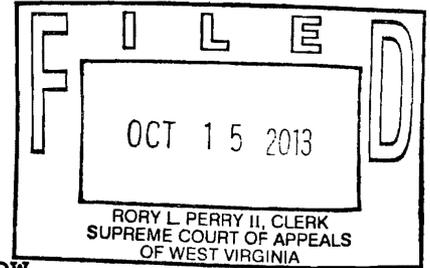


IN THE SUPREME COURT OF APPEALS OF WEST VIRGINIA

Docket No. No. 13-0742
CONFIDENTIAL CASE



IN RE:
THE MARRIAGE OF
KIMBERLEY A. MORRIS,
Petitioner and Respondent Below,
and
DOUGLAS SHANE MORRIS,
Respondent and Petitioner Below.

From the Circuit Court of Gilmer County,
West Virginia

BRIEF OF RESPONDENT DOUGLAS SHANE MORRIS

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Rule 18(a)(3), WVERRAP

Rule 19, WVERRAP

STATEMENT OF FACTS AND NATURE OF THE RULING BELOW

This case concerns the validity of a post-nuptial agreement signed by the parties, Kimberley A. Morris and Douglas Shane Morris, nearly three years prior to filing for divorce in 2012, and the treatment of corporate retained earnings in the distribution of property.

Although not required under Rule 10(d) of the West Virginia Rules of Appellate Procedure, it is necessary to include this statement of the case to supplement Petitioner's presentation of the facts leading up to the Family Court's evidentiary findings regarding the validity of the Agreement Respecting Marital Rights (the "Agreement"), the Circuit Court's analysis of the Family Court's decision, and Circuit Court's application of the law in upholding the validity of the Agreement. Unfortunately, Petitioner's Statement of the Case is replete with irrelevant, unsubstantiated, and frequently inaccurate factual allegations and characterizations of the proceedings below, which have no support in the Appendix Record,¹ and which were not a part of the evidence presented to the Family Court.

¹ Petitioner chose not to include in the Appendix Record the transcripts of the evidence presented in Family Court regarding the Agreement and the circumstances surrounding its formation.

The relevant facts are as follows:

The parties were married on June 30, 1992. Prior to their marriage, the couple voluntarily entered into a pre-nuptial agreement which was substantially similar to the agreement that is the subject of this appeal. Sometime after the marriage, however, they mutually rescinded their pre-nuptial agreement. Appendix, p. 54. Later, however, on February 11, 2009, the parties reinstated the pre-nuptial agreement previously in place, and entered into a post-nuptial agreement respecting their marital rights going forward. In the resulting Agreement Respecting Marital Rights ("the Agreement") -- the subject of the lower courts' scrutiny -- the parties acknowledged their "loving and caring relationship" and expressed their mutual intent and belief that "theirs will be a long and lasting relationship, and have entered into this Agreement with the express intention of achieving this goal." Appendix, p. 2.

The terms of the Agreement, distinctly spelled out, contemplate a specific distribution of marital property upon divorce. The Agreement states that "all joint and marital property shall be divided equally," but that Petitioner/wife "shall have the option of occupying the residence located at 230 Hillcrest Drive, Glenville, West Virginia, rent free, and Husband

shall assume and pay the then current mortgage on said residence, or Husband and Wife shall sell said residence, pay the mortgage in full and Wife shall receive all excess funds from the sales proceeds left after the mortgage is paid in full." Appendix, p.

8. The Agreement also provides for significant long-term financial support for the wife, stating that "if the marriage is dissolved by a decree or order of divorce, Wife shall receive a monthly payment from Husband in the amount of \$5,000.00 for the shorter of fifteen (15) years from the date of such order or divorce decree or the first day Wife remarries or cohabitates with another man." Appendix, p. 9.

In the Agreement, Petitioner warrants that she "understands the nature and extent of her rights in and to the estate of Husband under the law in the absence of execution of a postnuptial agreement and she understands that this Agreement is a postnuptial agreement; ... she is entering into this Agreement freely and voluntarily, under circumstances free of fraud, duress or misrepresentation, and with full knowledge and understanding of its provisions and their legal effect; [and that] this Agreement is substantially and fundamentally fair, equitable and reasonable." Appendix, p. 10. Petitioner further acknowledged that "she has had the opportunity to fully deliberate the terms

of this Agreement and to seek the advice of independent legal counsel regarding this Agreement and the matters contemplated herein and has had the advice of Timothy B. Butcher, Esq." *Id.* Petitioner warrants and agrees that "she has an adequate knowledge of the property, expectancies, debts and obligations of Husband and understands that such net worth is as shown on Exhibit A." She "voluntarily and expressly waives any right to disclosure of the property, expectancies, debts or obligations of Husband beyond the disclosure provided by Exhibit A." *Id.* Significantly, Exhibit A to the Agreement clearly and unequivocally sets forth that Respondent has an interest in Flying "W" Plastics, Inc., a closely held business entity, valued at \$4,500,000.00. Appendix, p. 15. The Agreement states that Respondent's equity interest in Flying "W" Plastics, Inc. is "expressly included in the definition of Separate Property." Appendix, p. 5. The Agreement also makes clear that any appreciation in the value of Respondent's equity interest in the company shall also be considered the separate property of the Respondent. *Id.*

There is no express language in the Agreement stating that a promise from Respondent's father to provide financial assistance needed to build a new \$750,000.00 home for the parties to live

in, was given as consideration for any term or condition in the Agreement.²

Approximately three years after making the Agreement, on February 23, 2012, the Respondent herein, husband Douglas Shane Morris, filed a Petition for Divorce from his wife, Kimberley A. Morris, in the Family Court of Gilmer County, West Virginia. In the divorce proceedings, Petitioner/wife opposed the enforcement of the Agreement, alleging that the Agreement was entered into as a result of undue influence by a third-party, duress, and coercion. The Family Court provided the parties an opportunity to brief the legal issues surrounding the validity of the Agreement, set aside one-half day for the presentation of the evidence on the validity of the Agreement, and gave the parties an additional opportunity to argue the factual issues related to the enforcement of the Agreement. Appendix, pp. 25 - 26.

