GUIDE

TO THE LEGAL ASPECTS OF

DOING BUSINESS IN THE UNITED STATES

FOR THE FOREIGN BUSINESS PERSON

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TABLE OF CONTENTS

USING THIS PUBLICATION

To paraphrase the ancient Greeks, it is not reality that affects us but rather our *perception* of reality. To the foreign national business person, the United States can seem to be a massive, complicated, and unknowable place to do business. Compared to other more centralized economies, the diversity and complexity of the U.S. legal system and its markets can seem mysterious and almost unfathomable to foreign national business persons.

Aside from the differences in business practices and business cultures, the legal authority in the U.S. federal-state-local political system is decentralized, diffuse, and even in conflict with one another. This makes the legal system and the court system quite perplexing, even to U.S. citizens. Business persons are expected to conduct their activities within a complicated web of laws and government regulations while also protecting themselves within the law in dealing with other business persons. Except for certain tax laws, a foreign business person must observe and comply with the business laws at each level of government in the same way and to the same extent as does a U.S. business person. The old maxim that "ignorance of the law is no defense" applies literally and strictly in the U.S.

THE OBJECTIVE OF THIS PUBLICATION

There is an old business expression in the U.S. that says, "an educated consumer is our best customer." In the U.S., it is essential that a business person consult an attorney on the business laws and the legal issues which are implicated in any business plan. An attorney can most effectively advise the business person when the business person has some knowledge of the laws and legal issues and can at least ask meaningful questions. We present the framework of U.S. business laws as well as the most immediate legal issues, which the foreign business person must consider when formulating a plan to do business in the U.S. A basic understanding of the laws and legal issues will enable the foreign business person to work effectively with attorneys and other advisors.

No single publication can or should provide a complete presentation of the legal aspects of doing business in the U.S. More importantly, no print publication can present U.S. business laws in a timely manner because the laws and practices often change. We have determined that the most competent and effective way to present U.S. business laws is in an electronic format on a website which is accessible on the Internet. For this reason, we have placed this publication on our website (http://www.ngklaw.com) rather than publishing it in hard copy. The electronic format enables us to modify and update this publication. Consequently there is no limit on the number of pages or how often we can modify and update this publication.

THE STYLE OF PUBLICATION

When writing a legal publication, U.S. lawyers are trained to support each sentence they write with footnotes and citations to cases, statutes, and law review articles. We have chosen not to include footnotes and citations because we believe they are not useful in this type of publication. We just present the information in a simple and comprehensible format. Nothing in this publication is, or intended to be, a substitute for the actual case law, statutes, and regulations.

DEFINITIONS

For the purpose of this publication:

A. "U.S. person" means an individual or business entity that is a citizen of the U.S., a legal permanent resident of the U.S, or a business formed under the laws of a state of the U.S.

B. "Foreign business person", "foreign national" or "non-U.S. person" means an individual who is not either a citizen of the U.S. or a legal permanent resident of the U.S. and a business entity, which is formed under the laws of a jurisdiction which is not a state or territory of the U.S.

C. "State" means any one of the 50 states of the U.S., the District of Columbia and any territory of the U.S.

D. "U.S." means the United States.

E. "Federal" means the U.S. or the government of the U.S.

F. "Interest Holder" or "Owner" means a person who owns shares in a corporation, membership interests in a limited liability company, an ownership interest in a partnership or a beneficial owner of a statutory trust.

G. "Company" means a corporation, limited liability company, partnership or statutory trust.

H. "Business Entity" means a corporation, limited liability company, partnership or statutory trust.

I. "IRS" means the Internal Revenue Service which is the tax authority of the U.S.

<u>CHAPTER 1: THE UNITED STATES LEGAL SYSTEM IN PERSPECTIVE</u>

Section 1-1 The Federal and State System

A. United States Constitution

Great Britain established and controlled thirteen colonies on the Atlantic seaboard of North America between 1607 and 1783. In 1783, after a war for independence, the thirteen colonies united and became the United States. The people of the U.S. voted for the U.S. Constitution in 1789. The U.S. Constitution has been amended twenty seven times since 1789. The U.S. Constitution as it was enacted is the primary legal document upon which all laws of the U. S. are based. The U.S. Constitution creates a federal government which has certain enumerated powers. The enumerated powers of the federal government include regulating interstate commerce, coining money, national defense and conducting foreign affairs. The state and local governments have any powers or authorities which the U.S. Constitution does not confer on the federal government.

The first ten amendments to the U.S. Constitution are known as the Bill of Rights. These amendments guarantee fundamental civil rights such as freedom of speech, religion and the right to petition the government. They also entitle persons to the due process of law and protects them from unreasonable searches and seizures and from cruel and unusual punishment. For legal purposes but not immigration purposes, each person who lives in the U.S. is a resident of the U.S. and a resident of the state in which the person lives.

B. Federal Government

The federal government is composed of three separate but co-equal branches. These branches are the legislative branch, the executive branch and the judicial branch. Each branch has certain exclusive powers which serve to check the powers of each other branch and balances how each branch exercises these powers.

The legislative branch is the Congress. The Congress is composed of the House of Representatives and the Senate. Each House member is elected by the people of districts which are drawn in each state. The districts are drawn by the state legislature every ten years. Each House member serves for two years. The number of districts in each state is determined by the population of each state. Usually there is one district for every 500,000 people so that there is one House member for every 500,000 people. There is no limit on the number of times a House member may run for re-election. The Senate is often referred to as the "upper house." The people of each state elect two Senators without regard to the size of the population of a state. There are one hundred Senators. Each Senator serves for six years and there is no limit on the number of times a Senator can seek re-election. The Vice President serves as the President of the Senate and votes only if the margin of vote in the Senate on particular legislation is tied.

The executive branch consists of the President, Vice President and the departments and agencies of the executive branch. The President is elected by the people for a four-year term and may run and serve for one more four-year term. The President appoints the heads of the executive departments which include the departments of State, Defense, Treasury and Homeland Security. Referred to as Secretaries, each Secretary and assistant secretaries can take office only if they are confirmed by a majority vote of the Senate but serves only as long as the President so desires. The President also appoints the heads of each executive agency. The executive agencies have regulatory authority and are empowered to act independently from the President. Each head of these agencies is appointed by the President and confirmed by a majority vote of the Senate. They generally serve for a specified term.

The judicial branch is organized into three levels of courts. The federal district courts are the courts of original jurisdiction. The federal circuit courts of appeal hear appeals from the federal district courts which involve errors of law. The highest court is the Supreme Court of the U.S. The Supreme Court hears appeals from the federal circuit courts of appeal which involve errors of law. The Supreme Court also hears appeals from the highest courts of each state.

C. State and Local Government

There are fifty states of the U.S. and the District of Columbia (Washington, D.C.) is the seat of the federal government. The District of Columbia is not a state but performs many of the functions of both a state and a municipality for its residents. There are U.S. territories such as Puerto Rico and American Samoa which are not states but have a substantial measure of home rule. Neither the District of Columbia nor any U.S. territory has voting representation in the U.S. Congress.

Each state has enacted a constitution which is similar in substance and scope to the U.S. Constitution. Each state government is organized like the federal government with a legislative branch, executive branch and a judicial branch. The U.S. Constitution guarantees to each state a republican form of government. Except for the State of Nebraska, the legislative branches of each state consists of a two chambers. The head of the executive branch is the governor who is elected by popular vote. In many states, the heads of the state departments and agencies which provide services to state residents and enforce state regulatory laws are also elected by popular vote. No state is empowered to conduct its own foreign policy.

Each state is further sub-divided into counties, cities, towns and villages. Each of these subdivisions has a popularly elected executive and a legislative government. In some states, local judges are elected as well. These local governments provide services and enforce laws and regulatory schemes of a local nature.

Section 1-2 The Common Law Legal System

A. Case Law - Stare Decisis

The common law system originated in medieval England after the Norman French conquered England in 1066. The common law system is the foundation of the legal systems of former British colonies such as the U.S. (except Louisiana and Puerto Rico), Canada, Australia, Cyprus, India, Pakistan and Anglophone Africa. The common law system has been described as "anything that is not prohibited is permitted." The law which judges are bound to apply is the law which derives from the prior decisions of other judges. The law does not exist in a code enacted by a sovereign. Referred to as the doctrine of *stare decisis* (Latin for "stand by the decided matter"), common law courts reason from the decisions in prior cases which involve similar facts and circumstances and must apply the holdings in those prior cases to present cases. Another distinctive attribute of the common law system is that trials are conducted by the adversary tradition rather than the inquisitorial tradition of the civil law system.

The civil law tradition evolved from the given law of antiquity through Roman Law, the Codes of Theodosius and Justinian, the Salic Code and the Code of Napoleon. The civil law is foundation of the legal systems of continental Europe, Scotland, francophone Africa, South

America and Middle Eastern countries that were under French dominion such as Egypt, Lebanon and Syria. In the civil law systems, all law flows from a coherent set of legal principles contained in a written code which is provided by or enacted by the sovereign. The civil law tradition has been described as "anything that is not permitted is prohibited."

As modern political and commercial systems have become more complex, common law nations have increasingly codified their laws into statutes. However, courts continue to use the doctrine of *stare decisis* as a method for interpreting or applying a statute. A court is bound by the prior decisions of courts which have interpreted or applied the same or a similar statute.

B. Codes of Laws and Regulations

At all levels of government, law in the U.S. has become increasingly codified. At the federal level, a proposal is enacted into law when it is passed by the House of Representatives and the Senate and signed by the President. These laws are contained in the United States Code. Each federal department and agency is authorized to issue regulations which implement the laws enacted by the Congress and the President and which each such department or agency has the jurisdiction to enforce. These regulations are contained in the Code of Federal Regulations.

At the state level, a proposed law is enacted into law when a majority of the state legislature votes for the law and the governor signs the law. Each state has a code which contains these laws. Each state department and agency issues regulations which implement the enacted laws. These regulations are contained in a state code of regulations. A similar system exists at the county, city, town, and village level.

Whether at the federal, state, or local level, laws that are in statutes are the result of a political compromise among the legislators. While the legislators may agree on the policy underlying the statute, they leave portions of a statute intentionally vague because they disagree on the details of the means by which the statute is to be implemented. They often insert general language or undefined terms in the statute and leave it up to the government agencies or the courts to interpret or apply. Agencies and courts often complain that the terms of a statute they are asked to apply should have decided by the legislators.

Consequently, the agencies and courts have developed a "common law" which interprets and applies statutes. The decisions of agencies and courts make up the law of a statute just as much as does the words of a statute. It is not sufficient to consult only the words of a statute. The judicial or agency decisions which interpret the statute must also be consulted to determine the full meaning and actual application of a statute.

C. Uniform State Laws

Except for the original thirteen states, the other thirty-seven states have joined the U.S. at different times, under different circumstances, and have different histories. The laws of the states traditionally differ, in some ways quite substantially, from one another. In an effort to foster uniformity and predictability among the state laws, the states formed an organization named the National Conference of Commissioners on Uniform State Laws (NCCUSL). The NCCUSL drafts statutes on areas of law, which are not governed by federal law, and recommends these uniform statutes to the states for enactment. The states are not obligated to enact any uniform law. However, over the years, the states have enacted many of these uniform laws in the areas of commercial transactions, family law, and company law.

D. Notaries in the United States

The functions of a notary in the U.S. differ substantially from the functions of a notary in civil law systems. A notary public is commissioned by the states. A notary public need not be an attorney and takes a fairly simple examination which the state gives to qualify as a notary public. The notary public is authorized to take sworn statements and certify the identity of persons who execute legal documents. A notary public does not review the legality of contracts nor authenticate the legal sufficiency of documents.

Section 1-3 The Court System and Dispute Resolution

A. Federal Courts

The judicial branch of the federal government is organized into three basic levels of courts: the federal district courts, federal courts of appeal, and the Supreme Court.

Federal District Courts

The federal district courts are the trial level courts. Federal district courts are allocated to each state. The number of federal courts in a state depends on the size and population of each state. The federal district courts hear both civil and criminal cases. The federal district courts try civil cases which involve either a substantial issue of federal law or causes of action between citizens of different states in which the amount in controversy exceeds $75,000.00. The federal district courts also try criminal cases which allege that an accused person has violated a federal criminal law which is set forth in the U.S. Code. There also specialized federal district level courts which hear tax cases, tort claims against the U.S. government and bankruptcy. The judges are nominated by the President and must be confirmed by a majority vote of the Senate. The judges serve for life or voluntary resignation.

Federal Circuit Appeals Courts

Each federal district court is part of a federal circuit court. Each federal circuit court hears appeals as of right from the decisions of federal district courts which are located in its circuit. Referred to as either federal circuit courts or federal courts of appeal, these courts consider only whether or not the federal district court has made an error of law. The federal courts of appeal take the facts as they have been developed in the federal district courts and do not review the facts for accuracy or credibility. The judges are nominated by the President and must be confirmed by a majority vote of the Senate. The judges serve for life or voluntary resignation.

The Supreme Court of the U.S.

