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QUALIFICATION REQUIREMENTS FOR FOREIGN CORPORATIONS: THE NEED FOR A NEW DEFINITION OF "DOING BUSINESS" BASED ON IN-STATE SALES VOLUME

All states require foreign corporations¹ to register with state authorities before they may carry on business in the state.² These qualifications³ statutes require that corporations "doing business"⁴ in the state must pay licensing fees, report certain information, or submit to other forms of regulation. The statutory definition of "doing business,"⁵ therefore, is important to

¹ A corporation doing business in one state though chartered or incorporated in another state is a "foreign" corporation as to the first state. 17 FLETCHER CYCLOPEDIA OF THE LAW OF CORPORATIONS § 8290 (1977) (hereinafter FLETCHER).

² Many states have separate but similar registration requirements for non-profit corporations. See, e.g., ILL. REV. STAT. ch. 32, § 163a66 (Smith-Hurd 1970).

³ "Qualification" is distinct from "domestication." Qualification refers to the licensing or regulation of a foreign corporation without an attempt to change its status. Domestication is sometimes synonymous with qualification. See, e.g., OKLA. STAT. ANN. tit. 18, § 1.201 (West 1951). Domestication, however, sometimes refers to the re-incorporation of a foreign corporation which is available as an alternative to qualification. See, e.g., NEB. REV. STAT. § 21-20.122 (1943).

⁴ "Doing Business" is the expression utilized in the statutes of many states. See, e.g., KAN. STAT. ANN. § 17-7301 (1974); N.Y. BUS. CORP. LAW § 1301 (McKinney Supp. 1978-79). Section 106 of the MODEL BUSINESS CORPORATION ACT and other statutes use the term "transacting business." See, e.g., CONN. GEN. STAT. § 33-397 (1958); GA. CODE ANN. § 22-1401(b) (1977). A variety of other expressions are used in qualification statutes: "engaging in business," see, e.g., ALA. CODE tit. 10-2-250, § 90(a) (1977); OKLA. STAT. ANN. tit. 18, § 1.199 (1951); S.D. COMPILED LAWS ANN. § 47-8-2 (1967); "carrying on business," see, e.g., HAW. REV. STAT. § 174-7.5 (1976); "commencing business," see, e.g., NEV. REV. STAT. § 80.010 (1977); "conducting affairs," see, e.g., TENN. CODE ANN. § 48-1101 (1979); W. VA. CODE § 31-1-49 (Supp. 1979).

Courts are divided over the question of whether the expressions "doing business" and "transacting business" are equivalent. Compare *General Conference of Free Baptists v. Berkey*, 156 Cal. 466, 105 P. 411 (1909) and *Griffin v. Implement Dealers' Mut. Fire Ins. Co.*, 62 N.D. 21, 241 N.W. 75 (1932) (same meaning) with *People v. Montreal & B. Copper Co.*, 40 Misc. 282, 81 N.Y.S. 974 (Sup. Ct. 1903) and *S.R. Smythe Co. v. Forth Worth Glass & Sand Co.*, 105 Tex. 8, 142 S.W. 1157 (1912) and *Nagle Motors, Inc. v. Volkswagen N. Cent. Distrib., Inc.*, 51 Wis. 2d 413, 187 N.W.2d 374 (1971) (different meanings).

⁵ The issue of the level of contacts necessary to constitute "doing business" for qualification purposes should not be confused with the separate questions of the level of con-

entrepreneurs whose operations affect states other than their home state, or who are considering expanding their business to other states. Efficient marketing decisions require that the statutory definition of "doing business" be susceptible to easy and precise determination. The definitions of "doing business" in present statutes, however, make it impossible in many situations to decide whether a corporation is "doing business" in a foreign state. Imposing qualification requirements under these uncertain conditions makes business decisions to expand into other states unnecessarily difficult.

A change in existing model legislation is needed to remedy the ambiguity and uncertainty of current law. Part I of this article examines the mechanics of the present qualification system, paying special attention to the problems created by a multiplicity of vague state standards. Part II discusses the historical justification and purposes of the present system, concluding that only the protection function justifies the continued existence of the system. Finally, Part III proposes that "doing business" be defined in terms of the annual volume of in-state sales. This solution would remedy the problems which plague the present system while furthering the legitimate protection function of the state qualification requirements.

I. THE PRESENT SYSTEM

Present state qualification statutes often fail to indicate clearly whether a foreign corporation must qualify. The decision whether or not to qualify, moreover, involves considerable risk: a court may later determine that the corporation in fact conducted business in the state, and thus impose sanctions.

A. *The Mechanics of Qualification: Procedures and Penalties*

Section 106 of the Model Business Corporations Act⁶ (MBCA) provides that a corporation shall not have the right to transact business⁷ in the state until it procures a certificate of authority from the Secretary of State. MBCA Section 106 does not define

tact necessary for either the assertion of personal jurisdiction, or for the imposition of taxes by a state. See note 60 and accompanying text *infra* (qualification and personal jurisdiction); note 68 and accompanying text *infra* (qualification and taxation).

⁶ 2 MODEL BUSINESS CORPORATION ACT § 106, (2d ed. 1971 & Supp. 1977).

⁷ See note 4 *supra*.

“transacting business,” but does provide a “safe harbor”: a non-exclusive list of business activities which, alone or together, do *not* constitute transacting business in the state.⁸ Even in the states which have adopted section 106⁹, business activities not listed in the safe harbor provision present a major source of uncertainty. Most states, however, have either failed to adopt the “safe harbor” section without alteration or decided to omit it altogether.¹⁰ Thus, the resolution of many qualification cases de-

* The second paragraph of MBCA § 106 states:

Without excluding other activities which may not constitute transacting business in this State, a foreign corporation shall not be considered to be transacting business in this State, for the purposes of this Act, by reason of carrying on in this State any one or more of the following activities:

- (a) Maintaining or defending any action or suit or any administrative or arbitration proceeding, or effecting the settlement thereof or the settlement of claims or disputes.
- (b) Holding meetings of its directors or shareholders or carrying on other activities concerning its internal affairs.
- (c) Maintaining bank accounts.
- (d) Maintaining offices or agencies for the transfer, exchange and registration of its securities, or appointing and maintaining trustees or depositories with relation to its securities.
- (e) Effecting sales through independent contractors.
- (f) Soliciting or procuring orders, whether by mail or through employees or agents or otherwise, where such orders require acceptance, without this State before becoming binding contracts.
- (g) Creating evidences of debt, mortgages or liens, on real or personal property. (Changed in 1973 to read: Creating as borrower or lender, or acquiring indebtedness or mortgages or other security interests in real or personal property.)
- (h) Securing or collecting debts or enforcing any rights in property securing the same.
- (i) Transacting any business in interstate commerce.
- (j) Conducting an isolated transaction completed within a period of thirty days and not in the course of a number of repeated transactions of a like nature.

2 MODEL BUS. CORP. ACT ANN. 2d § 106, 2d Par. ¶ 1 (1971 & Supp. 1977).

* Among the states with definitions not modeled after MBCA § 106, several employ an abbreviated list of activities: ALA. CODE §§ 10-2-250, 10-2-256, 10-2-273 (1977); DEL. CODE ANN. tit. 8, §§ 371, 373 (Supp. 1978); D.C. CODE ANN. § 29-933 (1973); KAN. STAT. ANN. § 17-7303 (1974); OHIO REV. CODE ANN. §§ 1703.02, 1703.03 (Page 1978); NEV. REV. STAT. §§ 80.010, 80.240 (1979); VT. STAT. ANN. tit. 11, § 2101 (1973).