Over the course of two days in June and July 2012, the Family Court heard evidence related to Petitioner/wife's challenge to the validity of the Agreement. At those hearings, Respondent/husband presented evidence and witnesses supporting his argument that the Agreement was fair, was not the product of

²Nonetheless, the evidence below supported the theory expressed by Petitioner that both parties desired that Respondent's father should assist them in building an "upscale home." Appendix p. 31 "([T]he parties were wanting a new house.") (emphasis supplied).

fraud, duress, or coercion, was knowingly signed by Petitioner/wife, with full disclosure of its terms and effect, after having consulted with independent counsel, and that the agreement was therefore valid and enforceable. The Court also heard testimony and evidence regarding the origin and value of the Respondent/husband's interest in Flying "W" Plastics, Inc. During these hearings, Petitioner/wife testified that she did not know that the agreement "had anything to do with divorce or anything of that nature." The Family Court dismissed this argument, finding her testimony was not credible. Appendix, p. 33.

Petitioner/wife called no witnesses and presented no evidence to rebut the presumption that the Agreement was valid and enforceable, or otherwise support her contention that the Agreement was the product of coercion, undue influence, or fraud, although she did testify, as the husband's adverse witness, and her counsel cross-examined the other witnesses.

On August 9, 2012, based on all the evidence presented at the hearing, and oral argument of counsel, the Family Court entered its detailed Order Upholding Agreement Respecting Marital Rights, announced at the conclusion of the evidence, wherein it weighed and summarized the evidence presented, and set forth

Findings of Fact and Conclusions of Law regarding Petitioner/wife's challenge to the validity of the Agreement. Appendix, pp. 28 - 36. In that Order, the Family Court upheld the Agreement and ruled that "[b]ecause the [Agreement] was freely, voluntarily, and knowingly executed, without force, threat, promise or undue influence, there is no reason why it should not be enforced." Appendix, p. 34. The Court elaborates:

(1) "The 'four corners' of the document describe, and the parties each acknowledged in the document that there had been full disclosure, and the document contains detailed exhibits which set forth the assets and liabilities of the parties, with assigned values." Appendix, p. 29.

(2) "If, in fact, this asset [husband's interest in Flying "W" Plastics, Inc.] is a separate asset not subject to distribution in the parties' divorce case, then there is little disparity in the division of assets as contemplated by the agreement." *Id.*

(3) "The estimated value of the petitioner's [husband, Doug Morris] interest in Flying W Plastics, Inc. in 2009 may have been substantially overstated, considering the income of the corporation at that time." Appendix, p. 30.

(4) "The parties were each represented by separate counsel as shown by the document and by the testimony received at the hearing." *Id.*

(5) "Timothy Butcher, who represented the [wife, Kimberley Morris], is an attorney who currently has been practicing law for 32 years, and who is recognized as one of, if not the, pre-eminent tax law attorneys in the local area. He regularly deals with corporate law, contracts and estates, and has experience in family law." *Id.*

(6) Attorney Butcher, on behalf of his client Kimberley Morris, negotiated several favorable terms for his client, including that his client would be entitled to the marital home, and \$5,000 monthly alimony, in the event of a divorce. Appendix, p. 31.

(7) Attorney Butcher, clearly advocating for his client, Ms. Morris, and not a third-party, advised his client not to sign the agreement, but her desire to have a new home built for her and Mr. Morris was her "overriding concern." Appendix, p. 32.

(8) The question of whether Mr. Morris's father's promise to build the parties a brand new upscale home constituted "third-party influence," was "irrelevant to the validity of this contract." *Id.*

(9) "Kimberley Morris, has a college degree, is well-educated and knew exactly what she was signing." Appendix, p. 34.

(10) The Agreement was validly procured, and therefore enforceable, under the guidelines laid out in Ware v. Ware, 224 W. Va. 599, 687 S.E.2d 382 (2009). Appendix, p. 33.

11) Lastly, the Family Court inexplicably held that, even though the Respondent's husband's interest in Flying "W" Plastics, Inc. was clearly a separate asset of Mr. Morris, the retained earnings of the company, or undistributed profits held by the company, were "marital" in nature because those retained earnings had been taxed to the Morrises as if they were the income of the marital couple. Appendix, p. 34.

After the Family Court had determined that the terms of the Agreement regarding distribution of marital property should be upheld, the Court held a final divorce hearing on December 26, 2012³. There was still a need for further hearing because, at

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Actually, soon after upholding the post-nuptial agreement, the Family Court erroneously dismissed the case after it had been pending seven months, based on

that time, there was no admission of irreconcilable differences and grounds for divorce were contested. A key witness at the final hearing was Eric Brown, a certified public accountant and the comptroller for Flying "W" Plastics, Inc., who was qualified and testified as an expert witness. His testimony focused primarily on the financial management of Flying "W." He explained the tax differences between a C-corporation and an S-corporation, and that this particular corporation became an S-corporation on July 1, 2007. He testified that the Respondent/husband Doug Morris, is the president, and his sister, Shelly DeMarino, is the secretary/treasurer, and that they have been the sole shareholders since the death of Kenneth Greenlief a few years earlier.

