The Problem of Suspended Corporations in the Present Economic Downturn

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I. INTRODUCTION

Corporations that do not pay their state taxes may be suspended in California.¹ Once suspended, a corporation effectively finds itself in a legal coma from which it can neither defend nor prosecute civil actions during the pendency of its suspension. In the context of a complex civil lawsuit, the limitations placed on a suspended corporation that is a party to the suit present unique circumstances for all concerned, for example:

- As to *the suspended corporation*, it is still a party to the lawsuit, but can neither prosecute its claims, nor defend itself from others;
- As to *the attorney* representing the now suspended corporation in the litigation, he or she risks criminal penalty and possible disbarment by continuing to defend or prosecute claims on behalf of the suspended corporation;
- As to the other parties to the lawsuit, the suspended corporation is still a party, but legally incapacitated; the situation creates strategic risks and opportunities for those other parties;
- As to *insurance carriers for suspended corporations*, they face the difficult choice of intervening and becoming parties to the action, or not intervening and possibly being held liable for any judgment entered against the insured; and
- As to the *court*, it must be aware that an insurer intervening on behalf of a suspended corporation can alter the character of the lawsuit with respect to how the case is tried under the circumstances.

The purpose of this article is to discuss some of the issues that arise when a suspended corporation is a

party to a lawsuit. First, this article will explain what a suspended corporation is, and how suspended status differs from bankruptcy and dissolution. Second, it will discuss the implications of and options for dealing with an entry of default judgment against a suspended corporation. Third, it will address the risks and issues involved in representing a suspended corporation. Fourth, it will address the issues and problems that can arise when a suspended corporation's insurance carrier intervenes in a lawsuit to which the suspended corporation is a party.

II. WHAT IS A SUSPENDED CORPORATION?

1. Suspended Corporation Defined

Pursuant to <u>California Revenue and Taxation Code</u> <u>Section 23301</u>, the exercise of corporate powers, rights and privileges may be suspended for the failure to pay taxes. A suspended corporation, then, is a corporation that has failed to pay its state taxes and, as a result, can no longer exercise corporate powers, rights and privileges, including the right to defend against and prosecute legal claims.² California, while somewhat unique, is not alone in its treatment of corporations that fail to pay their state taxes.³

2. Motions to Dismiss and Revival of a Suspended Corporation

The purpose of <u>California Revenue and Taxation</u> <u>Code Section 23301</u> is to encourage the payment of taxes by corporations.⁴ For this reason, a suspended corporation can revive itself, i.e. return to its prior corporate status, by simply paying its back taxes and filing the appropriate paperwork. Further, once a corporation has been revived, its tax delinquencies, upon correction, are viewed as mere irregularities.⁵ The same, however, is not true with respect to legal action taken by and against the corporation during the period of suspension.

Since the purpose of <u>California Revenue and Taxa-</u> tion <u>Code Section 23301</u> is to encourage the payment of taxes by corporations, the California Supreme Court has held that the revival of corporate powers has the effect of validating prior legal action taken during the period of suspension.⁶ This rule, however, is limited to procedural acts, and does not apply to negate substantive defenses that have accrued during the period of suspension.⁷ To illustrate, consider a scenario in which a complaint is filed by a corporation during a period of suspension, and then, prior to the corporation's revival, the applicable statute of limitations runs. In this scenario, the suspended corporation's revival would not toll the statute of limitations, even though the complaint was filed prior to the statute running, as the statute of limitations provides a substantive defense.⁸

While a suspended corporation's revival will not "unring the bell" of a substantive defense, it can defeat a motion to dismiss based on the suspended status of the corporation. For instance, when faced with claims made by a suspended corporation, a party may assert the suspension of corporate powers as a defense during the period of suspension.⁹ This defense, which is a plea in abatement, will be defeated by the subsequent revival of the corporation.¹⁰

When a party pleads the suspension of corporate powers as a defense, the court may grant a continuance in order to allow the suspended corporation to revive itself.¹¹ Although the granting of a continuance would further the purpose of California Revenue and Taxation Code Section 23301, and pleas in abatement are generally disfavored in law,¹² a court maintains discretion to deny a request for a continuance where it deems it appropriate to do so. For example, in Old Fashion Farms v. Hamrick, the California Appellate Court found the plaintiff suspended corporation's request for a continuance was properly denied because the lawsuit was lacking in merit and the suspended corporation had made no efforts to revive itself.¹³ In light of this, a suspended corporation that intends to request a continuance must be prepared to show diligence in seeking a revival, as well as facts evidencing that its claim or defense is not meritless.

