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STATE LICENSING OF EQUIPMENT LESSORS

For most of us, equipment leasing is a multistate activity. Lessors in one state routinely lease equipment to lessees in other states, often buying it from vendors in a third state and sometimes working through brokers residing in yet another state. This issue of Dispatches from the Trenches addresses the common questions of what state licensing laws apply and whether it is necessary to qualifying to do business as a foreign corporation.

QUALIFICATION TO DO BUSINESS

In order for a corporation formed under the laws of one state to “transact business” in another, the corporation must obtain certification from the second state’s Secretary of State. This process is referred to as “qualification to do business as a foreign corporation.” Most states have adopted at least some portions of either the Model Business Corporation Act or the Revised Model Business Corporation Act. Under both (and the U.S. Constitution), it is clear that transactions in interstate (as opposed to intrastate) commerce do not constitute “transacting business” for purposes of requiring qualification.

The dividing line between a transaction in interstate commerce and one that is sufficiently a matter of intrastate activity to constitute “transacting business” is often a difficult judgment call. Unfortunately, courts do not always follow what seems to most business professionals to constitute common sense or plain English. Providing replacement units from a local inventory or services in



connection with leases, rather than financing alone, is likely to cross the line into intrastate activity. Other activities that constitute "transacting business" include maintenance of an office in the state in question or having an agent located in the state or who travels to the state as a routine matter in order to conduct business. Isolated transactions, mere ownership of real or personal property, soliciting or taking orders by mail to be accepted outside the state are generally not considered to be "transacting business".

While considering these issues, most lawyers advise that the lessor consider the advantages and disadvantages of qualifying. Under most state laws, a corporation that qualifies to do business in a state submits to the jurisdiction of the courts of that state and may be served with process in that state. This means that, subject to some limitations, the corporation may be sued in the foreign state. In addition, annual report filings and franchise taxes (usually based on the amount of assets or business in the state and therefore not too onerous) must be paid and the headache and enterprise cost must be considered.

On the other hand, in every state except Alabama, the failure to qualify to do business can be remedied by subsequent qualification. This is because every state except Alabama has adopted a "cure" statute under which qualification to do business retroactively cures any failure to obtain qualification for most purposes.

Except for the payment of fees, and except in Alabama, the principal penalty for failure to qualify to do business in a state is that the foreign corporation will be barred from use of the state's courts. For example, Section 124 of the Model Business Corporation Act provides "no 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." If the issue is raised, the foreign corporation usually dismisses the litigation, qualifies to do business, and initiates a new lawsuit (if within the applicable statute of limitations).



The sole exception is Alabama in which contracts made by a corporation which, although required to qualify to do business has not done so are void. *AllState Leasing Company v. Scroggins*, 541 So.2d 17(ALA. APP. 1989). To make matters worse, Alabama's Business Code varies from that of many states in its absence of any statutory definition of what constitutes "transacting business." That term, as it has been defined through Alabama case law, is unclear and each case must be decided based on its own particular facts. In *Scroggins* the court reasoned that the volume of leases AllState had in Alabama was enough in and of itself to require the lessor to obtain a certificate of authority. Unfortunately, another Alabama court has held that an isolated business deal may require qualification. *Vines v. Romar Beach* 670 So.2d 902 (Ala. 1995).

For this reason, lessors with any substantial amount of leasing business in Alabama are well advised to qualify to do business in that state. Other states require a cost-benefit analysis that often weighs in favor of not qualifying unless the presence of a business office or other activities make qualification clearly necessary.

OTHER STATE LICENSING REQUIREMENTS

A review of state licensing requirements for the fifty states indicates that very few require personal property lessors to obtain any form of license for non-consumer true leasing, as opposed to lease-purchases.

There are two major exceptions: First, several states require some form of license for the financing of motor vehicles. States with such requirements include Arizona, Arkansas, Connecticut, Delaware, Florida, Kentucky, Louisiana, Michigan, Mississippi, Missouri, Nevada, West Virginia (necessary for titling purposes) and Wisconsin. Second, most states require some form of registration in order to facilitate the collection of a rental or other tax.

Several states, most notably California, require licensing in order to make loans to commercial enterprises. States with some form of loan or small loan license include Alaska (loans of \$25,000 or



less), California (discussed below), Connecticut (installment contracts of \$16,000 or less), Iowa (regulating loans of \$25,000 or less), Minnesota (which has confirmed orally that the license is not required of out of state lenders), Nevada (from a Nevada location or routinely solicited from out-of-state), New Mexico (loans of \$2,500 or less), New Hampshire (regulated loans of \$10,000 or less), North Carolina (really a taxation statute that can be retroactively cured).

Of these, the best known and most generally-applicable is the California Finance Lenders Law (Financial Code §22000). The California law requires finance lenders to be licensed for transacting business. The statute does not, on its face, apply to leases and leasing companies generally consider themselves exempt. The laws applied to an out of state lender in *People v. Fairfax Family Fund, Inc.* 235 Cal. App. 2nd 881, 47 Cal. Rptr. 812 (1965) Appeal Dismissed 382 U.S. 1, 86 S.Ct. 34 (1965). The Fairfax case involved a Kentucky corporation that was enjoined from conducting a small loan business in California at a high rate of interest. (It should be mentioned that obtaining a California Finance Lenders License allows the lender to charge interest without regard to California's usury laws).

To date, no court has held that a lessor under a non-true lease has ever been held subject to the California Finance Lenders law. It is generally agreed by leasing practitioners, however, that non-true leases should be considered loans for most legal purposes and an equipment lessor may possibly be subject to penalties for failure to comply with the California Finance Lenders law with respect to its non-true leases to California businesses.

Marks & Weinberg, PC is a law firm with significant experience in dealing with virtually every type of equipment and facility lease financing. The lawyers of the firm have participated in leasing financings for more than a billion dollars of equipment and are recognized throughout the industry. If you would like more cases or articles on leasing, or have any questions or comments about this Article or other leasing issues, please visit www.lease lawyer.com or contact Barry Marks at 205-251-8303 or Ken Weinberg at 205.251.8307.

