

SENATE JUDICIARY COMMITTEE
Senator Thomas Umberg, Chair
2023-2024 Regular Session

SB 1168 (Limón)
Version: March 21, 2024
Hearing Date: April 9, 2024
Fiscal: Yes
Urgency: No
AWM

SUBJECT

Business entities: Secretary of State: document filings

DIGEST

This bill permits the Secretary of State to cancel a limited liability company (LLC) or corporation if, after a court order issues a finding that the entity has misused an individual's identifying information and orders that information to be removed, the entity does not update its records within 60 days; and provides a mechanism for a person who learns that their identifying information has been improperly used in an entity filing to have a disclaimer of the use of their information placed in the entity's file.

EXECUTIVE SUMMARY

The 2022 Budget Act¹ provided a one-year waiver of the filing fees for the registration of new corporations, LLCs, and limited partnerships (LPs) with the Secretary of State. The measure was intended to eliminate a cost barrier for new businesses in California. According to the Secretary of State, the fee holiday did result in increased entity filings; however, many of the entities appear to have been registered using names and/or addresses of persons who are not associated with the entities and who were not aware their personal information was being used. While Committee staff has not received information suggesting that the individuals whose personal information was used have suffered any actual harm as a result of these false filings – for example, there are no reports of identity theft or lawsuits arising from the filings – it is unquestionably troubling to have one's personal information used in a filing.

Current law establishes a mechanism by which a person who claims that their information is unlawfully included in an entity filing may seek a court order to have the information removed. But for those who do not have the time or resources to seek a

¹ SB 154 (Skinner, Ch. 43, Stats. 2022).

court order, there is no other method by which a person can create a record that their information is being misused.

This bill would permit a person whose personal identifying information has been used unlawfully in a business filing to file a disclaimer of proper authority, under penalty of perjury, with the Secretary of State. The disclaimer will be placed in the entity's file, thereby putting persons conducting an entity search on notice that the entity's use of the person's name or address has been contested. Additionally, the bill provides that, when the court issues an order requiring an entity to remove a person's name or address from a filing due to unlawful use, and the entity does not update the information within 60 days, the Secretary of State may cancel the entity.

This bill is sponsored by the California Secretary of State. The Committee has not received timely opposition to this bill. If this Committee passes this bill, it will then be heard by the Senate Banking and Financial Institutions Committee.

PROPOSED CHANGES TO THE LAW

Existing law:

- 1) Establishes a procedure through which a person who has learned or reasonably suspects that their personal identifying information has been used unlawfully in a business entity filing may petition the superior court for an order directing the person using the personal identifying information in the business filing to appear and show cause why the petitioner's information should be associated with the business entity. (Civ. Code, § 1798.201.)
 - a) A "business entity filing" means a document required by law to be filed with the Secretary of State pursuant to the Corporations Code, Financial Code, or Insurance Code. (Civ. Code, § 1798.200(a).)
- 2) Provides that, after the hearing in 1), if the court finds that the petitioner's personal identifying information has been used unlawfully in the business entity filing, the court shall issue an order certifying this determination; order the name and associated personal identifying information in the business entity filing to be redacted or labeled to show that the information is impersonated; and order the data to be removed from publicly accessible electronic indexes and databases. The order shall be filed with the Secretary of State. (Civ. Code, § 1798.202.)
- 3) Sets forth procedures for the establishment of general corporations, nonprofit corporations, and cooperative corporations in this state, which include executing and filing with the Secretary of State articles of incorporation; the articles of incorporation must include, among other information, the street and mailing address of the corporation, and may include the names and addresses of persons

appointed to act as initial directors. (Corp. Code, §§ 200, 202, 5120, 5130, 7120, 7130, 9120, 9130, 12300, 12310.)