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3. Distinguishing Suspension from Bankruptcy and Dissolution

What makes the suspension of a corporation drastically different from bankruptcy and dissolution is this: a bankrupt or dissolved corporation can legally continue to defend itself and prosecute claims, while a suspended corporation cannot. With respect to bankruptcy, there is an immediate statutory stay on litigation against the corporation following the filing of the bankruptcy petition.¹⁴ This stay, however, does not necessarily put an end to all litigation, as relief from the stay will be granted to a party in interest for cause, such as protecting an interest in property.¹⁵ With respect to dissolution, the corporation continues to exist for the purpose of prosecuting and defending claims.¹⁶ Therefore, bankrupt and dissolved corporations, or their insurance carriers, may defend and litigate the merits of legal claims.¹⁷ This is not the case with a suspended corporation.

A suspended corporation is incapacitated, but not protected. Other parties to a lawsuit may still prosecute claims against the suspended corporation, while also asking the court to prevent the suspended corporation from defending against or prosecuting its claims. In a complex multi-party lawsuit, for instance, a plaintiff could seek damages for personal injuries from a suspended general contractor, but the general contractor would be unable to seek indemnity from the responsible subcontractors via crosscomplaint. The plaintiff could even move for default judgment against the suspended corporation, and then seek to establish coverage under the suspended corporation's general liability policies in a subsequent direct action against the suspended corporation's insurance carrier.18

III. DEFAULT JUDGMENT

An entry of default judgment conclusively establishes the facts as to liability.¹⁹ Consequently, the entry of default judgment against a suspended corporation greatly limits the coverage defenses available to its insurer in the event the plaintiff seeks to enforce the default judgment against the insurer. In addition, the available coverage defenses may be further limited insofar as the failure to intervene is somewhat analogous to the failure to defend, and an insurer that has an opportunity to defend, but does not, is bound by the issues adjudicated as to its insured.²⁰

Instead of contesting coverage after a default judgment has been entered, a more effective strategy may be for the carrier to intervene in the lawsuit to which its insured, the suspended corporation, is a party, in order to prevent the entry of default judgment in the first place

When faced with liability for a default judgment entered against its insured, one option available to the carrier is to argue that its policy's cooperation clause²¹ bars coverage. This argument would apply in instances where the insured, by virtue of its suspension, is unable to cooperate with the carrier in the underlying action, and, as a result, has a default judgment entered against it. This argument, however, is unlikely to succeed, as the burden will be on the carrier in the subsequent action to establish that had the cooperation clause not been breached, there is a substantial likelihood the trier of fact in the underlying action would have ruled in favor of the insured.²²

Instead of contesting coverage after a default judgment has been entered, a more effective strategy may be for the carrier to intervene in the lawsuit to which its insured, the suspended corporation, is a party, in order to prevent the entry of default judgment in the first place. A carrier is permitted to intervene where preventing an entry of default judgment against its insured is necessary to protect its own interests.²³ Moreover, in *Kaufman & Broad Communities, Inc. v. Performance Plastering*, the California Appellate Court observed the following:

Some cases, however, have sanctioned intervention as an appropriate approach. For example, in Reliance Ins. Co. v. Superior Court (2000) 84 Cal. App. 4th 383, 388, the appellate court concluded the trial court abused its discretion in refusing to allow the insurance company (Reliance Insurance Company) to intervene in a lawsuit against the insured suspended corporation ... The Sixth District Court of Appeal concluded the insurance company had a direct interest in the litigation. (Id. at pp. 386–387.) Under Insurance Code section 11580, a judgment creditor can sue the insurance carrier for the defendant against whom a judgment is obtained. (Reliance Ins. Co. v. Superior Court, supra, at p. 386.) As a result, where there is a danger that a judgment will be entered by default, the insurance carrier is entitled to intervene in the underlying case to contest its insured's fault or the available damages. (Id. at p. 387) O'Hearn v. Hillcrest Gym & Fitness Center, Inc. (2004) 115 Cal. App. 4th 491, 494, footnote 1, comes to this same conclusion.24

Under California law, an insurance company is permitted to intervene in a lawsuit where its insured is a suspended corporation and a party to the lawsuit. Failure to intervene may ultimately result in the insurance company being found liable for a default judgment entered against its insured, unless, of course, there was no coverage for the claim to begin with. Intervention, and the issues associated therewith, will be discussed in more detail in Section V of this article.