The definitions in the other states employ no list at all: ARK. STAT. ANN. § 64-1201 (Supp. 1979); ILL. ANN. STAT. ch. 32, § 157.102 (Smith-Hurd 1954); IND. CODE ANN. § 23-1-11-1 (Burns Supp. 1978); MINN. STAT. ANN. § 303-03 (West 1969); N.H. STAT. ANN. § 300:3 (Supp. 1979); OKLA. STAT. ANN. tit. 18, § 1.199 (West 1953); S.D. COMP. LAWS ANN. § 47-8-1 (1967); VA. CODE § 13.1-102.1 (1978); WYO. STAT. ANN. § 17-1-701 (1977).

¹⁰ Statutory definitions modeled after MBCA § 106 include the following: ALASKA STAT. § 10.05.600 (1968); ARIZ. REV. STAT. ANN. § 10-106 (West 1956); CAL. CORP. CODE ANN. § 2105 (Deering Supp. 1980); COLO. STAT. ANN. § 7-9-101 (Supp. 1979); CONN. GEN. STAT. ANN. § 33-397 (West 1958); FLA. STAT. ANN. § 607.304 (West 1977); GA. CODE ANN. § 22-1401 (1977); HAW. REV. STAT. § 418-6 (1976); IDAHO CODE § 30-1-106 (Supp. 1980); IOWA CODE ANN. § 496A.103 (West Supp. 1980-81); KY. REV. STAT. § 271A.520 (Supp. 1980); LA. REV. STAT. ANN. § 12:302 (West Supp. 1980); ME. REV. STAT. ANN. tit. 13-A, § 1201 (West. 1964 & Supp. 1980); MD. CORP. & ASS'NS CODE ANN. § 7-103 (1980-81);

pends upon judicial construction of "doing business" or similar phrases.¹¹

State qualifications impose upon a business both direct and indirect costs. First, foreign corporation laws typically provide for a fee to be paid when applying for a certificate of authority to do business. In some states, this is a flat "filing fee."¹² Other states impose a "license fee" based upon the amount of the corporation's capital located in the state.¹³ Second, state qualification schemes often impose annual taxes. Some of these assessments are referred to as "license fees" and are generally fixed in amount.¹⁴ Others are labeled "franchise taxes"; these assess-

MASS. ANN. LAWS ch. 181, § 3 (Michie/Law Co-op 1977); MICH. STAT. ANN. § 21.200 (1012) (Supp. 1979); MISS. CODE ANN. § 79-3-211 (1972); MO. ANN. STAT. § 351.570 (Vernon Supp. 1980); MONT. REV. CODES ANN. § 35-1-1002 (Supp. 1979); NEB. REV. STAT. § 21.20,105 (1977); N.J. STAT. ANN. § 14A:13-3 (West 1969); N.M. STAT. ANN. § 53-17-1 (1978); N.Y. BUS. CORP. LAW. § 1301 (McKinney Supp. 1980-81); N.C. GEN. STAT. § 55-131 (1975 & Supp. 1979); N.D. CENT. CODE § 10-22-01 (1976); OR. REV. STAT. § 57.655 (1979); PA. STAT. ANN. tit. 15, § 2001 (Purdon 1967 Supp. 1980-81); R.I. GEN. LAWS § 7-1.1-117 (1969); S.C. CODE § 33-23-10 (1976); TENN. CODE ANN. § 48-1101 (1979); TEX. BUS. CORP. ACT. ANN. art. 8.01 (Vernon 1980); UTAH CODE ANN. § 16-10-102 (1973); WASH. REV. CODE ANN. § 23A.32.010 (Supp. 1980-81); W. VA. CODE § 31-1-49 (Supp. 1980); WIS. STAT. ANN. § 180.801 (4) (West Supp. 1980-81). *But see* KAN. STAT. ANN. § 17-7301 (1974) (Gives a list of three activities which *do* constitute "transacting business" in addition to a list of activities which *do not* constitute "transacting business").

The categories of business activities enumerated in MBCA § 106 are representative of the safe harbor activities established in pre-MBCA judicial and legislative decisions. 2 MODEL BUS. CORP. ACT ANN. § 106, 2d Par. ¶ 2 (2d ed. 1971) (Official Comment to § 106, 2d Par.). The following states have adopted the entire list of activities in MBCA § 106; ALASKA STAT. § 10.05.600 (1968); FLA. STAT. ANN. § 607.304 (West 1977); HAW. REV. STAT. § 418-6 (1976); IOWA CODE ANN. § 496A.103 (West Supp. 1980); KY. REV. STAT. § 271A.520 (Supp. 1980); NEB. REV. STAT. § 21-20,105 (1977); N.M. STAT. ANN. § 53-17-1 (1979); N.D. CENT. CODE § 10-22-01 (1976); OR. REV. STAT. § 57.655 (1977); PA. STAT. ANN. tit. 15, § 2001 (Purdon 1967); R.I. GEN. LAWS § 7-1.1-117 (1970); UTAH CODE ANN. § 16-10-102 (1973); WASH. REV. CODE ANN. § 23A.32.010 (1969).

¹¹ See note 4 *supra*. See also CT. CORPORATION SYSTEM, WHAT CONSTITUTES DOING BUSINESS (1976) (grouping the holdings in the various states by type of business activity involved); Barrett, *Advising a Corporation "Doing Business" in Other States*, 19 PRACTICAL LAW. 85 (April 1973) (dealing with the types of activity to be avoided in order to avoid qualification).

¹² See, e.g., MBCA § 128(n); IDAHO CODE § 30-1-128(k) (Supp. 1980). Although California imposes a filing fee of \$350, CAL. GOV'T CODE § 12211 (Deering Supp. 1980), most filing fees range between \$10 and \$100. E.g., ARIZ. REV. STAT. ANN. § 10-129(3) (1977) (\$50); COLO. REV. STAT. § 7-10-104(1)(e)(I) (Supp. 1979) (\$100); MICH. STAT. ANN. § 21.200(1060)(b) (Supp. 1979) (\$10).

¹³ See, e.g., MBCA § 131; FLA. STAT. ANN. § 607.367 (West 1977). License fees typically are assessed in an amount which is dependent upon the amount of capital employed in the state. E.g., MBCA § 131; FLA. STAT. ANN. § 607.367 (West 1977) (number of authorized shares); ARK. STAT. ANN. § 64-1210(1) (Supp. 1977) (par value of authorized shares). Most fee schedules are regressive. E.g., FLA. STAT. ANN. § 607.367 (West 1977). Some set a minimum fee, e.g., ALASKA STAT. § 10.05.708 (1978); others set a maximum fee, e.g., MISS. CODE ANN. 79-3-755 (1972).

¹⁴ See, e.g., CONN. GEN. STAT. § 33-405 (Supp. 1980).

ments are sometimes based upon income¹⁵ or fixed in amount,¹⁶ although most are computed upon some measure of the capital employed in the state.¹⁷ Third, the statutes typically require a foreign corporation to furnish certain information in the application for a certificate.¹⁸ Qualification statutes, therefore, cause foreign corporations to incur the costs of complying with reporting requirements. Moreover, states commonly require the filing of an annual report with the Secretary of State.¹⁹ Although these costs are not substantial for larger corporations, they are a factor to be considered in the decision of whether or not to qualify to do business in a state.

State qualification schemes are enforced primarily by imposing sanctions on corporations who fail to comply. Denial of access to the state's court system is one of the most prevalent techniques. The statutes of all fifty states and the District of Columbia disable nonqualified corporations from bringing suit. In forty-eight jurisdictions, an unqualified foreign corporation is forbidden to maintain *any* action in the courts;²⁰ three states

¹⁵ See, e.g., IDAHO CODE § 30-1-130 (West Supp 1980).

¹⁶ See, e.g., ALASKA STAT. § 10.05.615 (1968).

¹⁷ See, e.g., MBCA § 133 (stated capital); GA. CODE ANN. § 92-2401 (Supp. 1979) (net worth).

¹⁸ See, e.g., MBCA § 110.

¹⁹ See, e.g., MBCA § 125.