Mr. Brown testified that the net income of Flying "W" is down 40%, and "things are slow now." He described the retained earnings, or accumulated adjustment account ("AAA"), of the corporation as the "lifeblood of keeping the company afloat," and how it is treated by the IRS as a corporate asset and not a personal asset of the shareholders. When specifically questioned by the Family Court Judge about what would happen with the AAA in

the time-standards requiring that 75% of divorce cases be completed in eight months. The parties jointly appealed this dismissal to the Circuit Court, which reversed the dismissal and remanded the case to the Family Court for hearing. Upon getting the decision, the Family Court scheduled the hearing for 9:00 a.m. on the day after Christmas in Glenville.

the event that the corporation closed its doors, he described the process by which all of the liabilities, including expenses, loans, and money owed to employees, would have to be determined before any distributions were made. Upon further questioning, expert Brown testified that forcing the company to surrender its retained earnings -- paying out \$2.5 million -- would have a severe and detrimental effect on the company's operations. He expressed reservations about whether the company could continue to keep its doors open. Appendix, p. 59 - 60.

At the December 26, 2012 hearing, no additional evidence or testimony was elicited regarding the previously-settled matter of the validity of the Agreement. Nor was there any evidence presented to rebut the Respondent/husband's testimony at the hearing on the validity of the Agreement that his interest in Flying "W" Plastics, Inc. was his separate property, acquired by gift. Nonetheless, in its Final Divorce Decree entered following the hearing, the Family Court reversed its earlier decision upholding the Agreement because it found that the Agreement "would not achieve an equitable distribution of the parties' property as contemplated by W. Va. Code 48-7-101 et seq." taking into consideration other assets not covered by the Agreement -- particularly the retained earnings of Flying "W" Plastics.

Appendix, p. 41. The Court then set aside the Agreement, and distributed what it considered to be the marital assets, including an order that required the parties to sell their marital home and all furnishings and appliances as soon as possible, splitting equally the net proceeds of the sale. The Family Court Judge announced, that day, that the Order was "effective from pronouncement." At no point during the proceedings, or in any Order, did the Family Court ever hold that the Agreement Respecting Marital Rights was the result of fraud, duress, undue influence, or coercion.

At this final hearing, the Family Court also Ordered the Respondent/husband to transfer to the Petitioner/wife one-half (½) of his interest in Flying "W" Plastics, Inc. In doing so, the Court ignored the evidence that the Respondent's interest in Flying "W" Plastics, Inc. was gifted to him by his father, and that under West Virginia law, his interest in the company is therefore considered his "separate property." Appendix, p. 55 (footnote 2). The Family Court's Final Divorce Decree is devoid of any legal analysis, or discussion of any new evidence, to support its decision to void the Agreement. Although the Family Court had already given Petitioner one-half (½) of Respondent's shares in Flying "W" Plastics, Inc., the Family Court then also

gave Petitioner a share of the retained earnings of the company itself. This last ruling, awarding the retained earnings, was not announced by the Family Court at the December 26, 2012 hearing, but was hand-written by the Family Court Judge into the Final Divorce Decree submitted after the hearing.

Respondent/husband successfully appealed the Family Court's order to the Circuit Court, and was granted a stay while the appeal was pending. In the appeal, he asked the Circuit Court to vacate the ruling which set aside the Agreement and awarded the wife half of his interest in Flying "W" Plastics, Inc., and the subsequent award of retained earnings to her. The Circuit Court agreed that the wrong analysis had been applied to set aside the Agreement, and further found that the retained earnings were improperly classified as "marital property" of the couple, and that Petitioner/wife had expressly waived any claim to this asset of the corporation. The Circuit Court applied straightforward West Virginia law, in affirming the initial decision of the Family Court that the Agreement was not the result of undue influence or other factors claimed by the Petitioner/wife. Since the retained earnings were improperly classified as marital property, this fact could not make the Agreement "inequitable,"

as the Family Court had determined. It is from the Circuit Court's ruling that the Petitioner/wife appeals.

SUMMARY OF ARGUMENT

By this appeal, Petitioner is attempting to acquire half of Respondent's valuable separate property consisting of his interests in Flying "W" Plastics, Inc. However, Petitioner faces several significant legal hurdles. First, during the marriage, when both parties were happily married and anticipated remaining married, the parties executed a valid and enforceable post-nuptial agreement wherein Petitioner/wife acknowledged Respondent/husband's interest in Flying "W" Plastics, Inc. was the Husband's separate property -- valued at approximately \$4.5 million (including retained earnings) and gifted to him by his father -- and then knowingly and permanently waived any marital interest that she might arguably have had in that company. Further, notwithstanding the waiver, the husband's interest in Flying "W" Plastics, Inc. has always been his "separate property" under West Virginia law, and is not subject to equitable distribution in divorce. Next, even if the terms of the Agreement resulted in a substantially inequitable distribution of property, the Agreement was nonetheless validly procured, and

fundamentally fair, as that term is interpreted in the context of marital agreements, as expressed by this Court in Gant vs. Gant, 174 W.Va. 740, 329 S.E.2d 106 (1985). The Family Court's reasoning for finding the Agreement to be "inequitable," and therefore invalidating the Agreement, is fundamentally flawed: the retained earnings of a corporation belong to the company itself, not its shareholders; the company's retained earnings were necessarily accounted for and included in the valuation of the company as disclosed to Petitioner prior to signing the Agreement; and therefore, retained earnings should never be the sole basis of a judicial determination that a contemplated distribution of marital assets is inequitable.