IV. THE PENALTY FOR REPRESENTING A SUSPENDED CORPORATION AND THE RESULTING ETHICAL CONFLICT

California Revenue and Taxation Code Section 19719 states that any person who *attempts* to exercise the powers, rights and privileges of a suspended corporation (which would include prosecuting or defending claims) may be punished "by a fine of not less than \$250 and not exceeding \$1,000, or by imprisonment not exceeding one year". In 1998, this statute was amended to exclude counsel retained by an insurer on behalf of a suspended corporation.²⁵ This exclusion, however, was not extended to counsel retained directly by the suspended corporation, or an entity, other than an insurer, acting on its behalf. Consequently, an attorney that represents a suspended corporation in a litigated matter, but was not retained by an insurance company on behalf of the suspended corporation, is in violation of Section 19719.

[A]n attorney, other than one retained by an insurance company, who knowingly advances the legal interests of a suspended corporation, puts his or her license in jeopardy

There are two instances in which Section 19719 is implicated vis a vis a suspended corporation's attorney. The first would be where an attorney is directly retained by a corporation that, subsequent to the attorney's retention, fails to pay its taxes and is suspended. The second would be where an attorney is retained directly by a suspended corporation that intends to seek a reviver. In both instances, especially the former, it is possible that the attorney representing the corporation may be unaware of its suspension, and, as a result, continue in good faith to defend and prosecute the corporation's legal interests. It seems unlikely that a judge would imprison a lawyer that represents the client in good faith and without knowledge of the corporation's suspension; nonetheless, an attorney retained directly by a corporation would be well served to remember the draconian penalty permitted by Section 19719.

In addition to potential criminal penalty, an attorney, other than one retained by an insurance company, who knowingly advances the legal interests of a suspended corporation, puts his or her license in jeopardy, as the California Supreme Court has long held: "It has always been considered a sufficient cause for disbarment for an attorney and counselor ... to encourage the commencement of proceedings which he knows, or has reason to know, are illegal or unjust."²⁶ This professional tenet

has been codified under California Rule of Professional Conduct No. 3-210, which provides that an attorney shall not advise the violation of any rule or law with respect to the prospective conduct of the client, the interaction between the attorney and the client, or the specific legal services sought by the client.²⁷

The threat of criminal penalty and disbarment provides substantial disincentive for an attorney retained by a suspended corporation to vigorously represent the corporation's interests, especially in instances where the attorney learns of the corporation's suspended status subsequent to undertaking the representation. Though there appears to be no case law directly addressing this ethical issue, an attorney would be well served to treat a suspended corporate client as any other client with whom a conflict of interests may exist, by providing the suspended corporate client with written disclosure of the conflict and, if necessary, obtaining the suspended corporation's informed written consent.²⁸

V. THE RIGHT OF THE INSURER TO INTERVENE AND NEW ISSUES CREATED BY THE PRESENCE OF THE INSURER

As noted, the *Kaufman & Broad Communities, Inc.* decision indicates that an insurer may intervene in a lawsuit against its insured where its insured is a suspended corporation. The right to intervene arises from <u>California Insurance Code Section 11580</u>,²⁹ which permits a party securing a judgment against a suspended corporation to proceed directly against the suspended corporation's insurance carrier to enforce the default judgment.³⁰ In order to prevent an entry of default judgment, an insurer may intervene in a lawsuit to contest its insured's (the suspended corporation) liability and damages.³¹

The intervening insurer, however, may not expand the scope of issues in the lawsuit to include coverage issues,³² despite the fact that the insurer, as an intervenor, is a party to the lawsuit.³³ Instead, the intervening insurer must wait until a subsequent action is filed to litigate insurance coverage issues, but even then can only litigate coverage "to the extent that the issues relevant to coverage were not actually litigated in the first lawsuit."³⁴

The law is still developing with respect to which coverage issues are properly reserved for a subsequent direct action. For instance, is the subsequent suit limited to the ultimate issues of coverage, such as whether an exclusion applies, or can facts that support liability and may impact coverage also be litigated? Without a clear answer to these questions, a practitioner representing an intervening insurer must develop a strategy with respect to the adjudication of issues in the initial lawsuit.

1. How is an intervening insurer to be referred to during the course of the litigation?

When an insurance company intervenes in a lawsuit to which its insured, a suspended corporation, is a party, the insurer becomes an actual party to the suit,³⁵ as opposed to the suspended corporation in a representative capacity.³⁶ This makes sense, as the purpose of intervention is to afford the insurer an opportunity to protect *its interests* by contesting the liability and damages claims against its named insured, the suspended corporation.³⁷ This, however, also creates some uncertainty with respect to how the insurance carrier is to be referred to during the litigation.

Evidence of liability insurance is inadmissible to prove negligence or other wrongdoing.³⁸ Further, evidence of liability insurance is generally "regarded as both irrelevant and prejudicial to the defendant."³⁹ With respect to an intervening insurer, then, any reference to the insurer in front of a jury would likely prejudice its insured, the suspended corporation. So how should the intervening insurer be referred to during the course of the litigation?