²⁰ MBCA § 124 states that "[n]o foreign corporation transacting business in this State without a certificate of authority shall be permitted to maintain any action, suit or proceeding in any court of this State, until such corporation shall have obtained a certificate of authority." 2 MODEL BUS. CORP. ACT ANN. 2d § 124, ¶ 1 (1971). States which forbid a violating corporation to bring any action include: ALASKA STAT. § 10.05.690 (1968); ARIZ. REV. STAT. ANN. § 10-124 (West 1956); CAL. CORP. CODE ANN. § 2203 (Deering 1947); COLO. REV. STAT. § 7-9-103 (1973); CONN. GEN. STAT. ANN. § 33-412 (Supp. 1979); DEL. CODE ANN. tit. 8, § 383 (Supp. 1978); D.C. COD ANN. § 29-934f (Supp. 1980); FLA. STAT. ANN. § 607.354 (West Supp. 1979); GA. CODE ANN. § 22-1421 (1977); HAW. REV. STAT. § 418-13 (1980); IDAHO CODE § 30-1-124 (Supp. 1979); ILL. ANN. STAT. ch. 32, § 157.125 (Smith-Hurd Supp. 1979); IND. CODE § 23-1-11-14 (Supp. 1979); IOWA CODE ANN. § 496A.120 (West Supp. 1979); KAN. STAT. ANN. § 17-7307 (1974); KY. REV. STAT. § 271A.610 (Supp. 1980); LA. REV. STAT. ANN. § 12:314 (West Supp. 1979); ME. REV. STAT. ANN. tit. 13-A, § 1214 (1964); MD. CORP. & ASS'NS. CODE ANN. § 7-301 (1975); MASS. ANN. LAWS ch. 181, § 9 (Michie/Law Co-op 1977); MICH. COMP. LAWS ANN. § 450.2051 (1974); MINN. STAT. ANN. § 303.20 (West 1969); MISS. CODE ANN. § 79-3-247 (1972); MO. ANN. STAT. § 351.635 (Vernon Supp. 1979); MONT. CODES ANN. § 15-22-117 (1967); NEB. REV. STAT. § 21-20,121 (1977); NEB. REV. STAT. § 80.210 (1979); N.H. REV. STAT. ANN. § 300:8 (1977); N.J. STAT. ANN. § 14A-13-11 (West 1969); N.M. STAT. ANN. § 53-17-20 (1978); N.Y. BUS. CORP. LAW § 1312 (McKinney 1963); N.C. GEN. STAT. § 55-154 (1975); N.D. CENT. CODE § 10-22-19 (1976); OHIO REV. CODE ANN. § 1703.29 (Page 1978); OKLA. STAT. ANN. tit. 18, § 1.201 (West 1951); OR. REV. STAT. § 57.745 (1979); PA. STAT. ANN. tit. 15, § 2014 (Purdon 1967); R.I. GEN. LAWS § 7-1.1-117 (1970); S.C. CODE § 33-23-150 (1977); S.D. COMPILED LAWS ANN. § 47-8-30 (1967); TENN. CODE ANN. § 48-1106 (1979); TEX. BUS. CORP. ACT. ANN. art. 8.18 (Vernon 1956); UTAH CODE ANN. § 16-10-120 (1973); VA. CODE § 13.1-119 (1978); WASH. REV. CODE ANN. § 23A.32.190 (1969); W. VA. CODE § 31-1-

forbid the corporation to bring actions to enforce contracts.²¹ The disability to sue extends to suits brought in the federal courts,²² and usually extends to successors and assignees of the unqualified corporation.²³ Subsequent qualification may cure the

66 (1975); WIS. STAT. ANN. § 180.847 (West Supp. 1980); WYO. STAT. ANN. §17-1-719 (1977).

²¹ ALA. CODE § 10-2-254 (1975); ARK. STAT. ANN. § 64-1202 (1966); VT. STAT. ANN. tit. 11, § 2120 (1973).

²² *Woods v. Interstate Realty Co.*, 337 U.S. 535 (1949). *But see Walker, Foreign Corporation Laws: Re-examining Woods v. Interstate Realty Co. and Reopening the Federal Courts*, 48 N.C. L. REV. 56 (1969).

There is, however, no disability to sue where jurisdiction is based upon the existence of a federal question. *Metropolitan Paving Co. v. International Union of Operating Eng'rs*, 439 F.2d 300 (10th Cir. 1971), *cert. denied*, 404 U.S. 829 (1971); *American Export Lines, Inc. v. J & J Distrib. Co.*, 452 F. Supp. 1160 (D.N.J. 1978).

²³ MBCA § 124 extends the disability to "any successor or assignee" of the unqualified corporation. 2 MODEL BUS. CORP. ACT ANN. 2d § 124, ¶ 1 (1971). The following states extend the disability to the same or similar persons: ALA. CODE § 10-2-254 (1975) (persons claiming through or under the contract); ALASKA STAT. § 10.05.690 (1968); ARIZ. REV. STAT. ANN. § 10-124 (West 1956); CONN. GEN. STAT. ANN. § 33-412 (West Supp. 1979); D.C. CODE ANN. § 29-934f (1973); FLA. STAT. ANN. § 607.354 (West 1977); GA. CODE ANN. § 22-1421 (1977); IDAHO CODE § 30-1-124 (Supp. 1979); ILL. ANN. STAT. ch. 32, § 157.125 (Smith-Hurd Supp. 1979); IOWA CODE ANN. § 496A.120 (West Supp. 1979); KY. REV. STAT. § 271A.610 (Supp. 1980); ME. REV. STAT. ANN. tit. 13-A § 1214 (West 1964) (no disability for subrogees); MD. CORP. & ASS'NS CODE ANN. § 7-301 (1975) (any person claiming under the contract); MICH. STAT. ANN. § 21.200 (1051) (1974); MINN. STAT. ANN. § 303.20 (West 1969) (holder in due course doctrine not altered); MISS. CODE ANN. § 79-3-247 (1972); MONT. REV. CODES ANN. § 35-1-1004 (1979); NEB. REV. STAT. § 21-20,121 (1943); N.J. STAT. ANN. § 14A-13-11 (West 1969) (holder in due course doctrine not altered); N.M. STAT. ANN. § 53-17-20 (1978); N.Y. BUS. CORP. LAW § 1312 (McKinney 1963) (any successor in interest); N.C. GEN. STAT. § 55-154 (1975); N.D. CENT. CODE § 10-22-19 (1976); OKLA. STAT. ANN. tit. 18, § 1.201 (West 1951); OR. REV. STAT. § 57.745 (1979); PA. STAT. ANN. tit. 15, § 2014 (Purdon 1967); R.I. GEN. LAWS. § 7-1.1-117 (1969); S.C. CODE § 33-23-150 (1976) (no disability for subrogees); S.D. COMPILED LAWS ANN. § 47-8-30 (1976); TENN. CODE ANN. § 48-1106 (1979); TEX. BUS. CORP. ACT ANN. art. 8.18 (Vernon 1956) (holder in due course doctrine not altered); UTAH CODE ANN. § 16-10-120 (1953); VT. STAT. ANN. tit. 11, § 2120 (1973) (assignee and any person claiming under such assignee or corporation); WASH. REV. CODE ANN. § 23A.32.190 (1976); W. VA. CODE § 31-1-66 (1975); WIS. STAT. ANN. § 180.847 (West Supp. 1980); WYO. STAT. ANN. § 17-1-719 (1977).

The statutes in the following states provide that the disability does *not* extend to assignees: DEL. CODE ANN. tit. 8, § 383 (1974); KAN. STAT. ANN. § 17-7307 (1974).

The statutes in the remaining states do not indicate whether the disability to sue extends to assignees, leaving the courts to decide the question.