The Supreme Court is the highest court in the U.S. It is composed of nine justices. The justices are nominated by the President and confirmed by a majority vote of the Senate. The justices serve for life or voluntary resignation. The Supreme Court hears appeals from the federal circuit courts as well as appeals from the highest court of each state. There is no appeal as of right to the Supreme Court. An appellant must request that the Supreme Court hear the case. This request is made in a petition for a *writ of certiorari*. The justices of the Supreme Court decide which cases to hear. Of the hundreds of requests made to the Supreme Court each year, it hears on average about eighty cases per year.

B. State and Local Courts

Each state has a judicial branch, which is composed of three basic levels of courts. The trial level courts are referred to as the superior courts. Each county of each state is allocated a state superior court. The superior courts hear all civil and criminal matters arising under state law. Each superior court is part of an appellate division within the state. The appellate divisions hear appeals from the superior courts. Each state has a supreme court which hear appeals from the appellate divisions. The Supreme Court hears appeals from the supreme courts of the states.

C. Alternate Dispute Resolution

Litigation in either federal courts or state courts is time-consuming and expensive. Other forms of dispute resolution have become increasingly popular. Arbitration is the most common form of alternate dispute resolution. The parties submit their dispute to an arbitrator(s) which the parties choose. Before the arbitration begins, the parties can agree either to be bound or not be bound by the decision of the arbitrator. In binding arbitration, the parties are bound by the decision just as they would be bound by a court decision. A binding arbitration decision is submitted to a court, recognized as a judgment of that court, and enforced in the same way in which a judgment of the court would be enforced. Generally, the parties cannot not appeal from the binding decision of an arbitrator. If the parties choose non-binding arbitration, then the decision of the arbitrator is only advisory. If one or more of the parties disagree with the non-binding decision, the parties go to trial in a court.

CHAPTER 2: IMPORTING INTO AND SELLING WITHIN THE UNITED STATES

Section 2-1 Means of Importation

A foreign business person may import into the U.S. either goods or services. As a practical matter, the importer engages the services of a representative, a distributor or a combination of the two. The importer is not required by law to establish any such relationship. However, it is the most efficient way to import into the U.S. The importation of goods is governed by a complex set of customs regulations. The availability of services over the Internet is substantially unregulated.

A. Representative

A representative promotes the goods or services of the importer, obtains and transmits orders and assists in the customs process by which goods enter the U.S. The representative does not take title to any goods nor does the representative perform the services of the importer. The representative is compensated on either a fee basis or a percentage of the dollar value of the sales that the representative generates. The term of the representative agreement is usually between twelve and thirty-six months. Whether the representative agreement is renewed or the term of it is extended depends on an agreed measure of how the representative has performed. That measure is usually a dollar value of the sales generated by the representative. A representative may but need not be an exclusive representative. The terms, scope and time of any such exclusivity are a matter for negotiation and agreement between the importer and the representative.

B. Distributor

A distributor takes title to the goods or performs the services of the importer under a license agreement. The distributor then resells the goods or services in the U.S. The distributor is compensated by the difference between the price at which the distributor pays the importer and the price at which the distributor resells the goods or services. The term of a distributorship agreement is usually based on a minimum level of sales rather than on time. A distributor is usually an exclusive distributor but limited in scope and time.

C. United Nations Convention on the International Sale of Goods (CISG)

The CISG is a default statute for transactions that involve the sale of goods across international borders. The purpose of CISG is to harmonize and unify international trade law in an effort to reduce legal obstacles to international trade and promote the orderly development of new legal concepts in international trade. The U.S. enacted the CISG on January 1, 1988. As of May 1, 2014, seventy-two nations have enacted the CISG. These countries are referred to as Contracting States.

The CISG applies where:

1. The contract is for sale of goods but not for services,
2. The parties have principal places of business are located in different countries.
3. The parties have not agreed to exclude the contract from all of or some of the provisions of CISG.
4. The parties have not agreed to exclude the contract from CISG.

The CISG does not apply to contracts which have the following subjects:

1. Sale of goods bought for personal or household use or by auction,
2. Stocks, negotiable instruments, investment securities,
3. Ships and aircraft,
4. Electricity,
5. The seller sells goods where the preponderant obligation of the seller is to provide services.

The CISG is a default statute. Contracting parties can agree as to whether to have the CISG apply or not apply to the sale of goods contract. However, if the parties do not manifest any such agreement, then CISG applies.

D. The UNIDROIT Principles of Commercial Contracts (UNIDROIT Principles)

The UNIDROIT Principles of Commercial Contracts (referred to as the UNIDROIT Principles) are issued by the International Institute for Unification of Private Law. The Institute is an independent inter-governmental organization based in Rome, Italy. Its purpose is to examine ways of harmonizing and coordinating the private domestic law of member states and prepare for adoption by the member states uniform laws of private law. The Institute serves as a group of uniform law commissioners similar to NCCUSL. Formed in 1926, the Institute has issued uniform laws on international leasing, international wills and international franchising.

The UNIDROIT Principles codify the contract law to be applied in international business transactions. They draw from both civil law legal concepts and common law legal concepts. In form and purpose they are similar to the U.S. Restatement of Contracts. The UNIDROIT Principles can be found at the Institute's website www.unidroit.org.

The UNIDROIT Principles differ from CISG in the following three respects:

1. The CISG is limited to contracts for the sale of goods. The UNIDROIT Principles apply to any type of commercial contract including personal services.

2. The CISG is a treaty between and among nations. Once a nation ratifies CISG, it becomes the domestic law of that nation. The UNIDROIT Principles are a model act, which parties can negotiate and choose to govern their contract.

3. The CISG is a default law, which applies unless the parties agree to exclude their contract from the provisions of CISG. By contrast, he UNIDROIT Principles do not apply unless the parties agree that they apply to the contract.

4. The UNIDROIT Principles are a model act rather than a treaty. They are more practical because they more closely reflect international business practices rather the political and diplomatic compromises that were necessary to conclude CISG.

Section 2-2 U.S. Customs and Border Protection: Entry of Goods

A. Importer of Record

The entry process of goods into the U.S. is regulated and enforced by the U.S. Customs and Border Protection (CBP) which is an agency of the Department of Homeland Security. The entry process begins when goods reach a port of entry of the U.S. from a port outside of the U.S. Goods legally enter the U.S. only after the CBP has authorized entry of the goods and the estimated duties have been paid. The CBP has instituted the Automated Manifest System (AMS) which expedites and simplifies entry of goods process.

The importer must designate a person in the U.S. to serve as the importer of record. The importer of record can be the purchaser of the goods, a licensed agent appointed by the exporter or the purchaser or a consignee. Whatever the legal relationship between the importer and the U.S. person may be, the CBP deems the U.S. person to be the importer of record and the "owner" of the goods for entry purposes even though the U.S. person who is deemed the importer of record does not have legal title to the goods. The CBP will look to the importer of record for the documentation necessary for the CBP to authorize entry of the goods and pay estimated duties.

B. Entry Documents

No later than fifteen days after the goods arrive at the U.S. port of entry, the importer of record or its agent must file the following documents with the port director:

1. Entry Manifest which identifies the goods, importer and the importer of record,

2. Documentation that identifies the importer of record such as a bill of lading or carrier certificate,

3. Commercial invoice or other documentation which sets forth the country of origin, importer, importer of record, description of the goods and the transaction value of the goods,

4. Surety bond for customs duties,

5. Packing lists, if applicable.

C. Examination of Goods

The CBP examines the goods to determine the following:

1. The value of the goods for assessing customs duty which is generally the transaction value reflected on the commercial invoice,

2. Whether the goods are properly marked with the country of origin and any required special marking or labeling,

3. Whether the goods have been correctly invoiced,

4. Whether entry of any of the goods is prohibited,

5. Whether the goods satisfy any special requirements set forth by other federal laws or regulations,

6. Whether the amount of goods listed on the invoice is correct so that there is no shortage or overage.

The CBP may analyze the goods at a CBP laboratory to make any of the foregoing determinations. If the CBP determines that the goods do not conform to the entry documents or otherwise violate U.S. laws, the CBP penalizes the importer of record. An importer of record may protest an adverse determination by the CBP through an administrative action.

D. Classification and Customs Duties

Every good imported into the U.S. is classified according to the categories set forth in the Harmonized Tariff Schedule of the U.S. (HTS). The purpose of HTS classification is to determine which goods are subject to duty and the dollar amount of the duty. The importer of record must properly classify the goods to be imported according to the HTS prior to entry. The importer of record must know the HTS and its system of interpretation to properly classify the imported goods. The HTS classifies goods into five broad categories:

1. goods identified by name
2. goods identified by a general description
3. goods identified by their component materials
4. goods identified by their actual or principal use
5. goods not subject to duty

If a good appears to fit two or more categories, then the good is categorized by applying the HTS system of interpretation, administrative ruling, and case law.

The HTS is set forth in a publication issued in hard copy and electronic form. It is updated periodically by the International Trade Commission of the U.S. Department of Commerce. The HTS is based on the international Harmonized Commodity Coding and Classification System (Harmonized System), which has been established by the World Customs

Organization. Most countries base their tariff schedules on the Harmonized System, making it easier to conduct international trade. The HTS assigns a ten-digit tariff classification number to goods in each category. A rate of duty is assigned to each classification number. There are over 17,000 unique ten-digit HTS classification code numbers.

If the CBP accepts the classification proffered by the importer of record, then the importer of record pays the duties, if any, and the goods are released for entry into the U.S. and the shipment is deemed “liquidated.” If the CBP does not accept the classification proffered by the importer of record then it may change the classification. If the importer of record does not accept the changed classification, the importer may protest the CBP change in classification.

E. Goods Which Require Entry Permission of other Government Agencies

Many categories of goods require the permission of other federal agencies and conformance with the rules of those agencies in addition to CBP rules to enter those goods. Food, alcoholic beverages, textiles, high technology equipment are subject to additional labeling rules and quotas. The importer of record must assure that the goods comply with the rules of the other federal agencies.

F. U.S. Free Trade Agreements

The U.S. has concluded bilateral and multilateral free trade agreements (FTAs) with about seventeen countries including Israel, Australia, Oman, Jordan, Morocco, Mexico and Canada. The primary purpose of the FTAs is to lower or eliminate duties, tariffs and quotas on specified goods usually on a generally reciprocal basis. Goods imported from countries with which the U.S. has an FTA are treated more favorably in terms of duties and quotas than goods imported from countries with which the U.S. does not have an FTA.

The U.S. is negotiating two comprehensive FTAs: the Transatlantic Trade and Investment Partnership (TTIP) with the European Union and the Trans Pacific Agreement (TPA) with twelve countries. Each of these FTAs entail many complicated issues which must be negotiated and resolved. If, however, these FTAs are ultimately agreed and implemented, they will fundamentally alter the means and methods by which international trade is conducted.

Generally, a business entity formed under the law of a state of the U.S. is a U.S. person for the purpose of FTAs. Even though all of the owners of the business entity are foreign nationals, the business entity itself is a U.S. person. Therefore, the business entity may avail itself of the benefits and advantages of an FTA to the same extent as does a business entity owned by U.S. citizens.

Section 2-3 Marking

A. Country of Origin Marking - Special Marking

The country of origin of each good imported into the U.S. must be conspicuously revealed to the ultimate purchaser. Country of origin means the country in which the goods were grown, manufactured or produced. Whether the country of origin must be marked on the individual good or on the outermost container in which the goods are placed depends on the character or nature of the goods. The goods or categories of goods for which the container but not the goods themselves must be marked are listed in the customs regulations. Any good or category of goods which is not on that list must be marked with the country of origin. In either instance, the mark must be legible, indelible and permanent. The country of origin marking must be accurate and not give the false impression that the country of origin of the good is a country other than the country in which the good was grown, manufactured, or produced.

In addition to country of origin marking, certain goods or categories of goods must be marked with other information which specifically describes the goods or lists the components of or the means by which the goods were produced. These special marking requirements are not set by the CBP but rather by the federal agency which regulates the particular good. Food products and alcoholic beverages are subject to additional marking requirements set by the Food and Drug Administration (FDA) and the Alcohol Tobacco Firearms Administration (ATFA).

B. Intellectual Property Rights - Trademarks, Copyrights, and Patents

An intellectual property right is a right in an item that has been produced through a creative process and the ownership of which is protected and enforced by law. Trade/service marks, trade names, copyrights and patents are items of intellectual property. An owner of intellectual property may record their rights with the CBP. The CBP is authorized to determine whether a mark on an imported good infringes a recorded mark or a good infringes a recorded copyright. If the CBP determines that an infringement has occurred the CPB can exclude the good from entry into the U.S. The importer of record must exercise reasonable care to determine that the imported goods do not infringe any recorded ownership right in intellectual property.

The U.S. International Trade Commission (ITC) is authorized to investigate the importation of goods. The ITC enforces U.S. laws which prohibit a foreign person from unfairly competing with domestic goods, substantially injuring a domestic producer of the same goods or restraining or monopolizing commerce and trade in the U.S. If the ITC finds a violation, it is empowered to exclude the goods from entry and issue orders requiring the foreign person to desist from further violations.