- 4) Permits the Secretary of State to cancel the filing of articles of incorporation if the filing fee or franchise tax is not paid, as follows: within 90 days of receiving notice that the item presented for payment has not been honored, the Secretary of State must give written notice to the corporation of the failure to pay and a date in the future, no fewer than 20 days from the mailing date of the notice, by which the corporation must pay the fee or tax. If the amount has not been paid by cashier's check or equivalent before the date stated in the notice, the articles of incorporation shall be canceled. (Corp. Code, §§ 110.5, 5008.5, 12214.5.)
- 5) Sets forth procedures for the formation of a limited partnership, which include filing a certificate of limited partnership with the Secretary of State, which must include the street and mailing address of the limited partnership and the names and addresses of each general partner. (Corp. Code, § 15902.01.)
- 6) Sets forth procedures for the formation of a partnership, which may include filing a statement with the Secretary of State executed by at least two partners. (Corp. Code, § 16105.)
- 7) Sets forth procedures for becoming a registered limited liability partnership or a partnership other than a limited partnership, which include filing a registration with the Secretary of State, executed by one or more authorized partners, which must include the street and mailing address of the principal office. (Corp. Code, § 16953.)
- 8) Sets forth procedures for the formation of a limited liability company (LLC), which include filing articles of organization with the Secretary of State, which must include the street and mailing address of the LLC and may include information about the members. (Corp. Code, § 17702.01.)
- 9) Requires a limited partnership or LLC formed under the laws of a different jurisdiction to apply for a certificate of registration to transact business in this state by delivering an application to the Secretary of State; the application must include the entity's street address and mailing addresses and, for a limited partnership, the names and addresses of each of the general partners. (Corp. Code, §§ 15909.02, 16959, 17708.02.)
- 10) Permits the Secretary of State to cancel the business entity filings set forth in 5)-9) for nonpayment of specified fees and taxes under generally the same procedure as for corporations under 4), except that a second notice must be given after the first notice, and the filing may be canceled only if the fee or tax still has not been paid 20 days after the second notice. (Corp. Code, §§ 15902.01(f), 15909(c), 16105(g), 16953(d), 16959(d), 17701.01(f), 17708.06(c).)

This bill:

- 1) Permits the Secretary of State, after an order has been filed within the record of a corporation or LLC finding that a person's personal identifying information has been used unlawfully in a business entity filing, to cancel the business entity that is the subject of the order if, after 60 days, an updated statement of information has not been filed on behalf of the entity with the Secretary of State. The new statement of information shall not contain any information ordered to be redacted by the court.
- 2) Permits a person who has learned that their personal identifying information has been used unlawfully in a business entity filing to file with the Secretary of State a disclaimer of proper authority, so long as the entity has not been dissolved or terminated at the time of filing, as follows:
 - a) The disclaimer must be on a form prescribed by the Secretary of State.
 - b) The disclaimer shall be signed and verified under penalty of perjury by the person claiming their personal identifying information was unlawfully used in the business entity filing, and contain:
 - i. The name of the entity.
 - ii. The Secretary of State file number for the entity.
 - iii. The entity type.
 - iv. The date the business entity document containing their personal identifying information was filed.
 - v. The title of the business entity document that contained their personal identifying information.
 - vi. A description of the type of personal identifying information that the person claims was used unlawfully in the business entity filing.
 - vii. A statement that the person signing the disclaimer of proper authority did not authorize the use of their personal identifying information within the business entity document and that they reasonably suspect that their personal identifying information was included in furtherance of an unlawful purpose, as described in Penal Code section 530.5.
 - viii. A statement that the disclaimer of proper authority does not constitute a determination of any court or law enforcement investigation surrounding the facts and circumstances of the use of the information within the business entity document.
 - c) The filing fee for the disclaimer shall be \$30.

COMMENTS

1. Author's comment

According to the author:

Business identity theft is a growing problem that was exacerbated by a recent fee holiday for filing new business documents. The Secretary of State has identified more than 18,000 corporations and limited-liability companies created in 2022-23 that the Secretary of State presumes to be fraudulently created. In many cases, fraudsters have included on those filings the names of Californians as officers of the business, when those Californians have nothing to do with the business and did not provide their permission to be associated with the business. Criminals may try to use these fraudulent business entities to illegally take out loans, apply for government grants, and take advantage of tax credits or refunds.

Under current law, the Secretary of State has limited authority to address business entity filings that misuse a person's information, which opens the door for these business entities to be used for fraudulent activity and maintains a public record of the false association of innocent Californians with these businesses. This bill provides a process for a person whose information has been used improperly to file a disclaimer of proper authority with the Secretary of State, alerting anyone who accesses the related business entity filing that the person is not associated with the business. Additionally, the bill allows the Secretary of State to cancel a business entity that is the subject of a court order stipulating that a person's name has been used unlawfully in a business entity filing, if that business entity does not file an amended statement of information.

2. California's business entity filing fee waiver and an uptick in potentially fraudulent entities

As a general rule, a person wishing to establish an LLC or corporation in California must file articles of incorporation and pay a filing fee.² The filing fee is \$100 for an in-state corporation with shares and \$70 for an in-state LLC or LP.³ The 2022 Budget Act waived these filing fees for the 2022-2023 fiscal year;⁴ the fees were reinstated the following year.⁵

While the fee holiday was intended to foster business growth in the state, the Secretary of State reports that it appears that a number of the entities established in that window were not established for legitimate purposes. According to the author, the Secretary of

² Corp. Code, §§ 108, 200.

³ Gov. Code, §§ 12186, 12188, 23290.