During the pretrial process, referring to the intervening insurer as a party would likely pose little threat of prejudice to the suspended corporation. The same, however, is not true of the trial itself, where reference to the intervening insurer in front of the jury would likely result in substantial prejudice to the insured. With this in mind, a court will likely identify the intervening insurer as a party during the pretrial process only. Should the case proceed to jury trial, and the client of the attorney representing the intervening insurer need to be identified, either by the court, or the attorney stating an appearance, the court will likely identify the suspended corporation as the attorney's client, and direct the attorney to do the same. Another possibility would be to not identify a client, but instead indicate that the attorney is representing the interests of the suspended corporation. Regardless of how it is done, the court and parties to the suit must refrain from referring to the intervening insurer in front of the jury.

2. Does the lawyer retained by the intervening insurer represent the insurer or its insured, the suspended corporation?

As discussed, the purpose of intervention is to afford the insurer an opportunity to protect its interests in the lawsuit.⁴⁰ While this will typically involve contesting the liability and damages issues as to the intervening carrier's named insured, the attorney retained by the intervening carrier does not represent the insured. Rather, the attorney represents the intervening insurer, so that, should the interests of the intervening insurer and suspended corporation diverge, the attorney would be obligated under most circumstances to represent the interests of the intervening insurer.

3. Is an intervening insurer that defends its interest to the detriment of its insured, the suspended corporation, exposed to bad faith liability if the suspended corporation revives?

Implied in every insurance policy is a covenant of good faith and fair dealing.⁴¹ Pursuant to this covenant, an insurer must consider the insured's interests to the same extent it considers its own, and not act so as to deprive the insured of its rights under the policy.⁴²

Typically, an insurer that provides a defense to its insured will retain defense counsel on behalf of the insured, thereby creating a tripartite relationship between the insurer, the insured and defense counsel.⁴³ This triumvirate will generally have a common interest in limiting liability to a third party plaintiff or cross-plaintiff.⁴⁴ This common interest, however, will be undermined should it become clear that some or all of the third party's allegations against the insured fall outside the scope of coverage afforded by the insurer's policy.⁴⁵

When a suspended corporation is named as a defendant or cross-defendant to a lawsuit, the relationship between the insurer, the insured, and counsel is of a completely different nature than the tripartite relationship that exists when the insured is not suspended. The suspended corporation's insurer becomes a party to the lawsuit through intervention for the purpose of representing its interests, not those of its insured

In a situation where the interests of the insurer and insured begin to diverge, the insurer is still subject to the covenant of good faith and fair dealing, and so must refrain from action that deprives the insured of its rights under the policy.⁴⁶ With respect to discovery and motions, for example, an insurer would be acting to deprive its insured of rights under the policy were it to direct defense counsel to fail to oppose a motion seeking to establish that the insured intentionally caused the alleged damage at issue, or to propound discovery with the intention of establishing that the insured's work did not cause damage, but, instead, was simply defective (and therefore not an "occurrence" causing "property damage"). In both instances, the insurer's action or inaction would help to establish liability on the part of the insured, while also helping to establish that the loss is not covered under a standard general liability policy.

When a suspended corporation is named as a defendant or cross-defendant to a lawsuit, the relationship between the insurer, the insured and counsel is of a completely different nature than the tripartite relationship that exists when the insured is not suspended. The suspended corporation's insurer becomes a party to the lawsuit through intervention for the purpose of representing *its* interests, not those of its insured. The question, then, is whether an intervening insurer faces bad faith exposure if in defending its interests it acts contrary to the interests of its insured, the suspended corporation. Though this question is of particular concern because of a suspended corporation's ability to revive itself, it appears that no court has squarely addressed this issue.

Imagine a scenario in which an intervening insurer has established undisputed facts that would entitle it to a declaration of non-coverage, only to have the suspended corporation revive itself. Upon revival, the suspended corporation would once again be a party to the action, but would not be entitled to a defense from its insurer, the intervening carrier, due to facts established by the insurer during the period of suspension.⁴⁷ In this scenario, would the insured then have a claim against the carrier for prejudicing its defense and rights to coverage under the carrier's policy? It seems unlikely that an insured, upon revival, would have an actionable bad faith claim against its insurer, where its insurer intervened in a lawsuit during a period of suspension and represented its interests to the detriment of the insured's. Simply put, the law allows the carrier to intervene in the lawsuit to protect its interests; subjecting the carrier to bad faith liability for protecting its interests would undermine the purpose of intervention in the context of suspended corporations. Nonetheless, a carrier considering intervention would be wise to retain an attorney with experience in the substantive area of law with which the lawsuit is concerned, as well as insurance coverage and bad faith. On the other side of the coin, an attorney representing a suspended corporation intending to revive must be mindful of and plan for the possibility that the suspended corporation's insurer will intervene in a lawsuit and take action that is detrimental to the suspended corporation.

