal entity rationalization

The difficulty of managing a subsidiary structure increases as a company grows globally, creating additional risk and liabilities. Without undertaking legal entity rationalization regularly, an organization can quickly face substantial costs and the threat of the legal entity not being in "good standing" with the local government. To illustrate this, we have outlined the three most common challenges large structures face.

Cost

Recurring services such as payroll, accounting, and tax and compliance obligations result in additional burden and cost regardless of the quantity of overseas employees.

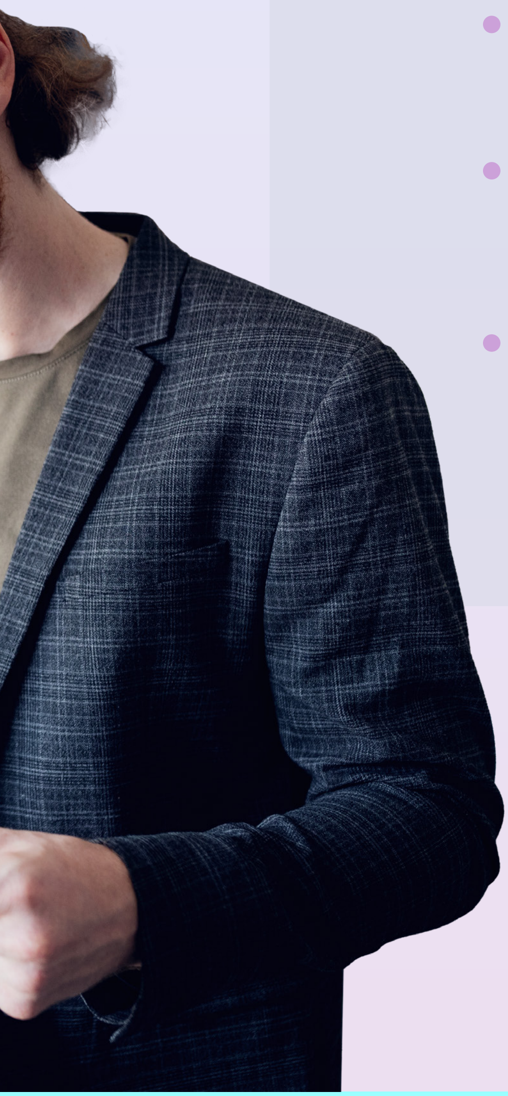
Risk

Every new legal entity is unique, and the organization must be prepared for a unique set of risks, which will grow as the group structure grows. As companies expand to new markets and create new entities, they must increase monitoring and management to reduce issues such as forgotten filings, missed new regulation and insider trading.

Resourcing

As a company expands, the challenge of resourcing becomes impossible to ignore. The compliance team often becomes overburdened or hiring more people onto the team becomes a must. One requires a larger budget, while the other can cause dissatisfaction among employees and a deterioration of control or governance.

Determining the core steps of legal entity rationalization



- Make sure to develop an accurate, real-time chart of the existing structure. Include all legal entities, types and locations.
- Understand the ownership structure, corporate governance and purpose of each legal entity. Document everything. It will enable your team to identify the role each entity plays on a local and global scale.
- Review each entity on the chart to identify any unnecessary elements. Determine the purpose, structure and legal format to decide if each entity is necessary.
- Make sure to run various scenario planning to develop mock entity diagrams for the possible new structures after the legal entity rationalization. This will give the organization a chance to review and ensure the proper alignment.
- Finally, an organization can determine targets for legal entity rationalization. Establish a budget, timeline and project plan to reduce any potential disruptions. This includes policy or procedural changes that need to occur prior and post rationalization.

Complexities of closing business operations

Businesses that decide to close operations in foreign countries will need to be aware of several important considerations, including:

- Repatriating employees to the home country
- Terminating facility or office leases
- Liquidating or moving office equipment and supplies
- Gathering and transferring all documents and data to headquarters
- Closing bank accounts and arranging for transfer of funds
- Ensuring local suppliers and vendors are paid for products or services prior to closing
- Liquidating capital investments, and obtaining funds
- Completing final payroll and tax steps, including required notices and fees

Depending on the country, businesses could experience significant delays and complications. Many countries have regulations and restrictions in place, such as preventing liquidation of investments and transferring funds out of the country. There may also be termination penalties in place for certain leases or contracts. If the company is not growing in a certain country but wants to continue operations or keep valuable in-country talent, it might make more sense to switch to an employer of record solution.

As a leader in global workforce solutions, Safeguard Global can help you evaluate and determine the best course of action for your rationalization initiative.

Speak with a global solutions advisor today to learn how our legal entity and EOR services can help you achieve your international growth goals.

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