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CORPORATIONS: SUSPENSION OF COURT PRIVILEGES UPON FAILURE TO PAY TAXES

Florida Statutes §610.11 (1949)

All states have statutes requiring domestic corporations to file annual reports and pay annual franchise, license, or charter fees.[1] In addition, most of these acts provide for one or more of the following penalties: suspension of the right to maintain an action in the courts of the particular state;[2] a similar suspension of the right to defend;[3] suspension of the corporate and charter privileges;[4] and forfeiture or dissolution of the charter itself.[5] The judicially declared purpose of these provisions is merely to enforce the payment of the taxes levied.[6] A feature common to these statutes is revival of suspended privileges upon later payment of the delinquent taxes plus any penalty.[7]

Some of the statutes speak of "forfeiture" and "dissolution";[8] others purport merely to "suspend" certain or all of the corporate privileges.[9] But even when they go so far as to declare forfeiture or dissolution, the majority of the courts construe them to mean suspension.[10] These

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[1]Those interested in the specific statutes will find them tabulated in Note, 48 YALE L.J. 650 (1939).

[2]Boston Towboat Co. v. John H. Seson Co., 199 Fed. 445 (D. Wash. 1912); Motor City Engineering Co. v. Fred. E. Holmes Co., 241 Mich. 446, 217 N.W. 25 (1928); West Side Telephone Co. v. Kenison, 147 Wash. 542, 266 Pac. 706 (1928).

[3]*E.g.*, FLA. STAT. §610.11 (1949); Ocean Park Bath House & Amusement Co. v. Pacific Auto Park Co., 37 Cal. App.2d 158, 98 P.2d 1068 (1940); Ross Amigos Oil Co. v. State, 134 Tex. 626, 138 S.W.2d 798 (1940).

[4]*E.g.*, Sunset Oil Co. v. Marshall Oil Co., 16 Cal.2d 651, 107 P.2d 393 (1940); Dolese Bros. Co. v. Pacific Engineering Co., 95 Okla. 72, 218 Pac. 798 (1923).

[5]*E.g.*, Nebraska Cent. Bldg. & Loan Ass'n v. Yellowstone, Inc., 140 Neb. 422, 299 N.W. 474 (1941).

[6]*E.g.*, Sale v. Railroad Comm'n, 15 Cal.2d 612, 104 P.2d 38 (1940); Wax v. Riverview Cemetery Co., 2 Terry 424, 24 A.2d 431 (Del. Super. 1942); Christie v. Highland Waterfront Co., 114 Fla. 263, 153 So. 784 (1934); Shreveport Long Leaf Lumber Co. v. Jones, 188 La. 519, 177 So. 593 (1937); Ross Amigos Oil Co. v. State, 134 Tex. 626, 138 S.W.2d 798 (1940).

[7]See note 1 *supra*.

[8]See note 5 *supra*.

[9]See note 4 *supra*.

[10]*E.g.*, Smith v. Highland Mary Mining, Milling & Power Co., 82 Colo. 288, 259 Pac. 1025 (1927); Wax v. Riverview Cemetery Co., 2 Terry 424, 24 A.2d 431 (Del. Super. 1942); Gray v. Central Fla. Lumber Co., 104 Fla. 446, 140 So. 320 (1932).

results may be supported on two grounds: (1) the general judicial antipathy to forfeiture of any sort;[11] and (2) the provisions in most jurisdictions for reinstatement of lost privileges when back taxes have been paid.[12] A majority of the decisions indicate strongly an inclination of the judiciary to construe statutes of this nature in favor of the delinquent corporations.[13]

In 1931 the Florida Legislature passed the statute under which all of the pertinent Florida cases to date have been decided.[14] It provided that any corporation delinquent for six months in filing the required reports or paying the required fees forfeits its charter and corporate privileges. In *Gray v. Central Florida Lumber Co.*,[15] the Supreme Court of Florida, in the first case construing the statute, held that it did not declare a forfeiture but merely suspended charter privileges until payment of tax. It was sustained against attack on the grounds of defective title, discriminatory classification for tax purposes, and contravention of the Florida Constitution[16] in denying delinquent corporations access to Florida courts. In disposing of this latter contention, the Supreme Court stated:[17]

> "A franchise to transact business in this state by either a domestic or foreign corporation is a privilege which may be granted or withheld as the state deems proper. This premise established, it necessarily follows that such a franchise may be granted on such terms as the sovereignty may prescribe so long as not in conflict with the Constitution."

