CHAPTER 10

CORPORATION LAW

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I. INTRODUCTION

Corporate law is primarily statutory, both federal and state, and these statutes may be grouped into four general categories: (1) state general corporation acts; (2) state non-profit corporation acts; (3) state general statutes which affect various aspects of corporate life; and (4) federal corporation law.

Thus, in addition to being knowledgeable about the first two categories (*i.e.*, general corporation laws of West Virginia, both business and nonprofit), the West Virginia practitioner must, at the least, be aware of the existence of other West Virginia and federal statutes. West Virginia statutes regulate a myriad of subjects that affect the daily operations of the West Virginia corporation, including, for example, the sale of securities,[1] taxation,[2] commercial transactions,[3] public utilities,[4] motor carriers,[5] labor relations,[6] workers' compensation,[7] unemployment compensation,[8] banking,[9] environmental regulation[10] and others.[11] In addition, federal statutes frequently provide overlapping or independent regulations or requirements, especially in such areas as taxation,[12] securities regulation,[13] labor relations,[14] corporate bankruptcy liquidations and reorganizations[15] and antitrust regulations.[16]

It is beyond the scope of this chapter to cover all aspects of the corporate practice. Instead, this chapter will cover those basic areas of West Virginia corporation law most frequently encountered by the West Virginia corporate practitioner in dealing with business corporations. These areas include the considerations involved in deciding whether to incorporate; the formation, operation, dissolution and merger of corporations;

and transacting with foreign corporations. This chapter will not deal with nonprofit corporations.

In 2002, the West Virginia Legislature repealed the former West Virginia Corporation Act (W. Va. Code §§ 31-1-1 to -160), which was an amalgam of the Model Business Corporation Act and the Model Nonprofit Corporation Act. The current West Virginia Business Corporation Act was passed by the 2002 West Virginia Legislature 2nd Special Session and took effect October 1, 2002.[17]

The current West Virginia Business Corporation Act ("Act") (W. Va. Code §§ 31D-1-101 to 31D-17-1703) is based on the Revised Model Business Corporation Act. Unlike the former act, the current Act deals only with business corporations. An entirely new act, the West Virginia Nonprofit Corporation Act, was passed in 2002 and became effective on October 1, 2002, to address the law with regard to nonprofit corporations. (W. Va. Code §§ 31E-1-101 to 31E-16-1603). This act is similar to the West Virginia Business Corporation Act in many regards, but establishes a separate body of law dealing specifically with nonprofit corporations.

The formation, internal operation, organization, merger and dissolution of a corporation are closely regulated by the Act. The Act has 16 sections: Section 1 addresses General Provisions; Section 2 addresses Incorporation; Section 3 addresses Purposes and Powers; Section 4 addresses Name; Section 5 addresses Office and Agent; Section 6 addresses Shares and Distributions; Section 7 addresses Shareholders; Section 8 addresses Directors and Officers; Section 10 addresses Amendment of Articles of Incorporation and Bylaws; Section 11 addresses Mergers and Share Exchanges; Section

12 addresses Disposition of Assets; Section 13 addresses Appraisal Rights; Section 14 addresses Dissolution; Section 15 addresses Foreign Corporations; Section 16 addresses Records and Reports; and Section 17 addresses Transition Provisions.[18] The Secretary of State has prepared a set of corporate forms. These forms are available from the office of the Secretary of State.

Although this chapter provides ready access to applicable West Virginia Code provisions concerning the subjects discussed, amendments will continue to be made to the Act, and the practitioner should check the West Virginia Code for recent legislative amendments.

II. THE INCORPORATION PROCESS

A. Initial Considerations

The first decision to be made is whether a corporation is the best form of business organization to accomplish the purposes of any given client. The conscientious attorney should explore alternative forms of business organization with his client without assuming that incorporation will necessarily best meet the particular needs of the client. Although there are many forms of business organizations, six basic forms of business organization ordinarily should be considered: sole proprietorship, general partnership, limited liability partnership, limited partnership, limited liability company and corporation.

B. Basic Non-Tax Considerations

The non-tax considerations in choosing among alternative forms of business organization are numerous and varied. Those most often cited are:

1. Limitation of Liability. The corporate form, under most circumstances, limits the liability of the shareholders. Similarly, the limited liability company form,[19] under most circumstances, limits the liability of the members and manager.[20] A limited partnership generally limits the liability of its limited partners,[21] but not its general partners. A general partnership[22] and sole proprietorship do not limit liability.

A limited liability partnership is a form of general partnership which, in very general terms, limits a general partner's liability for the malpractice of his other general partners. Otherwise, as in all general partnerships, each partner is generally jointly and severally liable for partnership obligations.[23] If a limited liability partnership meets the applicable requirements of West Virginia law, a partner is not responsible for debts, obligations and liabilities of the partnership, whether in tort, contract or otherwise, arising from omissions, negligence, wrongful acts, misconduct or malpractice committed while the partnership is a limited liability partnership and in the course of partnership business by another partner or by an employee, agent or representative of the partnership. Of course, such a partner is still responsible for his own omissions, negligence, wrongful acts, misconduct or malpractice, or that of any person under the partner's direct supervision and control. A further discussion of limited liability partnerships is beyond the scope of this section.

The theoretical advantage, however, of limiting the shareholders' or members' liability for debts of the corporation, or limited liability company, as the case may be, is in practice often diminished in the case of a closely held corporation (or

limited liability company) by the requirement of many lenders that major shareholders (or members) become co-obligors with the corporation or guarantors of the corporation's debt; moreover, the potential tort liability present in the noncorporate forms may be reduced by insurance.

2. Continuity of Existence. A corporation has continuity of existence.[24] Sole proprietorships do not have continuity of existence. Similarly, neither general nor limited partnerships will have continuity of existence.[25] Depending on the facts and circumstances, a limited liability company may or may not have continuity of existence.[26] While general and limited partnerships and limited liability companies may provide for continuity of existence by agreement, those provisions may have negative consequences and should be entered into only after careful analysis of these issues.

3. Centralization of Management. Corporations, limited partnerships and sole proprietorships generally have centralized management, while general partnerships generally do not. Limited liability companies may or may not have centralized management, depending on whether they are manager-managed or member-managed.

4. Transferability of Ownership. Generally, transferring ownership of shares of corporate stock is easier and more flexible than transferring all of the assets of a going business or transferring interests in partnerships or limited liability companies.

5. Flexibility of Financing. Corporations have greater flexibility in the methods of financing available to them (*i.e.*, various forms of equity securities) than the other business forms, and internal financing of capital growth is more readily

accomplished by a corporation. Limited liability companies and partnerships may also offer flexibility in financing.

6. Operating Costs. Corporations, generally, have higher operating costs as a result of added record keeping and compliance with corporation laws than sole proprietorships, limited liability companies, or partnerships.

7. Regulation of Internal Activities. Corporations are more closely regulated than the other business forms (*e.g.*, statutory regulation of formation, merger, dissolution, consolidation, etc.), but limited partnerships and limited liability companies approach this degree of regulation.

C. Basic Tax Considerations

For federal income tax purposes, a corporation is generally considered an independent taxpaying entity. Generally, corporations are subject to graduated tax rates ranging from 15 percent on the first $50,000 of taxable income to 35 percent on taxable income exceeding $10 million.[27] More specifically, the first $50,000 is taxed at a rate of 15 percent, the next $25,000 at 25 percent, the excess over $75,000 up to $10 million at 34 percent and any remaining income is then taxed at a 35 percent rate.[28] The maximum marginal corporate tax rate for corporate taxable income between $100,000 and $335,000 is effectively higher than 34 percent as a result of a 5 percent surtax in this range to eliminate the benefits of the 15 percent and 25 percent graduated rates. Similarly, a 3 percent surtax on corporate taxable income between $15,000,000 and $18,333,333 raises the effective marginal tax rate on income in this range and eliminates the benefit of the 34 percent rate.[29] In addition to the corporate tax just discussed, corporations may be subject to the "alternative minimum tax."[30] Unlike individuals, corporations receive no preferential rate for net capital gains.

An individual conducting his business as a sole proprietor is taxed on his proprietorship income at the individual income tax rates ranging from 0 percent to 38.6 percent of taxable income.[31] Similar to the discussion above with respect to corporations, an individual's marginal tax rates may be affected by (1) the phase out of the benefit of the personal exemption,[32] (2) the limits on itemized deductions,[33] and (3) the two percent floor on itemized deductions.[34]

For individual net capital gains, the maximum rate is 15 percent for 2011 and 2012, and is scheduled to be 20 percent in 2013.[35] The deduction for capital losses is limited to capital gains, plus $3,000 per year of ordinary income.[36]

Generally speaking, unlike a corporation, a general or limited partnership is not a taxpaying entity for federal income tax purposes. Instead, the federal income tax law imposes the tax upon the individual partners, as distinguished from the partnership.[37] In this sense, the partnership is a mere conduit through which the income and deductions flow to the individual partners. Thus, the partnership may, in some circumstances, provide a significant tax advantage over the corporation. Corporate income is generally subject to two levels of tax, whereas, as a conduit, a partnership is generally subject to only one level of tax. If certain statutory requirements are met, however, a corporation may elect to be treated as an "S corporation," in which case its earnings are taxed directly to the shareholders, and not to the corporation.[38] In effect, an S corporation, like a partnership, is generally viewed as a conduit not subject to tax.[39]

The rates at which business income is taxed vary considerably depending on the form of business organization and the amount of taxable income. In some cases, the individual income tax rate may be less, and in other cases the corporate tax rate may be less. Moreover, if the business is conducted as a proprietorship, the proprietor, after paying the taxes on the income from the proprietorship, has full access to the after-tax earnings. In a corporation, unless the earnings are distributed as a dividend, the after-tax corporate earnings remain in the corporation.

If a corporation distributes its after-tax earnings to an individual shareholder as a dividend, the dividend is normally taxed to the shareholder as ordinary income, subject to a maximum tax rate of 38.6 percent, and is not deductible by the corporation, resulting in a double taxation of earnings (once to the corporation and once to the shareholder).[40] Reasonable salaries, wages, and certain fringe benefits paid to shareholder employees, however, are deductible by the corporation and, in the case of salaries and wages, constitute ordinary income to the recipients subject to the maximum tax rates set forth above.

There is a general tendency by closely held corporations to accumulate earnings instead of paying dividends. This is permissible, but if earnings are accumulated beyond the reasonably anticipated needs of the business, the excess accumulations may be subject to a severe penalty tax.[41]

Unlike a shareholder in a corporation, a partner in a partnership (or, generally speaking, a member in a limited liability company) will be taxed on its share of partnership (or limited liability company) income, irrespective of whether it is distributed to the partners or members.[42]

At one time, many small businesses and professional individuals incorporated because of the more liberal rules regarding corporate contributions and deductions to qualified retirement plans. Although slight differences in the tax laws continue to exist between qualified self-employed plans and corporate plans, these differences are so minor that qualified retirement plans are no longer a motivating factor in choosing between the corporate and non-corporate forms of doing business.[43]

For purposes of West Virginia personal income taxation, individuals are taxed at rates ranging from 3 percent to 6.5 percent on federal adjusted gross income, with no deductions other than a $2,000 personal exemption, and limited exclusions for certain retirement benefits and disability payments.[44] Corporations are subject to state corporate net income tax at an 8 ½ percent rate[45] and to business franchise tax equal to 0.34 percent of capital.[46] The Corporate net income tax rate is scheduled to reduce to 6½ percent by 2015 and the business franchise tax is set to disappear by 2014.

Therefore, in considering whether to incorporate, the tax advantages and disadvantages are among the most significant factors affecting the decision.

D. Pre-Incorporation Documents

Although in practice the first step in the incorporation process will usually be the preparation and filing of the articles of incorporation, some mention should be made of pre-incorporation agreements and stock subscriptions. These documents are used most often when a new corporation is to be created through the efforts of promoters or when a relatively large number of parties will ultimately own the shares of the corporation. An agreement to incorporate can be used to fix the relative rights and duties of incorporators and promoters, the purposes of the corporation, and the number and issuance of shares. A pre-incorporation stock subscription is ordinarily used to insure: (1) the availability of sufficient capital to begin the contemplated corporate operations; and (2) the right of incorporators and other interested parties to purchase shares in the corporation. A subscription constitutes a binding agreement to purchase shares of the corporation, and it can be called by the corporation's directors after formation. It is irrevocable for a period of 6 months unless the subscription agreement provides otherwise or unless all of the subscribers agree to its revocation.[47] The corporation may either take legal action to collect the subscription or rescind the agreement and sell shares if the debt remains unpaid for over 20 days after written demand for payment.[48] A subscription agreement can constitute a "security" under securities laws.

