

**"Winning Business Strategies"
Webinar Series**



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**"Winning Business Strategies"
Webinar Series**



**Doing Business
Beyond Your State Line**

Making Certain the Rules are not "Foreign" to You

Presented by:

Gale S. Finley & Geoffrey A. Frazier



Join us as Gale and Geoff discuss what to look for and how to avoid unwanted surprises when going into other states to transact business, and much more.

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Doing Business Beyond Your State Line

Do you own or operate a "foreign" corporation or limited liability company?

- The answer is, unequivocally, "Yes."
- Your company is a "domestic" company in one state and is a "foreign" company in the other 49 states.
 - A company is a "domestic" company only in the state in which it was organized (i.e., the state in which the Articles were filed).
 - It is considered a "foreign" company in every other state.



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What if my company started operations in Ohio, has exclusively operated here, has Ohio owners, but the Articles were filed in another state?

- Again, a company that was organized in one state is a "foreign" company in every other state
- A corporation owned by Ohio residents, that conducts all of its business in Ohio, but that filed its Articles of Incorporation in Delaware is a foreign corporation in Ohio



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What is the significance of being a "foreign" company?

- Every state has statutes relating to foreign companies obtaining authority to **transact business** in that state
- No worries if you are not transacting business in the state
 - The company is still considered a foreign company in that state, but the registration rules only relate to foreign companies that are within that state transacting business



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What is the basis for such inhospitable treatment?

- The rationale is that if a foreign company is going to transact business in that state, it needs to fulfill the same requirements as domestic companies
 - e.g., register with the Secretary of State, appoint a registered/statutory agent, report names of officers, file annual reports, etc.

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How do I know if I am "transacting business" as a foreign company in another state?

- Each state has its own specific rules
 - It is usually a case-by-case determination based upon the specific conduct of the foreign company
- Using Ohio, as an example, a foreign company is considered transacting business if it enters the state using agents (e.g., employees) to conduct its usual business in a continuous manner.
- Having a physical presence (e.g., offices) is usually a factor.

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Do I need to worry about registering as a foreign company if, for example, I make Internet sales to customers in other states or have independent sales reps in other states?

- Probably not
 - The rules generally do not apply to business conducted in interstate commerce
 - Many states have a list of what is **not** transacting business in that state. Common examples are:
 - Being involved in court proceedings, holding meetings, maintaining bank accounts, selling through independent contractors, soliciting or obtaining orders if acceptance out of the state is required, collecting debts, owning property, etc.

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What are the registration requirements for a foreign company?

- Depends on the state
 - The statutes of each state in question must be researched
 - Usually the foreign company must provide the same kind of information that a domestic corporation must provide



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What are the requirements for a foreign corporation in Ohio?

- File an application
 - Name of corporation
 - State of incorporation
 - Address of principal office
 - Appointment of a designated agent (resident of Ohio)
 - Provide a summary of the corporate purposes
- Submit a Certificate of Good Standing from the state of incorporation



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What happens if I don't jump through those hoops?

- The consequences of failing to register vary from state to state.
 - The typical consequence is that the foreign company may not take advantage of that state's courts (to bring an action or defend an action).
 - Some states give the Attorney General the right to enjoin the foreign company from transacting business within the state
 - Usually a civil penalty may be assessed
 - Often it is the amount that the company would have paid over the period it should have been registered, plus penalties and interest
 - Sometimes the penalty is a multiple of that amount (e.g., X 3) and sometimes additional amounts are tacked on



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Is that the best they got? Sounds fixable if I get caught.

- Maybe. But it may take time to prepare filings for the period of non-compliance. How quickly do you need to get to court to protect the company?
- Other parties doing business with you may care whether you are legally compliant.
- Keep in mind that if you plan to sell your company, the buyer is likely to require a representation and warranty that the company is qualified to transact business in each state in which is required to register. How long do you want to hold up the sale while you scramble to get qualified?



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There could be worse penalties.

- In Ohio, an officer who transacts business on behalf of a foreign corporation that has not obtained a license to transact business in Ohio (assuming that it is required to obtain a license) is guilty of a fourth degree misdemeanor.
 - Not to worry, though. The fine for a fourth degree misdemeanor is capped at \$250 and the jail term cannot exceed 30 days. Of course, there is that little thing about having a criminal record.



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Final thought:

- Legal compliance is usually the best course of action.
 - Compliance usually is more cost-effective than trying to remedy non-compliance.
- Find out what the state requires and obtain the necessary authority to transact business in that state.



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Activities That Can Establish Nexus:

- Physical location:
 - Sales office
 - Corporate headquarters
 - Production facility
 - Warehouse
- Property:
 - Inventory stored in a warehouse
 - Property at a customer's place of business (example: consignment inventory)
 - Property at a contract manufacturer location



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Activities That Can Establish Nexus:

- Employees in the state:
 - Sales representatives
 - Employees at a customer location
- Solicitation of sales:
 - "Regular and systematic" solicitation
 - Frequency or length of visits
- "Amazon" nexus
 - Applies to online sellers collection of sales/use tax
 - Introduced in about half of the states
 - Adopted in seven states



Doing Business Beyond Your State Line

Public Law 86-272

- A state **cannot** impose a **net income tax** on out-of-state companies if **all** of the following 4 conditions are met:
 - The out-of-state company's **sole** business activity is solicitation;
 - The out-of-state company solicits orders for sales of **tangible personal property**;
 - The orders are sent out of the state for approval or rejection; and
 - The orders are filled outside of the state.



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Public Law 86-272

- Solicitation requirement
 - Solicitation defined:
 - Speech or conduct that invites an order, or
 - Activities that are "entirely ancillary" to requests for an order. "Entirely ancillary" activities are those that serve no independent business function apart from their connection to the solicitation of an order.
 - Solicitation plus other in-state activities:
 - The out-of-state company may still be protected by PL 86-272.
 - In-state activities will only create tax liability if they result in a "nontrivial additional connection" with the state.

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Doing Business Beyond Your State Line

Public Law 86-272

- Activities Not Protected by PL 86-272:
 - Solicitation or other activities related to:
 - Sale or delivery of services other than those services ancillary to solicitation of TPP;
 - Leasing, renting, licensing tangible personal property;
 - Transactions related to the use of intangible assets (i.e. royalties, franchise fees, etc.);
 - Installation, repairs, or maintenance to the tangible personal property sold; etc.

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Nexus – Non Income Taxes

- Sales Tax
 - Physical presumably presence still required
 - *National Bellas Hess v. Dept. of Revenue of the State of Illinois*, 386 US 753 (1967)
 - *Quill Corporation v. North Dakota*, 112 S.Ct. 1904 (1992)
 - "Amazon" nexus for online sellers
- Other Taxes (Gross receipts, Capital stock, Margin)
 - Economic presence?
 - Exploitation of the market?

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