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Crossing to Sell

The three separate US thresholds a foreign seller can cross, in what order they usually arrive, and what each one costs to comply with.

Selling into the United States: nexus, presence and the entity

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Selling into the United States: nexus, presence and the entity

Selling into the United States can create three different obligations that have nothing to do with each other: a federal income tax presence, a state income tax presence, and a state sales tax registration. Most companies cross the sales tax line first and notice it last.

Who this is for

- Canadian and other foreign companies with US customers, whether shipping goods, selling software or providing services.
- Founders deciding whether the US sales need a US entity at all.
- Finance teams who have had a US state registration letter arrive and want to know what triggered it.

Three thresholds, three regulators, no shared paperwork

The federal question is whether your activity in the United States amounts to a taxable presence — a permanent establishment, under the treaty, or a trade or business under domestic law. A treaty raises the bar meaningfully for a resident of a treaty country, which is why the same activity can be taxable for a company from one country and not another.

The state income tax question is separate and is not governed by the treaty at all. States apply their own nexus standards, and a state can assert an income or franchise tax filing obligation on facts that do not create a federal permanent establishment. This surprises almost every company that discovers it.

The sales tax question is separate again. It is a transaction tax collected from the customer, and economic thresholds mean a purely remote seller with no people or property in a state can be required to register, collect and remit there. Marketplace rules can shift that duty to the platform for platform sales while leaving your direct sales with you.

What actually creates a permanent establishment

A fixed place of business in the United States is the obvious case: an office, a warehouse you control, a workshop. The less obvious cases are the ones that catch growing companies — an employee working from a US home who habitually concludes contracts, a dependent agent with authority to bind you, a project delivered on a customer site over a long enough period, or equipment installed and operated by you.

The distinctions are factual and they are decided on how things actually work rather than on what the contract says. A sales representative who negotiates but cannot commit is treated differently from one who signs. A subsidiary is a separate person, but a subsidiary whose premises and staff are effectively at the parent's disposal can still create a presence for the parent. Our page on permanent establishment riskworks through the fact patterns.

Where a treaty position is being relied on to say there is no permanent establishment, that position is often disclosed on a filed US return rather than asserted silently by not filing. A protective filing that discloses the position is a very different posture from an absence of filings.

The entity question, and why "just set up an LLC" is bad advice

The right structure depends on where the profit should be taxed, who owns it, and what the two systems each do with the vehicle. A US limited liability company is the standard local answer and one of the worst available answers for many Canadian owners, because the two countries can characterise it differently and the mismatch can strand foreign tax credits. Our page onwhy a Canadian should rarely own an LLCexplains the mechanism.

A branch — selling directly, with no US entity — is often the right first step for a company testing the market, and it keeps the structure simple while volumes are small. A corporation is usually right once there are US staff, US contracts and a need for local credit or credibility. Whether to hold it directly or under a holding company is a separate decision driven by exit plans and dividend flows.

Whatever the answer, the entity comes with its own annual filings, and a foreign-owned US entity has additional information reporting that applies even in a loss year with no activity worth mentioning. Those filings carry per-form penalties, so the maintenance cost of a structure is part of choosing it.

Withholding on payments, in both directions

Once there is money moving between the group and the United States, withholding enters. Payments of US-source income to a foreign person are generally subject to withholding at a statutory rate unless a treaty reduces it, and the reduction is claimed by giving the payer a completed certification form before payment — not by asking for a refund afterwards.

The same applies in reverse when a US entity pays a foreign affiliate for services, royalties or interest, and the character of the payment determines the rate. Getting the certification into the payer's hands early is one of the highest-return administrative tasks in the whole expansion, because recovering over-withheld tax by return is slow.

The expansion sequence that avoids surprises

In this order, because each step changes the answer to the next.

1. **Map the actual activity, not the plan** Where are people, where is inventory, who signs contracts, where is the work performed, and which states do customers sit in. This single page of facts drives every threshold test that follows.
2. **Test federal presence and treaty position** Decide whether the activity creates a permanent establishment, and if the answer is no, decide how that position will be documented and disclosed.

3. **Run the state income nexus review** State by state, on the same facts. States differ, and the answer for one is not the answer for its neighbour.
4. **Run the sales tax review** Economic thresholds by state, marketplace rules for platform sales, and the taxability of what you actually sell — which for software and services varies by state.
5. **Choose the entity, if one is needed** Branch, corporation, or a holding structure, decided on the tax outcome for the owners and on the annual filing burden each choice carries.
6. **Register, certify and set the calendar** Employer and tax registrations, withholding certifications in the payers' hands, and a compliance calendar covering federal, state income and sales tax filings.

Papers to gather

What a US expansion review is built from:

- A customer list by state with revenue and transaction counts for the last two years.
- A description of what is sold, in enough detail to test taxability by state.
- Contracts with US customers, and any US agent or representative agreements.
- Employment or contractor arrangements for anyone performing work in the United States.
- Details of US inventory, equipment or leased space, however small.
- Group structure chart with ownership percentages and countries of residence.
- Any US registrations, tax identification numbers or notices already received.
- Intercompany agreements for anything the group already charges between entities.

Where it goes wrong

- **Treating the treaty as covering everything** It addresses federal income tax. It does not stop a state asserting income tax nexus and it has nothing to do with sales tax, which is where most remote sellers first become non-compliant.
- **Forming a US LLC because the bank suggested it** The vehicle can be read differently by each country, and the mismatch can leave foreign tax credits unusable. The right vehicle depends on who owns it and where they are resident.
- **Ignoring the information returns in a loss year** Foreign-owned US entities carry information reporting that applies regardless of profit, and the penalties are per form and per year rather than a percentage of tax.

Questions this raises

Do I need a US company to sell to US customers?

Often not, at least at first. Selling directly from your existing company is a legitimate structure and it keeps the compliance load low. What decides it is whether you have people, premises or contract authority in the United States, and what your customers require of you commercially.

If the treaty says no permanent establishment, do I still file in the US?

Usually yes, as a protective and disclosing filing. A treaty position that reduces or removes US tax is a position taken on a return, and the difference between disclosing it and simply not filing is significant if the question is ever asked.

Does the treaty protect me from state taxes?

Generally no. States are not bound by the federal treaty in the way the federal government is, and several assert income or franchise tax on facts that would not create a federal permanent establishment. The state review has to be done separately.

We sell software remotely with no US staff. Are we really exposed?

For federal income tax, possibly not. For state sales tax, very possibly yes: economic thresholds mean revenue or transaction volume alone can create a duty to register and collect, and how software is taxed differs from state to state.

What to do next

Start with the activity map and the state review — they are quick, they are cheap, and they tell you whether the entity question is urgent or can wait a year. Companies that do this before their first US hire almost never need a remedial project later.

We run the expansion review, the nexus study and the setup as one fixed-fee engagement, agreed in writing before work starts. The expanding from Canada to the USpage covers the whole path, and thestate nexus review fee pageshows what that piece costs.

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