E. Securities Law Implications

When forming corporations, limited partnerships and limited liability companies, the West Virginia practitioner should consider the implications of federal and state securities laws. Under Section 2 of the Securities Act of 1933, as amended,[49] and W. Va. Code § 32-3-301, every offer and sale of a security must be registered unless the offer and sale are exempt from registration. Failure to register when required to do so can be expensive and time consuming. Both federal and state law imposes civil and criminal liability on any person who unlawfully offers or sells an unregistered security.

Not every sale of a security falls within the registration requirements of state and federal securities laws, and there are a number of "exempt securities" and "exempt transactions" provided under W. Va. Code § 32-4-402(a) and (b), and Sections 3 and 4 under the Securities Act of 1933.[50] The most useful federal exemption is the "private offering exemption" under Section 4(2) of the Securities Act of 1933.[51] West Virginia has a very limited statutory exemption for private offerings. West Virginia Code § 32-4-402(b)(9) exempts offers to up to ten persons within a twelve-month period. Under this exemption, an investor must purchase the security for investment purposes only, and no one may receive a commission in connection with the sale of the security. The practitioner should review the precise wording of that exemption carefully before relying on it.

In addition to the statutory private placement exemption of W. Va. Code § 32-4-402(b)(9), the Securities Act of 1933 prevents state registration and review of specified securities and offerings. Generally, states may not require a company to

register if that company's securities are listed on the New York Stock Exchange, the American Stock Exchange or the Nasdaq National Market System. Also preempted are company offerings of most exempt securities found in Section 3 of the Securities Act of 1933. Although preempted from state registration, federal law permits states to require companies to file notices with respect to these offerings. West Virginia requires the filing of such notices.

Many offerings are not preempted and remain subject to state regulation. These offerings include: (1) securities quoted on the Nasdaq Small Cap Market; (2) securities listed on regional exchanges; (3) securities issued in Section 4(2) private placements that do not meet the safe harbor requirement of Rule 506 of Regulation D[52] of the Securities Act of 1933; (4) securities issued in Rule 504 and Rule 505[53] offerings under Regulation D; and (5) securities issued in offerings under Regulation A of the Securities Act of 1933.

Practitioners should keep in mind that both federal and state securities fraud provisions apply to all offers and sales of securities, whether or not the offer and sale are exempt from registration.

The Securities Commission of the West Virginia State Auditor's Office administers West Virginia's securities laws. The address for the Securities Commission is Building One, Room W-110, Charleston, West Virginia 25305. The Securities Commission's web site is located at http://www.wvsao.gov/securitiescommission.

F. Articles of Incorporation

The articles of incorporation must set forth: (1) the corporate name; (2) authorized shares and par value of the shares; (3) the street address of the initial registered office, if any, and initial registered agent, if any, at that office; (4) the name and address of each incorporator; (5) the purpose for which the corporation is organized; (6) the mailing address of the corporation's principal office; and (7) an email address where notices and annual filing reminders may be sent.[54] In addition, the articles may set forth: (1) the names and addresses of the initial directors; (2) provisions not inconsistent with the law regarding (a) managing the business and regulating the affairs of the corporation, (b) defining, limiting and regulating the powers of the corporation, its directors and shareholders, or (c) imposition of personal liability on shareholders for the debts of the corporation to a specified extent and upon specified conditions; (3) any provision that is required or permitted to be set forth in the bylaws; (4) a provision eliminating or limiting the personal liability of a director to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director; and (5) a provision permitting or making obligatory indemnification of a director for liability to any person for any action taken, or any failure to take any action, as a director.[55] Sample articles of incorporation ("articles") which conform to the form prescribed by the Secretary of State are contained in the Appendix. Although this form seems self-explanatory, the practitioner should be aware of the following considerations affecting the use of the form.

1. Name. The name of a corporation must contain the word "corporation," "company," "incorporated" or "limited," or the abbreviation "corp.",

“inc.”, “co.” or “ltd.” or words or abbreviations of like import in another language.[56] The name must be distinguishable upon the records of the Secretary of State from the name of any domestic corporation or any foreign corporation authorized to do business in West Virginia or the name of any other entity on record with the Secretary of State.[57] The availability of a name can be determined through the Secretary of State’s office, and an available name can be reserved for a nonrenewable 120 days by submitting an application to the Secretary of State.[58]

2. Purposes and Powers. Every corporation formed under the Act has the purpose of engaging in any lawful business unless a more limited purpose is set forth in the articles of incorporation.[59] The articles are no longer required to enumerate the purposes and powers of a corporation.[60] Historically, the purpose clause of a corporate charter was characterized by a lengthy recitation of corporate purposes and powers, but now the purpose for which a corporation is organized may be simply stated to be “the transaction of any or all lawful business for which corporations may be incorporated.”[61] This will be sufficient for most purposes, and, indeed, specification of purposes and powers in the articles may serve to restrict, rather than broaden, the corporation’s purposes. If for some reason the incorporators desire to limit the purposes of a corporation, they may do so by specifying those purposes and deleting the broad general purpose clause.[62] The Act gives all corporations broad powers,[63] and, consequently, enumeration of powers in the articles serves little or no purpose.

3. Authorized Capital Stock. There is no minimum amount of capital stock that corporations must be authorized to issue; and, contrary to earlier corporate law,

there is no requirement that the corporation commence business with any specific minimum amount of capital paid into the corporate treasury. However, a corporation with little or no capital may be more susceptible to having its corporate veil pierced. A way to increase the capital without a proportionate increase in the corporate license tax is to pay an amount into the corporation exceeding the par value of the capital stock issued and treat it as capital surplus.[64]Shares of stock may be authorized or issued with or without par value.[65] Authorized capital stock may be divided into one or more classes of shares. A single corporation, for example, may issue common stock, nonvoting common stock and preferred stock, provided that the articles authorize one or more classes of shares that together have unlimited voting rights and one or more classes of shares that together are entitled to receive the net assets of the corporation upon dissolution.[66] The articles may authorize the board of directors to determine, in whole or in part, the preferences, limitations and relative rights of any series or class of shares before the issuance of any shares of that class.[67] However, each series of a class must be given a distinguishing designation, and before issuing any shares of a class or series, the corporation must deliver to the Secretary of State for filing articles of amendment, which are effective without shareholder action, and which set forth the relative rights preferences, and limitations of such shares.[68] Issuing different types of equity securities is often an efficient way to accommodate the varying financial contributions, goals, and participations among shareholders.

In determining the amount of authorized capital for a new corporation the practitioner should consider that in a closely held corporation there must be a sufficient

amount of equity capital, relative to the debt, issued by the corporation to prevent the debt owed to shareholders from being treated as equity for tax purposes.

4. Preemptive Rights. Unless specifically authorized in the articles, shareholders have no preemptive rights to acquire unissued or treasury shares of a corporation.[69] Accordingly, if shareholders are to have preemptive rights, the articles must specifically provide for them. In addition, there are no preemptive rights for certain types of issuances, including shares issued as compensation to directors, offices, agents, etc., stock options, shares issued within six months of the date of incorporation and shares sold otherwise than for money.[70] If shareholders do have preemptive rights and do not exercise them, the shares may be sold without regard to preemptive rights for a period of up to one year after being offered to the shareholder at a consideration not lower than the consideration set by the board of directors.[71]

5. Incorporators. One or more persons may act as the incorporator or incorporators by delivering articles of incorporation to the Secretary of State, and the incorporator may be a natural person or a domestic or foreign corporation.[72] Generally, it is easier to use only one incorporator in most simple incorporations.

6. Registered Office and Registered Agent. Each corporation may continuously maintain in West Virginia a registered office and registered agent.[73] The registered office may be the same as any of the corporation's places of business.[74] A corporation's registered agent is the corporation's agent for service of process, notice or demand required or permitted by law to be served on the corporation.[75] A registered agent may be (1) an individual who resides in West Virginia and whose business office is

identical with the registered office, (2) a domestic corporation or domestic nonprofit corporation whose business office is identical with the registered office, or (3) a foreign corporation or foreign nonprofit corporation authorized to transact business in West Virginia whose business office is identical with the registered office.[76] If the corporation has no registered agent, the corporation may be served by registered certified mail, return receipt requested, addressed to the secretary of the corporation at its principal office.[77] In addition to the above, the Secretary of State is considered the attorney-in-fact for each corporation.[78] Appointment and designation of a person may be beneficial to insure that notices and processes are transmitted timely to the proper person (*e.g.*, president, corporate counsel, etc.). A small, closely-held corporation, however, may have no need to appoint and designate a person to receive process. A consideration in the decision of whether to appoint a person to receive service of process is the requirement that the Secretary of State be notified each time a change in the designated person or his or her address occurs.[79]

7. Provisions for Internal Regulation of Corporate Affairs. The Act provides that the articles may contain "provisions not inconsistent with law."[80] Various sections in the Act make it necessary to consider several internal regulation provisions for inclusion in the articles, since failure to include certain provisions for internal regulation may result in unintended freedom or restriction of corporate management.

The Act gives both the shareholders and the board of directors the power to alter, amend, or repeal the bylaws or to adopt new bylaws, unless reserved to the shareholders in the articles.[81] Also under the Act, a majority of shares entitled to vote

constitutes a quorum at a meeting of shareholders, unless the quorum requirement is altered by a provision in the articles.[82] To constitute the act of the shareholders, the affirmative vote of the holders of a majority of the shares represented at a meeting at which a quorum is present is required, unless the vote of a greater number or voting by classes is required by law or the articles.[83]

An example of another provision regulating the internal affairs of a corporation which might be inserted in the articles is a provision *requiring* corporate indemnity of corporate officers, directors and employees against expenses, judgments, fines, etc., incurred while acting on behalf of the corporation.[84] The articles may also include a provision limiting or eliminating the liability of a director to the corporation or its stockholders.[85]

8. Initial Board of Directors. The Act does not require inclusion of the initial board and their names and addresses in the articles.[86] Because of organizational requirements discussed below, the safer practice is to name the board in the articles. There is no minimum number of directors required by the act; therefore, a single director is permissible.[87] If there are nine or more directors, the articles of incorporation may provide for staggered terms.[88]

9. Filing and Recording Articles. The articles must be filed with the Secretary of State.[89] The articles must be typewritten in English and signed by the incorporator.[90] The articles may, but do not have to be, acknowledged.[91] The Secretary of State may accept several methods for filing articles including electronic transmission and has become extremely user friendly in assisting practitioners with filing documents.[92]

The Secretary of State will issue a certificate of incorporation upon filing of the articles. This certificate does not have to be recorded in the office of the clerk of the county commission in which the corporation's principal office is located as was the case under prior law. Any person who knowingly signs a false document is guilty of a misdemeanor and shall be fined for not more than one thousand dollars or confined not more than one year, or both.[93]

G. Organizational Meeting and Adoption of Bylaws

A sample set of organizational minutes and an annotated set of sample bylaws are contained in the Appendix. These are general in form and are not intended to cover all contingencies. Below is an explanation of the key provisions in the organizational minutes.

1. Call of Organizational Meeting. If the initial board of directors is named in the articles, the initial directors shall hold an organizational meeting, at the call of a majority of the directors, to complete the organization of the corporation by appointing officers, adopting bylaws, and carrying on any other business brought before the meeting.[94] If the initial directors are not named in the articles, the incorporators shall hold an organizational meeting at the call of a majority of the incorporators to elect directors and complete the organization of the corporation or to elect a board of directors who shall complete the organization of the corporation.[95] There is no statutory time limit within which the organizational meeting must be held following incorporation.