Courts are divided over whether the prohibition extends to counterclaims. *Compare Moore v. Northern Homes of Pa., Inc.*, 80 F.R.D. 278 (W.D. Va. 1978) and *Levitt Multihousing Corp. v. District Court*, 188 Colo. 360, 534 P.2d 1207 (1975) and *Gibraltar Const. and Eng'r, Inc. v. State Nat'l Bank of Bethesda*, 265 Md. 530, 290 A.2d 789 (1972) and *Bozzuto's Inc. v. Frank Kantrowitz & Sons, Inc.*, 117 N.J. Super. 146, 283 A.2d 907 (1971) (disability to sue applies to counterclaims) with *Park v. Cannco Contractors, Inc.*, 446 F. Supp. 24 (N.D. Miss. 1977) and *Aberle Hosiery Co. v. American Arbitration Ass'n*, 337 F. Supp. 90 (E.D. Pa. 1972) and *Burley Newspapers, Inc. v. Mist Publishing Co.*, 414 P.2d 460 (Id. 1966) (disability to sue does *not* apply to counterclaims) and *State v. Cook United, Inc.*, 463 S.W.2d 509 (Tex. Civ. App. 1971), *modified*, 469 S.W.2d 709 (Tex.

disability to sue: only four states completely bar causes of action accruing before qualification.²⁴ Where qualification does cure the disability to sue, the corporation may have to complete the procedure prior to the commencement of the action in order to avoid a dismissal without prejudice;²⁵ in some states, however, courts allow corporations to qualify during trial or at any time prior to the entry of a final judgment.²⁶

The effects of a disability to sue may be severe. In two circumstances, the curable denial of access may have the same impact as a dismissal of the action with prejudice. First, in states where later filing of an action does not relate back to the date of the original filing,²⁷ the statute of limitations may run on the corporation before it qualifies.²⁸ Second, if the failure to qualify is not raised initially as a defense, the corporation may be barred before it ever learns of the need to qualify. Even dismissal *without* prejudice may have economic costs. Corporate agents will weigh the benefits of access to the courts against the costs of qualification. The value of the benefits would be the expected value of recovery in the instant suit and all future suits to be brought in that state.²⁹ If costs outweigh these benefits of qualification, corporate agents would not continue a suit after failure

1971). The statutory language of two states appears to prohibit an unqualified corporation from even defending a suit. See NEV. REV. STAT. § 80.210 (1977); WIS. STAT. ANN. § 180.847 (West Supp. 1980). The courts of both states, however, have held otherwise. See *Scott v. Day-Bristol Consol. Mining Co.*, 37 Nev. 299, 142 P. 625 (1914) (bringing suit constitutes implied waiver of claim of inability to defend); *Bazan v. Kux Mach. Co.*, 52 Wis. 2d 325, 190 N.W.2d 521 (1971) (prohibition is limited to counterclaims).

²⁴ See ALA. CODE tit. 10, § 10.2-254 (1975) (contracts are "void," but the foreign corporation is "estopped from setting up the fact that the contract or agreement was so made in violation of law"); ARK. STAT. ANN. § 64-1202 (1966) (contracts are unenforceable); MISS. CODE ANN. § 79-3-247 (1972) (modified version of MBCA § 124); VT. STAT. ANN. tit. 11, § 2120 (1973) (contracts are unenforceable).

Statutory provisions identical to MBCA § 124 would appear to allow subsequent qualification to cure the disability to sue. See note 23 *supra*. But see *Thomas Indus., Inc. v. Wells*, 403 Mich. 466, 472, 270 N.W.2d 98, 101 (1978) (despite statutory language identical to MBCA § 124, the disability to sue may not be curable).

²⁵ See, e.g., GA. CODE ANN. § 22-1421 (1977); N.C. GEN. STAT. § 55-154 (1975).

²⁶ See, e.g., *Pedi Bares, Inc. v. P & C Food Mkts., Inc.*, 567 F.2d 933 (10th Cir. 1977); *Typh, Inc. v. Typhoon Fence, Inc.*, 461 F. Supp. 994 (E.D. Pa. 1978); *Rigid Component Sys. v. Nebraska Component Sys., Inc.*, 202 Neb. 658, 276 N.W.2d 659 (1979); *Lawler v. Ginochio*, 584 P.2d 667 (Nev. 1978); *Grow Farms Corp. v. National State Bank, Elizabeth*, 167 N.J. Super. 102, 400 A.2d 535 (1979).

²⁷ 51 Am. Jur. 2d *Limitations of Actions* § 224 (1970).

²⁸ See, e.g., *Kitchen v. Himelfarb*, 254 A.2d 694 (Md. App. 1969) (six-month statute of limitations for filing of mechanics' lien claim ran before re-filing). The likelihood of such an occurrence is greater in states where the corporation need not qualify until just before the conclusion of the proceedings.

²⁹ For small corporations with uncertain business in the state, the recovery in future suits will be an insignificant benefit.

to qualify is raised as a defense.

Most states also impose financial penalties for failing to qualify. A majority of the states make the corporation liable for all fees and franchise taxes which would have been imposed while the corporation should have been qualified, as well as penalties for failure to pay on time.³⁰ For a corporation which has been doing business for a number of years, payment of such an accumulated amount may be a substantial hardship even if it could have paid the fees and taxes on a timely basis. Moreover, a majority of states³¹ impose a fine on the offending corporation.

³⁰ MBCA § 124 provides:

A foreign corporation which transacts business in the state without a certificate of authority shall be liable to this State, for the years or parts thereof during which it transacted business in this State without a certificate of authority, in an amount equal to all fees and franchise taxes which would have been imposed by this Act upon such corporation had it duly applied for and received a certificate of authority to transact business in this State as required by this Act and thereafter filed all reports required by this Act, plus all penalties imposed by this Act for failure to pay such fees and franchise taxes. The Attorney General shall bring proceedings to recover all amounts due this State under the provisions of this Section.

MODEL BUSINESS CORPORATION ACT § 124. The following states have adopted a similar provision: ALASKA STAT. § 10.05.696 (Supp. 1980); ARIZ. REV. STAT. ANN. § 10-124 (West 1956); CAL. CORP. CODE ANN. § 2203 (Deering Supp. 1980); COLO. REV. STAT. § 7-9-103 (1973 & Supp. 1979); CONN. GEN. STAT. ANN. § 33-412 (Supp. 1980); DEL. CODE ANN. tit. 8, § 383 (1974) (liability only as a condition of using the courts); D.C. CODE ANN. § 29-934f (1973); FLA. STAT. ANN. § 607.354 (Harrison 1977); GA. CODE ANN. § 22-1421 (1977); IDAHO CODE § 30-1-124 (1980); ILL. ANN. STAT. ch. 32, § 157.125 (Smith-Hurd Supp. 1980-81); IOWA CODE ANN. § 496A.120 (Supp. 1980-81); KY. REV. STAT. § 271A.610 (Supp. 1980); LA. REV. STAT. ANN. § 12:314 (West 1969 & Supp. 1980); ME. REV. STAT. ANN. tit. 13-A, § 1214 (1974); MISS. CODE ANN. § 79-3-247 (1972); MONT. REV. CODES ANN. § 15-22-117 (1979); NEB. REV. STAT. § 21-20,121 (1943); N.M. STAT. ANN. § 53-17-20 (Supp. 1979); N.Y. BUS. CORP. LAW § 1312 (McKinney 1963) (liability only as a condition of using the courts); N.C. GEN. STAT. § 55-154 (1975); N.D. CENT. CODE § 10-22-19 (1976); OHIO REV. CODE ANN. § 1703.29 (1978) (liability only as a condition of using the courts); OKLA. STAT. ANN. tit. 18, § 1.201 (West 1951); OR. REV. STAT. § 57.745 (1979); R.I. GEN. LAWS § 7-1.1-117 (1969); S.C. CODE § 33-23-150 (1976); S. D. COMPILED LAWS ANN. § 47-8-32 (1967); TENN. CODE ANN. § 48-1106 (1979) (also as a condition of using the courts); TEX. BUS. CORP. ACT ANN. art. 8.18 (Vernon 1956); UTAH CODE ANN. § 16-10-120 (1953); VT. STAT. ANN. tit. 11, § 2120 (1973); WASH. REV. CODE ANN. § 23A.32.190 (1969); W. VA. CODE § 31-1-66 (1975); WYO. STAT. ANN. § 17-1-719 (1977).