Section 2-4 Selling within the United States

A. Interstate Commerce

The Commerce Clause of the U.S. Constitution authorizes Congress to regulate commerce between and among states in order to ensure the flow of interstate commerce is free from restraints imposed by the states. No state can impose barriers to trade and the free movement of goods and services across state borders which would directly burden or interfere with interstate commerce. The states have the inherent right to regulate commerce within state borders. The states may also indirectly affect interstate commerce when the states exercise their legitimate police powers.

B. Contracts of Sale

The fundamental law of contracts is the common law and is not set forth in a code of laws. Contract law is a matter of state law. Except for contracts governed by the Uniform Commercial Code (UCC), contracts for goods and services are governed by the common law of contracts in effect in the state having jurisdiction over the contract. Contract law is not contained in a code but rather in judicial opinions written by judges over the decades. There is no federal contract law except for certain issues in government contracts which are governed by federal law. Contracting parties in the U.S. draft and negotiate contracts which are more comprehensive than contracts drafted and negotiated under the laws of civil law countries.

C. Uniform Commercial Code (UCC)

The UCC is a set of uniform rules that have been enacted, with certain differences, by almost all states and the District of Columbia. It consists of nine Articles:

1. Article 1 contains the general provisions that apply to all transactions covered by the UCC.

2. Article 2 governs the sale of goods,

3. Article 2A governs leases of goods,

4. Article 3 governs commercial paper,

5. Article 4 governs bank deposits and collections,

6. Article 5 governs letters of credit,

7. Article 6 governs bulk transfers,

8. Article 7 governs warehouse receipts, bills of lading and other documents of title,

9. Article 8 governs investment securities and Article 9 governs secured transactions.

The purpose of the UCC is to codify the law of contracts and business practices with respect to the particular areas governed by the nine Articles. Article 2 is especially important because it governs the sale of goods and many of its provisions apply only to sales between merchants. The parties to a sale that would be governed by the UCC can choose not to have the sale governed by the UCC. Article 2 makes substantial changes to the common law of contracts. Article 2 does not govern contracts for labor, services or the sale of land so that those types of contracts are governed by the prevailing common law of contracts.

Section 2-5 Exporting from the United States

A. Export Controls

A good is exported from the U.S. when it is placed with a carrier in a U.S. port and moved outside the U.S. to a foreign destination. The U.S. Constitution prohibits the federal government and any state government from imposing any tax or controls on exports. However, the U.S. government is authorized to impose controls on items which have or may have military or intelligence uses. Controlled items are listed on the International Traffic in Arms Regulation (ITAR). ITAR is administered by the U.S. Department of State. Within ITAR is the U.S. Munitions List (USML).

In 2013, the federal government fundamentally reformed the export control system. The reforms are set forth in a series of rules referred to as the Export Control Reform (ECR). Under ECR, items which are not critical to military or intelligence use are moved from ITAR to a list called Export Administration Regulations (EAR). The EAR is administered by the U.S. Department of Commerce. Items which had been listed on the USML of ITAR are listed on the Commerce Control List (CCL) of EAR. These items are classified into ten categories called the 600 Series. Each item within each category is assigned an Export Control Classification Number (ECCN). The purpose of the ECR is make the export control system more flexible and to assist U.S. manufacturers to sell items in the international market which are not critical to military or intelligence uses.

B. Export Licensing

An exporter who seeks to export a controlled item must determine whether the exporter must obtain an export license. Most of the items in the 600 Series can be exported under an exception to the license requirement. The exception is called the License Exception Strategic Trade Authorization (STA). Items which are eligible to be exported under STA can be exported only to thirty six countries. These countries are NATO countries, most European Union member states and some other countries with which the U.S. has special treaties. If the exporter seeks to export an item which not under STA, then the exporter must apply for and obtain a license to export the item. If a country is not on the STA list, then the exporter is prohibited from exporting most controlled items to that country.

CHAPTER 3: ESTABLISHING A BUSINESS IN THE UNITED STATES

Business entities in the U.S. are established and exist under the laws of the states. Except for certain special types of entities, any business entity formed by a foreign business person is governed by the law of the state in which the business entity is formed as well as the law of each state in which the business entity does business. The law of the state in which the business entity is formed governs the internal affairs of the business entity and the legal relations between and among the owners and managers.

The law of a state in which the business entity does any business governs the legal relations of the company with persons in that state. A business entity which does business in a state other than the state in which it is formed is considered by that state to be a "foreign business entity." The term "foreign business entity" means a business entity which is formed under the laws of a jurisdiction which is not the state in which the business entity does business. In this context, there is no difference between a business entity which is formed under the laws of another state of the U.S. or under the laws of a foreign country.

A foreign business entity must register to do business in any state in which the foreign business entity does "substantial" business. The foreign business entity must comply with the same state laws and regulations which apply to business entities formed and doing business in that state. However, the laws and regulations of the state do not apply to the internal affairs of the foreign business entity. The internal affairs of the foreign business entity are governed by the state or jurisdiction in which the foreign business entity is formed.

Section 3-1 Forming a Legal Entity and Limited Liability

A. The Business Entity and Formation

The business entity is a legal person under the law. Except for a sole proprietorship, a business entity is separate and distinct from its owners. A business entity has virtually the same rights and obligations under the law as does an individual. A business entity can own property in its own name, conclude contracts in its own name and sue or being sued in its own name. Traditionally, there were two categories of legal entities: corporate and non-corporate entities. While the conceptual difference still exists between the two categories, the practical differences between them have mostly been eliminated.

Every state has enacted general business entity formation statutes. The existence of a business entity begins by simply filing the appropriate organizational document with the appropriate department or agency of the state government and paying of the required fee. The document must be signed by an organizer. The organizer can be any person who is authorized by the interest holders and need not be an interest holder. Except for non-corporate business entities formed in the State of New York, no state requires that the formation of a corporate or non-corporate company be published in a newspaper. In most states, with only a computer and a credit card, a company can be formed online.

The interest holder of a corporation, limited liability company and a statutory trust can be a single person. A partnership requires two or more persons. The interest holder can be an individual or another business entity.

B. State Company Statutes

Once the business entity is formed, the interest holders must create the rules by which the internal affairs of the business entity are conducted. These rules are contained in an agreement by the interest holders which includes the rights and obligations of the interest holders with respect to each other. The interest holders have broad discretion on the rules by which the internal affairs of the company are conducted. The state statutes contain mandatory provisions and default provisions for this agreement.

1. Mandatory provisions contain the rules and requirements which must be followed to form the company. Very few mandatory provisions govern the internal affairs of the company. The mandatory provisions with which the interest holders must comply almost always contain the connector “shall” or “must” in the language of the provision.

2. Default provisions contain rules or requirements which govern the internal affairs of the company only if the interest holders have not agreed on an issue covered by the default provisions. Default provisions usually contain the clause “unless otherwise agreed by the [interest holders]” or “in the absence of agreement by the [interest holders].”

3. To avoid the legal effect of a default provision and assure that the particular agreement which the interest holders have made controls on a particular issue, that agreement must be manifested either orally or, preferably, in a written agreement.

C. The Doctrine of Limited Liability

The doctrine of limited liability protects the personal assets of the ultimate interest holder of a business entity. The doctrine prevents a claimant of the business entity from being able to satisfy an obligation which the business entity owes to a creditor of the business entity from the personal asserts of the interest holder. The effect of the doctrine is that a claimant of the business entity can only sue the business entity for an obligation which the business entity incurred to the claimant. The claimant can satisfy any judgment obtained by the claimant only from of the assets of the business entity and not from the personal assets of the interest holders. Traditionally, only shareholders of a corporation had limited liability. Over the years, limited liability has been extended to the partners and members of non-corporate legal entities. The scope and application of the doctrine of limited liability is governed by the law of each state in which the business entity does business.

The doctrine of limited liability does not protect an interest holder from liability if the interest holder commits a wrongful act while he, she or it is an agent of the company. Also, the doctrine of limited liability does not protect an interest holder who has personally guaranteed a contractual obligation of the business entity.

The circumstances under which the doctrine of limited liability does not extend are distinct from those circumstances under which the limited liability is disregarded. The doctrine of limited liability is disregarded if the interest holders are found to be operating the business entity for their personal benefit and not for the purpose for which the business entity was formed and the interest holders are found to be using limited liability for fraudulent purposes, criminal activity or some other improper or unjust purpose. Whether limited liability is disregarded is an issue which is governed by the law of the state in which the company is formed or does business.

Section 3-2 Corporate Business Entities

A. C Corporation

The C Corporation is the basic corporate form. It is available in all states. It is the functional equivalent of a *societe anonyme.* The C Corporation can be a closely-held corporation. In a closely-held corporation the shareholders are also the directors and officers.

The shareholders actively participate in the management of the corporation. The shareholders acquire their shares directly from the corporation.

The C Corporation can also be a public held corporation. The majority of the shares of the corporation are held by the public who acquire the shares through a regulated stock exchange after shares have been duly registered under the federal and states securities laws. The public shareholders elect the directors but are generally passive and do not participate in management. The directors set corporate policy. The directors appoint the officers who actively manage the corporation.

A C Corporation (which has not elected to be an S Corporation) is a taxable entity and must pay tax on its income. Shareholders may transfer any percentage of shares to and from themselves and no such transfer will affect the continuity of the corporation as a taxable entity. Because the corporation is a taxable entity and the shareholders are taxable entities, the income of the corporation is taxed when the corporation receives it. The shareholders must recognize any dollar amount of dividends which the corporation pays to them as income for tax purposes. The C Corporation has the following attributes:

1. The power to act, hold property, sue and be sued in its own name;
2. A legal existence that is separate and distinct from the shareholders;
3. Centralized management in a board of directors which appoints the officers;
4. Free transferability of shares;
5. Shares can be held privately or by the public subject to securities laws;
6. Limited liability for shareholders;
7. Perpetual duration;

8. Must comply with corporate formalities such as formal shareholder meetings, bylaws, elections of directors and board of directors resolutions;

9. Must have at least one shareholder, one director and a president, who may be the same person in single shareholder corporation; and

10. A shareholder can be an individual or another business entity.

A C Corporation can be formed by one or more persons referred to as incorporator(s). The incorporator files articles of incorporation under the laws a state. The purpose of the articles of incorporation is to notify the public that the corporation is formed and exists as a legal person. To be accepted for filing, the articles of incorporation ***must*** contain the following information:

1. Name of the corporation,

2. Number of authorized shares,

3. Designation of a registered agent,

4. Name and address of one or more incorporators, none of whom must be a shareholder, director, or officer of the corporation.

The following items are not required to be included in the articles of incorporation. However, if the shareholders want these items to bind the corporation, management and the shareholders, these items ***must be set forth in the articles of incorporation and not just in the shareholder agreement or by-laws.***

1. Business purpose,

2. Definition or limitation on powers of the corporation,
3. The powers and authority of directors versus shareholders unless the shareholders eliminate the board of directors,

4. Par value for authorized shares, classes or reclassification of shares,

5. Means of internal management of the corporation if not by the board of directors,

6. Whether any personal liability is imposed on the shareholders,

7. Any limitation on the liability of a director,

8. Any obligation of the corporation or shareholders to indemnify a director,

9. Shareholder proposal for and approval of disposition of corporate assets,

10. Pre-emptive or anti-dilution rights of shareholders,

11. Restriction or elimination of the right of the board of directors to sell, lease or exchange all or substantially all of the assets of the corporation in the ordinary course of business.

Governance and Management - No Shareholder Agreement

Unless the shareholders conclude a shareholder agreement, the board of directors has essentially total control over the corporation. For the corporation to be validly formed, the shareholders must elect a board of directors which must consist of at least one director. The directors adopt by-laws which set forth the rules and procedures for the board of directors. The board of directors hires officers to operate the day to day business of the corporation. The shareholders must hold a meeting at least once a year.

The only issues over which the shareholders have absolute approval without a shareholder agreement are:

1. The disposition or sale, lease, exchange the assets of the corporation which would leave the corporation without significant business activity must be approved by a majority of the shares entitled to vote after the directors submit a proposal to the shareholders. The corporation is conclusively deemed to be without significant business activity if any disposition would represent more than 25% of the total assets and 25% income or revenues determined as of the end of the most recent fiscal year.

2. A dissolution of the corporation requires the approval of a majority of the shares entitled to vote after the directors submit a proposal to the shareholders.

Governance and Management - With Shareholder Agreement

The shareholders should but are not required to conclude an agreement which sets forth the legal relationship of the shareholders with each other and with the corporation. Although the shareholder agreement can be set forth in the by-laws or even in the articles of incorporation, the better practice is to make the shareholder agreement a separate document. The shareholder agreement must be in writing. The provisions of the shareholder agreement are enforceable even though these provisions are inconsistent with the state statute which governs corporations.

A shareholder agreement is enforceable even if it:

1. Eliminates the board of directors or restricts the discretion or powers of the board of directors,

2. Governs the authorization or making of distributions whether or not in proportion to ownership of shares subject to certain limitations,

3. Appoints directors or officers of the corporation, their terms of office, or manner of their selection or removal,

4. Governs generally or specific matters, the exercise or division of voting power by or between the shareholders and directors or by or among any of them,

5. Sets the terms and conditions of any agreement for the transfer or use of property or the provision of services between the corporation and any shareholder, director, officer, or employee of the corporation or among any of them,

6. Transfers to one or more shareholders or other persons all or part of the authority to exercise the corporate powers or to manage the business and affairs of the corporation, including the resolution of any issue about which there exists a deadlock among directors or shareholders,

7. Requires dissolution of the corporation at the request of one or more of the shareholders or upon the occurrence of a specified event or contingency; or

8. Otherwise governs the exercise of the corporate powers or the management of the business and affairs of the corporation or the relationship among the shareholders,

> the directors, and the corporation, or among any of them, and is not contrary to public policy.