2. Notice. The incorporators or board members calling the meeting are required to give notice by mail or electronic transmission, but such notice may be, and

usually is, waived by unanimous consent of the incorporators or directors named in the articles.[96] The organizational meeting may be taken without a meeting if unanimously signed by each incorporator or initial board member.[97]

3. Adoption Of Bylaws. The initial bylaws of a corporation are adopted by the incorporators or the initial board of directors.[98] A corporation's shareholders and board of directors both have the power to alter, amend or repeal the bylaws or adopt new bylaws, unless such power is specifically reserved to the shareholders by the articles or by statute.[99] Although bylaws ordinarily contain certain basic provisions, there is great latitude to tailor bylaws to fit the specific needs of any given corporation. The Act provides that the "bylaws may contain any provision for managing and regulating the affairs of the corporation that is not inconsistent with law or the articles of incorporation."[100] Indeed, numerous provisions scattered throughout the Act which specify procedures for certain corporate acts expressly permit variations in procedure to be specified in the articles or bylaws.[101] For example, the shareholders may enter into an agreement to eliminate the board of directors, but such agreement must be set forth in the articles or bylaws.[102]

4. Issuance Of Stock. Issuance of the corporation's capital stock is authorized by the board unless reserved to the shareholders in the articles of incorporation.[103] Customarily, although not mandatory, the issuance of part or all of the corporation's authorized shares of stock is authorized at the organizational meeting. At that time preincorporation subscriptions may be called and new offers to purchase stock considered. Shares are issued for the consideration, expressed in dollars, fixed from time

to time by the board.[104] Before the corporation issues shares, the board of directors must determine that the consideration received or to be received for the shares is adequate.[105] Consideration for shares may be paid in cash, in other property, or in labor or services actually performed for the corporation, and, in the absence of fraud, the judgment of the board or the shareholders as to the value of consideration received for shares is conclusive.[106] Unlike the former Act, under the current Act, promissory notes and future services constitute payment or partial payment for shares.[107]

As a general rule, the formation of a corporation and the issuance of stock is not a taxable transaction provided certain technical requirements are met.[108] The corporation's minutes of its organizational meeting should probably reflect that its stock is intended to qualify under Internal Revenue Code § 1244, if the following requirements of § 1244(c) are met: (1) the corporation's capitalization does not exceed one million dollars; (2) the stock was issued for money or other property, excluding stock and securities; and (3) the corporation derived over fifty percent of its gross income for the prior five years from non-passive investments (*e.g.*, rents, royalties, dividends, interest, annuities, and sales of stocks or securities).[109] Section 1244 allows a shareholder to recognize an ordinary loss rather than a capital loss if the stock becomes worthless, up to $100,000 per year for married taxpayers filing a joint return and $50,000 for shareholders filing single returns. Section 1244 is automatic, and the corporation need not affirmatively elect treatment thereunder.

Certificates for shares may be issued but are not required.[110] Unless otherwise provided in the Code, the rights and obligations of shareholders are identical

whether or not their shares are represented by certificates.[111] If a corporation issues uncertificated shares, an information statement must be sent to the security holder containing the information required to be set forth on the certificate pursuant to W. Va. Code § 31D-6-625.[112]

The articles of incorporation, bylaws or an agreement among shareholders may impose restrictions on the transfer or registration of transfer of shares of the corporation.[113] Such a restriction is authorized if it is (1) to maintain the corporation's status when it is dependent on the number or identity of its shareholders, (2) to preserve exemptions under federal or state securities laws, or (3) for any other reasonable purpose.[114] Such a restriction may (1) obligate the shareholder first to offer the corporation or other persons an opportunity to acquire the restricted shares, (2) obligate the corporation or other persons to acquire the restricted shares, (3) require the corporation, the shareholders or another person to approve the transfer of restricted shares, if the requirement is not manifestly unreasonable, or (4) prohibit the transfer of restricted shares to designated persons or classes of persons, if the prohibition is not manifestly unreasonable.[115] If there is a restriction, it must be noted on the certificate or in the information statement sent to the holders of uncertificated shares.[116]

Corporations may issue fractional shares, arrange for the disposition of fractional shares, or issue scrip which is tradable and which may be exchanged for full shares.[117]

III. AFTER ORGANIZATION

After organization, a new corporation must comply with certain filing requirements. It must obtain a business registration certificate for each location where it maintains a place of business,[118] and it must obtain a federal employer identification number. If the corporation is to have employees, it must obtain workers' compensation and unemployment compensation coverage. Additionally, any applicable licensing statutes must be checked for compliance. State tax forms and information about state taxes are routinely sent by the state tax department to the principal office of the corporation after articles of organization are filed. After organization, a corporation or partnership, generally speaking, may amortize organizational expenses under Internal Revenue Code § 248[119] and § 709(b).[120]

In a small, closely-held corporation, meetings of directors and shareholders are ordinarily held on an informal basis. Additionally, the shareholders may by agreement eliminate the board of directors or restrict the discretion or powers of the board.[121] Meetings of directors and shareholders of a larger corporation are regularly scheduled with all requisite formalities. All corporations, however, are required to hold an annual meeting of shareholders.[122]

Under the Act, unless the articles or bylaws provide otherwise, directors and shareholders may participate in meetings by means of a conference telephone or similar electronic communication if all persons participating in the meeting can hear each other.[123] Compliance with the requirements of corporate operation is also made easier by statutory authorization for signed agreements in lieu of meetings of both directors and shareholders.[124] The Act provides that, whenever a vote of shareholders or directors is

required or permitted in connection with any corporate action, the meeting and vote of shareholders or directors may be dispensed with if all those persons who were entitled to vote upon the action agree in writing to the action.[125] Thus, if an informal decision is made among directors or shareholders that has the same effect and validity as a unanimous vote at a meeting actually held, it can be easily formalized by a unanimous agreement in lieu of meeting.

Although some level of informality frequently attaches to the meetings of closely-held corporations, the importance of preparing minutes of meetings or agreements in lieu thereof cannot be overemphasized, as it is one of the ways to help protect against piercing the corporate veil.

IV. BOARD OF DIRECTORS

A. Composition of the Board

The board must have one or more members, and the number is fixed by the articles or by the bylaws.[126] The articles or bylaws may provide for a range of the size of the board of directors rather than specifying a number.[127] As discussed previously, the initial board of directors can be named in the articles, and, because this may be done before the full board is known, very often the initial board is simply one or more of the incorporators. The first board serves until the next annual meeting of the shareholders[128] or until its successors have been elected and qualified.[129] Directors need not be residents of West Virginia or shareholders of the corporation unless required by the articles or bylaws.[130] Directors are elected annually unless the articles permit staggered terms of directors, in which case only those directors whose terms expire are elected annually.[131]

Shareholders have the right to vote cumulatively for directors if (1) the meeting notice or proxy statement states conspicuously that cumulative voting is authorized, or (2) a shareholder gives notice to the corporation at least forty-eight hours prior to the meeting of an intent to cumulate votes.[132] A vacancy in the board (whether from removal, retirement or an increase in the number of directors) can be filled by a vote of a majority of either the shareholders or the remaining directors, unless the articles provide otherwise.[133]

B. Board of Directors' Meetings

Meetings of the board may be held in or out of West Virginia, with regular meetings held either with or without notice as determined in the bylaws.[134] Special meetings must be preceded by at least two days notice unless the articles or bylaws provide for a longer or shorter period.[135] Board members may participate in meetings by telephone or any means of communication by which all directors participating may simultaneously hear each other during the meeting.[136] Attendance of a director constitutes a waiver of notice of the meeting, unless the director attends for the purpose of objecting to the manner in which a meeting was called.[137] A majority of the board constitutes a quorum unless the articles or the bylaws provide for a larger number, and a vote of the majority of the directors present at a meeting (at which there is a quorum) constitutes action by the board, unless a greater or lesser number is required by the articles or the bylaws.[138]

C. Powers and Duties of Directors

The business and affairs of a corporation are managed by the board. If the articles or bylaws provide, the board may designate committees of the board to exercise the authority of the board, subject to certain express limitations spelled out in the Act.[139] The board has numerous other powers, including the power to declare dividends;[140] lend money to, or use the corporation's credit to assist employees for the benefit of the corporation; and elect and remove officers.

D. Standards of Conduct and Liabilities of Directors

Each board member is subject to the standard of conduct set forth in the Act which requires the directors, when discharging the duties of a director, to act: (1) in good faith; and (2) in a manner the director reasonably believes to be in the best interest of the corporation.[141] Directors are required to have the knowledge a reasonable person would deem necessary in their decision-making process, but directors are entitled to rely on the knowledge of officers, employees, professional advisors and committees of the board in determining whether the director has obtained sufficient information in the decision-making process.[142]

Generally, directors are liable to the corporation for decisions if (1) the action was not in good faith, (2) the action was not in the best interests of the corporation (in the eyes of a reasonable director), (3) the director was not informed to the extent reasonably believed appropriate, (4) there was a lack of objectivity due to conflicts of interest, or (5) the director voted for an unlawful distribution.[143] The Act contains statutes of limitation of two years or one year, depending upon which subsection of the Act is violated.[144]

A director present at a meeting of the board is deemed to have assented to the action taken at the meeting, unless (1) he or she objects at the beginning of the meeting or promptly upon his or her arrival to holding the meeting or transacting business at it, (2) his or her dissent or abstention from the action taken is entered in the minutes of the meeting, or (3) he or she delivers written notice of his or her dissent or abstention to the presiding officer of the meeting before its adjournment or to the corporation immediately after adjournment.[145] The right of dissent is not available to a director who votes in favor of an action.[146]

Note, the articles of incorporation may eliminate or limit the personal liability of a director to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director; provided, that such section may not eliminate or limit the liability of a director (1) for any breach of the director's duty of loyalty, (2) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (3) for wrongful distributions or (4) for any transaction from which the director derived an improper personal benefit.[147]

Finally, Section 31D-8-860 of the Act provides rules for director conflicts of interest and limits liability if the conflict is disclosed to other directors and approved or the transaction is fair to the corporation at the time of authorization, approval or ratification.

E. Indemnification of Directors and Officers

Directors and officers may be provided indemnification by the corporation only as permitted by the Act.[148] The Act requires mandatory indemnification of directors

and officers for reasonable expenses incurred by him or her in connection with any proceeding if any such director or officer is wholly successful, on the merits or otherwise, in the defense of the proceeding to which he or she was a party.[149] The Act provides for permissible indemnification of officers and directors if he or she acted in good faith and he or she reasonably believed such conduct was in, or not opposed to, the best interests of the corporation and, with respect to a criminal proceeding, if he or she had no reasonable cause to believe his or her conduct was unlawful.[150] The articles of incorporation may provide for permissible or mandatory indemnification in other situations provided liability is not being asserted because such director was for (1) receipt of a financial benefit to which he or she was not entitled, (2) intentional infliction of harm, (3) unlawful distributions, or (4) intentional violation of criminal law.[151] The Act empowers circuit courts to order indemnification and advances of expenses.[152] Corporations may purchase insurance against liability incurred by officers and directors in their capacity as such.[153]

A director of a non-profit, volunteer organization, who serves without compensation for personal services, is generally immune from any personal liability for negligence absent a finding of gross negligence.[154]

V. SHAREHOLDERS

A. Shareholder Agreements

Under the current Act, shareholders may unanimously agree to do a number of things not previously allowed, including:

- Eliminating the board of directors or restricting the discretion or powers of the board of directors;
- Governing the authorization or making of distributions;

- Establishing who are to be directors or officers;
- Governing the exercise of voting powers between the shareholders and directors, including weighted voting rights and directors' proxies;
- Establishing the terms and conditions of the transfer or use of property or services between the corporation and any affiliated person;
- Transferring power to manage the business to shareholders or resolving deadlocks;
- Requiring the dissolution of the corporation at the request of one or more shareholders; or
- Governing the exercise of corporate powers or management of the business generally.[155]

A shareholder agreement must be set forth (1) in the articles of incorporation or bylaws and approved by all persons who are shareholders at the time of the agreement or (2) in a written agreement that is signed by all persons who are shareholders at the time of the agreement and is made known to the corporation.[156] A shareholder agreement is valid for ten years unless the agreement provides otherwise.[157] The existence of the agreement must be noted conspicuously on the front or back of each stock certificate.[158] Additionally, any shareholder agreement ceases to be effective once shares of the corporation are listed on an established securities exchange.[159] If such an agreement limits the powers and authorities of the board of directors, such agreement also relieves the directors of liability for such actions.[160] Finally, nothing in a shareholder agreement may be used as grounds for imposing personal liability on the shareholders for the acts or debts of the corporation.[161]

The Act also provides for voting trusts[162] and voting agreements[163] among shareholders.