⁴ SB 154 (Skinner, Ch. 43, Stats. 2022).

⁵ SB 101 (Skinner, Ch. 12, Stats. 2023).

State believes that approximately 18,000 corporations and LLCs created during the fee holiday were fraudulently created, and many of those entities were formed using the names/and or addresses of Californians who are not actually associated with the entity. Finding out that one's name or address has been appropriated for a business filing is certainly troubling; the silver lining is that the Secretary of State has not reported any additional adverse consequences for the individuals whose information has been wrongfully used.

Under current law, persons who believe that their name, address, telephone number, or other personal identifying information has been used unlawfully in a business filing, and who have also initiated a law enforcement investigation, may file a petition in the superior court to have the entity show cause as to why the information should not be removed.⁶ An "unlawful" purpose includes using the personal identifying information to obtain credit, goods, or services,⁷ so the mere use of the person's information without consent in order to form a business entity should be sufficient to obtain relief. If the court determines, after a hearing, that the petition is meritorious and there is no reasonable cause to believe that their information was used lawfully in the business entity filing, the court shall make an order to that effect.⁸ Additionally, the court must order that the personal identifying information be redacted from the entity filing or labeled as impersonated, and that the data be removed from publicly assessable electronic indexes and databases.⁹ The order shall be filed with the Secretary of State.

3. This bill adds mechanisms to address the unlawful use of personal identifying information in entity filings

This bill is intended to provide additional avenues to address the misuse of personal identifying information in business entity filings.

First, the bill permits the Secretary of State to cancel a corporation or LLC if the entity has been the subject of an order finding that it unlawfully listed a person's personal identifying information in its filings, if the entity does not, within 60 days the order was filed with the Secretary of State, provide the Secretary of State with updated information to replace the unlawfully included information. Entity cancellation is a harsh consequence – the results can range from crushing personal liability to the termination of agreements the entity needs to survive – but the safeguards surrounding the issuance of these orders make the possibility of a mistaken cancellation low. First, a person seeking such an order must also have initiated a law enforcement investigation,¹⁰ which is likely to weed out baseless claims. Second, the entity is given the opportunity to defend its use of the information, and it should be on notice that

⁶ Civ. Code, §§ 1798.200, 1798.201; Pen. Code, § 530.55.

⁷ Civ. Code, § 1798.201; Pen. Code, § 530.5.

⁸ Civ. Code, § 1798.202.

⁹ *Ibid.*

¹⁰ *Id.*, § 1798.201.

information contained in its filings needs to be updated. Finally, the fact that the Secretary of State may not cancel an entity until 60 days after the entity has been given the opportunity to update the impersonated information means that the entity has a reasonable opportunity, even after the court's order, to update its filing with legitimate information. These safeguards appear to make it unlikely that legitimate entities – which were already found to include impersonated information in their filings – will be canceled.

Second, this bill creates a “disclaimer of proper authority” that a person may file with the Secretary of State if their information is unlawfully included in an entity filing, which will be placed in the entity's records with the Secretary of State. A disclaimer of proper authority must include the name of the corporation, LLC, or LP; the entity type; the date the document containing the personal information was filed and the title of the document; a description of the type of personal information that is unlawfully included in the filing; and a statement that the person did not authorize the entity to use their information. The person filing the disclaimer of proper authority must sign the disclaimer under penalty of perjury. The Secretary of State is tasked with establishing the form for the disclaimer, and it must also include a statement that the disclaimer does not constitute a determination by a court or law enforcement regarding the use of the information. The disclaimer of proper authority is intended to provide a less onerous process to address the unlawful use of personal information in an entity filing; while the disclaimer does not, unlike the court procedure, entitle the person to have their information removed from the filing, it does put other parties on notice that the veracity of the entity's information is in question.

SUPPORT

Shirley N. Weber, Ph.D., California Secretary of State (sponsor)

OPPOSITION

None received

RELATED LEGISLATION

Pending Legislation: None known.

Prior Legislation:

SB 446 (Wilk, Ch. 151, Stats. 2023) provided two mechanisms by which a California nonprofit corporation or cooperative corporation may ratify or validate an otherwise-lawful corporate act that was not in compliance with relevant state corporations laws or the corporation's articles or bylaws when it was made.

SB 218 (Jones, Ch. 217, Stats. 2022) provided two ratification mechanisms by which a California general corporation may ratify or validate an otherwise-lawful corporate act that was not in compliance with relevant state corporations laws or the corporation's articles or bylaws when it was made.

SB 1196 (Jackson, Ch. 696, Stats. 2018) established the procedure by which a person who learns or reasonably suspects that their personal identifying information has been used for an unlawful purpose in a business entity filing may obtain a court order redacting the unauthorized information.
