

# Keep improperly registered companies out of court

By Mark Wagner

In California, all persons and companies (e.g., corporations and LLCs) can sue and defend lawsuits brought in any court in California. This right to be able to sue and defend against a lawsuit is generally referred to as having the "capacity" to sue (which is different than having standing to sue). As always, there are exceptions to the rules. Among the various exceptions to the lack of capacity to sue or defend against a lawsuit include instances where companies have run afoul of California's corporate registration or tax laws. Unfortunately, California has enacted a statutory scheme that is spread into different codes (e.g., Corporations Code and Revenue and Taxation Code) which seem contradictory, and frankly does not make sense, especially during these economic times when California cannot afford to lose revenue it is entitled to by law. It is time to simplify the law: if a company (of any corporate type) does not properly register to do business in California and pay the proper fees and taxes as required by law, it should be prohibited from filing a lawsuit, maintaining a lawsuit or defending a lawsuit in California.

A corporation that has been suspended for nonpayment of taxes cannot sue or defend a lawsuit in California. Revenue and Taxation Code Sections 23301 *et seq.*; *Reed v. Norman*, 48 Cal.2d 338 (1957). This has been held to include the lack of the right to appeal from an adverse judgment, renew a proper judgment previously obtained while in good standing or seek a writ of mandate. Further, it is a misdemeanor to try to exercise the rights and powers of a suspended corporation in California. Revenue and Taxation Code Section 19719. Similarly, a foreign corporation (an out-of-state company doing business in California) whose powers have been suspended in its home state for nonpayment of corporate taxes also lacks capacity to sue in California. That is, if the company lacks capacity in its home state, it lacks capacity in California. Once a corporation pays all back-taxes, along with the interest, penalties and fees owed, its powers are "revived," and it then has capacity to sue or defend a lawsuit in California. Revenue and Taxation Code Sections 23305 *et seq.* One thing that does not change, however, is that contracts entered into by a corporation while suspended are voidable at the option of the other party. Revenue & Taxation Code Sections 23304.1 *et seq.*;

*Damato v. Slevin*, 214 Cal. App. 3d 668, 675 (1989).

Foreign corporations that want to do business in California must obtain a "certificate of qualification" from the Secretary of State, which requires filing certain papers and paying certain fees. Corporations Code Section 2105. A foreign corporation that has not qualified with the state can be subject to criminal fines. Further, the company may file a lawsuit but may not "maintain" a lawsuit without complying. Corporations Code Section 2203(c); *United Med. Management Ltd. v. Gatto*, 49 Cal. App. 4th 1732, 1739 (1996). If the corporation files a lawsuit, the other side can raise the defense that the plaintiff lacks the capacity to do so. At that point, the trial court will generally stay the action a short period to allow for the corporation to qualify. If the foreign corporation then qualifies to do business, and pays the fees, penalties and taxes due as required, it may then "maintain" an action commenced before qualification. Unlike suspended corporations, a foreign corporation that has failed to qualify with the Secretary of State may nevertheless defend an action brought against it in California courts without qualifying. In other words, the prohibition on "maintaining" an action does not ap-

ply to defending an action. The same general rules apply to other types of entities, e.g., foreign limited liability corporations. See, e.g., Corporations Code Section 17456 (a foreign LLC transacting intrastate business shall not maintain any action, suit or proceeding in any court until it has registered in California).

As shown, laws for companies doing business without proper registration and payment vary in California, sometimes permitting the company to sue but not maintain the suit, sometimes allowing nothing, and sometimes allowing a defense of a lawsuit but nothing else.

This scheme makes no sense. A California company that is suspended cannot sue or defend a lawsuit in California, but a foreign company that operates in California without properly registering and paying the required fees and taxes *can* defend a lawsuit in California. Any given rationales outlined by the Legislature and the courts make no sense. If these businesses want to come into California, have employees and make money in California, but choose to ignore registration and tax laws here, why should they be allowed to use California courts? If such a company violates the labor code by committing wage and hour violations, and then wrongfully

terminates an employee who then sues, why should the company be allowed to avail itself of the privileges of California law and defend a lawsuit filed against it here? Just as a California corporation that has been suspended for nonpayment of taxes in California cannot sue or defend a lawsuit in California, *any* entity — foreign or domestic — that operates illegally in California should not be able to sue or defend a lawsuit in California.

The Legislature should simplify the rules and make it clear that any entity that does not properly register in California and pay the required fees and taxes cannot file a lawsuit, maintain a lawsuit or defend a lawsuit in California. Moreover, the Legislature should add that any willful violation of the law prohibits

a revivor from using a California court. A company that operates in California illegally for an extended period of time, willfully cheating the state out of money and fees, should not be allowed to simply cure the violation at a later date when the company decides it has a lawsuit it wants to defend here that makes it worthwhile to pay back all the money it has cheated from California. Perhaps a 6-month stay of the right to litigate from the date of proper registration and payment would be a sufficient deterrent for such behavior.

Simply put, California needs money and cannot allow for companies — foreign or domestic — to cheat the state out of money while reaping the benefits of its legal system. As the saying goes, "you have to pay to play."



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