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[11]*E.g.*, State v. Sunset Ditch Co., 48 N.M. 17, 145 P.2d 219 (1944); see 3 COOK, CORPORATIONS §637 (8th ed. 1923); 16 FLETCHER, CORPORATIONS §8035 (Perm. ed. 1933).

[12]*E.g.*, Watts v. Liberty Royalties Corp., 106 F.2d 941 (10th Cir. 1939); Smith v. Highland Mary Mining, Milling & Power Co., 82 Colo. 288, 259 Pac. 1025 (1927); Wax v. Riverview Cemetery Co., 2 Terry 424, 24 A.2d 431 (Del. Super. 1942); Eagle Oil Co. v. Cohassett Oil Corp., 263 Mich. 371, 248 N.W. 840 (1933).

[13]*E.g.*, Klamath Lumber Co. v. Bamber, 74 Ore. 287, 145 Pac. 650 (1915); Deveny v. Success Co., 228 S.W. 295 (Tex. Civ. App. 1921). The statutes, being penal in nature, are strictly construed, of course.

[14]FLA. STAT. §610.11 (1941), enacted as Fla. Laws 1931, c. 14677, §5. This same section in FLA. STAT. 1949 contains the important 1949 addition of the words "or defend."

[15]104 Fla. 446, 140 So. 320 (1932), *cert. denied*, 287 U.S. 634 (1932).

[16]FLA. CONST. Decl. of Rights §§1, 4, 12.

[17]Gray v. Central Fla. Lumber Co., 104 Fla. 446, 459, 140 So. 320, 326 (1932).

This statement, of course, settles nothing; it merely restates the constitutional issues raised in the first place. The opinion indicates that the Court was influenced in its thinking by the more stringent penalties prescribed in other jurisdictions and by the reinstatement ab initio, under Florida law, of the suspended privileges upon payment of delinquent taxes.

The Court has never been called upon to consider the effect to be accorded transactions taking place during the period of suspension. Texas, in construing a similar provision,[18] takes the position that the corporation can make valid contracts during suspension, and that business then transacted is not void;[19] the only right lost is that of suing and defending in the Texas courts.[20] Other jurisdictions go so far as to nullify any acts performed,[21] including contracts made,[22] during suspension. The prevailing view as regards the legal status of the corporation is summarized in *Watts v. Liberty Royalties Corp.*:[23] "Its powers are only in suspension and reinstatement of its charter restores it to all of its powers and validates all of its acts, including the acts done while its charter was suspended."

This position appears analogous to the results of action by an agent outside the scope of his authority. His act, though done in behalf of his principal, is not binding upon the latter unless ratified.[24] Reinstatement is in the nature of ratification, since it relates to the date of suspension, and accordingly the corporation is thereupon regarded as never having been suspended.[25]

In *Jarvis v. Chapman Properties, Inc.*[26] appellee, a Florida corporation, filed its bill to foreclose a mortgage on November 24, 1931. On the following January 1 it became subject to forfeiture of privileges by reason of delinquency. On March 14 Jarvis answered, challenging its right to maintain suit by reason of its delinquency. It paid its fee and filed its report on March 21; and on August 22 a final decree favorable to it was entered. Jarvis did not at any time move to dismiss.

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[18]*E.g.*, TEX. STAT., REV. CIV. art. 7091 (Vernon's 1948).

[19]Federal Crude Oil Co. v. Yount-Lee Oil Co., 122 Tex. 21, 52 S.W.2d 56 (1932); see 11 TEXAS L. REV. 250 (1932).

[20]Isbell v. Gulf Union Oil Co., 147 Tex. 6, 209 S.W.2d 762 (1948).

[21]Sunset Oil Co. v. Marshall Oil Co., 16 Cal.2d 651, 107 P.2d 393 (1940).

[22]Irvine & Meier v. Wienner, 212 Mich. 199, 180 N.W. 492 (1920).

[23]106 F.2d 941, 944 (10th Cir. 1939).

[24]Texas Pacific Coal & Oil Co. v. Smith, 130 S.W.2d 425 (Tex. Civ. App. 1939).

[25]Watts v. Liberty Royalties Corp., 106 F.2d 941 (10th Cir. 1939).

[26]110 Fla. 17, 147 So. 860 (1933).

By the terms of the statute the corporation was not deprived of the privilege of maintaining the suit at the time of institution thereof, since it was not then in arrears. The Court held that although the right of complainant corporation to maintain suit was in suspension from January 1 to March 21, 1932, the cause was merely dormant during that period, and that ". . . when complainant filed its report and paid its tax the right to continue to maintain the suit was revived . . . ."[27] The opinion further states that there is ". . . no law or rule of court which required the dismissal of the cause by the court of its own motion. . . ."[28] What the result would have been had a motion to dismiss been filed during the pendency of the suspension was expressly left undecided. Seemingly the answer is the opposite today in view of two later decisions now to be considered.

