

Foreign Entities Should Get Acquainted With State Rules

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Many foreign business entities, both corporations and limited liability companies (LLCs), transact business in California. It is important for these foreign entities to be aware of statutory requirements that must be met to transact business in California because severe penalties attach for non-compliance. This article discusses compliance with Corporations Code and Revenue and Taxation Code requirements.

A foreign business entity is one that was formed in a jurisdiction other than California. Foreign entities typically transact intrastate business in California under the following circumstances: 1) an entity may be initially formed in another state because that is the state where the business activity originated and the company expands into California, or 2) in the case of a business that originates in California or that exists exclusively in California, principals may form the entity in another state, such as Nevada or Delaware, to take advantage of certain tax laws or anonymity protections offered in that jurisdiction.

To determine which requirements must be met by a foreign business entity, it must first be determined whether that entity is transacting intrastate business.

The California Corporations Code defines “transacting intrastate business” as “entering into repeated and successive transactions of its business in this state other than foreign or interstate commerce.” The statutory definition does not include maintaining a bank account in California, holding board meetings in the state, maintaining a California office the sole purpose of which is to transfer or register the company’s securities, selling products or services through independent contractors, offering sales by mail where acceptance of the offer must take place outside of California, creating evidence of debt or security on real property, or entering into an isolated transaction that is completed in fewer than 180 days.

The California Secretary of State monitors the identity of business entities and makes certain information pertaining to those entities available to the public. When a California business entity is formed, it must file its original registration document (i.e. Articles of Incorporation or LLC-1) with the Secretary of State. This filing puts the state and the public on notice of the company’s existence and triggers the necessity to file an annual statement, listing whether the company is publicly traded, the identity of officers and directors of a corporation, managers of an LLC, and general partners of a limited partnership, as well as the name and address of the agent for service of process. Foreign business entities that plan to engage in activities which fall under the statutory definition of transacting intrastate business in California must provide the same information to the Secretary of State.

Foreign corporations and LLCs that transact intrastate business must first obtain a Certificate of Qualification to do business in California and file an Annual Statement of Information with the Secretary of State. This process is akin to the initial filings that bring a domestic entity into existence. To obtain a Certificate of Qualification to do business in California, the foreign entity must provide a Certificate of Good Standing from the state in which the entity was formed to ensure that all of that

state's legal requirements have been met. This ensures that the entity has been properly filed in its home state and that it has paid all required taxes. The foreign entity must then file a Statement of Information so that the public can identify the business' officers and directors, or managers in the case of an LLC, and its agent for service of process in California. One of the primary reasons that this information is required and is made public is that personal service of summons and complaint is mandatory when a lawsuit is filed. The identity of the agent for service provides the members of the public knowledge regarding whom to serve.

If the entity is doing business under a name other than the corporate or LLC name, it must also file a fictitious business name statement in every county in California in which business is conducted. This filing provides potential plaintiffs a paper trail so that the agent for service can be identified. The Fictitious Business Name is filed with the corporation or LLC as its owner. This way the public can track down the agent for service of process in case the need arises.

Penalties for failure to file the mandatory documents with the Secretary of State include daily fines, misdemeanor charges, and the entity may be prevented from maintaining a lawsuit in California.

The Revenue and Taxation Code articulates certain requirements which must be met by foreign entities transacting intrastate business in California as well. Such companies must pay state income tax on all revenues earned in California, and like domestic entities, they are required to pay a minimum franchise tax for the privilege of doing business in California. All such state taxes are paid to the Franchise Tax Board.

Minimum franchise tax requirements differ depending upon the type of entity and the year it was formed. A new corporation that qualifies to do business in California after January 1, 2000, and that estimates its gross receipts to be less than \$1,000,000.00 must pay \$800 annually to the Franchise Tax Board beginning the second year that it is qualified in California. A Foreign LLC must pay a minimum of \$800.00 annually when it first qualifies to do business in California and annual franchise tax based on California's graduated schedule every year thereafter. The graduated tax on LLCs is based on gross revenues and tops out at \$11,790.00 for LLCs grossing over \$5,000,000.00 annually.

Penalties for failure to pay mandatory franchise taxes include daily fines and parties may void any contracts entered into with the non-complying company.

Foreign entities can prosper in California and contribute to this state's economy as long as they pay the proper taxes and are appropriately registered with the Secretary of State. It is important to evaluate, first whether the entity is in fact transacting intrastate business and if so, to comply with Corporations Code and Revenue and Taxation Code requirements.