WEST VIRGINIA LEGISLATURE

2017 REGULAR SESSION

Introduced

Senate Bill 270

BY SENATORS MULLINS AND CLINE

[Introduced February 13, 2017; referred

to the Committee on the Judiciary]

A BILL to amend the Code of West Virginia, 1931, as amended, by adding thereto a new article, designated §55-7K-1, §55-7K-2 and §55-7K-3, all relating to standards of proof in civil actions where the corporate, limited liability company or other business structure is alleged to be insufficient to the point it should be disregarded.

Be it enacted by the Legislature of West Virginia:

That the Code of West Virginia, 1931, as amended, be amended by adding thereto a new article, designated §55-7K-1, §55-7K-2 and §55-7K-3, all to read as follows:

ARTICLE 7K. STANDARDS RELATED TO CAUSES OF ACTION WHERE THE CORPORATE, LLC, OR OTHER BUSINESS STRUCTURE IS SOUGHT TO BE DISREGARDED.

§55-7K-1. Legislative findings and declaration of purpose.

(a) Whereas, the West Virginia Legislature recognizes the importance of family businesses in growing the economy, creating jobs and generating tax revenue and,

(b) Whereas, individual family member protection against business liabilities is recognized to be socially desirable by encouraging creation of family businesses but the current law providing protection to the owners of family businesses is unduly complex and exposes the owners to excessive and unfair liabilities, of which they are generally not aware.

(c) It is public policy of the state of West Virginia to maximize the protections provided to current and former owners, managers, directors, officers, and other representatives of family businesses. Resolution of all questions of law and fact and all matters relating thereto shall favor strong support for this public policy.

§55-7K-2. Burden of proof; applicable standards.

(a) All factual and legal issues required to create personal liability for business debts or liabilities shall be established by clear and convincing evidence.

(b) The following standards shall be utilized as the sole and exclusive basis for assessing a business liability or debt against an individual:

(1) There shall be a strong presumption that current and former owners, managers, members of the board of directors, officers, or other representatives are not liable for the debts or liabilities of the family business.

(2) To be liable for the debts or liabilities of the business, plaintiffs must establish personal responsibility on the defendant, by clear and convincing evidence, that:

(A) The business failed to hold itself out as operating as a business or type of business entity. A business of any kind shall be deemed to be holding itself out as operating as a business entity if it generally uses within its name, on its letterhead or in other publicly available information, abbreviations such as Inc., LLC., LP., or other words or information indicating it operates as a legal entity, or it generally operates in a manner that an individual would reasonably assume that it is a business entity and not an individual, and

(B) The defendant was actively participating in day-to-day operation of the business and, in cases involving a contract or other transaction, the defendant expressly represented to the plaintiff that the defendant was acting personally as an individual and not as a representative of the business, and

(C) The business itself is not "financially sound" as defined herein.

§55-7K-3 Definitions.

For purposes of this article,

(a) "Family Business" is defined as a business organization however structured (including, but not limited to corporations, limited liability companies, limited partnerships, and including subsidiaries of such business, etc.,) which is not publicly traded on any stock exchange and which is owned (directly or through use of another entity such as parent – subsidiary business, a family trust, etc.) by members of not more than 5 families. A family includes those individuals commonly recognized as family members including a sole individual, an individual parent or grandparent, their lineal descendants, and the parent or grandparent's siblings and the siblings' lineal descendants, including stepchildren, adopted children, and spouses of all such family members.

(b) "Financially Sound" means that, given the totality of circumstances, the business had adequate capital to meet ordinary business needs, notwithstanding that the business does not maintain capital to pay for a potential judgment or liability incurred by the business. A business that meets at least one of the following safe harbor requirements shall be deemed financially sound, and adequately capitalized:

(1) The business has existed and has operated, no matter how structured or in what forms, for at least twenty years and it has never sought protection from creditors through bankruptcy proceedings.

(2) The owner has been an officer, director, manager, or owned an interest in one or more businesses totaling at least twenty years, none of which have sought bankruptcy protection during the owner's association with the business.

(3) If the business has audited financial statements for the business's most recent fiscal year immediately preceding the date during the alleged liability occurred, those statements do not contain a "going concern" qualification.

(4) The business has outside third-party verification that it is financially sound. Examples would include, but not be limited to, that a financial institution has made a loan to the business (or extended in-line of credit, whether or not used) during the time period when the alleged liability was incurred and the business was not in default of the loan.

(5) At the time the incident giving rise to the alleged liability occurred, the business entity financial condition would be deemed creditworthy and/or adequately capitalized, which may be established by showing that its capitalization was reasonably comparable to other businesses in the same or a similar line of business using average industry-wide ratios (current ratio, acid-test ratio, debt/equity ratio, etc.) obtained from sources such as Dunn & Bradstreet, Moody's *Manual of Investments*, Standard and Poor's *Corporation Records*, financial institutions, certified public accountants, etc.

(6) The business carried insurance that would be typical of this type and size of business, notwithstanding that the insurance does not cover the type or amount of liability alleged.

(7) The business is required by a government agency to meet financial standards to receive legal authority, a license or other approval to legally operate, or to participate in a government-sponsored program.

NOTE: The purpose of this bill is to revise existing standards and establish the burden of proof imposed on civil litigants seeking to circumvent corporate structure in civil litigation.

Strike-throughs indicate language that would be stricken from a heading or the present law and underscoring indicates new language that would be added.