B. Records and Reports

Generally, a shareholder and his or her agent or attorney[164] has the right to inspect the records of the corporation and photocopy the same upon written notice at least five business days prior to inspection.[165] Additionally, a corporation must furnish its shareholders annual financial statements, including the report of the public accountant, if any, on such statements, unless unanimously waived by the shareholders.[166]

VI. OFFICERS

A corporation has the officers described in its bylaws or appointed by the board of directors in accordance with the bylaws.[167] While there are no statutorily defined officers, the board of directors must delegate to one of the officers responsibility for preparing minutes of the directors' and shareholders' meetings and authenticating records of the corporation.[168] The same individual may simultaneously hold more than one office in the corporation.[169] The bylaws may provide for the appointment of assistant officers and agents.[170] The officers of the corporation have the authority to perform the duties provided in the bylaws, or the authority determined by the board not inconsistent with the bylaws.[171] Consequently, a corporate practitioner has broad discretion to craft the names and duties of the officers of the corporation to meet the needs and concerns of the corporation. Officers may be removed by the board with or without cause at any time.[172]

VII. MERGERS AND OTHER CHANGES IN ORGANIZATIONAL STRUCTURE

A. Mergers and Share Exchanges

Frequently, a corporate practitioner will be called upon to merge corporations. A merger may be accomplished either through a statutory merger or a share exchange. A merger is defined as a business combination pursuant to W. Va. Code §31D-11-1102, and a share exchange is a business combination pursuant to W. Va. Code §31D-11-1103.[173] Generally, in a merger only one of the parties to the merger survives, and in a share exchange both parties survive with one corporation acquiring all of the outstanding shares of another corporation. For purposes of compliance under the Act, a merger and share exchange are virtually identical; accordingly, unless otherwise noted, the following discussion will refer primarily to mergers.

A merger may result from the combination of two or more corporations with overlapping stock ownership, the desire to combine two compatible businesses that can be more profitably operated as a single enterprise, the desire to acquire a second corporation by means of a merger with the acquiring corporation or with a wholly-owned subsidiary or subsidiaries of a parent corporation, or any other valid business purpose. Whatever the reason and whatever form the merger is to take, consideration must be given to the tax consequences of the merger.

A merger may be a tax-free reorganization – an "A reorganization" under the Internal Revenue Code – to the extent shareholders of the constituent corporations receive stock in the surviving corporation.[174] A share exchange may be a tax-free reorganization – a "B reorganization" under the Internal Revenue Code – to the extent

shareholders of the acquired corporation receive only stock in the surviving corporation.[175] However, if a part of the consideration received by a shareholder in the merger is "boot," *i.e.* cash, securities or other property, the boot will be taxable to the shareholder in an A reorganization, and, in a B reorganization, the presence of boot will cause the entire merger to be taxable.[176] Moreover, in an A reorganization, there are limits on the amount of boot which may be received in a nontaxable merger, and other tax requirements, which if exceeded can cause the entire transaction to be taxable to the shareholder, including the fair market value of the stock received in the surviving corporation. While the Internal Revenue Service will not generally rule in advance as to whether a proposed transaction constitutes a tax-free reorganization for tax purposes, it may rule on other tax issues relating to the merger.[177]

After weighing the tax consequences of a merger and deciding to merge the corporation, the next consideration involves the mechanics of the merger. The first step is to agree upon the terms and conditions of the merger. Since the shareholders are giving up stock in constituent corporations for stock in the surviving corporation (which may constitute a "sale" of stock for purposes of federal and state securities laws), valuation of the stock of the respective corporations becomes a vital issue, and, in the case of closely held corporations, may be difficult. This valuation may be based on book value, earnings, appraisals, or any of numerous other valid considerations.

After the terms and conditions of the merger are negotiated, a plan of merger must be prepared. In addition to the terms and conditions of the merger, the Act requires that certain other matters be set forth in the plan of merger, including the names

of the corporations proposing to merge, the name of the corporation which will survive the merger, the manner of converting shares of the corporations into shares of the surviving corporation or into cash or shares of another corporation, a statement of any changes in the articles of the surviving corporation or documents to be prepared for the creation of a new entity, and any other provisions with respect to the proposed merger deemed desirable.[178]

Normally, the shareholders of each of the constituent corporations will require representations and warranties from the shareholders of the other corporations regarding their clear title to their shares of stock. In addition, representations and warranties may be required as to the constituent corporations' liabilities (fixed and contingent), their clear title to assets, and their good standing with the state of incorporation and any state in which they may be transacting business. These representations and warranties may be in a separate agreement from the plan of merger, or they may be combined into an agreement and plan of merger.

Once the plan of merger is prepared, it must be approved by the board of each constituent corporation.[179] The plan of merger, as adopted by the respective boards, must be submitted for approval to a meeting of the shareholders of each constituent corporation along with a recommendation that the shareholders approve the plan.[180] Notice of this meeting must be given to each shareholder of record, whether or not entitled to vote at the meeting.[181] This notice must include a copy or a summary of the plan of merger.[182]

At the meeting, the shareholders must vote on the proposed plan of merger, and the plan must receive the affirmative vote of a majority of the outstanding shares entitled to vote on the merger unless a greater vote is required by the articles.[183] If a class of shares is entitled to vote on the merger as a separate group, the affirmative vote of a majority of the outstanding shares of each separate voting group and of the total shares entitled to vote is required.[184] A class is entitled to vote as a class if the class of shares are to be converted under the plan of merger into shares or other securities, interests, rights to acquire shares, cash, or other property or if the articles of incorporation so provide.[185] Dissenting shareholders have the right to be paid the fair value of their shares providing they follow the specific procedures set forth in the Act.[186]

Unless the articles of incorporation provide otherwise, a corporation ("parent") owning at least 90% of the outstanding shares of another corporation ("subsidiary") may merge the subsidiary into the parent or another subsidiary, without the approval of the shareholders of either corporation, by having the board of the parent adopt a plan of merger and mail a copy of the plan to each shareholder of the subsidiary.[187] Generally speaking, if the subsidiary is solvent, for federal income tax purposes, such a "short-form" merger of a subsidiary into the parent corporation may be treated as a tax-free subsidiary liquidation under Internal Revenue Code § 332.[188]

After approval of the plan of merger by the shareholders[189] or, in the case of the parent and subsidiary, by the board,[190] articles of merger in the form specified by the Act[191] must be signed by an officer or other duly authorized representative of each constituent corporation,[192] and filed with the Secretary of State.[193] The articles of merger

must include the names of the parties to the merger, the date on which the merger is to be effective, any amendments to the articles of incorporation of the survivor or the articles of incorporation of the new corporation, and, if the plan of merger required approval by the shareholders a statement that the plan was duly approved by the shareholders and if voting by any separate voting group was required, a statement that the plan was duly approved by each separate voting group.[194] If the plan of merger did not require approval by the shareholders that were a party to the merger, a statement to that effect must also be included in the articles of merger.[195] In any merger, the constituent corporation owning or holding real estate in West Virginia must evidence title in the new or surviving corporation by executing and recording a confirmatory deed reciting the merger.[196]

In addition to a merger, a corporation may use a share exchange to acquire all of the shares of another corporation or all of the interests of another entity. In a share exchange all of the shares or interests of one or more classes must be exchanged for shares of securities or other property.[197] A plan of share exchange must include the name of each corporation or other entity whose shares or interests will be acquired, the name of the corporation or other entity that will acquire those shares or interests, the terms and conditions of the share exchange, the manner and basis for exchanging the shares or interests, and any other provisions required by the articles of incorporation or organizational documents of any party to the share exchange.[198] All other requirements and effects of a share exchange, including approval of a plan of share exchange, execution of articles of share exchange, and the effect of the share exchange mirror the requirements of a merger.[199]

A merger or share exchange of a domestic and a foreign corporation requires compliance with the laws of West Virginia as well as the laws of the state where the foreign corporation is organized.[200] Unless the name of the corporation is changed or unless it desires to pursue additional purposes in West Virginia, it is not necessary to procure a new or amended certificate of authority to transact business in West Virginia.[201]

B. Disposition of Assets

No approval of the shareholders is required (1) to sell, lease, exchange or otherwise dispose of any or all of the assets of the corporation in the usual and regular course of business, (2) to mortgage or otherwise encumber any or all of the assets of the corporation, (3) to transfer any or all of the assets of the corporation to a wholly owned subsidiary, or (4) to distribute assets pro rata to the shareholders.[202] Generally, shareholder approval is only required if the disposition would leave the corporation without a significant continuing business activity.[203] The corporation will be conclusively deemed to have retained a significant continuing business activity if it retains a business activity that represents at least 25% of the total assets (as of the most recent fiscal year-end) and 25% of either the income before taxes or revenues for continuing operations for that fiscal year.[204]

C. Appraisal Rights

A shareholder is entitled to appraisal rights and to obtain fair value of that shareholder's shares upon the occurrence of any of the following:

(1) Consummation of a corporate merger if shareholder approval is required for the merger and the shareholder is entitled to vote (unless the

shares are to remain outstanding after the merger) or if the corporation is a subsidiary in a short-form merger;[205]

(2) Consummation of a share exchange to which the corporation is a party as the corporation whose shares will be acquired if the shareholder is entitled to vote on the exchange;

(3) Consummation of a disposition of assets if the shareholder is entitled to vote on the disposition;

(4) An amendment of the articles of incorporation with respect to a class or series of shares that creates a fractional share if the corporation has the obligation or right to repurchase such fractional share; or

(5) Any other amendment to the articles of incorporation, merger, share exchange, or other disposition of assets to the extent provided by the articles, bylaws, or a resolution of the board of directors.[206]

Appraisal rights are not available for (1) any shares listed on the New York stock exchange or the American stock exchange or designated as a national market system security on an interdealer quotation system by the national association of securities dealers, or (2) any class of shares which has at least two thousand shareholders and the outstanding shares have a market value of at least twenty million dollars.[207]

Regardless of the foregoing, appraisal rights will be available for a publicly traded corporation or market value corporation as defined above if the shareholder is required to accept anything other than cash or shares of any corporation which is publicly traded or satisfies the market value exception as defined above or if the shares are being acquired or by certain related persons.[208]

The articles of incorporation may limit or eliminate appraisal rights for any class or series of preferred shares.[209]

If a shareholder is entitled to appraisal rights, he or she may not challenge a completed corporate action unless the action (1) was not effectuated in accordance with the applicable provision of West Virginia Code or governing documents, or (2) was procured as a result of fraud or material misrepresentation.[210]

The Act sets forth detailed procedures for a shareholder to exercise appraisal rights.[211] A practitioner must follow these procedures closely to secure certain rights and to abide by time frames for payments to any shareholder seeking appraisal rights. For example, the corporation may be required to tender payment for shares at the corporation's estimated value within a short time of the transaction giving rise to appraisal rights, even if the shareholder is going to challenge the corporation's valuation of the shares.[212]

VIII. DISSOLUTION

Dissolution of a corporation may be occasioned by the loss of profitable business or the desire to sell the business assets. Whatever the reason for the dissolution, the tax consequences to the corporation and the shareholders should be considered.

Internal Revenue Code § 336 generally requires recognition of corporate level gain or loss when a corporation distributes property in complete liquidation. Similarly, Internal Revenue Code § 331 requires recognition of gain at the shareholder level with respect to amounts received by a shareholder in complete liquidation. Thus, unless the corporation is an S corporation or the corporation being liquidated is an 80 percent owned subsidiary of another corporation, if the corporation has appreciated assets, liquidation will generally result in two levels of tax, *i.e.* tax once at the corporate level and again at the shareholder level.