If the shareholder agreement is not set forth in the articles of incorporation or the by-laws it must be set forth in a separate writing and signed by the shareholders and the corporation. Unless the shareholders otherwise agree, the shareholder agreement is enforceable for no more than ten years. The existence of the shareholder agreement must be noted conspicuously on the front or back of each certificate for outstanding shares or on any required information statement. If the shareholder agreement is not noted, then the purchaser of shares may rescind its purchase of the shares but the shareholder agreement remains in effect. If corporation becomes a publicly held corporation, the shareholder agreement terminates.

Shares and Transfer of Shares

A share of a corporation is in effect a “piece” of the corporation. Shares can be divided into classes that have different rights and obligations. In its simplest form, a share entitles the shareholder to a dividend which is a share of the profits of the corporation, a right to elect directors to the board and a right to share in the appreciation of corporate property. There is no distinction between common and preferred shares. The corporation should issue share certificates but share certificates are not required as evidence of ownership of the shares.

Shares are freely transferable unless the corporation has restricted the transfer of shares. The number and type of shares that a corporation is legally able to issue must be set forth in the articles of incorporation and are referred to as authorized shares. The number and type of authorized shares that the corporation sells to shareholders are referred to as “issued” shares. The number of issued shares can never exceed the number of authorized shares. The benefits and rights to which shares are entitled must be set forth in the shareholder agreement or the articles of incorporation.

The percentage of the shares which shareholder holds can be "diluted" with each additional share that a corporation issues. Anti-dilution rights entitle a shareholder to be issued a sufficient number of shares to maintain its percentage ownership in the corporation every time the corporation issues shares to any other shareholder. The shareholder with anti-dilution rights does not pay any additional consideration for the shares but rather the capital stock structure of the corporation is adjusted to maintain the percentage that existed before the new shares were issued. Anti-dilution rights must be set forth in the articles of incorporation or they do not exist.

Pre-emptive rights achieve the same objective as anti-dilution rights but the mechanism differs. A shareholder with pre-emptive rights is entitled to purchase for value a sufficient number of shares to maintain its percentage, usually but not necessarily at a discount, whenever the corporation issues new shares. Pre-emptive rights must be set forth in the articles of incorporation or they do not exist.

B. Statutory Close Corporation

The statutory close corporation (SCC) has the same corporate attributes as a C Corporation. The crucial difference is that an SCC can be operated and managed directly by the shareholders without a board of directors or officers. The SCC is not obligated to comply with any of the corporate formalities with which the C Corporation must comply.

To become and remain an SCC, the corporation must satisfy the following three conditions:

1. The number of shareholders is limited to 35;
2. The transfer of shares of all classes is restricted; and
3. The shares of the corporation have not been and will never be offered to the public.

If the SCC fails to comply with each of the three conditions, then the corporation is no longer has its close corporation status. The corporation must then operate as a C Corporation and elected directors, adopt bylaws and maintain all of the corporate formalities. If the event which causes the corporation to lose inadvertently or mistakenly occurs, the corporation can rectify the event and re acquire is close corporation status.

To be formed as an SCC, a C Corporation files the same articles of incorporation which it would file to be a C Corporation. In addition, the articles contain a notice that the C Corporation will operate as an SCC and comply with the three conditions. If C Corporation has already been formed, it can become an SCC by amending its articles of incorporation to include the notice and that it will comply with the three conditions.

The SCC is managed directly by the shareholders. The shareholders should but are not required to conclude a shareholder agreement. The SCC is not required to elect a board of directors and appoint officers. Any shareholder, who is appointed an agent by a shareholder resolution, can legally bind the SCC. An SCC is taxed in the same way in which a C Corporation is taxed. Due to changes in their corporate laws, many states have eliminated the SCC.

C. S Corporation Choice

An S Corporation is a C Corporation or a professional corporation which chooses not to be taxed at the corporate level. The S Corporation is taxed only at the shareholder level similar to the way in which a partnership is taxed. A C Corporation qualifies to be an S Corporation as long as the C Corporation:

1. Is formed under the laws of a state of the U.S.,
2. Has no more than one hundred shareholders, each of whom is an individual who is U. S. citizen or a foreign national who is permanent resident of the U.S.,
3. Has one class of stock,
4. Does not have shareholder which is a partnership, another corporation, a financial institution or an insurance company,
5. Does not have and will never have shares which are held by the public.

If the C Corporation conducts business before it has chosen to be an S corporation, then there is a limit on the amount of income the C Corporation can earn from rents, royalties, dividends and other passive income once the C Corporation becomes an S corporation.

A C Corporation becomes an S Corporation by filing the appropriate S Corporation form with the IRS and which must be filed at the times prescribed by the IRS. Each shareholder must consent to the S Corporation choice. By the vote of a simple majority, the shareholders can terminate the S Corporation choice. A C Corporation which is an S Corporation but then fails to comply with one or more of the S Corporation qualifications loses its S Corporation status without any act of the shareholders. The former S Corporation is then immediately taxed as a C Corporation.

Most items of income and loss are passed through to the shareholders. The effect of this "pass through" treatment is that the S Corporation reports items of income and deduction but does not pay any tax. Instead, the shareholders are taxed on their proportionate share of income, deductions and credits which accrue to them from the S Corporation even if they do not actually receive any dividends. Unlike a partnership, an S Corporation is still taxed at the corporate level on any items of income and losses which are not or cannot be passed through to the shareholders. The S Corporation status is effective only for federal taxes. Not all states recognize the S Corporation for state tax purposes. In those states, an S Corporation is taxed in the same way in which in which the state taxes a C Corporation.

D. Professional Corporation or Professional Association

The sole business purpose of a Professional Corporation (referred to as a PC or PA) is to render professional services through the shareholders, directors or officers of the PC. A professional service is one that can be lawfully rendered by a person who holds a duly issued license to render that service. The corporate name must contain the words "professional corporation", "P.C., "P.A." or "chartered" but cannot contain the words "company", "incorporated" or "limited" or any abbreviation of those words. In addition to the information which must be set forth in the articles of incorporation of a C Corporation, the articles of incorporation of a PC must set forth:

1. A description of the professional services to be rendered,
2. Names and addresses of the original shareholders of the PC,
3. A statement that each original shareholder and director is licensed to render the professional service for which the PC was organized.

The PC is managed by a board of directors and appointed officers like a C Corporation. The PC may elect to be an SCC and be managed directly by the shareholders. No person other than a licensed professional can be a shareholder, director or officer of a PC. There are no restrictions on the types or classes of shares in a PC. Like a C Corporation or SCC, the shareholders of a PC should conclude a shareholder agreement. Only a licensed professional can be a shareholder of a PC so that shares can be transferred only to a person who is a licensed professional. A PC must dissolve when it no longer has any shareholders who are licensed professionals.

E. Not For Profit Corporation

A not for profit corporation is a corporation in which no part of the income of the entity is distributed to its members, directors or officers. The not for profit corporation may compensate such persons for the reasonable value of services rendered to the corporation. A not for profit corporation does not have shareholders or shares. Persons participate in the management and governance of a not for profit corporation by becoming members or serving as directors or officers.

Although a not for profit corporation may carry on any lawful activity, such corporations traditionally engage in activities such as education, religion, trade and commercial promotion and charity. A not for profit corporation is not to be confused with a tax exempt corporation. A tax exempt corporation is a not for profit corporation that has applied for and been granted an exemption from taxation by the IRS. In many but not all states, if a not for profit corporation has been granted tax exempt status under the federal tax law, it will be granted tax exempt status under state tax law.

Section 3-3 Non-Corporate Legal Entities

A. Sole Proprietorship

A sole proprietorship is not a business entity. The operations and the assets of the business are controlled and owned by one person. That person receives all profits and bears all losses. The sole proprietor does not have limited liability. If there is a person who is associated with the sole proprietor, that other person must be either an employee or an independent contractor of the sole proprietor.

Other than registering for any necessary local business license, a sole proprietor is not required to make any government filings or maintain any organizational formalities. The sole proprietor is taxed in same way in which an individual is taxed.

B. General Partnership

Most states have enacted the Revised Uniform Partnership Act (RUPA) which enables the formation of a general partnership (GP). A GP is a legal entity which is separate and distinct from its partners. A GP does not have perpetual duration but may exist forever. It must be formed by two or more persons who become partners. The GP exists only as long as the GP has two or more partners. A partner can be a natural person or a business entity. Each partner is personally liable for each debt and obligation of the GP which cannot be satisfied out of the assets of the GP.

Formation

A GP is created by a contract between two or more persons to engage in a business for profit. The contract requires each person to make a contribution to GP which enables the GP to conduct it business. A contribution is an item of value which is usually cash but may also be property or services. A GP can be implied at law or be deemed to exist by estoppel if two or more persons act as partners. No document such as articles of incorporation is filed with a state authority to create a GP. A GP can be an "at will" partnership which means that the GP exists for so long as partners agree that it exists. A GP can be a "partnership for a definite term or undertaking" which means that the GP exists until a time or completion of a project set by the partners.

Governance and Management

The GP is a highly flexible form of business entity. The partners are able to arrange the financial, management and governance affairs of the GP as they agree among themselves. This agreement should be set forth in written partnership agreement. The only matters which the partners cannot change or restrict by agreement are the following:

1. Eliminate the duty of loyalty or unreasonably reduce the duty of care each of which is implied in every contract,

2. Eliminate the obligation of good faith and fair dealing which is implied in every contract

3. Eliminate or restrict the power of a partner to cease to be a partner,

4. Change the law which enables the GP to choose to be a limited liability partnership, and

5. Restrict the rights of persons other partners who deal with the GP.

The unit of ownership is called the ownership interest. An ownership interest is calculated as the percentage that the value of the contribution of a partner bears in relation to the sum total contributions of all of the partners. Partners can collectively hold a maximum of 100% in ownership interests. The ownership interest of a partner decreases with distributions made to a partner and increases with contributions made by a partner. Each partner participates in the financial, management and governance rights of the GP according to the percentage of the ownership interest of each such partner. For most partnership issues, each partner is assigned one vote for each one percent point of ownership interest. Some fundamental issues are decided *per capita* which means that each partner has one vote.

Dissociation

When a partner ceases to be partner, that partner is said to dissociate from the GP. A partner can dissociate from the GP by the express will of that partner. Dissociating by express will means that the partner has chosen voluntarily to cease to be a partner. The partners cannot agree to eliminate or restrict the power of a partner to dissociate by express will. However, the partners can agree that a partner who dissociates by express will is liable to the GP for damages caused by the dissociation. If the partners have agreed that the dissociation of a partner by express will does not cause the GP to dissolve, then the GP does not dissolve when a partner dissociates by express will. If the partners have not agreed on the effect of dissociation and the GP is an “at will” partnership, then a dissociation causes the GP to dissolve. Also, if the partners have not agreed but the GP is a “partnership for a definite time or undertaking,” then the dissociation of a partner by express does not dissolve the GP.

A partner can also dissociate from the GP as the result an event which is set forth in the GP statute. Expulsion of a partner, death, dissolution, or bankruptcy of a partner are statutory events in dissolution. The partners can agree as to whether or not all or any one of these events causes the GP to dissolve. If the partners have not made any such agreement and the GP is an “at will” GP, then no statutory event in dissociation causes the GP to dissolve. Also, if the partners have not made any such agreement and the GP is a "partnership for a definite time or undertaking" then the GP dissolves when a statutory event in dissociation occurs.

Dissolution and Wind-up

When an event in dissociation occurs which does not cause the GP to dissolve, the dissociated partner can no longer has or can exercise any financial rights, management rights or governance rights. The GP remains in existence and in business. Unless the partners have otherwise agreed, the GP must purchase the ownership interest of the dissociated partner for essentially the value that the ownership interest would have had if the GP had dissolved and wound up.

When an event in dissolution occurs which causes the GP to dissolve, the GP does not conduct any new business but continues to exist only to wind up. The winding up process involves settling accounts and returning contributions to the partners. When the wind up process is complete, the GP ceases to exist.

Taxation

A GP is not a taxable entity for federal tax purposes but must report to the IRS, for information purposes, the income distributed to the partners in each year. Items of profit, loss, deduction, and credit are passed through and allocated to each partner in proportion to either their respective ownership interests or as the partners have otherwise agreed. Any agreed allocations which are not in proportion to the ownership interests must be consistent with substantial economic reality.

C. Limited Liability Partnership

A limited liability partnership (LLP) is a special form of GP. The principle that each partner is individually liable for the debts and obligations of the partnership is altered. A partner in an LLP is not individually liable for any debt or obligation of the LLP, whether grounded in tort or contract, arising from any act or omission of the LLP or of any partner solely by reason of being or acting as a partner. An LLP has all of the other attributes of a GP.