³¹ ALA. CODE § 10-2-250 (1975) (\$1000); ARK. STAT. ANN. § 64-1202 (Repl. 1966) (not less than \$1000); CAL. CORP. CODE ANN. § 2203 (Deering 1947) (\$20 per day), § 2258 (Deering 1947) (misdemeanor, \$500-\$1000); COLO. REV. STAT. § 7-9-103 (Supp. 1979) (not more than \$5000); CONN. GEN. STAT. ANN. § 33-412 (West Supp. 1980) (\$1000); DEL. CODE ANN. tit. 8, § 378 (1974) (\$200-\$500 per offense); D.C. CODE ANN. § 29-934f (1973) (not in excess of \$500); FLA. STAT. ANN. § 607.354 (West 1977) (\$500-\$1000 per year); GA. CODE ANN. § 22-1801 (1977) (\$500 per year); HAW. REV. STAT. § 418-10 (Repl. 1976) (\$100 per 30 days); ILL. ANN. STAT. ch. 32, § 157.125 (Smith-Hurd Supp. 1980) (10% of unpaid fees and taxes); IND. CODE ANN. § 23-1-11-4 (Burns Supp. 1978) (not more than \$10,000); KY. REV. STAT. § 271A.610 (Supp. 1980) (\$250), § 271A.640 (\$100-\$1000) (Supp. 1980); LA. REV. STAT. ANN. § 12:315 (West 1969) (\$25-\$500 plus \$50 per day; \$1000 maximum);

These financial penalties, although not significant to many corporations,³² may severely affect a small business.³³

Finally, states have adopted a number of additional penalties. They include fines or imprisonment of agents, servants, or officers,³⁴ imposition of personal liability on officers or agents for the debts of the corporation,³⁵ denial of the benefit of the statute of limitation,³⁶ and susceptibility to an injunction forbidding the further transaction of business in the state.³⁷ Sanctions im-

ME. REV. STAT. ANN. tit. 13-A, § 1214 (1974) (\$25 per day); MD. CORP. & ASS'NS CODE ANN. § 7-302 (1975) (\$200); MASS. ANN. LAWS ch. 181, § 9 (Michie/Law Co-op 1977) (not more than \$500 per offense per year); MICH. STAT. ANN. § 21.200 (1055) (1974) (\$100-\$1000 per month; 5 year maximum; \$10,000 maximum); MINN. STAT. ANN. § 303.20 (West 1969) (not more than \$1000, plus \$100 per month after assessment and before compliance); MO. ANN. STAT. § 351.635 (Vernon Supp. 1980) (not less than \$1000); NEV. REV. STAT. § 80.210 (1979) (not less than \$500); N.H. REV. STAT. § 300:7 (1977), § 651:2 (1974) (felony; not more than \$50,000); N.J. STAT. ANN. § 14A-13-11 (West 1969) (\$200-\$1000 per year; 5 year maximum); N.M. STAT. ANN. § 53-17-20 (1978) (\$200); N.C. GEN. STAT. § 55-154 (1975) (\$500 plus costs); OHIO REV. CODE ANN. § 1703.29 (Page 1978) (\$250 plus 15% of unpaid fees and taxes as a condition of using the courts); OKLA. STAT. ANN. tit. 18, § 1.201 (West 1953) (10% of unpaid fees and taxes); S.C. CODE § 33-23-150 (1977) (\$10 per day); TEX. BUS. CORP. ACT ANN. art. 8.18 (Vernon 1980) (\$100-\$5000 per month); WASH. REV. CODE ANN. §§ 9.24.040, 9.92.020 (1979) (gross misdemeanor; not more than \$1000); WIS. STAT. ANN. § 180.847 (West Supp. 1979) (50% of unpaid fees and taxes); WYO. STAT. § 17-1-719 (1977) (\$500).

³² Fines can be moderate. See *State v. Bull Inv. Group, Inc.*, 32 Conn. Supp. 279, 351 A.2d 879 (1974) (\$500); *State v. Guy Mobil Home Corp.*, 149 S.E.2d 913 (S.C. 1966) (\$10 per day for 61 days).

³³ See, e.g., N.H. REV. STAT. § 300:7 (1977), § 651:2 (1974) (\$50,000); TEX. BUS. CORP. ACT ANN. art. 8.18 (Vernon 1980) (\$5000 per month).

³⁴ ALA. CODE § 10-2-254 (Repl. 1981) (misdemeanor; \$100-\$1000 and/or imprisonment in county jail or hard labor for county for not more than 12 months); ARK. STAT. ANN. § 64-1204 (1980) (misdemeanor; \$100-\$1000 per day); CAL. CORP. CODE ANN. § 2259 (Deering 1977) (misdemeanor; \$25-\$300); COLO. REV. STAT. § 7-9-103 (Supp. 1979) (civil penalty; not more than \$1000); DEL. CODE ANN. tit. 8, § 378 (1974) (fine: \$100-\$500); HAW. REV. STAT. § 418-10 (1976) (forfeiture; \$100); IND. CODE ANN. § 23-1-11-14 (Burns Supp. 1978) (Class C infraction); KY. REV. STAT. § 271A.640 (Supp. 1980) (fine; \$100-\$1000); LA. REV. STAT. ANN. § 12:315 (West 1969) (fine; \$25-\$500, or 3 days - 4 months imprisonment for non-payment); MD. CORP. & ASS'NS CODE ANN. § 7-302 (1975) (misdemeanor; not more than \$1000); NEV. REV. STAT. § 80.210 (1979) (fine; not less than \$500); OHIO REV. CODE ANN. §§ 1703.30, 1703.99 (Page 1978) (4th degree misdemeanor); OKLA. STAT. ANN. tit. 18, § 1.201 (West 1953) (misdemeanor; not more than \$1000 and/or not more than 30 days imprisonment); OR. REV. STAT. § 57.994 (1979) (fine; not more than \$200 and/or not more than 30 days imprisonment); VA. CODE § 13.1-119 (1978) (penalty; \$100-\$1000).

³⁵ ARK. STAT. ANN. § 64-1216 (Supp. 1979); VA. CODE § 13.1-119 (Supp. 1980). In the absence of a statute imposing liability, the courts will not do so. See, e.g., *Medley Harwoods, Inc. v. Novy*, 346 So.2d 1224 (Fla. App. 1977). But see *Gilham Advertising Agency, Inc. v. Ipson*, 567 P.2d 163 (Utah 1977) (imposing liability).

³⁶ HAW. REV. STAT. § 418-13 (Supp. 1979); NEV. REV. STAT. § 80.220 (1979). This sanction may be imposed in the absence of a statutory provision. *Weishaar v. Butters Pump & Equip. Co.*, 89 P.2d 864 (Kan. 1939).