An insurance carrier that intervenes in a lawsuit because its insured is a suspended corporation will have an interest in disproving coverage under its policies. The question is whether the intervening insurer, by virtue of trying to disprove coverage, will change the nature of discovery and the issues litigated.

The presence of an intervening insurer will not greatly change the nature of the issues litigated in a lawsuit, as an intervening party may not enlarge the scope of issues to be tried.⁴⁸ However, the intervening insurer may attempt to establish facts through discovery that, while relevant to the lawsuit, tend to disprove coverage. In this manner, an intervening insurer is likely to have a significant impact on a lawsuit, as the coverage-related discovery it pursues may affect the liability of the remaining parties to the suit, and the coverage afforded by their insurance carriers.

For instance, in a construction defect case, an intervening insurer could pursue discovery as to the dates the damages occurred in order to establish that the damages occurred outside the effective dates of its policy. The intervening insurer's primary motivation for seeking this information would be to disprove coverage under its policy. This information, however, would also likely affect the insurers of the other parties to the suit as well. In this way, an insurer's intervention and attendant litigation strategy could significantly impact the ability of the remaining parties to settle a lawsuit. For this reason, the parties to a lawsuit, regardless of size and complexity, need to anticipate an intervening insurer's litigation strategy when developing litigation strategies of their own.

5. May an intervening insurer file a motion for summary judgment on an issue that is determinative of coverage under its policies?

The *Kaufman & Broad Communities, Inc.* decision makes it clear that an intervening carrier may not expand the scope of a lawsuit by raising coverage issues.⁴⁹ Instead, the carrier is generally limited to contesting issues of damages and liability with respect to its insured, the suspended corporation, and must wait until a subsequent direct action is filed against it to litigate coverage issues.⁵⁰ It remains to be seen, however, whether a court would allow an intervening carrier to file a motion for summary judgment on an issue of damages that, if granted, would dispose of coverage under the carrier's policies.

While not addressing this issue directly, the Kaufman & Broad Communities, Inc. decision does provide some guidance insofar as it acknowledges that coverage issues can be litigated in a lawsuit to which an insurer intervenes.⁵¹ Specifically, Kaufman & Broad Communities, Inc. provides that "to the extent that issues relevant to coverage were not actually litigated in the first lawsuit" they can be litigated in a subsequent action brought to determine if the judgment is covered by insurance.52 Within the context of the Kaufman & Broad Communities, Inc. decision, this statement appears to be an acknowledgement that the adjudication of issues properly within the scope of the lawsuit to which the insurer has intervened may result in a determination of coverage issues as well. Such an acknowledgement would imply that an intervening carrier is permitted to litigate issues affecting coverage, so long as the issues fall within the scope of the lawsuit.

Though *Kaufman & Broad Communities, Inc.* arguably permits an intervening insurer to file a motion for summary judgment that, if granted, would dispose of coverage under the insurer's policies, it hardly provides a definitive answer to the question posed in this section. Until a definitive answer is provided, a court confronted with this question will likely be afforded a great deal of discretion when determining whether to hear the intervening insurer's motion.

6. May an intervening insurer pursue contribution from additional insured carriers?

The question posed by this section is most likely to arise within the context of a construction defect lawsuit. In a typical construction defect case, the developer of the construction project at issue will have contractually obligated the subcontractors that worked at the project to provide the developer with additional insured coverage. As a result of this contractual requirement, the liability policies maintained by the subcontractors will typically contain either "blanket" additional insured endorsements⁵³ or additional insured endorsements that specifically identify the developer as an additional insured to the policies. The question, then, is whether an intervening carrier to a construction defect lawsuit may pursue additional insured coverage for its insured, the suspended corporation, where the suspended corporation was the developer of the construction project at issue.

Any attempt by an intervening insurer to pursue additional insured coverage for the suspended corporation will likely be met with strong opposition from the additional insured carriers.⁵⁴ Specifically, the additional insured carriers will likely argue that because

the suspended corporation is prohibited from defending itself under California Revenue and Taxation Code Section 23301, a duty to defend cannot exist. Further, the additional insured carriers will likely point to the fact that the intervening insurer is not representing the interests of the suspended corporation in the lawsuit, but instead is representing its own interests as the suspended corporation's insurer.

