

The Illegal Practice of Engineering or Architecture by Companies in New York - A Compliance Guide [Part One]

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The laws governing the practice by business entities of engineering and architecture in New York are among the most restrictive in the country – but in many cases a solution to operate legally is available. This article consists of Part 1, which addresses the regulatory framework, compliance requirements and the risks arising from non-compliance, and Part 2, which offers possible compliance strategies.

PART 1 – THE REGULATORY FRAMEWORK – COMPLIANCE REQUIREMENTS AND RISKS ARISING FROM NON-COMPLIANCE

Design contracts with state and local government entities (e.g., the Metropolitan Transit Authority and the Office of General Services Procurement Services Group) in New York typically require the contracting engineering and architecture companies to be duly licensed to provide such services in New York and, in the case of a contracting engineering company, to submit a copy of its certificate of authorization issued by the Education Department of the State of New York ("EDSNY") to practice engineering. Such clauses are also becoming more common in private contracts. Nevertheless the principals of business entities active in engineering in other states are often surprised to learn that their company may not be in a position to obtain a certificate of authorization to practice engineering in New York, and therefore is ineligible to bid for an engineering contract. In addition to being eligible to provide services in New York, a business entity that meets New York's more stringent requirements will typically be able to meet the other states' less restrictive requirements, as long as it employs (or includes among its owners) locally licensed engineers or architects.

New York State remains an attractive market for many companies that provide engineering and architecture services in the construction sector, but New York also has some of the most restrictive legislation in the country governing which individuals and which business entities are permitted to provide engineering and architecture services. Most of the restrictions have been in place for about 100 years, evolving over time. Historically the restrictions have often been ignored, but a legal

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requirement that came into effect on January 1, 2000, requiring all business entities that provide engineering services in New York to have a certificate of authorization from the EDSNY to provide professional engineering services, has forced many companies to face the issue and become compliant.¹ This requirement to obtain a certificate of authorization to provide professional engineering services is different from, and in addition to, the requirement that the business entity be registered with the New York Department of State to do business in New York, although that requirement may also be difficult to satisfy for a business entity that cannot obtain the authorization from the EDSNY.² A similar certification requirement is not currently in effect for professional architecture companies, but in other ways the practice of architecture is even more restricted. For instance, providers of architecture services must be duly authorized and licensed in New York even prior to submitting an offer to provide architecture services.³

This article focuses on the authorization of professional business entities and not on the licensing of individual engineers. Regardless of the status of the business entity rendering architecture or engineering services in New York, an individual New York licensed engineer or architect must be in charge of the specific professional services provided in New York.⁴

The Governing Laws

The Education Law, the Business Corporation Law, the Limited Liability Company Law and the Rules of the Board of Regents contain many of the important pieces of the complex weave of rules and legislation that govern business entities' practice of engineering and architecture in the State of New York. The regulations and restrictions in these rules and laws will be examined in this article. However, it should be noted that several other pieces of legislation and regulations also affect various aspects of the practice of engineering and architecture in New York.

The mentioned laws also govern the practice of land surveying and landscape architecture. Engineers, land surveyors, architects and landscape architects may combine their practices,⁵ but this article focuses on engineers and architects.

Which Business Entities Can Practice Engineering or Architecture in New York? Which Ones Cannot?

The New York Education Law governs several professions. The Education Law lists the types of companies that are entitled to provide engineering services in New York. These include: (1) domestic or foreign professional service corporations; (2) professional limited liability companies; (3) various forms of professional partnerships; and (4) so-called "grandfathered" corporations.⁶ Regular business corporations (with the exception of grandfathered corporations), regular limited liability companies, and many partnerships cannot become authorized to provide professional engineering services in New York and are not permitted to render such services in New York.⁷ However, a proposed bill in the New York Senate ("the Bill") may make it possible in the future for a new type of domestic "design professional service corporation" to render engineering (and architecture) services in New York.⁸

The Education Law also governs the types of business entities that are allowed to practice architecture. It does not state the restrictions quite as clearly but is

generally interpreted as limiting the practice of architecture to the same types as those professional entities entitled to practice engineering.⁹

