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California Bill Aims To Make Foreign Nonqualified Limited Liability Company (LLC) Contracts Voidable

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As discussed in prior posts, “transacting intrastate business” is not the same as “doing business”. *See* You may Be Doing Business in California Even When Not Transacting Intrastate Business. The former is what determines whether a foreign corporation or limited liability company must qualify with the California Secretary of State. The latter determines whether a corporation or LLC must file a tax return with the Franchise Tax Board. The FTB takes the position that all LLCs classified as partnerships or disregarded entities that organize in California, register in California, or do business in California, must file California Form 568 Limited Liability Company Return of Income. An LLC that files a Form 568 must pay an annual tax of $800, and may be subject to an LLC fee based on total income from all sources derived from or attributable to the state of California.

As one might expect, bad things can happen when an LLC fails to file a tax return or pay its taxes. One of these bad things is that that the LLC may be suspended or forfeited. Another bad thing is that any contract entered into by that LLC may be voided by another party to the contract during the suspension or forfeiture period. However, these misfortunes do not fall equally on all LLCs. It turns out that only domestic LLCs and foreign LLCs qualified with the Secretary of State face the possibility of contract avoidance. Who’s been left out? Foreign LLCs that have not qualified with the Secretary of State. Alas, “*Hanc marginis exiguitas non caperet*“.

The important point for today is that Assemblymember Nancy Skinner has introduced a bill, AB 1143, that is intended to remedy this inequality of affliction. The bill has already passed through two committees without a single no vote. This is especially important because the bill is an “urgency bill” that requires a 2/3 vote of each house. Cal. Const. Article IV, Section 8(d). Urgency statutes take effect immediately.

The constitution imposes two additional requirements on urgency statutes. They must be “necessary for the immediate preservation of the public peace, health, or safety” and include a statement of facts explaining that necessity. One can only wonder at the statement included in AB 1143: ”In order to ensure that all entities doing business in California are treated equally under the Revenue Taxation Code, it is necessary that this act take effect immediately.” This hardly seems to be a statement of *facts*. It is a circular statement of purpose. It seems that even the legislators can’t bring themselves to claim that there will be civil disturbances, people will fall ill, or be endangered if this bill does not become law immediately.

However, challenging a legislative declaration of urgency is no easy task. Long ago, the California Supreme Court adopted the rule that a declaration of urgency by the legislature will not be declared invalid unless it appears clearly and affirmatively from the legislature's statement of facts that a public necessity does not exist. *Davis v. County of Los Angeles*, 12 Cal. 2d 412 (1935). Because AB 1143 includes no statement of facts, it would seem to be a good candidate for the application of the Supreme Court's proviso.

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