In her Brief, Petitioner relies on several alleged Assignments of Error, all of which center upon the argument that enforcement of the Agreement would result in an inequitable or unfair distribution of marital property. First, Petitioner contends that the Circuit Court committed error by not employing an indeterminate, but higher, standard of review for "post-nuptial" agreements. She then argues that enforcement of the Agreement would not withstand this higher scrutiny because the Agreement is unfair. In support, Petitioner argues that distribution of marital assets contemplated by the Agreement was

"vastly disproportionate," and the Agreement omitted or misrepresented the value of marital property and income. In support of her contention that the Agreement was unfair, Petitioner also argues that the Agreement was the product of coercion, undue influence or duress.⁴ Finally, Petitioner's argument that the Agreement should be set aside as inequitable and unfair is based on her presumption that the Respondent's interests in Flying "W" Plastics, Inc., as well as the retained earnings of the company, are marital property, thus tipping the balance of the distribution heavily in favor of Respondent/husband.

Regarding Petitioner's first Assignment of Error, West Virginia does not recognize a distinction between post-nuptial agreements and pre-nuptial agreements when assessing the validity of a marital, or separation agreement. See W. Va. Code §48-6-101 et seq. Recognizing this, the Circuit Court properly applied West Virginia law by examining whether both parties to the Agreement were represented by independent counsel. Affirming the Family Court's finding that the parties were both adequately represented

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Petitioner's argument regarding coercion, undue influence, or duress, was not an express assignment of error in her Brief, but is incorporated into her second Assignment of Error -- that the Agreement was generally unfair. Both the Family Court and the Circuit Court below rejected the Petitioner's argument that the Agreement was the product of coercion, undue influence, or duress, and focused instead on whether the Agreement was inequitable.

by independent counsel, the Circuit Court then analyzed whether the document was executed voluntarily, with knowledge of its content and legal effect, under circumstances free of fraud, duress, or misrepresentation, was not unconscionable, and was therefore validly procured. Again, the Circuit Court examined these factual issues, affirmed the Family Court's findings, and held that the Agreement was validly procured and should be upheld under principles expressed in Gant v. Gant, 174 W.Va. 740, 329 S.E.2d 106 (1985), and Ware v. Ware, 687 S.E.2d 382, 384 (2009). The Circuit Court then properly ordered the distribution of property to proceed in accordance with the intent of the parties as expressed in the Agreement.

This case presents no valid reason to change the law in West Virginia regarding interpretation of marital agreements, or to require the Circuit Court to deviate from its straightforward application of West Virginia law as stated in its Order. In this matter, applying Petitioner's proposed but undefined "heightened scrutiny" to the Agreement serves no purpose. In Gant, supra, this Court carefully examined modern marital contracts, recognizing that "courts still reserve more authority to review the substantive terms of prenuptial contracts than they do commercial contracts," and establishing a court's right to

conduct a limited inquiry into the fairness of marital agreements, inquiring whether the agreement is unconscionable as that term is defined under contract law. Thus, the circumstances and reasoning behind Petitioner's proposed "special scrutiny" for certain marital agreements, over and above traditional contract law, was considered and largely adopted by this Court in Ware and Gant.

Further, the alleged undue influence, coercion, or duress, that Petitioner suggests deserved more careful scrutiny at the lower court level, was duly considered by the Family Court. The Family Court rejected the allegation that the Agreement was the product of undue influence, coercion or duress, and the Circuit Court affirmed that factual finding. Petitioner cannot demonstrate that additional or "heightened scrutiny" of the validity of the Agreement is necessary or proper in this case, or as a practical matter, would have made any difference.

Addressing Petitioner's second Assignment of Error, even if this Court were to change the established analysis of the validity and enforceability of marital agreements as set out in Gant and Ware, the distribution of marital property set forth in the Agreement is clearly more than fair to the Petitioner. The Petitioner's second Assignment of Error, that the Agreement was

unfair and inequitable, relies on misrepresentations of the facts, and inappropriately uses the company's assets, or retained earnings, to shift the balance of the distribution in favor of the Respondent. In fact, the actual distribution of marital assets contemplated by the Agreement weighs heavily in favor of the Petitioner/wife, who would share equally in all marital property, but also receive the entire value of the marital home worth approximately \$750,000.00, the parties' marital asset of greatest worth. In short, Petitioner's argument that enforcement of the Agreement would achieve an unfair or inequitable result misconstrues or misstates the facts, and is demonstrably false. It is the Petitioner/wife who gets the overwhelming majority of marital assets.

Lastly, Petitioner's argument that the Accumulated Adjustment Account ("AAA"), or retained earnings, of Flying "W" Plastics, Inc., is the marital property of the couple subject to equitable distribution in divorce, is simply untenable. The bedrock legal principle to be observed in examining the retained earnings of a Subchapter S-corporation in this context is that the retained earnings are the property of the company itself, and not the shareholding spouse. Retained earnings are the undistributed profits of the company, and they should be no more

subject to equitable distribution than the company's computers, inventory, pallet jacks, trust accounts, insurance, or any other asset belonging to the company. Petitioner's Brief presents the Court with a "red herring," suggesting that the tax structure of the S-corporation, in which tax on company profits "flow through" to the shareholders, should operate to somehow convert company property to marital property.

Such an interpretation of an S-corporation's retained earnings is fundamentally incorrect, represents a myopic approach to the bigger question of the spousal interest in the S-corporation, creates the danger of double recovery for the non-shareholding spouse, and potentially unfairly degrades the shares of other shareholders. Moreover, such an interpretation would have potentially devastating repercussions on the administration and management of S-corporations in this State. Accordingly, the decision of the Circuit Court regarding the retained earnings of Flying "W" Plastics, Inc. should not be disturbed.