The Business Corporation Law ("BCL") permits a domestic New York professional service corporation to be created for the purpose of providing engineering and/or architecture services in New York.¹⁰ Only individuals who are licensed as engineers or architects in New York can be shareholders, directors or officers (with the exception of the secretary or assistant secretary if there is only one shareholder) of such a domestic New York professional corporation.¹¹ Substantially identical restrictions apply to other types of domestic professional entities whose ultimate owners, members, partners, managers etc. all must be engineers and/or architects licensed in New York.¹²

According to the BCL, a foreign professional service corporation organized under the laws of a state other than New York may become authorized to do business in New York as a foreign professional service corporation, provided the corporation is licensed to do such business in the state where the corporation is incorporated, and provided that the shareholders, directors and officers (with the possible exception of the secretary and assistant secretary) all are licensed and authorized to practice engineering in some state.¹³ Substantially similar restrictions apply to other types of foreign professional entities. Such a business entity must be authorized to provide engineering/architecture services in its home state, and its ultimate owners, members, partners, managers etc. must be engineers and/or architects licensed in some state.¹⁴ Of course the foreign professional entity also needs to comply with relevant law in its jurisdiction of incorporation with respect to any licensing requirements affecting the entity's owners or management. Although the legislation in place in New York does not expressly exclude professional corporations organized in other countries and/or with shareholders licensed in other countries, the EDSNY has not (to date) accepted the registration of professional corporations organized in other countries or professional corporations which include among their shareholders engineers/architects licensed in other countries and not licensed in a state in the United States.¹⁵ The EDSNY also has not granted individual licenses to any engineers or architects wholly educated and trained outside the United States.¹⁶

If the Bill (discussed above) is passed, from January 1, 2011, it will be possible to incorporate domestic New York "design professional service corporations" for the purpose of practicing engineering or architecture. More than 75 percent of the shareholders, 75 percent of the directors and 75 percent of the officers must be engineers/architects licensed in New York, but this new type of entity would be allowed to issue up to almost 25 percent of its shares to employees other than engineers and architects licensed in New York.¹⁷ It would also permit the employees to hold their shares through an employee stock option plan ("ESOP").¹⁸ Upon an employee's termination, the shares held by the employee must be redeemed by the corporation or transferred to another employee.¹⁹ The president, the chairperson, and chief executive officer must also be licensed engineers/architects in New York.²⁰ The single largest shareholder must be a licensed engineer/architect or an ESOP with more than 75 percent of the voting trustees and committee members being licensed professionals.²¹

The domestic or foreign professional service entity may only render professional services in New York through individuals who are licensed in New York.²² The entity

may employ engineers or architects licensed in other states, but such engineers may not perform engineering services in New York or for projects in New York, except pursuant to limited exceptions.²³

One general exception permits so-called grandfathered corporations to provide engineering and/or architecture services in New York. Such grandfathered corporations may have shareholders other than licensed engineers or architects, but the exception is available to a very limited number of corporations.²⁴ This exception will be discussed in more detail later in this article.

Only foreign and domestic professional entities and grandfathered corporations may provide engineering and/or architecture services in New York.²⁵ These entities may provide such services only upon having become registered with the Department of State as authorized to do business in New York and, for entities providing engineering services, only upon meeting the additional requirement of having applied for and received a certificate of authorization to provide professional engineering from the EDSNY.²⁶

Any business entity that tries to incorporate or register with the New York Secretary of State to do business in New York that includes among its stated purpose or in its name any references to engineering or architecture will be rejected unless it has obtained in advance and includes a certificate from the EDSNY certifying the New York licensing of those professionals that are to practice for the entity in New York.²⁷

The restriction that typically presents the largest obstacle for a business entity to become authorized to practice engineering or architecture in New York is the requirement that all of the ultimate owners of the business entity must be licensed engineers and/or architects. This provision prevents corporations that are listed on a stock exchange and most international corporations from becoming authorized to practice engineering and architecture in New York, but it also prevents many other corporations from becoming so authorized. For instance, a corporation that has 20 shareholders, 19 of whom are engineers and one (for instance the CFO) who is not an engineer cannot become authorized to practice engineering in New York. Corporations that have granted stock options to non-engineers may have unintentionally precluded themselves from becoming authorized to practice engineering in New York.