A West Virginia corporation may be dissolved voluntarily, administratively or judicially. Under the Act, a corporation which has neither issued shares nor commenced business may be voluntarily dissolved by its incorporators simply by having the incorporators execute articles of dissolution in the form specified in the Act and by filing of these articles with the Secretary of State.[213] If a corporation has issued shares or commenced business, the corporation's board of directors may propose dissolution for submission to the shareholders.[214] For such proposal to be adopted, the board of directors must recommend dissolution to the shareholders, unless the directors have a conflict of interest and the shareholders must approve the proposal by a majority vote at a meeting at which a quorum, consisting of at least a majority of the votes entitled to be cast, exists.[215]

The proposal approved by the shareholders may constitute the plan of liquidation for federal tax purposes. A Form 966 must be filed with the Internal Revenue Service within thirty days after adoption of the plan of liquidation.[216]

At any time after dissolution is authorized, articles of dissolution, setting forth the name of the corporation, the date dissolution was authorized, and a statement that the dissolution was duly approved by the shareholders must be filed with the Secretary of State.[217] A certificate of dissolution will then be issued by the Secretary of State after receiving a notice from the tax commissioner and bureau of employment programs to the effect that all taxes have been paid.[218]

A dissolved corporation continues its corporate existence but may not carry on any business except to take appropriate actions to wind up and liquidate its business and affairs.[219] To dispose of known claims, a dissolved corporation should notify the known claimants in writing of the dissolution at any time after its effective date.[220] If a claimant was given written notice meeting the requirements of the Act[221] and the claimant does not deliver the claim to the dissolved corporation by the deadline[222] the claim is barred.[223] To dispose of unknown claims, a dissolved corporation may publish notice of its dissolution.[224]

A corporation may revoke its dissolution within 120 days of its effective date if the revocation is authorized in the same manner as the dissolution was authorized.[225] When the revocation of dissolution is effective, it relates back to and takes effect as of the effective date of the dissolution and the corporation resumes carrying on its business as if dissolution had never occurred.[226]

The Secretary of State may commence an action to administratively dissolve a corporation if the corporation fails to pay any franchise taxes or penalties within sixty days after they are due, fails to notify the Secretary of State that its registered agent or registered office has been changed, or the corporation's period of duration stated in its articles of incorporation has expired.[227]

Also, a circuit court may dissolve a corporation in a proceeding by (1) the attorney general if it is established that (A) the corporation obtained its articles through fraud, or (B) the corporation has continued to exceed or abuse the authority conferred upon it by law;[228] (2) a shareholder if it is established that (A) the directors are deadlocked in the management of the corporate affairs, the shareholders are unable to break the deadlock and irreparable injury to the corporation is threatened or being suffered, (B) the directors in control of the corporation are acting in a manner or will act in a manner that is illegal, oppressive or fraudulent, (C) the shareholders are deadlocked and have failed to elect successors to directors whose terms have expired for at least two consecutive annual meetings, or (D) corporate assets are being misapplied or wasted;[229] (3) a creditor if it is established that (A) the creditor's claim has been reduced to judgment, the execution on the judgment returned unsatisfied, and the corporation is insolvent, or (B) the corporation has admitted in writing that the creditor's claim is due and owing and the corporation is insolvent;[230] or (4) by the corporation in a proceeding to have its voluntary dissolution continued under circuit court supervision.[231] The circuit court's authority to dissolve a corporation varies depending on who brought the proceeding.[232] In an action for dissolution by a shareholder, the corporation or the

shareholders may elect to purchase all shares owned by the petitioning shareholder at the fair value of the shares, provided that the corporation's shares are not traded on an established market. Such an election is irrevocable and may only be set aside by the court if it determines that it is equitable to do so.[233]

VIII. FOREIGN CORPORATIONS

The corporate practitioner's most frequent association with foreign corporations usually involves advising a foreign corporation on the necessity to obtain a certificate of authority before transacting certain business in West Virginia and to qualify the corporation if a certificate of authority is found to be necessary.

The Act provides that certain enumerated activities of a foreign corporation are not considered to be "transacting business" within West Virginia.[234] If, after examination of the activities of the foreign corporation, it appears necessary to obtain a certificate of authority, an application must be filed with the Secretary of State on the prescribed form.[235] The contents and requirements for this application are spelled out in the Act, and the Secretary of State's office has been generally helpful in responding to some of the areas of inquiry on that application.

The Secretary of State will issue a certificate of authority after receiving the application, along with a certificate that the corporation is in good standing with the state of incorporation and the requisite license tax and other fees.[236] An annual license tax and fee must be paid to the Secretary of State as statutory attorney-in-fact.[237] A certificate of authority authorizes the foreign corporation to transact business in West Virginia and provides such foreign corporation with the same rights and privileges as a domestic

corporation.[238] A foreign corporation is subject to the same duties, restrictions, penalties and liabilities as a domestic corporation.[239]A foreign corporation transacting business in West Virginia without a certificate of authority may not maintain a proceeding in any circuit court in the state until it obtains a certificate of authority.[240]

In the event that a foreign corporation authorized to transact business in West Virginia changes its corporate name, its period of duration or the state or country of its incorporation, the corporation must apply for an amended certificate of authority.[241] The same requirements for obtaining an original certificate of authority apply to obtaining an amended certificate of authority.[242]

Each foreign corporation authorized to transact business in West Virginia must continuously maintain in the state a registered office, which may be the same as any of its places of business, and a registered agent, who may be an individual who resides in the state, a domestic corporation, or another foreign corporation authorized to transact business in the state.[243] The registered agent must have a business office identical with the registered office of the foreign corporation.[244] The corporation may change its registered office or registered agent by filing a statement with the Secretary of State.[245]

A foreign corporation's certificate of authority may be revoked if the corporation does not pay any franchise taxes or penalties within sixty days after they are due; does not inform the Secretary of State that its registered agent or registered office has changed; submits a document signed by an incorporator, director, officer, or agent which such person knew was false; or dissolves or disappears as a result of a merger.[246] After receiving notice from the Secretary of State that grounds exist for revocation of its

certificate, the foreign corporation has sixty days to correct the grounds before a certificate of revocation is issued.[247] The foreign corporation may appeal the revocation of its certificate of authority.[248] Revocation of a foreign corporation's certificate of authority does not terminate the authority of the registered agent of the corporation.[249]

A foreign corporation authorized to conduct business in West Virginia may withdraw from the state by obtaining a certificate of withdrawal from the Secretary of State.[250] An application for a certificate of withdrawal must contain the name of the corporation, a statement that it is not transacting business in West Virginia and that it surrenders authority to do so, a statement that it revokes the authority of its registered agent, a mailing address to which the Secretary of State may mail a copy of process, and a commitment to notify the Secretary of State in the future of any change in its mailing address.[251] If the Secretary of State finds that the application conforms to the requirements of the law and that all fees have been paid, a certificate of withdrawal will be issued to the corporation. A certificate of withdrawal no longer needs to be recorded in the county in which the corporation's certificate of authority is recorded.

IX. LIMITED LIABILITY COMPANIES

A. Background

Over the past ten years, limited liability companies ("LLCs") have exploded in popularity because, when properly formed, they can combine the benefits of limited liability for all members (like a corporation) with favorable tax treatment. As discussed in more detail below, the type of favorable tax treatment received depends on whether the LLC has one member (a single-member LLC) or two or more members (a multi-member LLC).[252] Additionally, LLCs are often ideal entities for structuring joint ventures and can sometimes provide an effective substitute to consolidated groups. In sum, no other entity, including limited partnerships or corporations, offers this unique combination of potential benefits. For these, and additional reasons, practitioners may want to consider the benefits of using an LLC whenever involved in choice of entity issues.

In 1996, the West Virginia legislature adopted the Uniform Limited Liability Company Act (the "Uniform LLC Act") adding provisions dealing with professionals.[253] Adoption of the Uniform LLC Act has at least three significant consequences for West Virginia business lawyers. First, it allows West Virginia LLCs to take advantage of favorable Internal Revenue Service ("IRS") rules regarding the tax treatment of LLCs.[254] Second, it expressly provides that professional services may be rendered through an LLC.[255] Finally, the Uniform LLC Act provides for great freedom of contract. It makes clear that there are only a limited group of matters that an operating

agreement may not control.[256] It also provides a detailed series of default rules for LLCs that choose not to address or amend the statutory default rules.

The remainder of this section is intended to provide the practitioner with a general overview of the Uniform LLC Act.

B. Formation of Limited Liability Companies

An LLC, like a partnership or corporation, is a legal entity distinct from its members.[257] Forming an LLC is a simple process. An LLC can be organized for any lawful purpose.[258] LLC's must have at least one "member."[259] Members are persons or entities with an ownership interest in the LLC and are comparable to partners or corporate shareholders.

Articles of organization, along with the requisite filing fee, must be filed with the Secretary of State.[260] The articles contain very basic information much like a certificate of limited partnership or articles of incorporation. By law, the LLC's articles of organization must contain (1) its name[261], (2) the address of its initial designated office, (3) the name and street address of the initial agent for service of process, (4) the name and address of each organizer and member having authority to execute instruments on behalf of the LLC, (5) whether the LLC is to be a term LLC[262] and, if so, the term specified, (6) whether the LLC is to be manager-managed, and, if so, the name and address of each initial manager, (7) the purpose for which the LLC is organized, (8) an e-mail address where informational notices and reminders of annual filings may be sent, and (9) whether any of the members of the LLC are to be liable for its debts and obligations under W. Va. Code § 31B-3-303(c).[263] Articles of organization may recite

provisions to be set forth in an operating agreement or other matters not inconsistent with law.[264]

C. Operating Agreement

While not required by law, the members will also likely want a written operating agreement which, like a partnership agreement, or corporate bylaws, is an agreement concerning the relations between the members, managers and the LLC.[265] Generally, this agreement is the "paramount" agreement of the members and represents the essence of their bargain.[266] Accordingly, when in conflict with the articles, the operating agreement controls, except as to those who innocently and detrimentally relied upon a different result specified in the articles of organization.[267]

Certain provisions of the Uniform LLC Act may not be varied by the members. These are specified in W. Va. Code § 31B-1-103(b) and, generally, address certain fiduciary relationships and duties and the right to certain LLC financial information. The operating agreement need not be filed with the Secretary of State.

D. Management of the LLC

By law, management of an LLC is vested in its members. This is somewhat akin to the rule for general partnerships and is termed a "member-managed company."[268] In a member-managed company, each member has equal rights in the management and conduct of the LLC's business.[269]

Alternatively, the members may designate one or more "managers" to run the LLC.[270] In a manager-managed LLC each manager has equal rights in the management and conduct of LLC business, and, with certain exceptions,[271] any matter

relating to the business of the LLC can be determined by the manager (or a majority of the managers if there is more than one manager).[272] Accordingly, when choosing a form of management structure, practitioners should take care to alert clients that in a "manager-managed" LLC only a manager has authority to take actions on behalf of the LLC. This arrangement is somewhat akin to a corporation where officers and directors (not shareholders) take action on behalf of the entity. Moreover, unless the articles of organization limit their authority, any member of a member-managed LLC or manager of a manager-managed LLC may sign and deliver any instrument transferring or affecting the LLC's interest in real property.[273]

The Uniform LLC Act imposes certain fiduciary duties on members and managers. These duties may vary depending on whether the LLC is member or manager managed. Practitioners should review these duties and determine whether it is appropriate (or possible) to modify them. For example, while the duty of loyalty of a member to a member-managed LLC and its other members can not be eliminated, under W. Va. Code § 31B-1-103(b)(2), the Operating Agreement may (1) identify specific types or categories of activities that do not violate the duty of loyalty, if not manifestly unreasonable; and (2) specify the number or percentage of members or disinterested managers that may authorize or ratify, after full disclosure of all material facts, a specific act or transaction that would otherwise violate the duty of loyalty.

E. Liability of Members and Managers

Unless a provision to that effect is contained in the LLC's articles of organization and the member so liable has consented in writing to the adoption of the

provision or to be bound by the provision, the LLC's debts, obligations and liabilities, whether arising in contract, tort, or otherwise, are solely the debts, obligations and liabilities of the LLC. A member or manager is not personally liable for a debt, obligation, or liability of the LLC solely by reason of being or acting as a member or manager.[274]

F. Transferability of Interests in an LLC

The Uniform LLC Act introduces a new term with respect to the transfer of member's interest in an LLC - distributional interest. Distributional interest means all of a member's interests in distributions by the LLC.[275] Distributional interests in an LLC are personal property.[276] They may generally be transferred in whole or in part.[277] Importantly, a transfer of a distributional interest entitles the transferee to receive, to the extent transferred, only the distributions to which the transferor would be entitled.[278] It does not entitle the transferee to become or to exercise any rights of a member.[279] Thus, a transferee who does not become a member is not entitled to participate in the management or conduct of the LLC's business, require access to information concerning the LLC's transactions or copy any LLC records.[280]

A transferee of a distributional interest can become a member in one of two ways. First, if there is no operating agreement, or the operating agreement does not speak to this issue, a transferee may become a member by the unanimous consent of the members. Alternatively, the operating agreement may specify the authority necessary for the transferee to become a member.[281]

G. Dissolution/Dissociation

Articles VI through VIII of the Uniform LLC Act contain extensive provisions dealing with the consequences of a member's departure from the LLC and the dissolution and winding up of the LLC's business. These provisions are much more extensive than comparable provisions under the West Virginia Limited Partnership Act.[282] They are similar to provisions found in West Virginia's Uniform Partnership Act.[283]

Article VI of the Uniform LLC Act discusses events which cause a member to "dissociate" from the LLC. A dissociation, depending on the circumstances, can lead to a buy-out of a member's interest (see Article VII) or a dissolution and winding of the LLC's business (see Article VIII).[284] When reviewing these provisions it is important to keep in mind that they are merely default provisions which can generally be varied by an operating agreement.

