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## WORK-FROM-HOME WORKFORCES TRIGGER FOREIGN QUALIFICATION AND LOCAL OFFICE QUESTIONS



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Even before COVID-19 forced businesses to close their offices and send employees home to work, there was a shift in how businesses were deciding to operate. No longer does the automatic response to starting a business include leasing office space to which the employees commute each day and from which business is conducted. Technology has made it possible for companies to save all that money on rent, utilities, taxes, and other expenses associated with a physical location and instead have their employees work from home.

When the employer with a “work-from-home” workforce is a statutory business entity such as a corporation, limited liability company, limited partnership, or limited liability partnership — whether for-profit, not-for-profit, or professional service — it may have to deal with uncertainties that it may not have to deal with if it had the traditional brick and mortar office from which all workers worked.

One of these uncertainties is whether it will be considered doing business in those states other than its formation state where its employees are living and working. If it is transacting intrastate business in these so-called “foreign” states, it will be required by the foreign state’s business entity statute to qualify to do business — which could be an unanticipated expense for the employer. In contrast, when business is conducted from a physical location in a foreign state, the need to qualify is easier to anticipate.

Another issue is how does a statutory entity answer questions on the forms it must file with the Secretary of State that ask for an office location when it has no physical office.

This article will address these two quandaries. It describes one method of determining whether a corporation, LLC, or other statutory entity is doing business for foreign qualification purposes in states in which its employees are living and working. It will also discuss the options when a form asks for an office address, and suggests a solution to that problem.

It should be noted that the term “employee”, as used in this article, also includes other natural persons through which artificial persons act — such as a corporation’s sole shareholder, an LLC’s member, or an LP or LLP’s partner — who may not technically be employees.

It should also be noted that the determination of whether any particular statutory entity is doing business for foreign qualification purposes is a legal determination and depends upon the facts of each specific situation. This article discusses general concepts and should not be considered as providing legal advice as to whether any specific statutory business entity would be considered doing business.

*continued on page 2*

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## WHY DOES IT MATTER IF A STATUTORY ENTITY IS DOING BUSINESS IN A FOREIGN STATE?

In order to transact business in a foreign state, statutory entities are required by the foreign state's business entity statute to qualify – that is, to obtain the state's authorization.

A statutory entity doing business without authority is subject to penalties that can be severe. There are monetary penalties for the entity, and under some statutes, for the people doing business on its behalf. Additionally, it will not be able to maintain an action in the courts of the state until it is properly qualified.

## HOW DO YOU DETERMINE WHAT CONSTITUTES DOING BUSINESS?

The trigger for the foreign qualification requirement is the corporation, LLC, LP, or LLP transacting business in the state.

Determining whether a statutory business entity is transacting business in a foreign state is more art than science. The business entity statutes do not have bright-line rules like you might see in, for example, a sales tax law – which requires registration based on a threshold number of transactions or amount of revenue in the state.

Furthermore, the courts that have dealt with the “what constitutes doing business” issue have not provided bright-line rules either. One frequently cited definition of doing business comes from the Alabama Supreme Court, which stated: “it is established by well-considered general authorities that a foreign corporation is doing, transacting, carrying on, or engaging in business within a state when it transacts some substantial part of its ordinary business therein”. *Royal Insurance Co. v. All States Theatres*, 242 Ala. 417, 6 So.2d 494 (1942).

## A THREE-STEP METHOD OF ANALYZING THE “DOING BUSINESS” ISSUE

So how can you determine if a corporation, LLC, LP, or LLP is doing business in a foreign state based on the activities of its local, home-based employees? One helpful technique is to use the following three-step plan of attack.

### Step 1: Consult the qualification provisions

The first step is to consult the qualification provisions of the foreign state's business entity statute. The approach of these

statutes is not to set forth the activities that do constitute doing business, but instead to have a list of activities that do not constitute doing business. If the activities that the employees are doing on behalf of their employer fall solely into these exempted activities, the employer probably would not be considered doing business there.

### Step 2: Consult case law precedent

The next step would be to consult the case law precedent on the issue of what constitutes doing business for foreign qualification purposes.

There is a fairly large body of case law on the issue. Often, the court's determination comes down to whether the foreign statutory entity has “localized” its operations in the state. If so, qualification is likely to be required. However, if the activities are just incidental to its interstate activities qualification is likely not to be required.



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### Step 3: Analyze activities of employees in foreign states

The third step would be to analyze all of the in-state activities of the employees in the foreign state. Then, keeping in mind the statutory provisions and case law principles, make the determination of whether the statutory entity is doing business in the state based on what those employees are doing for their employer.

It can be helpful to ask certain questions which help focus on the issue of whether the employees' activities are localized. These questions could include, but would not be limited to the following:

- ▶ What is the business entity's purpose in the state and how vital are the in-state employees to accomplishing that purpose?
- ▶ What percentage of the business entity's overall sales or revenue comes from the activities of the in-state employees?

*continued on page 3*

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- ▶ Are the employees meeting with customers or clients in person in the foreign state?
- ▶ Are the employees entering into contracts or soliciting orders that are approved in the foreign state?
- ▶ Are the employees' activities incidental to otherwise interstate business transactions?

### **WHAT IS THE OFFICE ADDRESS OF A COMPANY WITH A WORK-FROM-HOME WORKFORCE?**

The application for authority that is filed in many states to qualify a statutory entity asks for the principal office address of the entity in that state. If the business entity does not have a physical location, how does it answer that question?

Business entities may try various options. They might provide an employee's address, or state that there is no office, or provide a post office box or virtual office address, or the address of their registered agent. However, unless the form

explicitly states what is being asked for, the entity cannot be sure it is providing an acceptable answer. And this is not only a problem for entities completing an application for authority. It can be a problem when completing any document filed with the Secretary of State that requests a street office address.

A better option would be for the document itself, or the instructions, to more clearly define what kind of address the filing office is looking for and explicitly state how an applicant without a physical office can answer the question.

### **CONCLUSION**

An increasing number of employers are shifting to a "work-from-home" workforce. And among the issues this business model raises is whether they are considered to be transacting intrastate business based on the activities of their "work-from-home" employees and how to complete the application for authority or other documents that ask for a place of business in the state.