STATEMENT REGARDING ORAL ARGUMENT AND DECISION

This appeal presents a dispositive issue that has been authoritatively decided. Accordingly, under West Virginia Rule of Appellate Procedure Rule 18(a)(3), oral argument is

unnecessary. If the Court determines that oral argument is necessary, the case is suitable for Rule 19 oral argument, as Petitioners bring assignments of error which trigger the application of settled law.

ARGUMENT

I. The Circuit Court Applied the Proper Legal Standard in Upholding and Enforcing the Parties' "Agreement Respecting Marital Rights."

The Petitioner's first Assignment of Error contends that the Circuit Court erred in applying settled West Virginia law regarding the validity and enforcement of marital agreements, and not a stricter standard requiring closer examination of whether the distribution of marital property contemplated by post-nuptial agreements is equitable, or fundamentally fair. However, the Circuit Court's application of West Virginia law was correct, and this case presents no valid basis to impose a higher standard in evaluating the validity and enforceability of post-nuptial marital agreements.⁵ Moreover, the distribution of assets

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Notably, the one West Virginia case cited by the Petitioner, expressly stated that "[w]e think the question of whether the marriage settlement contract is to be considered as being antenuptial or postnuptial can be of little significance, however, in view of our construction of the contract." Welsh v. Welsh, 69 S.E.2d 34, 37 (W. Va. 1952). Even so, much of guidance in Welsh was clearly overruled by Gant v. Gant, 174 W. Va. 740, 745, 329 S.E.2d 106, 111 (1985).

contemplated by the Agreement in this case was, in fact, fundamentally equitable.

In the West Virginia case of Gant v. Gant, the lower court had invalidated a pre-nuptial marriage agreement on the grounds that the agreement was "unfair, inequitable, overreaching, and that it did not take into account the size of the parties' estates." 174 W.Va. 740,745, 329 S.E.2d 106, 111 (1985) (overruled on other grounds by Ware v. Ware, 224 W. Va. 599, 687 S.E.2d 382 (2009)). In Gant, this Court took a long look at the legal history of marital contracts, the changing landscape of social attitudes toward marriage, and applied a reasoned approach to enforcement of marital agreements that focused on the validity of the agreement, and the foreseeability of the consequences of the agreement. The Gant Court recognized that "the basic requirement of a prenuptial contract is fundamental fairness...under the totality of the circumstances." Gant, at 745, 112. However, the Court noted that:

[Marital agreements] will almost always be entered into between people with property or an income potential to protect on one side and people who are impecunious on the other. Measuring an agreement by an undefined judicial standard of fairness is an invitation to the very wealth redistribution that these agreements are designed to prevent."

Gant, at 114, 748. The Court stated that "we are loathe to apply a vague and entirely subjective standard of 'fairness.'" *Id.* Instead, borrowing from the reasoning of other jurisdictions, the Gant Court stressed that "fairness" in the setting of a marriage agreement, is concerned with "foreseeability." *Id.* at 114-115, 748. In Gant, the Court applied this foreseeability/fairness inquiry and found that, in that case, "circumstances have transpired exactly as the parties foresaw that they might transpire at the time the prenuptial agreement was made." In other words, as the Gant Court emphasized, "fair" means that "you saw this coming."

Lastly, the Court expressly rejected an analysis that focused on whether a marital agreement was equitable, or substantially fair. "[N]o matter what rules we adopt there will be cases when the application of those rules will be inequitable ... Unless a prenuptial agreement is so outrageous as to come within the unconscionability principles as developed in commercial contract law, W. Va. Code §46-2-302 [1963], West Virginia courts will not evaluate the substantive fairness of prenuptial agreements; most prenuptial agreements are designed to protect the property interests of the stronger party." *Id.* at 116, 749.

Applying Gant's reasoning to this case, it is clear that no error was committed by the Circuit Court in upholding and reinstating the Agreement. The Family Court's error in invalidating the Agreement because it created an "inequitable" or unequal distribution of property was based on its clearly wrong finding that retained earnings were "marital property." The Circuit Court corrected that error. The Agreement was not unconscionable as the Petitioner/wife suggests, claiming that the Respondent/husband was to receive 98.11% of the assets, compared to the Petitioner/wife's 1.89%. Excluding the clearly separate asset of Flying "W" stock, the marital assets were actually to be divided nearly equally, as the Family Court found, not even counting or considering that the Petitioner/wife would enjoy ownership and sole possession of the parties' upscale \$750,000 house. If anything would "shock the conscience" it is that the Petitioner/wife walked away with the parties' major marital asset, the home. However, the Respondent/husband was clearly fine with that and did not and does not complain. There is nothing "unfair" about upholding this Agreement. Just like in Gant, things transpired just as the parties expected or foresaw in three short years after they made the Agreement.

Petitioner/wife's theory that post-nuptial agreements should be judged by a different, higher standard than pre-nuptial agreements does not withstand rational scrutiny. Unlike couples contemplating marriage, spouses have lived the reality of marriage and do not need to engage in speculation, but can create contracts which confront the problems they are currently facing. Such agreements are, if anything, likely to be more equitable than the pre-nuptial agreements, and they are largely self-regulating. The spouse who chooses not to sign a post-nuptial agreement has an alternative: divorce. By entering into a post-nuptial agreement, spouses are contracting, privately, to assure a certain and predictable result, if, in fact, the divorce alternative becomes necessary.