Upon a member's dissociation, generally speaking, the member's right to participate in the management and conduct of the LLC's business terminates.[285]

Dissociation events include, in the case of a member who is an individual: (1) the LLC's having notice of the member's express intent to withdraw; (2) an event described in the operating agreement; (3) a transfer of all the member's distributional interest (other than a transfer for security purposes); (4) the member's expulsion pursuant to an operating agreement; (5) the member's bankruptcy or death; (6) the appointment of a guardian or general conservator for the member; or (7) a judicial determination that the

member has otherwise become incapable of performing the member's duties under the operating agreement.[286]

If a dissociation event results in a dissolution and winding up of the LLC, the dissolution rules apply.[287] An LLC is dissolved and its business must be wound up, upon the occurrence of, among other things: (1) an event specified in the operating agreement; (2) consent of the members as specified in the operating agreement; or (3) dissociation of a member who is also a manager or, if none, a member of an at-will company, and dissociation of a member who is also a manager or, if none, a member of a term company but only if the dissociation was for a reason provided in W. Va. Code §§31B-6-601(7) through (11) and occurred before the expiration of the specified term.[288]

Dissolution of an LLC can have significant tax and business consequences. It is important to remember that an LLC can be continued upon the occurrence of a dissolution event caused by a dissociation if within 90 days after the dissociation, (1) the remaining members that would receive a majority of any distributions that would be made to them assuming the business of the LLC were dissolved and wound up on the date of dissociation and (2) the remaining members entitled to receive a majority of any future distributions that would be made to them assuming the business of the LLC were continued, agree to continue. Alternatively, the business of the LLC can be continued under some other right stated in the operating agreement.[289]

In an at-will LLC, the LLC must purchase the dissociated member's distributional interest for "fair market value" determined as of the date of the member's

dissociation if the member's dissociation does not result in a dissolution and winding up of the LLC's business.[290]

In the case of a term LLC, the rules are slightly more complex, particularly if the member wants to dissociate prior to the term's expiration. In that case, the LLC is required to buy the dissociating member's interest for fair value on the date of the expiration of the term specified.[291]

If a member's dissociation is wrongful (*e.g.* in the case of a member of a term LLC who wishes to dissociate prior to the end of the specified term) he or she is liable to the LLC and to the other members for damages caused by such dissociation.[292]

It is important to remember that dissociation events and required purchase of a member's LLC interest are merely default provisions which generally can be waived by an operating agreement. Additionally, the Uniform LLC Act does not currently provide perpetual existence to an LLC.

H. Annual Reports

LLCs, and foreign LLCs authorized to transact business in West Virginia, are required to file an annual report between January 1 and July 1 of each year with the West Virginia Secretary of State.[293] Failure to do so may result in dissolution of the LLC.[294]

I. Tax Classification: Check the Box Regulations

Prior to January 1, 1997, the tax classification of an LLC with more than two members was based upon the presence or absence of four corporate characteristics.[295] The four corporate characteristics were (1) limited liability, (2) centralization of

management, (3) free transferability of interest, and (4) continuity of life.[296] If an LLC had no more than two of the corporate characteristics, it would be taxable as a partnership. If an LLC had more than two of the corporate characteristics, it would be taxable as a corporation. If an LLC had only one member, the tax classification was unclear prior to January 1, 1997.

After December 31, 1996, the tax classification of an LLC is determined under the check-the-box regulations.[297] If a domestic LLC has two or more members, it will be taxable as a partnership unless it makes an election to be taxable as a corporation.[298] Generally, partnership tax treatment is a favorable result. Partnerships are "flow through entities." As such, the income flows through the partnership to its partners (or members in the case of an LLC) resulting in only one level of taxation.[299] By comparison, a corporation (unless it has made an S election) is subject to two levels of tax, once at the corporate level and once at the shareholder level.[300]

If the LLC has only one member, it will be disregarded as a separate entity from its owner for tax purposes, unless it makes an election to be taxable as a corporation.[301] Thus, the owner reports the income (or loss) from a single-member LLC on its tax return. For example, depending on the facts, an individual will report this income on Schedule C or E of his or her IRS Form 1040, and a corporation would report this income on its Form 1120 or 1120S, as applicable.

J. General Comparison of LLCs Having Two or More Members and Other Entities

1. LLCs vs. General Partnerships: The main distinction between general partnerships and LLCs is that LLC members enjoy limited liability. Both partnerships and LLCs receive favorable partnership tax treatment.

2. LLCs vs. Limited Partnerships: Both generally receive favorable partnership tax treatment, but LLCs have no need of a general partner who is personally liable for the partnership's debts. Additionally, unlike limited partners,[302] members can take an active role in LLC business.

3. LLCs vs. C Corporations: For LLCs, income is taxed once at the member level. C Corporation earnings, on the other hand, are taxed twice, once at the corporate level and again when they are distributed to shareholders. One relatively minor distinction between LLCs and C corporations is the deductibility of health insurance premiums paid by the entity. A C corporation may fully deduct health insurance premiums it pays for its shareholder/employee while health insurance premiums paid by an LLC for the benefit of its members is subject to the deductibility limitations.[303] Additionally, a member's share of LLC income may be considered self-employment income to the member when it may not be considered self-employment income to a shareholder.

4. LLCs vs. S Corporations: Both enjoy limited liability for all members and in general one level of tax. However, LLCs have two distinct advantages. LLCs are generally simpler to organize and maintain than an S Corporation. For example, an LLC is not required to make a specific and timely election and is not restricted in the number or type of shareholders it may have. Conversely, S Corporations

can have no more than 100 shareholders and those shareholders must be either living persons (other than non-resident aliens), certain trusts and estates, or tax-exempt, charitable organizations.[304]

An S Corporation can now own up to 100% of the stock of another corporation.[305] If an S Corporation owns 100% of another corporation, it may make an election to treat such other corporation as a Qualified Subchapter S Subsidiary ("QSub").[306] If the S Corporation does not make this election, income of the subsidiary will be subject to two levels of tax, once at the corporate level and once at the shareholder level. If an S Corporation makes a QSub election for a wholly owned subsidiary, the QSub will not be treated as a separate corporation from the S Corporation, and all assets, liabilities, and income of the QSub will be treated as assets, liabilities, and income of the S Corporation for federal income tax purposes.[307]

Because an election to treat a wholly owned subsidiary as a QSub effectively liquidates the subsidiary, an S Corporation desiring to make such an election should consult its tax advisor to make certain that no gain will be recognized on the QSub election. LLCs are also able to take advantage of partnership tax rules. For example, while an S Corporation can have only one class of stock,[308] LLCs (within certain parameters) can have multiple classes of ownership interests and preferential returns. Further, if the LLC plans to make distributions of appreciated property to its members, its ability to use the favorable partnership rules may provide an additional advantage over S Corporations.[309] Very generally speaking, partnerships can make distributions of appreciated property (other than marketable securities) without triggering taxation of the

built-in-gain.[310] Distributions of such property by S corporations will trigger taxation of the built-in-gain.[311]

K. Derivative Actions

The Uniform LLC Act contains specific provisions regarding derivative actions.[312]

L. Professional LLCs

The Uniform LLC Act provides that professionals (*e.g.* physicians, podiatrists, dentists, optometrists, accountants, veterinarians, architects, engineers, social workers, osteopathic physicians and surgeons, chiropractors, and attorneys) may form professional limited liability companies ("PLLCs"). Note, the Uniform LLC Act also instructs the various licensing boards to promulgate rules for the formation and approval of PLLCs for specific professions.[313] Each professional should consult the appropriate licensing board prior to forming a PLLC.

Unless the specific provisions governing PLLCs provide otherwise, the provisions of the Uniform LLC Act governing regular LLCs also apply to PLLCs.[314]

A member, manager, agent or employee of a PLLC is not personally liable for any debts or claims against, or the acts or omissions of, the PLLC or of another member, manager, agent or employee of the PLLC. Of course, he or she is still liable for his or her own malpractice.[315]

Formation of a PLLC is simple. The PLLC files articles of organization with the Secretary of State, and it must carry at least $1 million in professional liability

insurance or otherwise provide at least $1 million of segregated funds (*e.g.* bank escrow, certificate of deposit, bank letter of credit or insurance company bond).[316]

An existing professional services general partnership can be converted to a PLLC by adopting an agreement of conversion and filing articles of organization with the Secretary of State.[317] The IRS has indicated that such conversions will not generally result in adverse tax consequences to the converting partners or the partnership.[318] However, because there are limitations to this general rule, a tax advisor should be consulted prior to any such conversion. Because of potential adverse tax consequences, a professional corporation should not be converted to a PLLC without consulting a tax advisor.

M. <u>Conversions</u>

1. <u>Partnership to LLC</u>

The Uniform LLC Act expressly provides for the conversion of either general or limited partnership to LLCs.[319] Generally speaking, a partnership that has been converted is the same entity before and after the conversion.[320] Thus, for example, all property owned by the converting partnership vests in the LLC.[321] Conversions must be approved by a unanimous vote or such percentage as required by the partnership agreement.[322]

Conversions should generally result in no gain recognition other than (1) any potential investment tax credit recapture and (2) any 752 gain (e.g. from decrease in partners share of liabilities in new entity).[323] Note however that conversions may raise

other tax issues, such as the availability of the cash method of accounting. Accordingly, a tax advisor should be consulted prior to any conversion.

2. Corporation to LLC

A corporation in the state of West Virginia may convert to a limited liability company. A plan for the conversion approved by the board must be submitted to a shareholder vote at an annual or special meeting.[324] Approval of the plan for conversion requires the approval of all shareholders, whether or not they are entitled to vote.[325] After the plan for conversion is approved the corporation must file articles of conversion with the Secretary of State. The specific requirements for the articles of conversion are listed under W. Va. Code § 31D-11-1109(c). Upon filing and paying all applicable fees, the Secretary of State[326] will issue a certificate of conversion. The conversion of a corporation does not affect any obligations or liabilities of the corporation incurred prior to the conversion or the personal liability of any person incurred prior to the conversion. Once the corporation has been converted to a limited liability company, the limited liability company shall for all purposes be deemed to be the same entity as the converting corporation and all rights, privileges and powers of the corporation and all debts and liabilities due to the corporation shall remain vested in the limited liability company. Conversion to a limited liability company is a taxable liquidation of the corporation, potentially resulting in gain to both S and C Corporation shareholders. Such a conversion should be considered only after careful analysis of the income tax implications.

3. Single- to Multi-Member LLC/Multi- to Single-Member LLC

The conversion of a single-member entity that is disregarded for federal income tax purposes to an LLC with more than one member is governed by Rev. Rul. 99-5.[327] Generally, a purchase of an interest in a single-member entity from the owner is treated as a taxable sale of a proportionate share of the assets of the LLC by the single-member owner. A contribution to a single-member LLC in exchange for an interest in the LLC is generally treated as a tax-free transfer of property in exchange for an interest in the LLC.[328]

A conversion of a multi-member LLC that is treated as a partnership for federal income tax purposes to a single-member LLC that is disregarded for federal income tax purposes is treated as a dissolution of the partnership for federal income tax purposes.[329] Depending upon the factual circumstances, such a dissolution may or may not result in recognition of gain.

ENDNOTES

[1] W. Va. Code §§ 32-1-101 *et seq.* (West Virginia Uniform Securities Act).

[2] W. Va. Code §§ 11-12-1 *et seq.* (Business Registration Tax), §§ 11-23-1 to -28 (Business Franchise Tax) and §§ 11-24-1 to -42 (Corporation Net Income Tax). For other tax provisions which might affect the West Virginia corporation, *see generally* Chapters 11 and 11A of the West Virginia Code.

[3] W. Va. Code §§ 46-1-101 *et seq.* (Uniform Commercial Code).

[4] W. Va. Code §§ 24-1-1 *et seq.* (Public Service Commission).

[5] W. Va. Code §§ 24A-1-1 *et seq.* (Commercial Motor Carriers).

[6] West Virginia statutes govern many aspects of labor and labor relations, including unfair labor practices (W. Va. Code § 21-1A-4); employee safety and welfare (W. Va. Code §§ 21-3-1 *et seq.*); hours of labor (W. Va. Code §§ 21-1-1 *et seq.*); wage payment and collection (W. Va. Code §§ 21-5-1 *et seq.*); and minimum wage and maximum hours (W. Va. Code §§ 21-5C-1 *et seq.*).