A GP becomes an LLP by filing a statement of qualification with the state authority which sets forth the following:

1. Name of the LLP.
2. Name and address of the registered agent for service of process
3. Affirmative statement of election to be an LLP
4. Signed by a partner.

D. Limited Partnership

Most states have enacted the Revised Uniform Limited Partnership Act (RULPA). A limited partnership (LP) is a business entity which is formed by two or more persons in which at least one of the partners (referred to as the general partner) is not afforded limited liability. A creditor may satisfy its judgment or obligation against the LP from the personal assets of the general partner. At least one other partner must have limited liability, (referred to as the limited partner). In most other respects, an LP is similar or the same in concept as the GP. Generally, a limited partner may actively manage the business of the LP without the risk of being deemed a general partner. An LP is taxed in the same way as a GP.

Like the GP, the LP is a highly flexible form of business entity. The partners can arrange the financial, management and governance affairs of the LP as they so choose. An LP is formed by filing a certificate of limited partnership with the state authority. The certificate must set forth:

1. Name of the LP
2. Name and address of the registered agent for service of process
3. Name, address and signature of each general partner
4. The latest date on which the LP shall dissolve

E. Limited Liability Limited Partnership

A limited liability limited partnership (LLLP) is a limited partnership in which the partners have chosen to be a limited liability limited partnership. The effect of the election is that the general partner has limited liability.

An LP becomes an LLLP by filing a statement of qualification with the appropriate state authority which sets forth the following:

1. Name of the LLLP.
2. Name and address of the registered agent for service of process
3. Affirmative statement of election to be an LLLP
4. Signed by a partner.

F. Limited Liability Company

Attributes and Formation

A limited liability company (LLC) is a business entity separate and distinct from its members. An LLC must have at least one member. An LLC may hold property in its own name, conclude contracts in its own name and sue or be sued in its own name. The members of an LLC are afforded limited liability. The existence of an LLC commences when articles of organization are filed with the state authority. The articles of organization must set forth:

1. Name of the LLC
2. Name and address of the registered a for service of process
3. Principal office of the LLC
4. Duration of the LLC, either perpetual or time period
5. Name, address, and signature of at least one organizer who needs not be a member
6. Written consent of registered agent to serve as registered agent

Management

An LLC can be managed directly by the members or the members can delegate some or all management powers to managers designated by the members. A manager can but need not be a member of the LLC. The delegation of management powers to manager(s) must be made expressly in either the articles of organization or the operating agreement. An LLC must create and maintain at its place of business the names and identifying information of each member, copies of the articles of organization as they may be amended and the certificate of organization as it may be amended, copies of all local, state and federal l tax returns and reports for the three most recent years, copies of any operating agreement and a description of the contribution of each member to the LLC. The failure of the LLC to create and maintain the foregoing information does not cause the LLC to lose its status as an LLC. However, a member may seek redress against the LLC for such failure.

Operating Agreement

The operating agreement is the contract made by the members that governs the relationship between the members and the LLC and the relationship between and among the members. An operating agreement is not required for the LLC to be validly formed. However, it is the most significant document in an LLC because it sets forth the internal affairs of the LLC and the manner in which the business will be conducted. It may contain any provision for the governance, management and operation of the LLC that the members so choose. It may also govern the legal and financial relationship between and among the members. If the members do not conclude an operating agreement, then the internal affairs of the LLC will be governed by the default provisions of the applicable state LLC statute. Wisconsin, Minnesota and New York require that the operating agreement be in writing to be enforceable.

Dissolution and Termination

An LLC must dissolve and terminate when an event which is specified in the articles of organization or the operating agreement occurs, upon the unanimous consent of the members, upon judicial dissolution or if the LLC has no members for ninety consecutive days. No other event can cause an LLC to dissolve and terminate.

Taxation

An LLC may choose whether to be classified as a corporation or a partnership for federal fax purposes. Most of the states recognize the choice made by the LLC for federal tax purposes when classifying an LLC for state tax purposes. If the LLC chooses to be classified as corporation it will be taxed on income at the entity level and distributions to the members are taxed to the members as individuals. If the LLC chooses to be classified as a partnership, then the LLC is not taxed at the entity level and all tax effects are passed through to the members.

G. Business Trust

Attributes

The business trust (BT) is also referred to as a Massachusetts trust or a common law trust. The BT was traditionally a "half measure" between a corporation and a partnership. Legal title to the property of the trust is held by trustees for the benefit of the owners of the property under a trust instrument that sets forth the terms and conditions of the management of the trust property and the duties of the trustees. Trust agreements and trustee-beneficiary relationships are governed by the law of trusts. Mutual funds, real estate investment trust and other businesses which have passive investors whose investments are managed by other persons use the BT.

The primary advantages of a BT are that it is a flexible business entity and that it is governed by trust law. The primary disadvantage is that only about twenty five states have enacted some form of a statute governing BTs. In a state that has not enacted a BT statute, the BT may be subject to the common law of business trusts which can be uncertain and non-uniform.

Formation

A BT is formed by filing a Certificate of Trust that contains the following:

1. Name of the BT,
2. Name and address of the resident agent, and
3. Address of principal office in the state.

Governing Instrument

A BT may conduct any lawful business except insurance and banking. BTs are most popular with investment companies and mutual funds. A BT is a separate legal entity and distinct from the beneficial owner. A BT may sue or be sue in its own name, contract in its own name and hold real and personal property in its own name. A BT is managed by a trustee(s). The beneficial owner can be a trustee. The trustee may appoint officers to act for or on behalf of the BT. Each beneficial owner is afforded limited liability. A creditor of a beneficial owner cannot reach the assets of the BT. A trustee is not personally liable to third persons while acting as a trustee. A trustee is liable to the trust and the beneficial owner to the same extent that a director of a corporation is liable to the corporation and the shareholders.

The governing instrument is the functional equivalent of the operating agreement or shareholder agreement. There are virtually no mandates or requirements as to the contents of the governing instrument except that it must be in writing and must contain language indicating a present intent to create a trust. A BT has perpetual duration. It can dissolve only as set forth in the governing instrument. A BT is generally taxed in the same manner as an LLC.

H. Cooperatives

The cooperative is an entity which is owned and democratically controlled by persons who use the goods or services of the cooperative and the business benefits are distributed equitably among the users based on the magnitude of the use that each user makes of the goods or services. The cooperative is based on three interrelated principles: the member-owner principle; the member-control principle and the member-benefits principle. The business purpose of a cooperative is to purchase and market the products or services of its members and procure supplies for resale to the members. The members are afforded limited liability.

The member-owner principle holds that a cooperative is owned by those who use the goods or services of the cooperative. Ownership by persons who are not users is discouraged or even prohibited. The member-control principle holds that the governance and management rights of the cooperative are exercised in a democratic manner. Each member has only one share and each share has only one vote.

Other entities distribute profits to its owners based on the percentage interest which each owner has received in exchange for an investment in the entity. By contrast, a cooperative distributes profits based on the percentage of the total use of the goods or services of the cooperative each member makes. Use of the goods and services is referred to as "patronage." The more a member uses the goods or services of a cooperative, the greater share of the profits the member receives.

Cooperatives are not taxable entities but may pay taxes on profits from non-member businesses. Cooperatives pay property taxes, sales and use taxes. For tax purposes, cooperatives are treated like other pass-through entities such as partnerships and LLCs. Individual cooperative members are each taxed on the distributions they respectively receive based on their patronage.

I. Unincorporated Not For Profit Association

A UNA is a legal entity which is separate and distinct from its members which performs a non-profit purpose. The members have limited liability. Two or more members can form a UNA by agreement for a non-profit purpose. The governing instrument sets forth the management and governance of the UNA. No filing with any state authority is required unless the UNA seeks to purchase or sell real property.

Section 3-4 Employer - Employee Relationship

A. At Will Employees

Most workers in the U.S. who are not union members are “at will” employees. This means there is no formal contract between the employer and the employee. The employer can terminate the “at will” employee at any time, for any lawful reason or for no reason at all. Similarly, an “at will” employee can terminate his or her employment with the employer at any time, for any reason or for no reason at all. The employer is obligated to withhold federal, state and local income taxes and social security taxes from the pay of the employee and pay those dollar amounts to the appropriate federal and state tax authority. An employer cannot legally terminate an “at will” employee if the law of the state in which the place of employment is located implies a contract between the employer and the employee or if the reason for termination is prohibited by statute.

Even if there is no formal contract which sets forth the terms of employment and termination, most states will imply a contract, the terms of which are deemed to be items contained in written personnel policies of the employer, how the employer treats similarly situated employees and statements made to the employee by the management of the employer. An employer is prohibited from terminating an “at will” employee for any reason that is based on the race, color, creed, national origin, marital or disability status or sexual orientation of the employee.

B. Employee Under Contract

The legal relationship between an employee under contract and an employer is governed by the contract which the parties execute. The employment contract is governed by state law and generally enforced in the same manner as any other contract. The employer is obligated to withhold federal, state income taxes and social security taxes from the pay of the employee and pay those amounts to the appropriate federal and state tax authority. Employees under contract are usually management or executive employees. The terms and conditions of the contract will govern issues such as termination. However, the employer and employee under contract cannot agree to terminate the contract for any reason that is prohibited by statute.

C. Independent Contractors

An independent contractor is not an employee and has none of the legal or statutory protections of an "at will" employee or an employee under contract. The most common independent contractor is a person or legal entity that renders professional services such as a medical doctor, attorney or architect. The terms of the legal relationship are governed by the agreement between the parties. The employer is not obligated to withhold federal, state income taxes and social security taxes from the pay of the an independent contractor.

Whether a person is an independent contractor is determined by the economic realities of the relationship. The parties cannot merely label the person as an independent contractor. Although there is no legal definition of an independent contractor, the following factors are considered in determining whether a person is an independent contractor or an employee:

1. The most important factor, though not the dispositive factor, is the extent to which the employer has the right to control the "means and manner" by and in which the person performs

2. The kind of occupation, with reference to whether the work usually is done under the direction of a supervisor or is done by a specialist without supervision,
3. The skill required in the particular occupation,
4. Whether the person furnishes the equipment used and the place of work,
5. The length of time during which the person worked,
6. The method of payment,
7. The manner in which the work relationship terminated,
8. Whether annual leave is afforded,
9. Whether the work is an integral part of the business of the employer,
10. Whether the person accumulates retirement benefits.

D. Fair Labor Standards Act (FLSA)

The Fair Labor Standards Act (referred to as FLSA) is a federal law which mandates the minimum wage for hours worked and overtime pay for hours worked over fourty hours per work week. Many states have enacted similar laws. A similar state law can mandate a higher minimum wage, lower hours per work week and a higher rate of overtime pay. No state can mandate a lower minimum wage, higher hours per work week or a lower rate of overtime pay than is mandated by the FLSA.

The minimums in the FLSA apply to most employees. However, certain categories of employees are exempt (referred to as exempt employee) from the minimums because of the nature of the jobs they perform. An employer is not obligated to comply with the FLSA nor with any similar state law which sets forth similar exempt employee categories. The FLSA does not apply to independent contractors. The most common exempt categories are:

Executive Exemption

An employee is an executive if he or she is paid on a salary basis at a rate of not less than $455.00 per week, manages the enterprise or a department or subdivision of the enterprise, regularly direct at least two other full time employees, and is authorized to hire and fire or participate in such decisions in a meaningful way.

Administrative Exemption

An employee is administrative if he or she is paid on a salary or fee basis at a rate of not less than $455.00 per week, performs office or non-manual work directly related to the business or customers of the business, and exercises discretion and independent judgment on significant matters.

Professional Exemption

An employee is a professional if he or she is paid on a salary or fee basis at a rate of not less than $455.00 per week and performs work which requires advanced knowledge. Advanced knowledge must be in a field of science or learning and acquired through prolonged course of intellectual instruction.

Highly Compensated Employee Exemption

An employee is a highly compensated employee if he or she is paid total annual compensation that exceeds $100,000 on a salary or fee basis at a rate of not less than $455.00 per week. He or she must perform at least one duty under any of the Executive, Administrative, or Professional categories.

Computer Employee Exemption

An employee is a computer employee if he or she is paid on a salary or fee basis at a rate of not less than $455.00 per week or compensated at an hourly rate of no less than $27.63 per hour. He or she must be a computer systems analyst, computer programmer, software engineer, or similarly skilled worker in the computer field.

E. Collective Bargaining Agreements

Collective bargaining agreements are the result of negotiations between an employer and a group of employees with respect to the terms and conditions of employment. Generally, the group of employees is represented by a union or other labor organization. Collective bargaining is governed by federal and state statutory laws, administrative agency regulations, and judicial decisions. The federal collective bargaining laws preempt any state collective bargaining laws. The National Labor Relations Act (NLRA) is the federal statute that governs collective bargaining agreements and right of employees to unions.

The NLRA establishes procedures for the selection of a labor organization to represent a group of employees in collective bargaining. The NLRA prohibits employers from interfering with this selection. The NLRA requires the employer to bargain with the appointed representative of its employees. It does not require either side to agree to a proposal or make concessions but does establish procedural guidelines on good faith bargaining. The NLRA also establishes rules as to the tactics (e.g. strikes, lock-outs, picketing) each side may use in the course of collective bargaining. State laws regulate collective bargaining for employers and employees who are not subject to the NLRA.