In the case of the Morrises, Petitioner/wife, by signing the Agreement, guaranteed that she would have the ownership and possession of the "upscale" \$750,000 house and its possessions, half of the other marital assets, and substantial spousal support, equaling \$900,000 alone, were she to remain unmarried for fifteen (15) years following a divorce. What did she give up? Nothing, really, inasmuch as the Respondent/husband's interest in the closely-held corporation would have been his "separate property" not subject to distribution in the divorce.

Her gains, however, were substantial. What did he give up? 1) The uncertainty of a spousal support award, since this state has no alimony formula and the amount which might have been awarded his stay-at-home wife would have solely been the decision of a single judge, and 2) an "upscale" home, which really was not an overriding concern for him. It is interesting to note, too, that when the Family Court stopped the agreed monthly spousal support award in favor of a "lump sum" spousal support grant of half of the Respondent/husband's stock, effective January 1, 2013, Petitioner/wife soon afterwards claimed to be in "dire financial straits." Appendix, p. 107.

II. The Petitioner's Second Assignment of Error Regarding the Validity of the Agreement Has No Basis in the Record and Is Contrary to the Factual Findings of Both the Family Court and the Circuit Court

The Petitioner/wife's challenge to the validity of the Agreement ignores that the Agreement both contemplated and provided for an equitable division of property. Moreover, a promise by a third-party to assist the couple in building a new upscale home, which they could not otherwise afford on their own, cannot constitute coercion, undue influence, or duress. Finally, her claim that she was not represented by "independent counsel" has no support in fact.

The Agreement specifically says "All joint marital property shall be divided equally between the parties, by value." Appendix, p. 8. As the record unequivocally shows, the Respondent/husband was not assigned a "vastly disproportionate" percentage of marital assets, there was full and complete disclosure as to what property each party owned separately and as a couple, and there was not a "severe" understatement of the Respondent/husband's annual income. Again, the Petitioner has inaccurately stated the factual record and is misleading in her representations. The Circuit Court, in its Order (Appendix, p. 144) and the Family Court, in its initial findings regarding the Agreement (Appendix, p. 28), were unanimous in their findings and conclusions that there was no fraud, duress, or misrepresentation among the parties when the Agreement was made.

The Respondent/husband's interests in Flying "W" Plastics, Inc., as established at the hearings in June and July 2012, were his "separate property" under West Virginia law, inasmuch as he acquired this stock by gift from his father.⁶ W. Va. Code §48-1-

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Again, the Petitioner/wife has misstated facts, by telling this Court that the issue of the Respondent/husband's acquisition of his interests in Flying "W" were first raised in the Circuit Court on appeal. Quite the contrary, this was the subject of specific testimony by the husband at the hearings in Family Court regarding the validity of the Agreement. Reference is made to the Family Court's Order Upholding Agreement Respecting Marital Rights Executed on February 11, 2009, to show that this was, in fact, considered by the Family Court. See Appendix, p.29.

237, in defining "separate property," includes "property acquired by a party during a marriage by gift, bequest, devise, descent or distribution." The Petitioner/wife offered no evidence to the contrary. Moreover, this fact was never in issue at the December 26, 2012 hearing, inasmuch as the Family Court had already held that the Agreement was to be enforced and in the Agreement, the Petitioner/wife had expressly acknowledged that Respondent/husband's interest in the corporation was "separate property," and as the Circuit Court ruled, she had "signed away any potential rights of claims she may have had to the Flying "W" Plastics in the Post-Nuptial Agreement." Appendix, p. 150. In her brief, Petitioner/wife now claims that the active appreciation, or increases in the corporation's value during the marriage, on account of the Respondent/husband's labors, are marital property and should have been considered, but that was clearly and unequivocally waived by her in the Agreement. Appendix, p.5.

As discussed above, the division of marital assets contemplated by the agreement was intended to be equal. Petitioner/wife's claim that the division is "vastly disproportionate" necessarily lumps together that which is "marital property" and that which is "separate property." Simple

math shows that adding the value of Flying "W" Plastics, Inc. stock to the total assets, and then distributing them as contemplated by the Agreement would not be an "equal" distribution. However, it is not proper to add that asset because it was not subject to distribution either according to the Agreement or, absent the Agreement, because it clearly meets the statutory definition of "separate property" not subject to distribution.

The Respondent/husband also takes great issue with the claim that he "severely underestimated" his annual income at the time the Agreement was made. Moreover, the Petitioner/wife signed the tax returns and could see for herself exactly what her husband's income was, and what it had been. Portions of the parties' 2006 income tax return (before Flying "W" became an S-corporation), their amended 2008 return (filed on March 15, 2010) and their 2010 return (filed on October 15, 2010) were made Appendix exhibits, purportedly to support the Petitioner/wife's claim. However, the 2006 return showed less income than was disclosed with the Agreement's Exhibit A, and the other returns post-dated the Agreement. Appendix, p. 152 - 159.

Petitioner inexplicably asks the Court to revisit allegations of coercion, undue influence, or duress, on appeal.