³⁷ ARIZ. REV. STAT. ANN. § 10-124 (1956); COLO. REV. STAT. § 7-9-103 (Supp. 1979); DEL. CODE ANN. tit. 8, § 384 (1974); IND. CODE ANN. § 23-1-11-14 (Burns Supp. 1980);

posed on corporate officers for failure to qualify can be unduly harsh in relation to the nature of the offense.³⁸ The injunction penalty is also unnecessarily severe because of the possibility that a court may *permanently* enjoin the corporation from engaging in business in the state.³⁹

B. *The Qualification Quandary*

In spite of the widespread adoption of the MBCA,⁴⁰ states have developed numerous definitions of "doing business" for qualification purposes. Although a majority of the states have a statutory definition of "doing business" which is modeled after MBCA Section 106, few have adopted the provision without altering the safe harbor list of activities which do not constitute "doing business."⁴¹ Where statutes do not contain such a safe harbor, or where the business conduct at issue is not listed, the courts create further differences in interpreting the words "doing business."⁴² Definitions of "doing business," moreover, are based upon the type or nature of corporate activities.⁴³ Inherent vagueness plagues such definitions because of the infinite variations in the nature and types of business activities. Indeed, very few foreign corporations carry on identical activities within a given state. Since the question of whether a corporation conducts business within a state represents primarily a question of

KAN. STAT. ANN. § 17-7308 (Supp. 1978); ME. REV. STAT. ANN. tit. 13-A, § 1211 (Supp. 1980); MASS. ANN. LAWS ch. 181, § 9 (Michie/Law Co-op Supp. 1980); N.H. REV. STAT. ANN. § 300:7 (Supp. 1979); N.J. STAT. ANN. § 14A:13-12 (West Supp. 1980); S.C. CODE § 33-23-120 (Supp. 1979); VT. STAT. ANN. tit. 11, § 2120 (Supp. 1980).

³⁸ In Arkansas, an officer may be subject to a fine ranging from \$100 to \$1000 per day. ARK. STAT. ANN. § 64-1204 (Supp. 1979).

³⁹ Cf. *Wier v. Fairfield Galleries, Inc.*, 377 A.2d 28 (Del Ch. 1977) (denial of motion to dismiss in an action to permanently enjoin a corporation which was engaged in auction sales of jewelry).

⁴⁰ See note 10 *supra*.

⁴¹ See note 9 *supra*.

⁴² For example, courts treat differently the purchase and acceptance of merchandise within a state. Compare *Sunlight Produce Co. v. State*, 183 Ark. 64, 35 S.W.2d 342 (1931) and *State v. Pioneer Creamery Co.*, 211 Mo. App. 116, 245 S.W. 361 (1922) (qualification required) with *Stafford-Higgins Indus. Inc. v. Gaystone Fabrics, Inc.*, 300 F. Supp. 65 (S.D.N.Y. 1969) and *Humboldt Foods, Inc. v. Massey*, 297 F. Supp. 236 (N.D. Miss. 1968) (qualification not required).

⁴³ MBCA § 106 lists ten types of activities. The nature of business activities controls qualification: (1) the activities must constitute some substantial portion of the corporation's ordinary corporate business; (2) the activities must reflect an intent to carry on its business in the state; (3) the activities must reflect a continuity of act and purpose; (4) the determination of whether the activities constitute "doing business" does not depend upon the success or volume of business; (5) the activities must be actually performed and not merely authorized. 17 FLETCHER § 8466 (1977).

fact,⁴⁴ businesses can draw few firm conclusions from the results of such case law.

Although the definitions of "doing business" are both numerous and unclear, foreign corporations must nevertheless make the decision of whether or not to qualify in various states. The danger created by the present state of affairs is that penalties may be imposed if the corporation makes an erroneous decision *not* to qualify.⁴⁵ A company may find itself suddenly penalized if inexperienced counsel assumes that conduct insufficient to be considered "doing business" in one state will be similarly insufficient in another state, even one with identical statutory language. This danger becomes even more pronounced when the decision is made without legal counsel.⁴⁶

Frequently, the safest and most efficient method available for avoiding the risk of sanctions is to register in every state in which the corporation is engaged in even the slightest business activity. Corporations often employ such "precautionary" qualification.⁴⁷ Such a move is undertaken when the expense of making an accurate determination whether to qualify exceeds the costs of registration. The argument, however, that hardship can be avoided with precautionary qualification does not justify ambiguous state business regulation. Such an approach condones the existence of a second *de facto* standard of "doing business." This second standard requires less business contact than the vague present statutory standard, and thus encourages precautionary qualification at a lower level of commercial activity. As a result, businesses using precautionary qualification must bear hidden expenses which stem from the inherent ambiguity of the statutory standards.

Consequently, business executives or their attorneys, in deciding whether to qualify their company as a foreign corporation, are often in a quandary. They face stiff penalties if they fail to qualify and qualification turns out to be required; they want to avoid the needless expense of precautionary qualification; and they lack standards for making a reasoned decision. One solu-

⁴⁴ 17 FLETCHER § 8464 (1977).

⁴⁵ Because of the lack of uniformity in the various standards of "doing business," the corporation's agent is also in danger of reaching the erroneous conclusion that it is appropriate to rely on a previous decision not to qualify in a different state.

⁴⁶ The problem of an inadvertent failure to qualify is more likely to occur with small businesses. An attorney who advises a small business not to qualify may give advice based upon inadequate research when he knows that his client's resources are limited.

⁴⁷ See CT CORPORATION SYSTEM, WHAT CONSTITUTES DOING BUSINESS (1976), at vii. See also Babcock, "Doing Business": *The Feasibility of a Statutory Definition*, 5 BUS. LAW. 31, 31-32, 40 (1949).

tion, of course, might be to improve qualification statutes by expanding their list of approved activities. At present, states have made no attempt to expand substantially the statutory list of protected activities.⁴⁸ Expanding the definition's list, however, would lessen this statutory vagueness only to a very limited extent. In order to salvage the qualification regime, therefore, some other means must be found for rectifying the vagueness surrounding MBCA Section 106.

II. THE JUSTIFICATION AND PURPOSES OF THE PRESENT SYSTEM

A. *The Doctrine of Conditional Entry as a Historical Justification*

Courts assert that a state has the right to exclude arbitrarily, or license in any manner, a foreign corporation within its borders, so long as the corporation is not deprived of any constitutional rights.⁴⁹ A state may exercise power to exclude or restrict

⁴⁸ Some states with definitions modeled after MBCA § 106 have added a single type of activity to the list of ten. *See, e.g.*, PA. STAT. ANN. tit. 15, § 2001 (Purdon Supp. 1979) (ownership of real property); NEB. REV. STAT. § 21-20,105 (1977) (acting in a fiduciary capacity). The draftsmen of MBCA § 106, however, recognized the impossibility of formulating an exhaustive list of activities not requiring qualification. 2 MODEL BUS. CORP. ACT ANN. 2d § 106, 2d Par. ¶ 2 (1971) (Official Comment to § 106, 2d Par.).

⁴⁹ *Wheeling Steel Corp. v. Glander*, 337 U.S. 562, 571 (1949). *Accord*, *WHYY v. Borough of Glassboro*, 393 U.S. 117 (1968) (per curiam). Under the United States Constitution, a foreign corporation is protected by the equal protection clause of the Fourteenth Amendment. *Southern R.R., v. Greene*, 216 U.S. 400 (1910). Corporations, under the Fourteenth Amendment, may not be deprived of liberty or property without due process of law. *Grosjean v. American Press Co.*, 297 U.S. 233, 244 (1936)(liberty); *Minneapolis & St. Louis Ry. v. Beckwith*, 129 U.S. 26 (1889) (property). In addition, the Supreme Court has applied the protections of the interstate commerce clause to the licensing or qualification of foreign corporations. *Allenberg Cotton Co. v. Pittman*, 419 U.S. 20 (1974); *Eli Lilly & Co. v. Sav-On-Drugs, Inc.*, 366 U.S. 276 (1961); *Union Brokerage Co. v. Jensen*, 322 U.S. 202 (1944); *Furst & Thomas v. Brewster*, 282 U.S. 493 (1931); *Railway Express Agency v. Virginia*, 282 U.S. 440 (1931); *Dahnke-Walker Milling Co. v. Bondurant*, 257 U.S. 282 (1921); *Sioux Remedy Co. v. Cope*, 235 U.S. 197 (1914); *Buck Stove & Range Co. v. Vickers*, 226 U.S. 205 (1912); *International Textbook Co. v. Lynch*, 218 U.S. 664 (1910) (per curiam); *International Textbook Co. v. Peterson*, 218 U.S. 664 (1910) (per curiam); *International Textbook Co. v. Pigg*, 217 U.S. 91 (1910); *Pullman Co. v. Kansas*, 216 U.S. 56 (1910); *Western Union Telegraph Co. v. Kansas*, 216 U.S. 1 (1910); *Crutcher v. Kentucky*, 141 U.S. 47 (1891); *Cooper Mfg. Co. v. Ferguson*, 113 U.S. 727 (1885).