Section 3-5 Raising Capital

A. Debt Financing

Debt financing is merely an unconditional promise to pay a stated sum of money at a future time along with periodic payments of interest until or at that time. The obligation to pay is usually secured by assets of the borrower and takes many different forms from a simple loan to complicated bonds and debentures. The obligation to pay is usually but need not be superior to any other payment obligation of the borrower. Generally, the borrowing entity must have tangible and appreciating assets to obtain debt financing. Sophisticated debt financing such as bonds and debentures are generally available only to large publically traded companies.

If the borrower lacks assets to which it can grant a security interest to the lender, then the owner must personally guarantee the debt obligation. This means that the owner of the borrowing entity must pledge the owner's personal assets to repay the debt if the borrowing entity is unable to pay. Such a guarantee is a personal obligation of the owner. The limited liability of the borrowing entity does not protect the personal assets of the owner from levy by the lender.

B. Equity Financing

Equity financing is more common than debt financing privately held entities. Equity financing means that investors contribute cash or other assets to an entity which is used in the business of the entity in exchange for an ownership interest in the entity. With equity financing the owners can either participate fully in the management of the business or, if they so choose, concentrate management in managers or in a few members and not participate in the at all in the management of the business. Unlike debt financing, the entity is not obligated to pay back the amount of the contribution in equity financing. The investor is entitled to share in the profits of the business and the appreciation in the value of the assets of the entity.

The most significant difference between debt financing and equity financing is that most simple forms of debt financing are not subject to either the federal or state securities laws. There are also tax and bankruptcy consequences to debt financing that are different from the tax or bankruptcy consequences of equity financing. It is possible to combine debt and equity financing in creative ways.

C. Securities Laws

Generally, the securities laws regulate equity financing and not debt financing. The purpose of the securities laws is disclosure. A share of stock, an ownership interest in GP or LP and a membership interest in an LLC are securities. A business entity (referred to as the issuer) which sells securities to persons who participate in the profits but not in the management or governance of the entity must disclose certain information about the business entity, the management, and the business of the legal entity.

The disclosures are made in a document called a registration statement which must be filed with the U.S. Securities and Exchange Commission (SEC) and the securities regulatory authorities of each state in which the issuer intends to offer or sell its securities. The SEC and the relevant state securities regulatory authorities examine the registration statement to determine whether the issuer has fully and fairly disclosed the information which must be disclosed under the securities laws. Only after the SEC and the state authority have approved the registration statement is the issuer legally able to solicit investors and sell its securities. The registration process can be prolonged and costly. The penalties for selling securities without the requisite approvals can be severe. The mere offer or sale of securities even without any fraudulent or criminal intent is sufficient to incur at least civil liability. Violations of federal securities laws are punishable by fines and, in the case of willful violations, imprisonment.

Because it is neither necessary to the policy objective of the securities nor practical to subject all securities and securities transactions to the registration requirements of the securities laws, a narrow category of securities and certain types of securities transactions are exempt from the registration requirements. The types of securities that are exempt from registration are bonds or other securities issued by a governmental subdivision, industrial revenue bonds and securities issued by or for the benefit of certain not for profit entities.

Business entities generally are not qualified to issue exempt securities. However, they can structure the transaction in which they sell their securities to be exempt from the registration process. Among the types of securities transactions that are exempt are those transactions which do not involve an offering to the general public but rather an offering to a small group of investors who have a preexisting and substantial relationship with the issuer. If the transaction qualifies under one or more of the enumerated exemptions from registration, then the business entity is not required to file a registration statement. The exemption enables the issuer to avoid the registration process. But the issuer must still make disclosures to persons to whom the issuer offers securities of the issuer.

D. Crowdfunding

Crowdfunding is a method by which a business entity raises capital from a large number of people who pay relatively small dollar amounts. The business entity uses an online intermediary on the Internet as the mechanism for raising the capital. Referred to as platforms or portals, these intermediaries are websites or social media on which business entities make crowdfunding opportunities available to funders for the business entity. In a way, these intermediaries roughly perform the function of a stock exchange by creating an online "marketplace." The business entity places its business concept and financial information on the website. There are intermediaries which specialize in certain types of business concepts. The business entity should seek an intermediary which promotes the type of business in which the business engages. Crowdfunding is a new concept. The SEC and state securities authorities are still trying to determine whether to regulate crowdfunding and, if so, how to regulate crowdfunding.

Section 3-6 Non-Immigrant Business Immigration

A. Visa Waiver Program

A foreign national from a country which has been approved under the Visa Waiver Program (VWP) is eligible to enter and remain in the U.S. without a visa for no more than ninety days. The foreign national cannot extend the ninety day period except for a medical emergency and then only for thirty days. The foreign national cannot change to another immigration status while in the U.S. The foreign national must have a residence abroad and intend to return to that residence.

The purpose of the visit must be for business, pleasure or transit. These terms are broadly construed. For a foreign national who is a business person, that person cannot accrue or receive profits from a U.S. source. Any business activities which the business person conducts in the U.S. must be incidental to the business that the person conducts outside of the U.S. The business activities which that person conducts in U.S. cannot be primary or independent of the business which that person conducts outside of the U.S.

The foreign national must hold a biometric e-passport which is valid for at least six months beyond the last date of the intended visit. The foreign national must complete the online Electronic System for Travel Authorization (ESTA) no later than seventy-two hours before the time of travel. A foreign national who is excludable from the U.S. on any grounds such as criminal activity is not eligible for VWP and can be excluded at the point of entry.

Citizens of the following countries are eligible to enter the U.S. under the VWP: Andorra, Australia, Austria, Belgium, Brunei, Chile, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Japan, Latvia, Liechtenstein, Lithuania, Luxembourg, Malta, Monaco, the Netherlands, New Zealand, Norway, Portugal, San Marino, Singapore, Slovakia, Slovenia, South Korea, Spain, Sweden, Switzerland, Taiwan and the United Kingdom.

Canada is not a VWP country. However, Canadian citizens are entitled to the privileges of a foreign national from a VWP country as well as certain special privileges. Among these privileges is that the duration of the stay is six months on a single visit and no more than six months in the aggregate every twelve months.

B. B-1 (Business Visitor) and B-2 (Tourist) Visas

A foreign national who is not a citizen of a VWP country nor a citizen of Canada must apply for and obtain a B-1 or B-2 visa from a U.S. consulate. A foreign national who is a citizen of VWP country or a Canadian citizen but seeks to stay longer than ninety days or cannot obtain online travel authorization must apply for and obtain a B-1 or B-2 visa.

For a B-1 or B-2 visa, the foreign national must appear in person at a U.S. consulate. The foreign national must demonstrate that he or she:

1. is entering the U.S. for business, tourism or medical treatment,

2. has a residence outside of the U.S. and intends to return to that residence, and

3. has the means to support himself or herself while in the U.S. without working in the U.S.

C. Temporary Workers (H, P and O Visas)

A foreign national who enters the U.S. to work on a temporary basis must be at least one of the following persons:

1. A person of distinguished merit and ability who performs services of an exceptional nature which require merit and ability,

2. A person who performs other kinds of services or labor if persons capable of performing such services or labor cannot be found in the U.S., or

3. A person who is a trainee.

The prospective employer or trainer must apply to the USCIS on behalf of the foreign national. Each of the temporary worker visas is a nonimmigrant visa. A person who receives this type of visa cannot use this visa to apply for permanent residency or U.S. citizenship. There is a limit on the number of visas which the USCIS grant in each year.

D. Intra-Company Transferee (L-1A, L-1B Visa)

A foreign national who is a manager/executive or an employee with specialized knowledge of a non-U.S. company which has a U.S. parent, subsidiary or affiliate may enter and work for such a U.S. entity on an L-1A or L-1B Visa. The L Visa is a nonimmigrant visa. However, unlike the visas described in B above, the foreign national can use the L visa to apply for permanent residency or U.S. citizenship. Each of the foreign national and the U.S. entity must satisfy certain qualifications.

Foreign National Qualifications

The foreign national must have been employed abroad by the non-U.S. company for at least one year out of the past three years as either a manager or executive with supervisory authority (L-1A Visa) or as an employee with specialized knowledge with skills specific to the business of the non-U.S. company which are not readily available in the U.S., (L-2B Visa).

Non-U.S. Company Qualifications

The non-U.S. company must own 50% or more of the U.S. subsidiary and have the power to control the decisions of the U.S. subsidiary. Alternatively, the non-U.S. company qualifies if 50% or more of its interests are owned by a U.S. parent. The non-U.S. company also qualifies if 50% of the interests of a U.S. affiliate is owned by the same parent or by a branch office in the U.S. which is more than merely an agent or representative.

Time and Renewals

The L-1A Visa is granted for an initial three-year period and can be renewed two times for two years for each renewal for a total of seven years. The L-1B is granted for an initial three-year period and can be renewed once for two years for a total of five years.

E. Treaty Trader (E-1 Visa)

A foreign national may apply for an E-1 Visa which enables the foreign national to enter the U.S. to carry on substantial trade principally between the U.S. and the nation of the foreign national. The foreign national can be an individual, a legal entity or the employee of an individual or legal entity. As an initial requirement, a treaty of commerce, navigation and friendship must be in effect between the U.S. and the country of the foreign national.

The following conditions must be satisfied:

1. "Trade" means commercial exchanges of goods and services as well as international banking, insurance (generally maritime insurance), transportation, communications, news gathering enterprises and ticket sales by travel agencies but not advertising or promotion/facilitation of trade.

2. "Substantial Trade" means there is a sizable volume of regular trade in goods or services terms of dollars, products or services on a continuous basis and not merely periodic or irregular trade,

3. "Principally between the U.S. and foreign national country" means that more than 50% of the trade involved must be between the U.S. the foreign national country.

The foreign national must be employed in a supervisory or executive capacity or perform necessary functions based on special qualifications of the foreign national. As long as the activities of the foreign national satisfy the foregoing conditions, there is no limit on the number times that an E-1 Visa can be renewed. The E-1 Visa is a nonimmigrant visa so that the foreign national cannot apply for permanent residency or U.S. citizenship. Each of the U.S. Department of State (DOS) and U.S. Citizenship and Immigration Services (USCIS) is authorized to issue E-1 Visas. The foreign national who is on a different visa may apply to change that visa for an E-1 Visa at a U.S. consulate abroad or to the USCIS. There is no limit on the number of E-1 Visas that the USCIS grants in a year.

F. Treaty Investor (E-2 Visa)

A foreign national may apply for an E-2 visa. The E-2 visa enables the foreign national to enter the U.S. to develop and direct the operations of a *bona fide* enterprise in which the foreign national has invested or actively in the process of investing a substantial amount of its own capital in the U.S. The foreign national can be an individual, a legal entity or the employee of an individual or legal entity. As an initial requirement, a treaty of investment must be in effect between the U.S. and the country of the foreign national. If no such treaty exists then the foreign national cannot apply for an E-2 visa. A treaty of investment does not exist between the U.S. and the Hellenic Republic (Greece). A Greek national is not eligible for an E-2 visa. The following conditions must be satisfied:

1. "Investor in the process of investing" means placing funds or other assets at commercial risk in exchange for the possibility of generating profit.

2. "Own Capital" means that the funds or assets must derive from and be owned by the foreign national such that it is the foreign national who exclusively controls the capital and who sustains the risk of losing the investment. Also, the funds or assets cannot have been acquired through criminal activity.

3. "Substantial Capital" means the amount of capital bears a proportional relationship to the cost purchasing or creating a new enterprise which is the same as or similar to the enterprise on which the E-2 Visa application is based, the amount of capital must be sufficient in relation to the amount necessary for the enterprise to succeed and the amount of capital must be sufficient to motivate the foreign national to develop and direct the enterprise,

4. "*Bona Fide* Enterprise" means a real, active and operating commercial or entrepreneurial undertaking which produces goods or services for profit. Solely passive investments in real property or securities or in nonprofit entities do not qualify. Also, the enterprise cannot be marginal such that it will produce only enough income to support the foreign national.

5. "Ability to Develop or Direct" means that the foreign national owns 50% or more of the enterprise or holds actual operational control of the enterprise.

As long as the activities of the foreign national satisfy the foregoing conditions, there is no limit on the number times that the foreign national can renew an E-2 Visa. The E-2 Visa is a nonimmigrant visa so that the foreign national cannot apply for permanent residency or U.S. citizenship. Each of the U.S. Department of State (DOS) and U.S. Citizenship and Immigration Services (USCIS) is authorized to issue E-2 Visas. The foreign national who is on a different visa may apply to change that visa for an E-2 Visa at a U.S. consulate abroad or to the USCIS. There is no limit on the number of E-2 visas that the USCIS grants in any year.

The crucial difference between the E-1 Visa and the E-2 Visa is that the E-2 Visa does not require that there be business or commercial relations between the U.S. and the country of the foreign national. Consequently, a foreign national on an E-2 Visa can purchase or create a business in the U.S. and operate that business as a wholly U.S. business.