The restrictions that prevent a professional engineering and/or architecture business entity from appointing directors or officers other than licensed engineers and/or architects are typically easier to overcome because the business entity often can appoint directors and officers that meet such requirements.

Why Employees, Owners and Others Should Care: Sanctions for Non-Compliance

So why does it matter if the corporation a professional works for or owns is licensed to practice engineering or architecture in New York? A wide range of criminal and disciplinary sanctions and business reasons provide plenty of incentives for compliance. Both business entities and individuals who engage in or aid and abet another party in providing unauthorized engineering services are subject to criminal liability, disciplinary sanctions, may be prevented from successfully bidding on contracts awarded by New York State agencies and could forfeit their right to

payment under the engineering/architecture contracts they have entered into and already performed.²⁸ An initially successful bid for a project by an unauthorized and unlicensed bidder may also risk being challenged by a licensed and authorized competitor for lack of compliance with the terms in the invitation to bid and the law. In addition, although not analyzed in detail in this article, insurance companies may decline coverage under professional liability insurance policies if the corporate entity or the individuals providing professional services are not duly licensed and registered.

Disciplinary Sanctions

The Board of Regents may impose disciplinary sanctions, e.g., impose fines on or revoke or suspend the license or authorization of a licensed professional individual or business entity that helps an unlicensed individual or business entity perform professional services or engages in fee splitting with an unlicensed individual or entity.²⁹

The Education Law provides that a licensed engineer or architect commits professional misconduct if he engages in "permitting, aiding or abetting an unlicensed person to perform activities requiring a license" or if he or she commits "unprofessional conduct" as defined by the Board of Regents in its rules or by the Commissioner in regulations approved by the Board of Regents.³⁰ The rules issued by the Board of Regents, among other things, prohibit fee splitting.³¹ These rules are described in more detail below.

Professional misconduct is investigated by the EDSNY, which may prepare charges against the licensee.³² A hearing is conducted by a panel consisting of members of the state board of the relevant profession (engineers or architects), and the Board of Regents makes a decision based on the hearing. The decision of the Board of Regents may be reviewed by the courts.³³ The New York Office of Professions publishes disciplinary sanctions on its website and lists the names of the individuals and the business entities that have been disciplined.³⁴

The disciplinary sanctions imposed by the Board of Regents can involve censure and reprimand, suspension, revocation or annulment of the professional license or registration, fines up to \$10,000 and one hundred hours of public service.³⁵ The New York State Attorney General has authority to bring an action to enforce any fine imposed by the Board of Regents.³⁶ Business entities that are authorized to provide engineering/architecture services may be disciplined in the same manner as individual professional engineers/architects.³⁷ A professional licensed engineer/architect who is a shareholder in and/or who works for a corporation that provides engineering/architecture services in New York without proper authorization may become the subject of such disciplinary sanctions. Therefore it is important for the individual engineer or architect to make sure the corporation, on whose behalf he or she provides engineering or architecture services in New York, is properly authorized.

Criminal Liability

Practicing unlicensed engineering or architecture, or helping someone else to do so, is a felony and can result in prison sentences and in fines of up to twice the amount

of the defendant's gain from the crime.³⁸ For instance, a New York licensed engineer who, in his capacity as an officer of a corporation not licensed and authorized to practice engineering in New York, assists the corporation in doing so, could be held criminally liable.