Foreign corporations, however, are not entitled to the privileges and immunities of citizens under Article IV, Section 2 of the Federal Constitution. *Paul v. Virginia*, 75 U.S. (8 Wall.) 168 (1868) (contrasting corporate "citizenship" for diversity of citizenship purposes).

regardless of motive.⁵⁰ Courts have used this position, known as the "doctrine of conditional entry," as a central justification for qualification statutes.⁵¹ Although courts principally use the doctrine of conditional entry to justify the exercise of state power to regulate, rather than to exclude, foreign corporations,⁵² the doctrine has had considerable influence.⁵³

The doctrine of conditional entry rests on a faulty legal foundation, however, and provides little support for qualification statutes. Chief Justice Taney's dictum in *Bank of Augusta v. Earle*⁵⁴ provides the basis for the doctrine: "[A] corporation can have no legal existence out of the boundaries of the sovereignty by which it is created. It exists only in the contemplation of the law, and by force of the law; and where that law ceases to operate, and is no longer obligatory, the corporation can have no existence."⁵⁵ Taney's statement can be disputed because it rests on both an outdated territorial notion of law and an inaccurate concept of a corporation as a fictional creature of law.⁵⁶ This doctrine is an anachronism. State qualification requirements should be justified by something more than this traditional legal concept.

B. *The Purposes Served By Qualification Statutes*

Qualification statutes may also be justified by functional considerations. The only purposes which ought to justify the statutes' existence, however, are those purposes not fulfilled by other statutory schemes.

1. *The jurisdiction function*—Most qualification statutes require the appointment of an agent for the service of process.⁵⁷ This requirement reflects the state interest in providing a conve-

⁵⁰ *Security Mut. Life Ins. Co. v. Prewitt*, 202 U.S. 246, 257 (1906).

⁵¹ See *Allenberg Cotton Co. v. Pittman*, 419 U.S. 20, 37 (1974) (Rehnquist, J., dissenting).

⁵² A. Conard, *Federal Protection of the Free Movement of Corporations in the United States* (November 17, 1978) (unpublished report prepared for discussion at the Conference on Freedom of Interstate Movement in a Federal Community, Bellagio, Italy, July 16-21, 1979; Copyright, University of Michigan) at 11 (asserts that there are no reported cases of unconditional exclusion).

⁵³ See Walker, *Foreign Corporation Laws: The Loss of Reason*, 47 N.C. L. REV. 1, 8-10 (1968).

⁵⁴ 38 U.S. (13 Pet.) 519 (1839).

⁵⁵ *Id.* at 588.

⁵⁶ See Walker, *supra* note 53, at 29-30.

⁵⁷ Statutes typically state that a qualified foreign corporation must appoint a registered agent, and that it is deemed to have appointed the Secretary of State if it fails to do so. See, e.g., MBCA §§ 113, 115.

nient forum for its citizens for causes of action arising out of the acts of foreign corporations. States, however, do not need qualification statutes to obtain jurisdiction over foreign corporations, since modern long-arm statutes typically provide either for implied appointment of an agent for service of process in the state,⁶⁸ or for a method of service of process in the foreign state.⁶⁹ The jurisdiction function, then, is largely superfluous, and not a persuasive ground for qualification statutes.

Arguably, states have an interest in employing the same standard of "doing business" for qualification and jurisdiction purposes. The states, however, have chosen to establish different definitions in qualification and long-arm statutes. States often require less contact with the state for jurisdiction purposes than for qualification.⁶⁰ In these states, the qualifying foreign corporation's appointment of an agent does not extend the jurisdiction of the state beyond that of the long-arm statute.

Qualification statutes may have one important jurisdictional effect: registered foreign corporations may be subjected to suit *in* the state on causes of action arising from activities *outside* of the state. In these situations, jurisdiction could not be obtained under most long-arm statutes, which generally require that the cause of action arise within the state.⁶¹ States are not forbidden to assert jurisdiction in causes of action arising outside of the state.⁶² Qualification statutes, however, encourage the expansion of jurisdiction without the usual judicial analysis of its desirability.⁶³ The proper inquiry ought to be whether the business done in the state is "sufficiently substantial and of such a nature"⁶⁴ as to permit the state to require the corporation to defend a suit. The state can provide a forum for its citizens through statutes which deal solely with the question of jurisdiction. The state, consequently, does not need qualification statutes to extend the jurisdiction of its courts to foreign corporations and should pursue other means of doing so.

2. *The taxation function*—The imposition of franchise taxes

⁶⁰ See, e.g., IOWA CODE ANN. § 617.3 (West Supp. 1980).

⁶¹ See, e.g., ILL. ANN. STAT. ch. 110, § 16 (Smith-Hurd Supp. 1979).

⁶² See, e.g., *Continental Properties, Inc. v. Ullman Co.*, 436 F. Supp. 538, 541 (E.D. Va. 1977); *Goodwin Bros. Leasing, Inc. v. Nousis*, 366 N.E.2d 38, 42-43 (Mass. 1977); *Beltone Electronics v. Selbst*, 58 A.D.2d 560, 560, 396 N.Y.S.2d 21, 22 (1977); *Horton v. Richards*, 594 P.2d 891, 893 n.3 (Utah 1979).

⁶³ E.g., ILL. ANN. STAT. ch. 110, § 17 (Smith-Hurd Supp. 1980).

⁶⁴ *Perkins v. Benguet Consol. Mining Co.*, 342 U.S. 437 (1952).

⁶⁵ See Walker, *Foreign Corporation Laws: A Current Account*, 47 N.C. L. Rev. 733, 738 (1969).

⁶⁶ *Perkins v. Benguet Consol. Mining Co.*, 342 U.S. 437, 447 (1952).

is commonly tied to qualification,⁶⁵ reflecting the state interest in taxing foreign corporations which do business in the state. Although the method of computation varies from state to state, franchise taxes are essentially taxes upon the "privilege of doing business" in a state.⁶⁶ Most importantly, the reporting requirements of these statutes⁶⁷ provide information to state revenue authorities. The information also helps in identifying corporations and computing assessments for other state taxes.

These reporting requirements, however, are unnecessary for two reasons. One reason is that the usefulness of such information in locating corporations is limited: the constitutional level of minimum contact required for taxation purposes is less than the standard for qualification,⁶⁸ and enforcement difficulties occur where contacts are so slight that corporations need not qualify. Another reason is that state tax laws typically impose reporting requirements which are independent of qualification statutes.⁶⁹ While the taxation of foreign corporations is a legitimate state interest, a qualification scheme seems unnecessary to further it.

3. *The protection-through-information function*— Qualification statutes provide information for government officials and individual citizens through reporting requirements.⁷⁰ These requirements serve legitimate purposes by allowing the state to (a) supervise the corporations in order to protect its citizens; (b) subject foreign corporations to inspection to determine their condition, standing, and solvency; (c) treat them in the same manner as domestic corporations with respect to disclosure of information; and (d) provide evidence of their existence.⁷¹ Unlike the other objectives, the states cannot effectively accomplish these purposes through other statutory provisions already in existence.