Neither the Family Court, after hearing all the evidence, nor the Circuit Court, after reviewing the Family Court record, ever found there to be any coercion, undue influence, or duress in the formation of the Agreement. Even so, the Petitioner's argument that Respondent's father's promise to build the couple a brand new, "upscale home" constituted coercion, undue influence or duress, is patently illogical. First, Respondent's father is not a party to the Agreement. Second, the Agreement makes no mention of a promise by a third-party to assist with building a new home as a gift to the parties, or as consideration for any term or covenant within the Agreement. Most importantly, however, Petitioner fails to address the critical question of why a third-party's gratuitous promise to build a home for the couple to live in -- which neither of them could afford on their own -- somehow means the entire agreement is the product of coercion, undue influence, or duress. Many, if not most married couples do not have wealthy parents, or in-laws, with the means to buy them expensive gifts -- that fact does not make their marital covenants any more, or less, legally enforceable. Petitioner seems to suggest that, but for her father-in-law's promise to build a brand new home that the couple could not afford on their own, and which would be given to the Petitioner herself upon a

divorce or dissolution of marriage, she would never have signed the Agreement in the first place. Even if Petitioner's contention were true, Petitioner's argument conflates "coercion, undue influence, or duress" with good and valuable consideration for a contractual bargain. Finally, the Petitioner's argument ignores the facts that the home was built and the couple resided in it until their 2012 separation, the Petitioner is the sole current resident in the home, and the Respondent stands ready to carry out terms of the Agreement by paying the mortgage, or selling the home and distributing the proceeds to the Petitioner. In sum, the issue of the brand new upscale home has no place in the discussion of the validity of the Agreement.

Finally, As both the Family Court and the Circuit Court found, the Petitioner/wife was represented by independent and competent counsel, Timothy B. Butcher, in negotiations regarding the Agreement. This was the same lawyer who represented the Petitioner/wife when she signed the original pre-nuptial agreement prior to the marriage, seventeen (17) years earlier. The Family Court, well aware of Mr. Butcher, made explicit findings that he was both independent and competent. The Family Court further found that Mr. Butcher, on behalf of his client Kimberley Morris, negotiated several favorable terms for her,

including that she would be entitled to the marital home, and \$5,000 monthly alimony, in the event of a divorce. Appendix, p. 31. Importantly, advocating for her, Mr. Butcher advised Mrs. Morris not to sign the Agreement.

It is beyond belief that the Petitioner/wife would argue that her attorney was not independent when he negotiated many significant terms for her and especially, when he urged her not to sign the Agreement. If he was working for the Respondent/husband, he surely would have advised her to sign the Agreement, particularly when it was first presented, without any of the major changes he negotiated for her.

The fact that the Petitioner/wife did not pay Mr. Butcher's fee is irrelevant and distinguishable from the issue in Ware v. Ware. The issue in Ware was that the attorney was representing BOTH parties. (emphasis on "both" in original at 607, 390 of Ware.) Thus, in Ware, the attorney's statement to the wife that he would adequately represent her interests could not have been accurate. Mrs. Ware was denied her "opportunity" to seek independent legal counsel, because his representations took that opportunity away. That was clearly not the case with Mrs. Morris and Mr. Butcher, who had been her long-term lawyer.

Petitioner/wife's argument that the Agreement should be considered invalid because she did not receive the benefit of independent counsel is ironic, in that she is now asking the Court to treat the Agreement as if it was never signed to begin with--the very advice her lawyer, Mr. Butcher gave her in 2009. Petitioner cannot argue it both ways, contending that her counsel was ineffective, and also contending that this Court should structure her relief as if she had taken his advice. See Burnsworth vs. George (W. Va. No. 12-0991, October 3, 2103).

III. This Court should affirm the holding of the Circuit Court below that the retained earnings of Flying "W" Plastics, Inc., a corporation in which the Respondent/husband owned shares, were not subject to distribution in this divorce action because they were not "marital property" and because the Petitioner/wife waived any claim to such retained earnings in the valid Post-Nuptial Agreement.

In the Circuit Court Order reversing the ruling of the Family Court, it was clear that the Family Court had exceeded its jurisdiction by allocating to the Petitioner/wife certain retained earnings of Flying "W" Plastics, Inc., which the Respondent/husband did not own and could not convey. The corporation's retained earnings belong to the company, not its shareholders, and did not become "marital property" under West Virginia law, because the Respondent/husband did not have the power as a shareholder or director to force the company to

distribute the earnings instead of retaining them. The Family Court's ruling, which the Petitioner/wife urges this Court to adopt, is contrary to law and against public policy and represents an unconstitutional taking in violation of the due process rights of Flying "W" Plastics, Inc., which was not a party to this divorce action. Moreover, as the Circuit Court correctly concluded, the Petitioner/wife expressly signed away any potential rights or claims she may have had to Flying "W" Plastics, Inc. in the Agreement. This Court should uphold the Circuit Court's correct ruling.

Retained earnings are precisely what the names implies: earnings of a corporation retained by the corporation. At no time does the legal ownership of retained earnings change from the corporation to a shareholder. W. Va. Code §31D-6-623 and I.R.C. §316 provides that a corporation may declare a dividend per share to be paid to the shareholders from the earnings of the Corporation. When a dividend is declared, those retained earnings cease to be retained earnings, become dividends and legal ownership transfers from the corporation to the shareholders.

Petitioner compares retained earnings to a bank account where shareholders can withdraw funds at their leisure. That

comparison is not supported by the West Virginia Business Corporation Act, W. Va. Code §31D-1-1 *et seq.*, the Internal Revenue Code Subchapters C and S (C-corporations and S-corporations) §26 U.S.C. 301 and 1361 *et seq.* or Generally Accepted Accounting Principles ("GAAP.") Corporations legally own retained earnings, and shareholders have no right to access those retained earnings unless a corporation's board of directors elects to convert the retained earnings to a dividend payable to the shareholder. Petitioner's analogy to a bank account confuses retained earnings and dividends. Retained earnings are owned by the corporation; dividends are owned by the shareholders. Petitioner contends that Respondent made "additional non-payroll and third party draws" from the corporation's retained earnings account. That is an incorrect statement. At no time has a shareholder of Flying "W" taken personal draws from the corporation's retained earnings account. The figures that Petitioner cites as being "personal draws" made on the retained earnings account were, in fact, shareholder dividends declared by the corporation. At the time of declaration, those dividends ceased to be retained earnings. Petitioner emphasizes that the Respondent spent those funds on personal items. However, that has no bearing on the matter at hand. Shareholders own dividends,

and as a shareholder, Respondent was entitled to spend those funds as he chose. What Respondent did not do, and could not do, was take funds from the corporation's retained earnings account.