G. E-3 Visa (Australian Citizen Only)

An Australian citizen must have an offer from a U.S. employer in a "specialty occupation" and an approved Labor Condition Application (LCA). Specialty occupation means an occupation that requires theoretical and practical application of a body of highly specialized knowledge and satisfies one of the following:

1. A baccalaureate or higher degree or its equivalent which is normally required to take the position,

2. The degree is common to the industry in parallel positions among similar organizations or an employer shows that the position is so complex or unique that it can be performed only by an individual with a degree,

3. The employer normally requires a degree or its equivalent for the position or,

4. The nature of the specific duties is so specialized and complex that the knowledge required to perform the duties is usually associated with a baccalaureate or higher degree.

The approved LCA must demonstrate that the U.S. employer will pay the Australian citizen a wage at or above the prevailing wage. The U.S. employer must begin paying the wage no later than thirty days after the Australian citizen enters the U.S., or sixty days, if E-3 visa status is obtained by seeking change of status. There are only 10,500 E-3 visas available in each fiscal year. The Australian citizen can usually stay for two years and can be extended. Qualified family members of the Australian citizen are eligible. They need not be an Australian citizen.

H. Alien Entrepreneur (EB-5 Visa)

A foreign national who invests at least $1 million in a new *bona fide* enterprise which creates at least ten full time jobs for U.S. citizens or other employment authorized foreign nationals can apply for and obtain an EB-5 Visa. The investment dollar amount can be $500,000 if the investment is made in specified high unemployment rural or urban areas. Unlike the E-1 Visa and E-2 Visa, the EB-5 Visas are limited to 10,000 per year. Also, the EB-5 is an immigrant visa. This means that the foreign national can use it as a basis for permanent residency or U.S. citizenship.

CHAPTER 4: FRANCHISING IN THE UNITED STATES

Section 4-1 Definition of a Franchise

A. Definition of a Franchise

The term "franchise" is a functional term which is defined in statute. Whether a relationship is a franchise depend how the parties conduct their business. A franchise relationship exists if:

1. The franchisor grants the right to use intellectual property in combination with a business method or format such that part of the bargained for exchange that the franchisee receives is a certain brand identification.

2. The franchisor maintains a measure of quality control and uniformity over the products or services offered for sale by the franchisee as a result of the use of the franchisor's property or method by the franchisee.

3. The franchisor provides assistance to the franchisee in the form of common buying arrangements, site location or cooperative advertising.

4. The franchisee pays a fee to the franchisor which is more than $500.00.

B. Factors Demonstrating a Franchise Relationship

In determining whether a particular legal relationship satisfies the foregoing elements, courts and regulators will consider the following factors:

1. Whether the franchisees pays fees on a continuing and regular basis,

2. The nature and extent of quality control that the franchisor exercises over the franchisee's operation,

3. The nature and extent of the disparity of the positions between the franchisor and the franchisee,

4. Whether the franchisee has made a significant investment in the franchise such that the franchisee would stand to lose the investment if the relationship with the franchisor was terminated,

5. Whether within the scope of the quality control exercised by the franchisor, the franchisee exercises the incidents of ownership and proprietorship.

C. Franchises Distinguished from Other Legal Relationships

The following legal relationships resemble franchises but are not franchises and are not regulated by the federal and state franchise laws.

Distributorship

An exclusive right to distribute products or services within a specified geographical area or demographic segment is not a franchise relationship as long as the owner does not control the method or means of distribution. However, where the distributor is granted the right to use the owner's trademark or associate that trademark with the general business of the distributor, then a franchise relationship may exist.

Trademark/Name License

The primary difference between a license and a franchise is the extent to which the licensor exercises quality control over the activities of the licensee. A license that does not involve the right to use a trademark or a common business format will rarely be deemed a franchise. A license that involves the right to use a trademark or common business format will always risk being deemed a franchise because a certain but indeterminate amount of control is implied in any right to use a trademark.

Partnerships and Joint Ventures

A partnership is an agreement between two or more persons to engage in a business for profit. A joint venture is a partnership that lasts for a limited time or to accomplish a specified business purpose. A partnership will rarely be deemed a franchise because the partners exercise joint ownership over the assets of the partnership and are jointly liable for the debts and liabilities of the partnership. Under a franchise, the franchisee and not the franchisor owns the business assets and the franchisor is not liable for the debts and liabilities incurred by the franchisee.

Brokers and Sales Agents

Brokerage and agency agreements will rarely be deemed franchises because brokers and agents act either on behalf of a principal or on behalf of the transaction in exchange for a commission. The commission is usually a percentage of the value of the transaction and is paid only if the transaction is completed. A broker or an agent does not pay a continuing and regular fee.

Business Opportunity Ventures

These ventures are essentially enhanced distributorship arrangements. They are generally prepackaged business deals offered mainly to novice entrepreneurs through some form of public advertising. They include sale of vending machines, pay telephones, telephone cards, amusement devices and "work at home with your computer" deals. Although these ventures are not franchises, they are regulated by the FTC and many states in the same manner as franchises but under a separate regulatory scheme.

Section 4-2 Federal Regulation

A. Federal Trade Commission (FTC) Franchise Rule

The Federal Trade Commission (FTC) Franchise Rule regulates the offer and sale of franchises. The FTC Franchise Rule does not pre-empt or displace any state laws or regulations. Where the state law or regulation stricter than the FTC Franchise Rule, the state law or regulation prevails within the jurisdiction of that state. Where the state law or regulation is not as strict as the FTC Franchise Rule. The state has no such law or regulation, the FTC Franchise Rule prevails. The FTC Franchise Rule defines the franchise relationship, obligates franchisors to provide prospective franchisees with a written document which contains certain mandated disclosures and enables the FTC to impose penalties on franchisors for failing to comply with the disclosure requirements. The written disclosure document is referred to as the Franchise Disclosure Document (FDD).

B. Penalties for Violation

The FTC is empowered to seek injunctions, freeze assets, civil penalties and monetary redress. The FTC can also seek remedies against individuals who violate the FTC Franchise Rule and impose personal liability. The FTC Franchise Rule does not authorize private actions to enforce the Rule.

Section 4-3 State Regulation

There are generally two types of regulatory schemes: one, disclosure and registration and, two, disclosure, no registration but mandated termination/renewal provisions. Fourteen states require that a franchisor who offers or sells offering franchises in the state must submit the FDD to the state authority for review and approval. They are California, Hawaii, Illinois, Indiana, Maryland, Michigan, Minnesota, New York, North Dakota, Rhode Island, South Dakota, Virginia, Washington and Wisconsin. A franchisor cannot offer or sell franchises in those states until the state approves the FDD. Approval by the state means that the FDD has been duly registered. Even if the state approves the FDD, the franchisor is obligated to keep the information in the FDD current.

Even though the other states do not require that the FDD be approved, the franchisor must still provide the FDD to the franchisee under the FTC Franchise Rule. Most of these states do mandate the manner in which a franchise can be terminated or renewed.

A. Registration of Franchise Disclosure Document (FDD)

The franchisor is prohibited from offering or selling any franchises in those states which require registration until the disclosure document has been accepted for registration. In this respect a franchise is treated like a security. After the FDD is registered, the franchisor must amend it if there has been a material change in the information contained in the registered FDD. The FDD must contain an audited financial statement for each of the past three consecutive fiscal years and that it must file audited financial statements for its most recent fiscal year no later than one hundred and twenty days after the last day of that fiscal year. Changes in financial statements are deemed to be material changes. As a practical matter, the franchisor must amend its FDD at least once every twelve months and the amendment must be approved.

A franchisor may continue to offer franchises while the approval of an amendment to its disclosure document is pending. The franchisor may even sell franchises while the approval to an amendment is pending as long as the franchisor escrows any funds received from any franchisee, provides a copy of the amended disclosure document to the franchisee and provides a reasonable opportunity to the franchisee to rescind the sale.

B. No Registration; Termination/Non-Renewal Provisions

Most states which do not require that a franchisor register its FDD require that the franchisee give reasonable notice of termination to the franchisee and the cause for the termination. The term “cause” means that the franchisee has failed to renew at least sixty days before the date on which the franchise expires, failed to substantially comply with the terms of the franchise agreement, lacks of good faith in performing under the franchise agreement or voluntarily abandoning the franchise. The franchisor must enable the franchisee to cure any such failure within a reasonable period of time or in a reasonable manner.

C. Exemption from Registration

The states which require registration exempt certain franchisors and certain types of franchise sales from registration. Generally, a franchisor is exempt from registration if it has a net worth on a consolidated basis of $5 million or more according to its most recent audited financial statements or a franchisor with a net worth of $1 million or more according to its most recent audited financial statements and at least 80% of the interests in a franchisor are owned by a business entity which has a net worth on a consolidated basis of $5 million or more according to its most recent audited financial statements.

To obtain the exemption from registration, the franchisor must apply for the exemption and still the FDD to franchisees. A franchisor that has a net worth of $15 million need not apply for the exemption but still must provide the FDD to franchisees. Sales of franchises to banks or other financial institutions are exempt from registration. Isolated sales of franchises which are not made as part of a plan of distribution are exempt. Sales of franchises which occur between franchisees of the same franchisor are exempt but the franchisor must deliver a current FDD to the transferee franchisee. Offers made over the Internet are exempt under certain circumstances.

D. Penalties for Violation

The states are empowered to seek injunctions, freeze assets, impose civil penalties and order restitution. The state can also seek remedies against individuals who are responsible for violations and impose personal liabilities on such persons.

Section 4-4 Franchise Disclosure Document (FDD)

A. Time for Providing FDD to Potential Franchisee

The franchisor must deliver the FDD to the franchisee at least fourteen full calendar days before the franchisee does any one of the following:

1. Signs a binding franchise, or
2. Makes a payment to franchisor.
3. The franchisor must also provide the FDD earlier than required in the negotiating process if the prospective reasonably requests the disclosure document.
4. The franchisor must provide to the prospective franchisee a complete franchise agreement at least 7 full calendar days before franchisee executes the agreement.

B. Contents of the FDD

The FDD must contain the following twenty-three Items, each of which consists of a description of certain types or categories of information. The FDD must be arranged so that each Item is addressed. If the franchisor has no information that responds to a particular Item or if an Item is not relevant, the FDD must so state as to each such Item.

1. Franchisor and any Affiliates
2. Business Experience
3. Litigation
4. Bankruptcy
5. Initial Fees
6. Other Fees
7. Estimated Initial Investment
8. Restrictions on Sources of Products and Services
9. Franchisee's Obligations
10. Financing
11. Franchisor's Assistance, Advertising, Computer Systems and Training
12. Territory
13. Trademarks
14. Patents, Copyrights and Proprietary Information
15. Obligation to Participate in the Actual Operation of Franchise
16. Restrictions on What the Franchisee May Sell
17. Renewal, Termination Transfer and Dispute Resolution

18. Public Figures

19. Financial Performance Representations

20. Outlets and Franchisee Information

21. Financial Statements

22. Contracts

23. Receipt of the FDD

CHAPTER 5: DOING BUSINESS ON THE INTERNET

Section 5-1 Doing Business from a Website

A. Using a Website

Most business entities in the U.S. use websites on the Internet for business purposes. The use of websites has become such a common business practice that a business entity which does not have a website risks losing business. A business entity uses a website for one or any combination of the following purposes:

1. To promote and sell goods in a manner similar to a catalog,
2. To sell information on a subscription basis in a manner similar to a newspaper or magazine,
3. To promote and advertise the business in a manner similar to a brochure,
4. To provide a vehicle for third party advertising.

B. Internet and Jurisdiction of Courts

The development of the Internet has confounded traditional concepts of court jurisdiction which determine whether a court is empowered to hear a case. The courts have had to adapt these traditional concepts to circumstances for which these concepts were never intended. A court must have jurisdiction over the subject matter of the case and jurisdiction over the person or legal entity being sued. Subject matter jurisdiction means that a statute mandates the category or type of cases that a particular court is empowered to hear. Personal jurisdiction means that a statute or common law empowers a court to render and enforce judgments against a person or legal entity based on the physical or legal relationship which the person or legal entity bears to the state in which the state or federal court sits. Generally, Internet related cases do not raise any special issues. In contrast, Internet related cases raise novel and complicated issues in applying the traditional concepts of personal jurisdiction.

In its simplest form, a court has jurisdiction over a person or legal entity when he, she or it is physically present in the state in which the court sits or, if not physically present, transacts business in the state in a purposeful commercial manner. The issue raised is whether a website which can be accessed from virtually any place in the world is physically present in the state for personal jurisdiction purposes. If not physically present, the issue is whether a business that offers goods and services for sale over a website is transacting business in each state in which the website can be accessed.

The law on personal jurisdiction and the Internet has been developed by the courts and not by statute. The most fundamental concept of the law of personal jurisdiction is that a person or entity must have minimum contacts with the state in order for the courts in that state to exercise jurisdiction over that person or legal entity. No court has ruled that simply because a website can be accessed in a state, the business which owns or controls that website is present in the state and subject to the jurisdiction of the courts in that state. However, whether the website owner is transacting business in the state depends on whether the website is passive or active. A website is passive if it simply makes information accessible to Internet users. A website is active if goods, information, or services are exchanged in a commercial transaction through the website between the owner of the website and Internet users located in the state. Most courts will exercise personal jurisdiction over a business which owns an active website.