Under the Education Law, it is a class E felony for anyone who is not authorized to practice engineering/architecture to do so.³⁹ It is also a felony to aid or abet unlicensed persons to practice engineering/architecture.⁴⁰

In practical terms that would mean that the individual officers, directors and employees of a business entity that is not licensed to practice engineering/architecture may be committing a felony in aiding the business entity in practicing engineering/architecture in New York. It is also a felony for a business entity which is not licensed to practice engineering/architecture to do so.⁴¹

Investigations into unlicensed engineering practice are performed by the EDSNY. The EDSNY reports violations to the New York State Attorney General who prosecutes the alleged offenses.⁴²

Conviction for a class E felony may result in prison terms of at least 3 years but no more than 4 years, a \$5,000 fine or twice the amount of the defendant's gain from the commission of the crime, whichever is higher.⁴³ Gain is defined as the amount of money derived from the commission of the crime. With respect to a corporation it may also result in fines or a conditional or unconditional discharge.

Fee Splitting Prohibition

The Rules of the Board of Regents, which apply to all licensed professions including licensed engineers and architects, provide that it is unprofessional conduct to directly or indirectly offer, give, solicit, or receive or agree to receive any fee or other consideration to or from a third party for the referral of a client or in connection with the performance of professional services.⁴⁴ This rule prevents any arrangement between a business entity and a professional entity that would permit the professional entity to pay the business entity an origination fee for engineering or architecture contracts.

For engineers and architects in particular, unprofessional conduct also includes: "permitting any person to share in the fees for professional services, other than: a partner, employee, associate in a professional firm or corporation, subcontractor or consultant. This prohibition shall include any arrangement or agreement whereby the amount received in payment for furnishing space, facilities, equipment, or personnel services used by a professional licensee constitutes a percentage of or is otherwise dependent upon the income or receipts of the licensee from such practice."⁴⁵

The above rule prevents any arrangement between a non-professional business entity and a professional entity that would permit the professional entity to pay the non-professional business entity for services if such payment is calculated as a percentage of or in any way dependent on the profits of the professional entity earned by providing engineering or architecture services. Accordingly, any arrangement between a non-professional business entity and a professional entity whereby the non-professional business entity provides management assistance,

secretarial assistance, lease facilities and equipment would need to be structured so that the fee is not calculated as a function of the profit of the professional entity, e.g., a fixed fee, or a fee based on actual use of such services, e.g., hourly fees for secretarial and management assistance and fixed monthly or annual fees for facilities and equipment.

A violation of the rule against fee-splitting could also make the professional individuals in the professional entity subject to disciplinary sanctions as described above.⁴⁶

Commercial Risks Arising from Lacking Authorization and Unauthorized Practice

Several strong incentives are in place for business entities to comply with the authorization and licensing requirements in New York.

A business entity may be prevented from placing a successful bid with a New York State agency (as well as other local government agencies – and sometimes even private projects) for an engineering or architecture project if it cannot provide evidence of the contractually required authorizations and licenses. Even if a business entity without such authorization is initially successful in bidding for a project, bid protests may cost the business entity the award, if the business entity does not meet the authorization and licensing requirements.⁴⁷

Case law from New York State courts provides another strong financial incentive to make sure that providers of professional engineering and architecture services in New York are properly licensed and authorized. New York courts have held that corporations not authorized to practice engineering or architecture in New York (as well as individual engineers and architects not licensed in New York) seeking recovery on contracts to provide engineering/architecture services are precluded from recovery if their performance would have required a license or authorization under the Education Law.⁴⁸

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RESOURCES:

Websites:

Office of the Professions: <http://www.op.nysed.gov/>

Use this link to verify the professional licensing of corporate entities and individuals, find decisions of disciplinary sanctions and find the Education Law and the Rules of

the Board of Regents.

EDSNY: <http://www.nysed.gov/>
This is the website of the EDSNY.

New York State Department of State:
http://appsext8.dos.state.ny.us/corp_public/corpsearch.entity_search_entry
Use this link to verify if a corporate entity is registered to do business in New York.

The New York Business Corporation Law, the Limited Liability Company Law and the Partnership Law can be accessed on www.bloomberglaw.com.

Primary Governing Laws and Regulations:

Education Law (e.g., Article 130 General Provisions, Subarticle 3, Professional Misconduct, and Subarticle 4, Unauthorized Acts; Article 145, Engineering and Land Surveying; and Article 147, Architecture).