The foundation of the protection function derives from state's desire to protect its citizens from the misconduct of foreign cor-

⁶⁵ See notes 15-17 and accompanying text *supra*.

⁶⁶ The constitutional limitations on the assessment of "franchise" taxes are the same as those on other taxes imposed upon interstate commerce. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 288-89 (1977).

⁶⁷ See note 18 and accompanying text *supra*.

⁶⁸ The respective levels of contact actually required for taxation and qualification are similar. See, e.g., *Rochester Capital Leasing Corp. v. Sprague*, 474 P.2d 201, 203 (Ariz. App. 1970).

⁶⁹ Walker, *supra* note 63, at 746-47.

⁷⁰ See notes 18-19 *supra*.

⁷¹ 2 MODEL BUS. CORP. ACT ANN. 2d §§ 110-112, ¶ 2 (1971) (Official Comment to §§ 110-112).

porations. A qualification scheme should minimize the number of situations in which the state's citizens could be harmed by a foreign corporation deemed not to be "doing business" in the state. A state legislature, therefore, must weigh against the risk of corporate misconduct the value of increased business activity which stems from a less regulated commercial environment. In MBCA Section 106, the enumerated activities are unlikely to cause harm to local citizens and are justifiably excluded.⁷² The list of activities, however, is far from complete. While a more comprehensive statement of safe harbor activities would help, such an expansion could never provide a business with the certainty needed for making qualification decisions.

III. THE PROPER SOLUTION: ESTABLISH A TEST FOR "DOING BUSINESS" BASED SOLELY ON IN-STATE SALES VOLUME

The present system of state qualification requirements is obviously deficient. These requirements, however, should not be abolished⁷³ because they serve one legitimate purpose, as discussed above: furnishing general information about foreign corporations not subject to any other information disclosure scheme. What is needed is a qualification scheme which incorporates this protection function, but which reduces the amount of uncertainty involved in the decision whether or not to qualify.

Revising the definition of "transacting business" in the second paragraph of MBCA Section 106⁷⁴ would rectify the serious problems of the present qualification statutes. The new definition would provide that a foreign corporation shall be considered to be transacting business in a state *only* if its annual volume of sales in the state exceeds a specified amount. Each state would determine the minimum level of sales volume under the statute. "Sales in the state" should not, however, include sales which do not reflect a presence in the state of the corporation. Present qualification statutes have identified three categories which should be incorporated into the new definition. These sales in-

⁷² Of the ten activities enumerated in MBCA § 106, however, two appear to be codifications of constitutional limitations on the application of qualification requirements: See MBCA §§ 106(f), 106(i), *supra* note 8; 2 MODEL BUS. CORP. ACT ANN. 2d § 106, ¶ 4.05 (1971) (annotation of cases establishing constitutional limitations on qualification requirements).

⁷³ *But see* Walker, *supra* note 53, at 30 (suggesting abolition).

⁷⁴ See note 8 and accompanying text *supra*.

clude those effected through (a) independent contractors,⁷⁵ (b) solicitation or procurement of orders which require acceptance outside the state before becoming binding contracts,⁷⁶ or (c) a subsidiary corporation incorporated or transacting business in the state.⁷⁷

The proposed revision of Section 106 would provide greater uniformity among state statutes, reduce the vagueness of business regulation, and fulfill the protection-through-information requirements of the states. First, the revision would make state qualification requirements more uniform. Present qualification statutes provide fifty-one different definitions of "doing business" which differ in both statutory language and judicial construction.⁷⁸ Although the revision represents model legislation like the present Section 106, the proposal's simplicity and brevity would greatly increase the likelihood that states would adopt the provision without modification. Because the states would be able to establish different sales volume figures, the new system would not be uniform insofar as the ultimate decision of whether to qualify would be the same for a given level of activity. The various sales volume figures, however, would not create the same type of confusion caused by the present system. Instead, the qualification decision in all of the states would be uniform in the sense that the inquiry in each case would turn on one readily quantifiable factor: the volume of sales in the state. The proposal's simplicity and brevity, therefore, would reduce the necessity for judicial construction, decreasing the possible number of differences in state standards arising from varying interpretations.

Second, the revision would clarify the definition of "doing business." The various current definitions of "doing business" are vague.⁷⁹ The suggested solution is not a futile attempt to clarify the inherent vagueness of the present version of MBCA Section 106 by expanding the list of exempted business activities. Rather than defining "doing business" in terms of the type or nature of activity, the proposal utilizes a definition capable of objective determination. The proposal does not describe conduct which does *not* constitute "doing business"; rather, the proposal's definition avoids the problems of vagueness inherent in a

⁷⁵ See MBCA § 106(e), *supra* note 8.

⁷⁶ See MBCA § 106(f), *supra* note 8.

⁷⁷ See CAL. CORP. CODE ANN. § 2105 (Deering Supp. 1980); GA. CODE ANN. § 22-1401 (1977); S.C. CODE § 33-23-10 (1976).

⁷⁸ See notes 41-42 and accompanying text *supra*.

⁷⁹ See notes 43-44 and accompanying text *supra*.

“negative” and nonexclusive definition like MBCA Section 106.⁸⁰

Third, the revision satisfies the protection function of qualification statutes.⁸¹ The protection function is satisfied if the foreign corporations exempted from registration requirements are not likely to engage in conduct harmful to the state’s citizens. Rather than attempting to enumerate all activities which are unlikely to result in such injury, the suggested solution exempts from qualification foreign corporations whose sales in the state do not exceed a certain level. In general, as sales volume increases, so does the level of contact with the state’s citizens. Thus, a legislature can establish the acceptable level of risk of harm to its citizens from unqualified foreign corporations. Activities which create risks of harm unrelated to the level of sales volume, such as securities transactions, should be regulated with specific legislation directed at the particular activities.⁸²

In deciding what volume of sales would constitute “doing business,” state legislatures would make a judgment as to the point at which the level of contact, as reflected in sales figures, warrants qualification. The volume of sales, however, also provides a rough indication of the size of a corporation’s operations in the state. Thus, the legislatures could also weigh the benefits which flow to its citizenry from the activity of a number of small business operations which might not exist if required to qualify. For example, a legislature especially concerned about “fly-by-night” entrepreneurs, and less concerned about attracting small businesses to the state, could mandate qualification when annual sales in the state exceeded \$1000. By contrast, a legislature not convinced that unregistered foreign corporations presented a significant threat, or more concerned with attracting new businesses, might require registration only when the annual sales in the state exceeded \$100,000. In summary, the proposal better provides the state legislature with the opportunity to make an effective cost-benefit analysis when determining which corporations should register.

CONCLUSION

The present system of state qualification requirements has

⁸⁰ See Babcock, *supra* note 47. The author advocates that “doing business” be defined by statute in affirmative and exclusive terms. *Id.* at 38-39.

⁸¹ See notes 70-71 and accompanying text *supra*.

⁸² See, e.g., PA. CONS. STAT. ANN. §§ 1-101 to -704 (Purdon Supp. 1980) (Pennsylvania blue sky law).

significant weaknesses. A multiplicity of "doing business" definitions exist, coupled with an unacceptable degree of vagueness in those definitions. The resulting uncertainty makes most decisions not to qualify in a state risky. As a result, many foreign corporations are forced to qualify without regard to whether they are actually "doing business." Qualification requirements serve the legitimate purpose of gathering the information necessary to protect a state's citizens. The present system, however, must be modified in order to correct its deficiencies.

A change in the MBCA definition of "transacting business" is required. The new definition should abandon the previous attempts to define "doing business" in terms of the type or nature of the conduct. Instead, the definition should be formulated in terms of the volume of sales in a state. This definition would be simple and susceptible to objective measurement. It would provide uniformity and clarity, while allowing qualification schemes to serve proper state interests. Without this new definition, the very legitimacy of state qualification requirements for foreign corporations remains uncertain.

—*Stanley M. Klem*