Less than a year later the respondent below in *Christie v. Highland Waterfront Co.*[29] moved, more than twenty days after final decree in favor of a Florida corporation, to vacate this decree on the ground that the corporation had become delinquent during the suit and had remained so. Before the hearing on this motion the corporation cured its default, and the motion was denied. The Supreme Court affirmed. At approximately the same time *Diaz v. Parkland Estates*[30] raised the problem of dismissal of the suit of a Florida corporation delinquent not only upon entry of judgment but also at institution of suit. Diaz failed to plead the suspension, but on appeal sought reversal of an adverse judgment on this ground. The opinion, which unfortunately fails to state the facts clearly, does not indicate whether the court below was informed of the default before the appeal was taken. In reversing the judgment appealed from the Court stated:[31]

> ". . . the terms of the statute are . . . applicable to a corporation in actual default, and it becomes the duty of all the courts of this State to give effect to the statute by refusing to allow suits to be maintained in such courts of this State until defaults under the statute are duly remedied . . . ."

Dismissal must follow whenever the court learns of the default, ". . . despite the fact that until the point is raised on the record,

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[27] *Id.* at 20, 147 So. at 861.
[28] *Ibid.*
[29] 114 Fla. 263, 153 So. 784 (1934).
[30] 114 Fla. 273, 154 So. 199 (1934).
[31] *Id.* at 274, 154 So. at 200.

the right of a corporation to maintain a suit . . . will be presumed so long as the contrary is not made to appear."[32] Although a judgment rendered without knowledge of default is voidable, not void, the defendant need not plead suspension prior to such judgment.

The next case, *Irwin v. Gilson Realty Co.*,[33] was a foreclosure suit by a New York corporation. It filed its bill on February 21, 1933, although it was in default at the time; and on April 3 Irwin moved to dismiss on this ground. On April 26 the trial court denied his motion and required him to answer, which he did on May 27 after several extensions of time. On this date the corporation was still in arrears, but paid its fees a few days later. The Supreme Court held that the trial court erroneously denied the motion to dismiss, and that subsequent payment of the tax did not cure this error. On rehearing the corporation challenged the propriety of using a motion to dismiss in raising this issue. The Court rejected this argument, citing the *Diaz* opinion, and further held that the statute imposes a duty on the courts to recognize and enforce its terms whenever they learn of default existing at institution of suit and still continuing when the motion to dismiss is heard. In 1935 the corporation in *Burton v. Oliver Farm Equipment Sales Co.*[34] was delinquent at the time it instituted suit, but filed its report and paid its fee before entry of a final decree in its favor. Its right to maintain the suit was upheld on appeal.

Certain conclusions may be drawn from the *Jarvis, Christie, Diaz, Irwin* and *Burton* cases:

1. A motion to dismiss, an answer, or any other means designed to call the delinquency of the corporation to the attention of the court may be used to raise the issue; indeed, it can even be first raised on appeal, according to the *Diaz* opinion.
2. Contrary to the broad statement in the *Jarvis* opinion, the court, when informed of material delinquency of a corporation, is under a duty to dismiss the suit of such a complainant unless the default is remedied promptly and before the decision is rendered.
3. A corporation delinquent when instituting suit is denied the use of the courts, even though it removes this delinquency after the hearing on motion to dismiss.

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[32]*Id.* at 275, 154 So. at 200.
[33]117 Fla. 394, 158 So. 77 (1934).
[34]121 Fla. 148, 163 So. 468 (1935).

4. When the delinquency is raised by answer, the corporation can still proceed by curing it before final decree.
5. A corporation becoming delinquent after instituting suit can proceed if it cures its default before the hearing on a motion to dismiss on this ground.

Since the reasoning in all these cases is predicated on the basic aim of putting pressure on the corporation to file its reports and pay its taxes,[35] the crucial time should logically be that either of the hearing on motion or of the final decree whenever the default is raised by answer. The practical step, of course, is to raise the issue squarely by motion to dismiss upon discovery of the existence of default.

The 1931 statute, besides declaring "forfeit" the charter and corporate privileges, provided specifically that a corporation in default should not be permitted to "maintain" any action in the Florida courts.[36] In 1949, however, after the inadvertent[37] release of an opinion construing the 1931 act as not contemplating the suspension of a delinquent corporation's right to defend as distinct from its right to attack,[38] the Florida Legislature amended the penalty provision to read as follows:[39]

> "Any corporation failing to comply with the provisions of this law for six months shall not be permitted to maintain or defend any action in any court of this state until such reports are filed and all fees due under this chapter paid."