[7] W. Va. Code §§ 23-1-1 *et seq.* (Workers' Compensation).

[8] W. Va. Code §§ 21A-1-1 *et seq.* (Unemployment Compensation).

[9] W. Va. Code §§ 31A-1-1 *et seq.* (Banks and Banking).

[10] Numerous state statutes and state agencies regulate, control and monitor various environmental aspects of the operations of West Virginia corporations: Air Pollution Control (W. Va. Code §§ 22-5-1 *et seq.*); Natural Resources (W. Va. Code §§ 20-1-1 *et seq.*); Water Pollution Control Act (W. Va. §§ 22-11-1 *et seq.*); Transportation of Oils (W. Va. Code §§ 22-8-1 *et seq.*); and Public Service Commission (W. Va. Code §§ 24-1-1 *et seq.*).

[11] In addition, numerous state statutes control and monitor activities of corporations engaged in certain enterprises, such as insurance (W. Va. Code §§ 33-1-1 *et seq.*) and mineral production (W. Va. Code §§ 22-4-1 *et seq.*).

[12] I.R.C. §§ 1 to 9834.

[13] Securities Act of 1933 (15 U.S.C. §§ 77a to 77aa); Securities Exchange Act of 1934 (15 U.S.C. §§ 78a to 78kk); Trust Indenture Act of 1939 (15 U.S.C. §§ 77aaa to 77bbb); Investment Company Act of 1940 (15 U.S.C. §§ 80a-1 to 80a-64); and Securities Investor Protection Act of 1970 (15 U.S.C. §§ 78aaa to 78lll).

[14] Numerous federal statutes under Title 29 of the United States Code regulate labor and labor relations. *E.g.* Labor Management Relations Act, 1947 (29 U.S.C. §§ 141 to 197); Norris-La Guardia Act (29 U.S.C. §§ 101 to 115); Fair Labor Standards Act of 1938 (29 U.S.C. §§ 201 to 219); and National Labor Relations Act (29 U.S.C. §§ 151 to 168).

[15] 11 U.S.C. §§ 101 to 1174.

[16] *E.g.*, Sherman Antitrust Act (15 U.S.C. §§ 1 to 7); Clayton Act (15 U.S.C. §§ 12 to 27, 44 and 29 U.S.C. §§ 52, 53); Federal Trade Commission Act (15 U.S.C. §§ 41 to 58); Robinson-Patman Act (15 U.S.C. §§ 13 to 13b, 21a); Miller-Tydings Act of 1937; Celler Kefauver Act (15 U.S.C. §§ 18, 21); and Hart-Scott-Rodino Antitrust Improvements Act of 1976 (15 U.S.C. § 18a).

[17] 2002 W. Va. Acts, 2d Ex. Sess., C. 25.

[18] Note, Section 9 of the Revised Model Business Corporation Act was omitted from the West Virginia Act. This section addressed shareholder derivative suits, and West Virginia=s omission means that there is no statutory guidance on such suits. Consequently, shareholders will have to rely on common law to bring derivative suits.

[19] For a more thorough discussion of limited liability companies, see *infra* Part IX of this Section.

[20] *See generally* W. Va. Code § 31B-3-303

[21] *See generally* Uniform Limited Partnership Act, W. Va. Code §§ 47-9-1 *et seq.* for laws specifically governing limited partnerships.

[22] *See generally* Uniform Partnership Act, W. Va. Code §§ 47B-1-1 *et seq.* for laws specifically governing partnerships.

[23] W. Va. Code § 47B-3-6(a).

[24] W. Va. Code '§ 31D-3-302.

[25] *See generally* W. Va. Code § 47B-8-1 and W. Va. Code §§ 47-9-44 to -45.

[26] W. Va. Code § 31B-2-203(a)(5). Limited liability companies may be either "term"@ (meaning they have a specified term of existence) (W. Va. Code§ 31B-1-101(22)) or "at will" (W. Va. Code § 31B-1-101(2)).

[27] I.R.C. § 11(b)(1)(A)-(D). However, certain "personal service corporations" are not eligible for graduated rates and their income is taxed at a flat rate of 35 percent. I.R.C. § 11(b)(2).

[28] I.R.C. § 11(b)(1)(A)-(D).

[29] I.R.C. § 11(b).

[30] I.R.C. § 55. The alternative minimum tax is beyond the scope of this discussion.

[31] I.R.C. § 1.

[32] I.R.C. § 151(d)(3).

[33] I.R.C. § 68.

[34] I.R.C. § 67

[35] I.R.C. § 1(h).

[36] I.R.C. § 1211(b).

[37] I.R.C. § 702.

[38] I.R.C. §§ 1361 to 1379. The S corporation rules, unlike the partnership rules, place significant restrictions on the types of shareholders an S corporation may have. For example, an S corporation cannot have more than 100 shareholders and shareholders generally must be either individuals who are U.S. citizens, certain types of permissible trusts, or tax-exempt, charitable organizations. I.R.C. § 1361(b)(1)(A)-(D). Additionally, S corporations generally can have only one class of stock. *Id.*

[39] However, S corporations which have a prior C corporation history may be subject to a corporate level tax. I.R.C. §§ 1374 and 1375.

[40] If the shareholder is a corporation, the impact of the two tier tax may be ameliorated by the dividends received deduction. *See generally* I.R.C. §§ 241 and 243 to 247

[41] I.R.C. § 531

[42] I.R.C. § 702. Note, however, that large publicly traded partnerships may be subject to an entity level tax. *See generally* I.R.C. § 7704.

[43] I.R.C. §§ 401 to 404A, and 406 to 409A.

[44] W. Va. Code §§ 11-21-1 *et seq.*

[45] W. Va. Code §§ 11-24-1 to -24.

[46] W. Va. Code §§ 11-23-1 *et seq.*

[47] W. Va. Code § 31D-6-620.

[48] *Id.*

[49] 15 U.S.C. §§ 77a-77aa.

[50] 15 U.S.C. §§ 77c-77d.

[51] 15 U.S.C. § 77d.

[52] 17 C.F.R. § 230.506.

[53] 17 C.F.R. § 230.504 and 17 C.F.R. § 230.505.

[54] W. Va. Code § 31D-2-202(a).

[55] W. Va. Code § 31D-2-202(b).

[56] W. Va. Code § 31D-4-401.

[57] *Id.*

[58] W. Va. Code § 31D-4-403

[59] W. Va. Code § 31D-3-301(a).

[60] *Id.*

[61] *Id.*

[62] *Id.*

[63] W. Va. Code § 31D-3-302.

[64] The former Corporation Act provided for a definition of capital surplus in W. Va. Code § 31-1-85. The current Act has no such definition, but presumably, any amount paid in over par value per share will still be considered capital surplus for corporate license tax purposes. *See* W. Va. Code §§ 11-12C-1 *et. seq.*

[65] W. Va. Code § 31D-2-202(a)(2).

[66] W. Va. Code § 31D-6-601(b).

[67] W. Va. Code § 31D-6-602.

[68] *Id.*

[69] W. Va. Code § 31D-6-630(a).

[70] *Id.* at -630(b)(3).

[71] *Id.* at -630(b)(6).

[72] W. Va. Code § 31D-2-201.

[73] W. Va. Code § 31D-5-501.

[74] *Id.*

[75] W. Va. Code § 31D-5-504(a).

[76] W. Va. Code § 31D-5-501.

[77] W. Va. Code § 31D-5-504(b).

[78] W. Va. Code § 31D-5-504(c).

[79] W. Va. Code § 31D-5-502.

[80] W. Va. Code § 31D-2-202.

[81] W. Va. Code § 31D-10-1020.

[82] W. Va. Code § 31D-7-725.

[83] *Id.*

[84] W. Va. Code § 31D-2-202(b)(5). *See also* W. Va. Code §§ 31D-8-850 to 859

[85] W. Va. Code§ 31D-2-202(b)(4).

[86] W. Va. Code § 31D-2-202(b)(1).

[87] W. Va. Code § 31D-8-803.

[88] W. Va. Code § 31D-8-806.

[89] W. Va. Code § 31DB2-203.

[90] W. Va. Code § 31D-1-120.

[91] W. Va. Code § 31D-1-120(e).

[92] *Id.*

[93] W. Va. Code § 31D-1-129.

[94] W. Va. Code § 31D-2-204(a)(1).

[95] W. Va. Code § 31D-2-204(a)(2)(A)-(B).

[96] W. Va. Code § 31D-1-151.

[97] W. Va. Code § 31D-2-204(b).

[98] W. Va. Code § 31D-2-205(a). Note, there are also provisions for emergency bylaws. W. Va. Code § 31D-2-206.

[99] W. Va. Code § 31D-10-1020.

[100] W. Va. Code § 31D-2-205(b).

[101] *E.g.,* W. Va. Code §§ 31D-8-821, -822.

[102] W. Va. Code § 31D-7-732.

[103] W. Va. Code § 31D-6-621

[104] *Id.*

[105] *Id.*

[106] *Id.*

[107] *Id.* The corporation may place in escrow shares issued for a contract for future services or a promissory note, or make other arrangements to restrict the transfer of the shares, and may credit distributions in respect of the shares against their purchase price until the services are performed or the note is paid. *Id.*

[108] I.R.C. § 351. For an example of circumstances potentially triggering gain recognition, *see* I.R.C. § 357 (26 U.S.C. § 357) (assumption of corporate liabilities in excess of basis of property contributed or for tax avoidance purposes may trigger gain recognition).

[109] I.R.C. § 1244.

[110] W. Va. Code § 31D-6-625.

[111] *Id.*

[112] W. Va. Code § 31D-6-626.

[113] W. Va. Code § 31D-6-627.

[114] *Id.*

[115] *Id.*

[116] *Id. See also* W. Va. Code § 31D-6-626.

[117] W. Va. Code § 31D-6-604.

[118] W. Va. Code § 11-12-3.

[119] I.R.C. § 248.

[120] I.R.C. § 709(b).

[121] W. Va. Code § 31D-7-732.

[122] W. Va. Code § 31D-7-701.

[123] W. Va. Code § 31D-8-820.

[124] W. Va. Code §§ 31D-7-704 and 31D-8-821

[125] *Id.*

[126] W. Va. Code§ 31D-8-803.

[127] W. Va. Code § 31D-8-803(c).

[128] W. Va. Code § 31D-8-805(a).

[129] W. Va. Code § 31D-8-805(e).

[130] W. Va. Code § 31D-8-802.

[131] W. Va. Code § 31D-8-806.

[132] W. Va. Code § 31D-7-728.

[133] W. Va. Code § 31D-8-810.

[134] W. Va. Code §§ 31D-8-820 and -822.

[135] W. Va. Code § 31D-8-822(b).

[136] W. Va. Code § 31D-8-820(b).

[137] W. Va. Code § 31D-8-823.

[138] W. Va. Code § 31D-8-824

[139] W. Va. Code § 31D-8-825.

[140] W. Va. Code § 31D-6-640.

[141] W. Va. Code § 31D-8-830.

[142] *Id.*

[143] W. Va. Code §§ 31D-8-831 and -833.

[144] W. Va. Code § 31D-8-833(c).

[145] W. Va. Code § 31D-8-824(d).

[146] *Id.*

[147] W. Va. Code § 31D-2-202(b)(4).

[148] W. Va. Code § 31D-8-859.

[149] W. Va. Code §§ 31D-8-852 and -856(c).

[150] W. Va. Code §§ 31D-8-851 and -856.

[151] W. Va. Code § 31D-2-202(b)(5).

[152] W. Va. Code § 31D-8-854.

[153] W. Va. Code § 31D-8-857.

[154] W. Va. Code § 55-7C-3.

[155] W. Va. Code § 31D-7-732.

[156] *Id.*

[157] *Id.*

[158] *Id.*

[159] *Id.*

[160] *Id.*

[161] *Id.*

[162] W. Va. Code § 31D-7-730.

[163] W. Va. Code § 31D-7-731.

[164] W. Va. Code § 31D-16-1603.

[165] W. Va. Code § 31D-16-1602.

[166] W. Va. Code § 31D-16-1620.

[167] W. Va. Code § 31D-8-840.

[168] *Id.*

[169] *Id.*

[170] *Id.*

[171] W. Va. Code § 31D-8-841.

[172] W. Va. Code § 31D-8-843(b).

[173] W. Va. Code § 31D-11-1101.