Section 5-2 Electronic Contracts

A. Definition of an Electronic Contract

An electronic contract is an agreement which the parties conclude using a means of communication other than either the physical presence of the parties or the postal service and which is made legally binding using a means other than a manually executed physical document. Any of a telephone conversation, reciprocal emails, online digital mode or website digital mode is a means of communication through which an electronic contract can be concluded and made legally binding. An electronic contract can be formed by parties who are remote from one another but who communicate directly with one another. An electronic contract can also be formed by automated means between parties who do not communicate directly with one another.

Whether a legally binding electronic contract is formed is determined by traditional concepts of contract law. There must be an offer and acceptance through which the parties manifest a "meeting of the minds." A contract is formed when the offeror communicates an offer to the offeree and the offeree communicates an acceptance to the offeror. The legal issue is to determine the time at which the offeree communicates its acceptance to the offeror which is the time at which the contract is formed. The time of acceptance is legally significant because the offeror can change or revoke the offer at any time before the time of acceptance.

B. Formation of Electronic Contracts with Direct Communication of the Parties

Where the parties are physically present, the issue of the time of acceptance does not arise because physical presence enables instantaneous communication between the parties. Where the parties are remote from one another, the legal issue is whether the acceptance occurs at the time at which the offeree dispatches the acceptance or at the time at which the offeror receives the acceptance. Certain modes of direct electronic communication such as telephone, skype or IM enable parties remote from one another to communicate instantaneously. In such circumstances, the rules of contract formation which apply when the parties are physically present will apply.

Other modes of direct electronic communication such as telex, telegram and email do not enable the parties to communicate instantaneously or, at least, enable the offeree to choose the time to communicate. These modes generally require a third party to transmit the communication. Where remote parties use a mode of electronic communication which does not enable instantaneous communication, a variation of the traditional "mailbox rule" applies. Under the "mailbox rule" rule, the offeree communicates its acceptance when the writing evidencing the acceptance is placed in the postal service so that the contract was formed when the offeree sent the acceptance and not when the offeror received the acceptance. Adapting this rule to electronic contracting, the acceptance is delivered when the offeree places the acceptance with the third party responsible for transmitting the communication.

C. Formation of Electronic Contracts by Automated Means

There are modes of electronic communication which do not require any direct communication between the parties but are formed by automated means. The most common such mode is the click-to agree contract which is displayed and used on many websites. The parties never communicate directly but can still form a contract. The legal issue is not the timing of an acceptance but rather whether there has been a "meeting of the minds" between the parties. The traditional rules for determining whether there has been a "meeting of the minds" are adapted to an automated electronic contract. The written terms and conditions of the contract must be accessible to the offeree on the website. The offeree must manifest assent to the terms and conditions. A party manifests assent usually manifested by clicking on an electronic "button" which is entitled "I agree."

D. Execution of an Electronic Contract

All states and the federal government have enacted statutes which set forth a set of rules by which electronic signatures and electronic records in any type of transaction are recognized, as binding legal acts and binding legal documents. Generally, an electronic signature means an electronic sound, symbol, or process attached to or logically associated with an agreement or adopted by a person with the intent to sign the record. Certain legal documents such as wills, court orders and certain consumer notices cannot be signed by electronic signatures and must be manually signed.

CHAPTER 6: U.S. TAXATION OF FOREIGN NATIONALS

The United States taxes the income of a foreign national under certain circumstances. The nature and extent of such taxation depends on whether the foreign national is a resident foreign national or a nonresident foreign national. A foreign national who is not permanent resident of the U.S. is not required to disclose on a tax return nor pay taxes on income which the foreign national earns from non-U.S. sources. The taxing authority of the U.S. is the Internal Revenue Service (IRS) which is an agency within the Department of Treasury. Most states also tax the income of a foreign nationals. Each such state has a state tax authority.

Section 6-1 Resident Foreign National

A. Lawful Permanent Resident - "Green Card" Status

A foreign national who has obtained lawful permanent resident status (otherwise known as "green card" status) under the relevant U.S. immigration laws is taxed to the same extent and in the same manner as a U.S. citizen. This means that, like a U.S. citizen, a foreign national who holds a green card is taxed on any income which the foreign national derives from any source in the world. Physical presence in the U.S. is not relevant. As long as the foreign national holds green card status he or she must file U.S. tax returns and pay income tax.

If a foreign national was a "green card" holder in any part of the preceding calendar and is a "green card" holder in any part of the current calendar year, then the foreign national is a U.S. resident for tax purposes from January 1 of the current year. Also, if a foreign national is a "green card" holder in any part of the current calendar year and is a "green card" holder in any part of the following calendar year, then the foreign national is a permanent resident of the U.S. for tax purposes through December 31 of the current year.

B. Substantial Physical Presence in the U.S.

A foreign national who does not have "green card" status is a U.S. resident for tax purposes during any calendar year in which the foreign national is physically present in the U.S. for any thirty-one or more calendar days in the current year and the sum total of the days equals or exceeds one hundred and eighty-three days. The one hundred and eighty-three days is calculated as the number of days the foreign national is present in the U.S. in the current year plus

1. One-third of the number of days the foreign national is present in the first preceding calendar year plus

2. One-sixth of the number of days the foreign national is present in the U.S. in the second preceding calendar year.

The foreign national is present for a day as long as he or she is physically present for any portion of the twenty-four hours that make up a day. In calculating the days for which the foreign national is present for tax purposes, the days need not be consecutive.

C. Tax Treaties

The U.S. has tax treaties with most countries. If a foreign national is a permanent resident of the U.S., then the foreign national may choose to be taxed as a non-resident for matters set forth in the tax treaty. Unlike the foreign national who is permanent resident of the U.S., the foreign national is not required to disclose on a tax return or pay taxes on income which the foreign national earns from non-U.S. sources. A tax treaty pre-empts the U.S. tax laws and regulations on matters to which the tax treaty applies. The maximum tax on passive income is 30%. Many tax treaties reduce the 30% tax to a lesser percentage. Tax treaties also exempt from U.S. taxation certain types of income such as compensation from a foreign employer which is not engaged in a U.S. trade or business, pensions from former U.S. employers and compensation to teachers who are temporarily working in the U.S.

Section 6-2 Nonresident Foreign National

A. U.S. Source Income Not Effectively Connected with U.S. Trade or Business

The foreign national must file tax returns and pay tax on certain income which the foreign national earns from U.S. sources even that income is not effectively connected with a U.S. trade or business. The types of income which are taxable are generally passive income such as interest, dividends, royalties, rents and other fixed or determinable income which is payable on a periodic basis. The tax on such income is a maximum of 30%. This percentage can be less if the U.S. and the country of the foreign national have a current a tax treaty which specifies a lesser percentage.

If a foreign national earns capital gains from the sale of any asset other than real property those capital gains are not taxed. The foreign national must pay tax on capital gains which the foreign national earns from:

1. The sale of real property located in the U.S., or
2. From any U.S. source while the foreign national is physically present in the U.S. for 183 days or during the year in which the foreign national earns capital gains.

The foreign national cannot set any deductions or credits of any kind against the tax on capital gains which the foreign national must pay.

B. U.S. Source Income Effectively Connected with U.S. Trade or Business

Even though a foreign national is not a permanent resident of the U.S., the foreign national must file tax returns and pay tax on income which the foreign national earns from U.S. sources which is effectively connected with a U.S. trade or business. The types of income which are taxable are generally active income such as fees for services, profits from a business operation, sale of a capital asset of a business, certain income from real property and income from a non-corporate entity which operates a business.

The tax on such income is calculated at the same graduated percentages as is the income of a U.S. citizen. The foreign national may apply such deductions and credits as are available to U.S. citizens. Unlike the foreign national who is s U.S. resident, the foreign national is not liable for filing returns or paying tax on income which he or she derives from non-U.S. sources.

Section 6-3 State Taxation of Foreign Nationals

A foreign national who files a U.S. tax return on which the foreign national pays income tax or from whose income state taxes are withheld must file a state tax return and pay any due state tax. There are seven states which do not tax the income of any individual resident of that state so that a foreign national who resides one of those states pays no state income tax. These states are Alaska, Florida, Nevada, South Dakota, Texas, Washington and Wyoming. New Hampshire and Tennessee do not tax wages or salaries.

The rates of state taxation are generally lower than the federal rates. The states are not obligated to follow the tax treatment for a foreign national set forth in a tax treaty. As a matter of practice most, but not all states, do follow the tax treatment set forth in tax treaties. A foreign national whose income is exempt from federal taxation under a tax treaty but resides in a state which does not follow the tax treatment set forth in tax treaties must pay state income tax on income that is otherwise exempt from federal taxation.

Section 6-4 International Taxpayer Identification Number (ITIN)

The IRS issues an ITIN to a foreign national who is not eligible to obtain a social security number but must file taxes in the U.S. The foreign national uses the ITIN only as an identification number for filing U.S. taxes. The foreign national cannot use the ITIN for any other purpose including but not limited to work in the U.S. or any kind of immigrant status.

CHAPTER 7: BANKS AND BANKING

Section 7-1 Banks in General

Banks are chartered at both the federal and state levels. Banks are highly regulated at each such level. The larger banks offer the full range of banking services such as deposit accounts, commercial and personal loans, and investment in financial instruments. Smaller banks, such savings and loan banks, offer only certain banking services. There are also institutions which offer banking type services but which are not banks such as credit unions and brokerage houses which are referred to as “non-bank banks.” A bank customer is a person or business entity which opens a deposit account or obtains a bank loan, a person or entity for whom the bank maintains an account and a person or entity for whom the bank facilitates transactions.

Section 7-2 Know Your Customer Guidelines

As a result of the attacks on September 11, 2001, the federal government enacted a series of laws and regulations which impose far stricter regulations on all financial institutions including “non-bank banks.” Referred to as the Patriot Act, banks must institute a program of rules based on “know your customer (KYC)” guidelines. The KYC guidelines are issued by the U.S. Department of the Treasury. Each bank must create and maintain a KYC program which is based on the KYC guidelines.

The purpose of the KYC guidelines is to prevent criminals from using bank services for money laundering and to prevent terrorists from using bank services. The KYC guidelines also enable banks understand the needs and dealings of their customers so that the bank can effectively assess the risks to the bank. The fundamental elements of the KYC guidelines are

Customer Acceptance Policy, Customer Identification Procedures, Monitoring Transactions, and Implementing the KYC guidelines.

The KYC program applies to anyone who is a bank customer. Banks strictly apply the KYC guidelines to non-US persons. A non-US person must be aware of and plan to comply with the requirements of the KYC program of the bank with which the non-U.S. person seeks to be a customer. KYC programs differ from bank to bank. The KYC programs do have common procedures by which the banks verify the identity of a non-U.S. person.

Simply opening a bank account can be delayed or even denied if the non-U.S. person cannot comply with the KYC program. The bank, in its sole discretion, determines whether a customer satisfies the requirements of its KYC program. No bank is legally obligated to offer banking services to any U.S. person or non-U.S. person who the bank determines does not satisfy the KYC program of the bank.

Section 7-3 Personal Account with Foreign Person Present - Identification and Documents

To determine the identity a non-U.S. person, the non-U.S. person must present in person to the bank one or more of following documents:

1. Duly issued and dated passport with photograph, number and country of issuance, preferably a biometric passport,

2. Identification card duly issued and dated by the country of citizenship or residence and has a photograph attached or

3. Any other document issued by a government which displays nationality/residence and has a photograph attached,

4. Duly issued ITIN although the ITIN must be provided along with 1 through 3.

Section 7-4 Opening an account – Non-U.S. Person not Present

Banks will almost never open any type of bank account for a non-U.S. person unless that person appears in person at the bank to open the account. If the non-U.S. person is not present then the non-U.S. authorize can authorize a U.S. person to open the account as long as the U.S. person appears at the bank in person.

1. If the account is a personal account, then the U.S. person must present:
   a. the documents which the bank requires for a U.S. person to open an account,
   b. a power of attorney which authorizes the U.S. person to open the account on behalf of the foreign person,
   c. a statement in a form acceptable to the bank that the U.S. person shall perform the duties which the bank requires the account holder to perform.
2. If the account is a business account, then the U.S. person must present:
   a. the documents which the bank requires for a U.S. person to open an account,
   b. evidence that the U.S. person is authorized to open the account on behalf of the business entity,
   c. evidence of the office in the business entity which the U.S. person holds,
   d. the organizational documents of the business entity,
   e. a statement in a form acceptable to the bank that the U.S. person shall perform the duties which the bank requires the account holder to perform.

Section 7-5 Business Account with Representative Present - Identification and Documents

If a non-U.S. person seeks to open an account in the name of a business entity, the non-U.S. person must hold a substantial interest in the legal entity. The business entity can be formed either under the laws of the state of the U.S. or under the laws of a foreign country. The non U.S. person must present in person to the bank the following documents:

1. The documents required in Section 7-3
2. The organizational documents of the legal entity such as articles of association in English,
3. Evidence of the authority of the person to open the business account,
4. Evidence of the authority of the business entity to open the business account,
5. Statement from an authorized person as to the business of the business entity