Business Corporation Law (Article 15, Professional Service Corporations, and Article 15-A, Foreign Professional Service Corporations).

Limited Liability Company Law (Article 12, Professional Service Limited Liability Companies, and Article 13, Foreign Professional Service Limited Liability Companies).

Partnership Law.

Rules of the Board of Regents.

1N.Y. EDUC. LAW § 7210 (2009).

2N.Y. BUS. CORP. LAW§ 1503 (2009).

3N.Y. EDUC. LAW §§ 7210, 7301.

4§ 7210(1).

5§ 7209(4).

6§ 7210.

7§§ 7209, 7210.

8 S. 3226, 2009-2010 Reg. Sess., 231 Leg. Sess. (N.Y. 2009).

9N.Y. EDUC. LAW § 7307.

10N.Y. BUS. CORP. LAW§ 1503(a)-(b).

11 §§ 1503(a)-(b), 1504(a), 1507, 1508.

12 § 1503(d).

13 § 1529.

14 § 1530.

15NEW YORK EDUCATION DEP'T, OFFICE OF THE PROFESSIONS, LICENSE REQUIREMENTS; PROFESSIONAL ENGINEERING, <http://www.op.nysed.gov/pelic.htm>.

16*Id.*

17 S. 3226, 2009-2010 Reg. Sess., 231 Leg. Sess. § 4 (N.Y. 2009) (proposing to amend N.Y. BUS. CORP. LAW § 1507).

18*Id.*

19 S. 3226 § 7 (proposing to amend N.Y. BUS. CORP. LAW § 11511).

20 S. 3226 § 4 (proposing to amend N.Y. BUS. CORP. LAW § 1507).

21 *Id.*

22N.Y. BUS. CORP. LAW§ 1526(a).

23§ 1529(a).

24N.Y. EDUC. LAW § 7209(6).

25§ 7210.

26*Id.*; N.Y. BUS. CORP. LAW§ 1503.

27 § 1503(b) and § 1530(b)(2).

28N.Y. EDUC. LAW § 6512(2).

29N.Y. BUS. CORP. LAW§ 1532.

30N.Y. EDUC. LAW § 6506(7), (9).

31 Rules of the Board of Regents, N.Y. COMP. CODES R. & REGS. tit. 8, § 29.3(a)(6) (2006).

32N.Y. EDUC. LAW § 6516.

33§ 6516(5).

34See <http://www.op.nysed.gov/>.

35N.Y. EDUC. LAW § 6511.

36 *Id.*

37§ 7210(3).

38§ 6512.

39*Id.*

40*Id.*

41*Id.*

42 § 6514.

43§ 6512.

44N.Y. COMP. CODES R. & REGS. tit. 8, § 29.1(a)(3).

45 § 29.3(a)(6).

46 N.Y. EDUC. LAW § 6509.

47 It is very easy to check if a business entity is authorized (or an individual is licensed) to practice engineering or architecture in New York. The Office of Professions at the EDSNY maintains a website where authorizations and licenses can be verified online. The business entity must be listed in the database, be current, and have a "yes" next to the line item stating whether or not it has a "Certificate of Authority to Provide Professional Engineering Services in New York State." Many business entities fail to register in the first place. Some register but fail to stay current. Others manage to stay current but fail to apply for and obtain the certificate. The database is accessible at the following link: <http://www.op.nysed.gov/opsearches.htm>.

48 See *Gordon v. Adenbaum*, 171 A.D.2d 841, 567 N.Y.S.2d 777 (2d Dep't 1991); *Marshall-Schule Assoc. v. Goldman*, 137 Misc.2d 1024, 523 N.Y.S.2d 16 (N.Y. City Civ. Ct. 1987); *Usdin v. Kvatinetz*, 69 N.Y.S.2d 634 (Sup. Ct. N.Y. Co. 1947); *American Store Equip. & Constr. Corp. v. Jack Dempsey's Punch Bowl, Inc.*, 174 Misc. 436, 21 N.Y.S.2d 117 (Sup. Ct. N.Y. Co. 1939).