In response to the opposition of the additional insured carriers, an intervening insurer will likely argue that the issue is one of equity, not strictly policy terms,⁵⁵ and that as a matter of equity, the additional insured carriers should be paying a share of the intervening insurer's legal costs. While persuasive arguments exist on both sides of the issue addressed in this section, it appears that the courts have not yet taken a position on this matter. As such, the extent to which an intervening carrier may pursue additional insured coverage remains uncertain.

VI. CONCLUSION

When a suspended corporation has been named as a party to a lawsuit filed in California, a number of issues arise which must be carefully considered by the parties to the lawsuit, the parties' attorneys, and the parties' insurance carriers. This is especially true with respect to the suspended corporation's attorney, who risks criminal punishment and disbarment by continuing to represent the suspended corporation in the lawsuit.

The presence of a suspended corporation in a lawsuit brings with it the possibility of intervention by the suspended corporation's insurance carrier. Should the suspended corporation's insurance carrier choose to intervene, the parties to the suit must be conscious of the fact that the intervening insurer is representing its own interests, as opposed to those of its insured, and that in doing so it can have a significant impact on the outcome of the lawsuit.

In the context of a civil lawsuit, there are currently more questions than answers when it comes to suspended corporations. For this reason, it is important for the parties to a lawsuit, their lawyers, and their insurers to be aware of the dangers and opportunities inherent in a lawsuit to which a suspended corporation is a party, and to develop a strategy for effectively managing the litigation.

² Kaufman & Broad Communities, Inc. v. Performance Plastering, <u>39 Cal. Rptr. 3d 33</u>, 136 Cal. App. 4th 212, 217–218 (2006).

Similarly, Oklahoma provides for the forfeiture of corporate rights where a corporation fails to pay taxes owed to the state. 68 Okl. St. <u>§ 1212</u>. The forfeiture of corporate rights includes the right "to sue or defend in Oklahoma courts." Century Inv. Group, Inc. v. Bake Rite Foods, Inc., 2000 OK CIV APP 48, 1 (2000); Okl. St. § 1212(c). Like Arizona, Oklahoma law provides that any person who attempts to exercise the rights or privileges of a suspended corporation "shall be guilty of a misdemeanor." 68 Okl. St. § 1212 (b).

In Texas, a corporation that fails to pay state taxes will forfeit its corporate privileges. Tex. Tax Code § 171.251. Falling in line with California and Oklahoma, Texas law provides that a corporation which has forfeited its corporate privileges "shall be denied the right to sue or defend in a court of this state." Tex. Tax Code § 171.252 (1). Despite the clear language of Section 171.252, it appears some Texas courts have "limited the statute to prohibit defendants from bringing cross actions, not from merely defending lawsuits." Anoco Marine Indus. v. Patton Prod. Corp., 2008 Tex. App. LEXIS 6662, 6 n. 4 (Tex. App. Fort Worth Aug. 29, 2008).

While California is not unique in its handling of corporations delinquent in their payment of taxes, other states employ different legal mechanisms for dealing with said corporations. In Washington, for example, a corporation that fails to pay license fees may be administratively dissolved. Rev. Code Wash. § 23B.14.200. Once a corporation has been administratively dissolved, "it continues its corporate existence but may not carry on any business except that appropriate to wind up and liquidate its business and affairs." Rev. Code Wash. § 23B.14.050. Administrative dissolution does not "[p]revent commencement of a proceeding by or against the corporation in its corporate name." Rev. Code Wash. § 23B.14.050(2)(e).

⁴ Peacock Hill Association v. Peacock Lagoon Construction Co., <u>105 Cal. Rptr. 29</u>, 8 Cal. 3d 369, 371 (1972).

⁵ Peacock Hill Association, <u>8 Cal. 3d at 371</u>.

⁶ Peacock Hill Association, 8 Cal. 3d at 373.

⁷ Welco Constr., Inc. v. Modulux, Inc., <u>120 Cal. Rptr. 572</u>, 47 Cal. App. 3d 69, 73 (1975).

⁸ Welco Constr., Inc., <u>47 Cal. App. 3d at 73</u>; Cleveland v. Gore Bros., Inc., <u>14 Cal. App. 2d 681, 683</u> (1936).

⁹ A party wishing to take advantage of a corporation's suspended status must affirmatively assert the suspended status as a defense. Peacock Hill Association, <u>8 Cal. 3d at 373</u> (referring to Diverco Constructors, Inc. v. Wilstein, <u>4 Cal. App. 3d 6</u> (1970)).

¹⁰ Peacock Hill Association, 8 Cal. 3d at 373; Traub Co. v. Coffee Break Service, Inc., <u>57 Cal. Rptr. 846</u>, 66 Cal. 2d 368, 370 (1967).