[174] I.R.C. §§ 354 and 368. Several tax-free corporation acquisitions, known as reorganizations, are available: (1) AA reorganization,@ a statutory merger; (2) AB reorganization,@ an acquisition of a controlling interest in a target corporation=s stock in return solely for the stock of the acquiring corporation; (3) A C reorganization,@ an acquisition of substantially all of the target corporation=s assets in return for the stock of the acquiring corporation (and up to 20% taxable boot); and (4) Atriangular mergers,@ using subsidiaries of the acquiring corporation to merge into the target corporation using stock of the acquiring parent corporation. *See generally* I.R.C. § 368.

[175] *Id.*

[176] I.R.C. § 356.

[177] Rev. Proc. 2003-3, 2003-1 I.R.B. 113; *see also* Rev. Proc. 2012-1, 2012-1 I.R.B. 1.

[178] W. Va. Code § 31D-11-1102.

[179] W. Va. Code § 31D-11-1104.

[180] *Id.*

[181] *Id.*

[182] *Id.*

[183] *Id.*

[184] *Id.*

[185] W. Va. Code § 31D-11-1104(6).

[186] W. Va. Code §§ 31D-13-1301 *et. seq.; see also* Section VII, C. Appraisal Rights.

[187] W. Va. Code § 31D-11-1105.

[188] I.R.C. § 332. I.R.C. § 332 is generally applicable when the corporation parent owns at least 80 percent of the total voting power and 80 percent of the total value of the stock of the subsidiary. I.R.C. § 332 does not apply to insolvent corporations.

[189] W. Va. Code § 31D-11-1104.

[190] W. Va. Code § 31D-11-1105.

[191] W. Va. Code § 31D-11-1106.

[192] W. Va. Code § 31D-11-1106(a).

[193] W. Va. Code § 31D-11-1106(b).

[194] W. Va. Code § 31D-11-1106.

[195] *Id.*

[196] W. Va. Code § 31D-11-1107(a)(4).

[197] W. Va. Code § 31D-11-1103.

[198] W. Va. Code § 31D-11-1103(c).

[199] See W. Va. Code § 31D-11-1104 for action on a plan of merger or share exchange, W. Va. Code § 31D-11-1106 for articles of merger or share exchange and W. Va. Code § 31D-11-1107 for effect of merger or share exchange.

[200] W. Va. Code § 31D-11-1102.

[201] W. Va. Code § 31D-15-1504.

[202] W. Va. Code § 31D-12-1201.

[203] W. Va. Code § 31D-12-1202.

[204] *Id.*

[205] Note, W. Va. Code § 31D-11-1105, governing subsidiary mergers.

[206] W. Va. Code § 31D-13-1302.

[207] W. Va. Code § 31D-13-1302(b).

[208] W. Va. Code §§ 31D-13-1302(b)(3) and (4).

[209] W. Va. Code § 31D-13-1302(c).

[210] W. Va. Code § 31D-13-1302(d).

[211] W. Va. Code §§ 31D-13-1320 through -1331.

[212] W. Va. Code § 31D-13-1324.

[213] W. Va. Code § 31D-14-1401.

[214] W. Va. Code § 31D-14-1402.

[215] *Id.*

[216] I.R.C. § 6043.

[217] W. Va. Code § 31D-14-1403(a)(1)-(3) and (b).

[218] W. Va. Code § 31D-14-1403(c).

[219] W. Va. Code § 31D-14-1405(a).

[220] W. Va. Code § 31D-14-1406.

[221] W. Va. Code § 31D-14-1406(b).

[222] W. Va. Code § 31D-14-1406(b)(3).

[223] W. Va. Code § 31D-14-1406(c).

[224] W. Va. Code § 31D-14-1407.

[225] W. Va. Code § 31D-14-1404(a) and (b).

[226] W. Va. Code § 31D-14-1404(d).

[227] W. Va. Code § 31D-14-1420.

[228] W. Va. Code § 31D-14-1430(1).

[229] W. Va. Code § 31D-14-1430(2).

[230] W. Va. Code § 31D-14-1430(3).

[231] W. Va. Code § 31D-14-1430(4).

[232] *See generally* W. Va. Code § 31D-14-1430.

[233] W. Va. Code § 31D-14-1434. Note, the corporation must provide notice of such rights within ten days of the commencement of the proceeding. W. Va. Code § 31D-14-1431.

[234] W. Va. Code § 31D-15-1501(b).

[235] W. Va. Code § 31D-15-1503.

[236] W. Va. Code § 31D-15-1503; *see also* W. Va. Code § 31D-1-128.

[237] W. Va. Code § 11-12C-2.

[238] W. Va. Code § 31D-15-1505.

[239] W. Va. Code § 31D-15-1505.

[240] W. Va. Code § 31D-15-1502.

[241] W. Va. Code § 31D-15-1504.

[242] W. Va. Code § 31D-15-1504(b).

[243] W. Va. Code § 31D-15-1507.

[244] *Id.*

[245] W. Va. Code § 31D-15-1508.

[246] W. Va. Code § 31D-15-1530.

[247] W. Va. Code § 31D-15-1531.

[248] W. Va. Code § 31D-15-1532.

[249] W. Va. Code § 31D-15-1531(e).

[250] W. Va. Code § 31D-15-1520.

[251] W. Va. Code § 31D-15-1520.

[252] 26 C.F.R. §301.7701-3.

[253] *See* W. Va. Code §§ 31B-1-101 to -13-1306.

[254] *See, e.g.*, Treas. Reg. § 301.7701-3.

[255] *See generally* W. Va. Code §§ 31B-13-1301 to 13-1306.

[256] W. Va. Code § 31B-1-103(b). *See infra* part C; *see also* commentary accompanying Section 103 of the Uniform Limited Liability Act approved by the National Conference of Commissioners on Uniform State Laws in 1995.

[257] W. Va. Code § 31B-2-201.

[258] W. Va. Code § 31B-1-112. Unless its articles of organization provide otherwise, an LLC has the same powers as an individual to do all things necessary or convenient to carry on business or affairs, including the specific powers set forth in the Uniform LLC Act. *Id.*

[259] W. Va. Code § 31B-2-202(a). This rule is the same for professional limited liability companies. W. Va. Code § 31B-13-1302. This is a significant change from the 1992 LLC Act which required at least two members for LLCs formed prior to July 1, 1996. W. Va. Code § 31-1A-7 (repealed 1996).

[260] W. Va. Code § 31B-2-206.

[261] The LLCs name must contain the words Alimited liability company,@ Alimited company,@ or the abbreviation AL.L.C.,@ ALLC,@ AL.C.,@ or ALC.@ ALimited@ may be abbreviated as ALtd.@ and Acompany@ may be abbreviated as ACo.@ W. Va. Code § 31B-1-105.

[262] West Virginia LLCs can be Aterm@ or Aat-will@ LLCs. A term LLC means an LLC in which its members have agreed to remain members until the expiration of a term specified in the articles of organization. W. Va. Code § 31B-1-101(22). An at-will LLC means an LLC other than a term LLC. W. Va. Code § 31B-1-101(2). Unlike many states, e.g., Delaware, Virginia, or Kentucky, West Virginia law does not make express provision for LLCs to have perpetual duration. This probably occurred because at the time the Uniform LLC Act was adopted, Congress had not adopted the check-the-box regulations, potentially making the tax status of LLCs with perpetual life unclear. *See* Del. Code Ann. tit. 6, § 18-801.

[263] W. Va. Code § 31B-2-203.

[264] *Id.*

[265] W. Va. Code § 31B-1-101(13).

[266] *See* commentary accompanying Section 103 of the Uniform Limited Liability Company Act (1995) approved by the National Conference of Commissioners on Uniform State Laws in 1995.

[267] W. Va. Code § 31B-2-203(c).

[268] W. Va. Code § 31B-4-404(a).

[269] *Id.*

[270] W. Va. Code §§ 31B-2-203(a)(6), -4-404(b).

[271] *See, e.g.*, W. Va. Code §§ 31B-4-404(c), -8-801(b).

[272] W. Va. Code § 31B-4-404(b).

[273] W. Va. Code § 31B-3-301(c).

[274] W. Va. Code § 31B-3-303.

[275] W. Va. Code § 31B-1-101(8).

[276] W. Va. Code § 31-B-501 (b).

[277] *Id.*

[278] W. Va. Code § 31-B-5-502.

[279] *Id.*

[280] W. Va. Code § 31B-5-503(d). The rights of a transferee who does not become a member are more fully detailed in W. Va. Code § 31B-5-503(e). Additionally, the Uniform LLC Act contains specific provisions dealing with creditor rights. Generally speaking, they provide that a court may enter a charging order against the distributional interest of a judgment debtor to satisfy the judgment. W. Va. Code § 31B-5-504. Importantly, the LLC may redeem the charged interest if

such a right is contained in its operating agreement. *Id.* Both existing and newly formed LLCs may want to provide such a right.

281 W. Va. Code § 31B-5-503(a).

282 *See* W. Va. Code §§ 47-9-1 to -63.

283 W. Va. Code §§ 47B-1-1 to -11-5.

284 For an excellent discussion of the dissociation and dissolution provisions as they relate to general partnerships, *see* Donald J. Weidner and John W. Larson, The Revised Uniform Partnership Act: The Reporters Overview, 49 Bus. Law. 1, 3-16 (1993).

285 W. Va. Code § 31B-6-603(b). A dissociated member or the LLC may file a statement of dissociation in the Secretary of State's office stating the name of the LLC and that the member is dissociated from it. W. Va. Code § 31B-7-704.

286 W. Va. Code § 31B-6-601.

287 W. Va. Code § 31B-6-603.

288 W. Va. Code § 31B-8-801(b).

289 *Id.* Moreover, even after dissolution, but before the LLC's business is wound up, the members (including the dissociating member whose dissociation caused the dissolution) may unanimously waive the right to have the LLC's business wound up, in which case, generally speaking, the LLC resumes its business as if dissolution had not occurred. W. Va. Code § 31B-8-802(b).

290 W. Va. Code § 31B-6-603 and -7-701. The Uniform LLC Act devotes a considerable discussion as to how fair value is determined. Members may want to examine this definition to determine if it is consistent with their expectations or if they wish to vary this provision.

291 W. Va. Code § 31B-6-603(a)(2).

292 W. Va. Code § 31B-6-602(c). *See* W. Va. Code § 31B-6-602(b) (defining wrongful dissociation).

293 W. Va. Code § 31B-2-211.

294 W. Va. Code § 31B-8-809.

295 *See* Treas. Reg. § 301.7701-3.

296 *Id.*

297 Treas. Reg. §§ 301.7701-3, -301.7701-3T(a).

298 *Id.*

299 I.R.C. § 702.

300 I.R.C. §§ 11, 301, 311.

301 Treas. Reg. § 301.7701-3.

[302] *See* W. Va. Code § 47-9-19.

[303] I.R.C. § 162(l).

[304] I.R.C. § 1361(b)(1), (c)(6).

[305] I.R.C. § 1361(b)(3). Under prior law an S corporation could not own more than 79% of another corporation without threatening its subchapter S status.

[306] *Id*.

[307] *Id.*

[308] I.R.C. § 1361(b)(1)(D).

[309] *See* I.R.C. § 731.

[310] *Id.*

[311] I.R.C. § 311.

[312] W. Va. Code §§ 31B-11-1101 to -1104.

[313] W. Va. Code § 31B-13-1301.

[314] W. Va. Code § 31B-13-1306.

[315] W. Va. Code § 31B-13-1305(b).

[316] W. Va. Code §§ 31B-13-1302, -1305(e).

[317] W. Va. Code § 31B-9-902.

[318] *See, e.g.*, PLR 9415005 (Jan. 10, 1994); Rev. Rul. 95-37, 1995-17 I.R.B. 10.

[319] *See* W. Va. Code §§ 31B-9-901 to -903, -907. The Uniform LLC Act also contains specific provisions dealing with mergers. *See* W. Va. Code § 31B-9-904 to -907.

[320] W. Va. Code § 31B-9-903.

[321] *Id.*

[322] W. Va. Code § 31B-9-902.

[323] Rev. Rul. 95-37, 1995-17 I.R.B.10; Rev. Rul. 84-52, 1984-1 C.B. 157.

[324] W. Va. Code § 31D-11-1109.

[325] *Id.*

[326] *Id.*

[327] Rev. Rul. 99-5, 1999-6 I.R.B. 8.

[328] *See id.*; *see also* I.R.C. § 721. Note that contribution to an LLC which qualifies as an Ainvestment company@ will not be tax-free. I.R.C. § 721(b) and Treas. Reg. 1.351-1(c).

[329] I.R.C. § 708.