

CAUSE NO. 2010-55766

Big Star II Elec. Co., Inc. § **IN THE DISTRICT COURT OF**
v. § **HARRIS COUNTY, T E X A S**
§ **157th JUDICIAL DISTRICT**
Cadence McShane Constr. Co., LLC, et al. §

Order

Pending before this Court is a rather perplexing motion. Defendant has filed a Motion to Strike plaintiff's petition on the ground that plaintiff's corporate charter has been revoked for failure to pay franchise taxes. Plaintiff relies on Tex. Tax Code § 171.252 which provides, "[i]f the corporate privileges of a corporation are forfeited under this subchapter...the corporation shall be denied the right to sue or defend in a court of this state." So far, the motion seems relatively straight forward.

Defendant, however, argues that § 11.356 of the Tex. Bus. Org. Code applies, which provides that "notwithstanding the termination of a domestic filing entity under this chapter, the terminated filing entity continues in existence until the third anniversary of the effective date of the entity's termination only for purpose of...prosecuting or defending in the terminated filing entity's name an action or proceeding brought by or against the terminated entity." Complicating this issue is the definition of a "terminated filing entity" which is defined as a "terminated entity" which is defined as a domestic entity the existence of which has been...forfeited pursuant to the Tax Code." Tex. Bus. Org. Code § 11.001(4).

At first glance, these provisions appear inconsistent. Indeed, other courts have stated that these two provisions¹ "may seem at odds with one another," *Guardian Life Ins. Co. v. Kinder*, 2008 WL 243707 (S.D. Tex. 2008), and "appear to clash." *Guaranty Residential Lending, Inc. v.*

¹ The predecessor to TEX. BUS. ORG. CODE § 11.356 is TEX. BUS. CORP. ACT § 7.12. The language in the two provisions are essentially identical.

Homestead Mortgage Co., 291 FED App. 734 (6th Cir. 2008). However, on closer scrutiny, the provisions can be harmonized.

In *In re ABZ Ins. Services, Inc.*, 245 B.R. 255 (Bankr. N.D. Tex. 2000), the bankruptcy court wrestled with this identical issue and concluded that the “the Tex. Tax Code provisions and the Tex. Bus. Corp. Act dissolution provisions are consistent with one another.” *Id.* at 261. To understand this harmony, one must examine the procedure for forfeiture under the Tax Code. The first step in the process is that the Comptroller forfeits corporate privileges of a corporation if the corporation “does not pay, within 45 days after the date notice of forfeiture is mailed, a tax imposed by the chapter or does not pay, within those 45 days, a penalty imposed by this chapter relating to that tax.” Tex. Tax. Code § 171.251. Once corporate privileges are forfeited, then the anti-suit provisions of the Tax Code are triggered: “If the corporate privileges of a corporation are forfeited under this subchapter...the corporation shall be denied the right to sue or defend in a court of this state.” Tex. Tax Code § 171.252. Forfeiture of privileges does not equate to dissolution. The corporation still has 120 days to make the required payments. Tex. Tax Code § 171.301. After the 120th day after corporate privileges are forfeited, the comptroller certifies the name of the corporation to the secretary of state. Tex. Tax Code § 171.302. Once the secretary of state receives such notification, the charter is subject to forfeiture. Tex. Tax Code § 171.309. Once the charter is forfeited, then the Texas Business Organizations Code kicks in and permits a limited revival of the corporation to permit it to prosecute or defend suits for three years. Tex. Bus. Org. Code § 11.356. Thus, for the first 120 days after a corporation fails to pay franchise taxes, its corporate rights are forfeited and it may not sue in Texas courts. However, after 120 days, and its corporate charter is forfeited, it then its right to sue and defend is reinstated for three years. As stated by the Sixth Circuit:

Although this right-granting provision of the Texas Business Corporation Act appears to clash with the right-stripping provision of the Texas Tax Code, Courts have harmonized the two statutes. When a corporation forfeits its privileges, its right to sue or defend in Texas courts is transferred to its shareholders pursuant to the Texas Tax Code. However, if a corporation goes on to ‘forfeit[] its charter for failure to pay franchise taxes, the Texas Business Corporations Act then becomes controlling and the corporation continues its existence for the limited purpose described under article 7.12 [now 11.356]’

Guaranty Residential Lending, Inc. v. Homestead Mortgage Co., 291 FED app. 734, 741 (6th Cir. 2008). See also *Guardian Life Ins. Co. v. Kinder*, 2008 WL 243707 (S.D. Tex. 2008); *In re ABZ Ins. Services, Inc.*, 245 B.R. 255 (Bankr. N.D. Tex. 2000).

In this case, the Texas Secretary of State received notice from the Comptroller under § 171.302 and forfeited plaintiff’s charter on July 24, 2009. For six months preceding the charter forfeiture, plaintiff could not institute suit. However, once its charter was forfeited, plaintiff’s right to sue was reinstated for 3 years. Plaintiff filed this action on September 3, 2010. Accordingly, defendant’s motion to strike is denied.

Signed September 12, 2011.

Hon. Randy Wilson