¹¹ A. E. Cook Co. v. K S Racing Enterprises, Inc., <u>79 Cal. Rptr. 123</u>, 274 Cal. App. 2d 499, 500 (1969); United States v. 2.61 Acres of *Land*, <u>791 F.2d 666, 671–672</u> (9 ¹² *Traub Co.*, 66 Cal. 2d at 37*v*.

¹ Cal. Rev. & Tax. Code § 23301.

³ A survey of several states indicates California is not alone in suspending the corporate rights and privileges of corporations that fail to pay state taxes. Much like California, Arizona also suspends "the corporate powers, rights and privileges of a domestic corporation" for failure to pay taxes. Ariz. Rev. Stat. 43-1152. Further, "[a]ny person who attempts or purports to exercise any of the rights, privileges or powers of any corporation suspended pursuant to section 43-1152 ... shall be guilty of a class 1 misdemeanor." Ariz. Rev. Stat. 43-1154.

¹³ Old Fashion Farms v. Hamrick, 61 Cal. Rptr. 254, 253 Cal. App. 2d 233, 236 (1967).

14 11 USCS § 362.

15 11 USCS § 362(d).

¹⁶ Cal. Corp. Code § 6720 (a).

¹⁷ Assuming that insurance is the only asset reachable by the claimant against the bankrupt or dissolved corporation, the attorney representing the corporation recognizes that the insurer is functionally, if not legally, the client.

¹⁸ Kaufman & Broad Communities, Inc., <u>136 Cal. App. 4th at 222</u>.

¹⁹ Geddes v. United Fin. Group, <u>559 F.2d 557, 560</u> (9th Cir. 1977).

²⁰ See Clemmer v. Hartford Ins. Co., 151 Cal. Rptr. 285, 22 Cal. 3d 865, 884 (1978).

²¹ In the Conditions Section of the industry standard general liability policy form, there is a provision requiring the insured to cooperate with the insurer in the defense of any lawsuit.

22 Nasongkhla v. Gonzalez, <u>34 Cal. Rptr. 2d 379</u>, 29 Cal. App. 4th Supp. 1, 4–5 (1994).

²³ See Truck Ins. Exchange v. Superior Ct., <u>70 Cal. Rptr. 2d 255</u>, 60 Cal. App. 4th 342, 347–348 (1997).

²⁴ Kaufman & Broad Communities, Inc., 136 Cal. App. 4th at 221–222.

²⁵ While the statute clearly excludes counsel retained by an insurance carrier, it is unclear if it also excludes independent counsel, or Cumis counsel, retained by the insured suspended corporation as a result of a conflict of interests with its insurance carrier. In California, an insurer is statutorily required to allow the insured to retain independent counsel where the insurer's reservation of rights creates a conflict between its interests and the interests of its insured. Cal Civ Code § 2860. However, in the case of a suspended corporation it is difficult to envision a scenario in which this issue would arise, as any attorney retained by the suspended corporation's insurance carrier would be representing the insurance carrier as an intervenor, not the suspended corporation. See Kaufman & Broad Communities, Inc., 136 Cal. App. 4th at 219-221.

²⁶ *In re* Disbarment of C.C. Stephens, <u>77 Cal. 357, 359–360</u> (1888).

²⁷ California Rule of Professional Conduct No. 3-210 provides that an attorney shall not advise the violation of any law, rule, or ruling of a tribunal unless the attorney believes in good faith that such law, rule, or ruling is invalid. The Discussion accompanying this Rule provides that the Rule applies to the prospective conduct of a client, the interaction between the attorney and client, and the specific legal service sought by the client from the attorney.

²⁸ California Rule of Professional Conduct No. 3-310(B)(4) provides that an attorney must provide the client with written disclosure where the attorney has legal, business, financial, or professional interests in the subject matter of the representation. Though the interests of the attorney representing a suspended corporation would lie in the representation itself, rather than the subject matter of the representation, this is the Rule that most closely addresses the conflict of interests inherent in the representation of a suspended corporation.

²⁹ <u>California Insurance Code Section 11580</u> (b)(2) states that an insurance policy shall contain, or be construed so as to contain a "provision that whenever judgment is secured against the insured ... in an action based upon bodily injury, death, or property damage, then an action may be brought against the insurer on the policy and subject to its terms and limitations, by such judgment creditor to recover on the judgment."

³⁰ This is type of suit is commonly referred to as an 11580 action. See Reliance Ins. Co. v. Superior Ct., <u>100 Cal. Rptr. 2d 807</u>, 84 Cal. App. 4th 383, 386 (2000).