Thus the Legislature eliminated the necessity of any further argument as to whether "maintain" embraces "defend."

At the same time, it removed from this section the provision for suspending the corporate and charter privileges. There was good reason for this deletion, however. Sections 610.10 and 610.11 of Florida Statutes 1941 were at best confusing, and perhaps in conflict,

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[35]See note 6 *supra.*

[36]See note 14 *supra.*

[37]The word "inadvertent" is used because the first opinion, printed in the Southern Reporter Advance Sheets of Sept. 22, 1949, was withdrawn after rehearing from the bound volume (see the caption Frisz, Inc. v. Sherry, 41 So.2d viii), and the memorandum affirmance on rehearing of the judgment below is published under the same caption in 42 So.2d 849 (Fla. 1949).

[38]Frisz, Inc. v. Sherry, *supra* note 37.

[39]FLA. STAT. §610.11 (1949).

as to the length of time required to convert failure of the corporation to file its report, and to pay its tax, into suspension of its charter and corporate privileges in Florida; and the 1949 amendment to Section 610.11 now leaves the matter of suspension exclusively within Section 610.10. Accordingly the only major change is the 1949 addition to Section 610.11 of the words "or defend."

Denial of the right of a delinquent corporation to defend raises the following questions:

1. Are the procedural due process requisites of both the United States [40] and Florida [41] Constitutions met when a claim is presented and a default judgment entered without giving the corporation a chance to be heard? Does not this procedure open the door to spurious claims?
2. Is equal protection afforded in the courts, as guaranteed by both the United States[42] and Florida[43] Constitutions, if the opponent of the corporation is permitted to use the courts while the corporation is denied such use in the same case?
3. How can any court inform the corporation that it cannot be in court, and in the same breath hold that it is there for purposes of a default judgment against it?

The following arguments have been used to sustain suspension of corporate privileges and other penalties as a constitutional exercise of legislative power:[44]

1. A corporation is the creature of the state, and is therefore subject to regulation and control by the state;[45]
2. Upon paying the required fees and filing its reports, the corporation can regain its lost privileges; and, since it has the choice as to whether it is to be barred from the courts, the due process

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[40]U.S. CONST. AMEND. XIV, §1.

[41]FLA. CONST. Decl. of Rights §12.

[42]U.S. CONST. AMEND. XIV, §1.

[43]FLA. CONST. Decl. of Rights, §§1, 4.

[44]Caveat: The transactions of some foreign corporations fall within interstate commerce, to which an enactment like FLA. STAT. §610.11 (1949) cannot apply, a limitation recognized in Schwartz v. Frango Corporation, 44 So.2d 292 (Fla. 1950).

[45]Gray v. Central Florida Lumber Co., 104 Fla. 446, 140 So. 320 (1932); Natchitoches Finance Co. v. Smith, 175 So. 915 (La. App. 1937).

and equal protection clauses are not violated;[46]

3. Third parties do not lose their remedy in any event, inasmuch as they can either sue the directors of the corporation as trustees or sue the de facto corporation.[47]

Constitutional attack on the 1949 denial of the right to defend, a denial added by amendment from the floor[48] with apparently little or no consideration of its constitutionality, may well materialize. Denying the corporation access to the courts in maintaining[49] a suit is unquestionably permissible. Designating it a legal nullity and directing suit against its trustees or a receiver will withstand constitutional challenge. But the propriety of authorizing anyone so desiring to bring the corporation itself into court, and at the same time forbidding it to appear, is highly questionable. Especially is this true when one can sue the legal representatives of a delinquent corporation, who are not only permitted but expected to defend its assets against spurious claims and thereby to secure a decision on the merits. From the standpoint of the state, even a strong desire to collect taxes does not justify disregard of procedural due process.

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[46]Boyle v. Lakeview Creamery Co., 9 Cal.2d 16, 68 P.2d 968 (1937).

[47]11 CALIF. L. REV. 40 (1922); *cf.* 4 U. OF FLA. L. REV. 96 (1951) re suit after dissolution.

[48]FLA. H.R.J. 949 (1949).

[49]As to whether "maintain" includes "institute," contrast Irwin v. Gilson Realty Co., 117 Fla. 394, 405, 158 So. 77, 82 (1934), inwhich Brown, J., states that ". . . institution of a suit is the beginning of its maintenance," with Burton v. Oliver Farm Equip. Sales Co., 121 Fla. 148, 149, 163 So. 468, 469 (1935). The logic of the former opinion seems inescapable.