³¹ Kaufman & Broad Communities, Inc., 136 Cal. App. 4th at 224.

³² In Kaufman & Broad Communities, Inc., the California Appellate Court indicated that the parties to a lawsuit could stipulate to allow an intervening insurer to litigate coverage issues in that lawsuit. Kaufman & Broad Communities, Inc., 136 Cal. App. 4th at 225. Kaufman & Broad Communities, Inc., 136 Cal. App. 4th at 224.

³³ See Hospital Council of Northern Cal. v. Superior Ct., <u>106 Cal. Rptr. 247</u>, 30 Cal. App. 3d 331, 336 (1973).

34 Kaufman & Broad Communities, Inc., 136 Cal. App. 4th at 224 (emphasis added).

³⁵ See Hospital Council of Northern Cal., 30 Cal. App. 3d at 336.

³⁶ See Kaufman & Broad Communities, Inc., 136 Cal. App. 4th at 218, 220.

³⁷ Kaufman & Broad Communities, Inc., <u>136 Cal. App. 4th at 218, 223</u>.

³⁸ Cal. Evid. Code § 1155.
³⁹ Neumann v. Bishop, <u>130 Cal. Rptr. 786</u>, 59 Cal. App. 3d 451, 469 (1976).

⁴⁰ See Kaufman & Broad Communities, Inc., <u>136 Cal. App. 4th at 218, 223</u>.

⁴¹ Rappaport-Scott v. Interinsurance Exchange of the Automobile Club, <u>53 Cal. Rptr. 3d 245</u>, 146 Cal. App. 4th 831, 836 (2007); Hand v. Farmers Ins. Exchange, 29 Cal. Rptr. 2d 258, 23 Cal. App. 4th 1847, 1854 (1994).

42 Comunale v. Traders & General Ins. Co., <u>50 Cal. 2d 654, 658–659</u> (1958); Century Surety Co. v. Polisso, <u>43 Cal. Rptr. 3d 468</u>, 139 Cal. App. 4th 922, 948 (2006); See Crisci v. Security Ins. Co., <u>58 Cal. Rptr. 13</u>, 66 Cal. 2d 425, 430-431 (1967).

43 See San Diego Fed. Credit Union v. Cumis Ins. Society, 208 Cal. Rptr. 494, 162 Cal. App. 3d 358, 364 (1984).

44 Cumis Ins. Society, <u>162 Cal. App. 3d at 364</u>.

45 Cumis Ins. Society, 162 Cal. App. 3d at 364.

⁴⁶ Comunale, <u>50 Cal. 2d at 658–659</u>.

⁴⁷ In California, extrinsic evidence can be used to create, as well as defend against, the duty to defend. Montrose Chemical Corp. v. Superior Court, 24 Cal. Rptr. 2d 467, 6 Cal. 4th 287, 291 (1993).

⁴⁸ Kaufman & Broad Communities, Inc., <u>136 Cal. App. 4th at 224</u>.

49 Kaufman & Broad Communities, Inc., 136 (____pp. 4th at 224.

50 Kaufman & Broad Communities, Inc., 136 Cal. App. 4th at 224.

⁵¹ Kaufman & Broad Communities, Inc., 136 Cal. App. 4th at 224.

52 Kaufman & Broad Communities, Inc., 136 Cal. App. 4th at 224.

 53 A "blanket" additional insured endorsement is one that provides coverage to any person or organization that the named insured is required by contract to provide with additional insured coverage.

⁵⁴ Under California law, an insurer's duty to defend generally applies to the entire action, Presley Homes v. American States Insurance Co., <u>108 Cal. Rptr. 2d 686</u>, 90 Cal. App. 4th 571, 575 (2001); Buss, et al. v. Superior Court, <u>65 Cal. Rptr. 2d 366</u>, 16 Cal. 4th 35, 49 (1997), but is subject to equitable allocation where multiple insurers owe a duty to defend. *See* Maryland Casualty v. Nationwide Mutual Insurance Co., <u>97 Cal. Rptr. 2d 374</u>, 81 Cal. App. 4th 1082 (2000). As such, an insurer that provides additional insured coverage to a suspended corporation will likely be in the same position as the suspended corporation's primary carrier. However, where the suspended corporation's primary carrier has intervened to contest damages and liability as to the suspended corporation, an additional insured carrier will likely have no incentive to do so as well.

⁵⁵ See Crowley Maritime v. Boston Old Colony Ins. Co., <u>70 Cal. Rptr. 3d 605</u>, 158 Cal. App. 4th 1061, 1068 (2008) (holding equitable contribution arises not from contract, but from equity).