The majority of courts in other jurisdictions have held that retained earnings are not an asset of a shareholder and are not marital property. Petitioner correctly states that authority on this issue is sparse. What Petitioner fails to state is that courts in seven jurisdictions have addressed the issue, and six of those seven states are consistent with the Circuit Court's holding that retained earnings are not marital property unless a divorcing shareholder has unfettered control over a corporation and can force that corporation to retain or distribute earnings.

The Supreme Court of Minnesota details its analysis in reaching that conclusion in Gottsacker v. Gottsacker, 664 N.W.2d 848 (Minn. 2003), where it examined a situation similar to this case. In Gottsacker, the wife was the shareholder of three S-corporations, along with her parents and brother. The shares were non-marital property, as she had received the shares as a gift from her parents during and throughout the marriage. She did not own the majority of the shares. In holding that the AAA accounts of the three S-corporations were not marital property, the Court reasoned that the wife did not have a right to force

distributions, nor did she have substantial control over the corporation. The Minnesota Court further expressed concern about the fundamental unfairness of deeming retained earnings as a marital property when there is no assurance that the wife would ever receive a benefit from the AAA because those funds may never be distributed to the wife. *Id.* at 856.

The same reasoning was applied in holding that retained earnings of a partnership were not marital property in Rayala v. Rayala, 781 N.W.2d 550 (Wis. App. 2002). In Rayala, the husband was a minority owner of a partnership with his parents. The court held that "based on the trial court's finding that Daniel [the husband] did not control the distribution of retained earnings, we conclude those earnings did not constitute divisible marital income." See also In re Marriage of Joynt, 375 Ill. App. 3d 817, 874 N.E.2d 916 (Ill. App. 2007) (holding that the retained earnings were not marital property because the shareholder-spouse was a minority shareholder who did not have the power to cause distribution of the retained earnings); Robert v. Zygmunt, 652 N.W.2d 537 (Minn. App. 2002) (holding that wife's interest in the S-corporation's retained earnings account was not marital property because wife did not have the control over the corporation necessary to force a distribution of AAA); In re

Marriage of Casten, 2012 WL 1860358 (Iowa App. 2012) (holding that retained earnings are not marital property because (1) the shareholder was not a majority shareholder, (2) he did not possess the ability to force dividend retention or distribution and (3) the record did not reflect that he colluded with other shareholders to control the retained earnings); Ramon v. Ramon, 963 A.2d 128 (Del. 2008) (holding that husband's unilateral control over the corporation as its sole shareholder caused retained earnings to be marital property); Heineman v. Heineman, 768 S.W.2d 130 (Missouri App. 1989) (holding that retained earnings were marital property because they were the undistributed wages of sole proprietor wife); Metz v. Keener, 573 N.W.2d 865 (Wis. App., 1997) (holding that retained earnings were marital property because the shareholder-spouse had full ownership and possession of all the corporate shares and that she was the sole managing force behind the corporation).

Petitioner relies heavily on Zaccardelli v. Zaccardelli, 2013 WL 1908880 (Oh App. Ct 9th District), the lone decision that is contrary to the weight of legal authority. Petitioner's reliance on Zaccardelli is misplaced because the case at hand can be factually distinguished from Zaccardelli. Unlike the husband in Zaccardelli, Respondent Doug Morris did not use retained

earnings for his personal use. The Ohio court cites the purchase of personal assets and payment of personal debts as evidence that the husband had control over whether the earnings were retained. In that case, the husband testified that the corporation "had purchased two vehicles for his personal use, paid the parties' property taxes, and paid contributions to the parties' health savings account from the retained earnings." *Id.*, at ¶13. Petitioner attempts to "stretch" the testimony of the corporation's controller, CPA Eric Brown, to suggest that Respondent and his sister used funds from the corporation's retained earnings account for personal use. However, that is not correct. The funds that Mr. Brown's testimony refers to were dividends declared by the Corporation and legally belonged to the shareholders, who could do with the dividends however they chose. No retained earnings were used by either shareholder of the corporation. Accordingly, Petitioner's analogy to Zaccardelli has no merit.

Petitioner/wife also confuses the issue of ownership of the retained earnings with an income tax concept when she asserts that because retained earnings were taxed to the couple, they must be owned by the couple. Ownership of the retained earnings and taxation of the retained earnings are two separate and

distinct matters. For tax purposes only, the corporation in this case has elected to be considered an S-corporation that passes through the taxation of its income to its shareholders for the singular purpose of avoiding taxation at both the corporate and shareholders levels. That election has no effect on the legal status of the corporation or its property, as Congress indicated at the time it promulgated Subchapter S.

In addition, the Petitioner's assertion that she paid income taxes on the retained earnings is factually incorrect. Retained earnings flowed through to the Respondent/husband, a shareholder, for tax purposes, but the corporation itself has paid all taxes on the retained earnings. At no time were marital funds used to pay those income taxes. Therefore, petitioner's reliance on the taxation of the retained earnings is misplaced.

Petitioner's contention that Respondent is a "co-majority shareholder" also has no merit. The term "co-majority shareholder" is a term made up by Petitioner's counsel. There is no such term in the West Virginia Business Corporation Act or any other applicable legal authority. On the contrary, the West Virginia Business Corporation Act contemplates that a majority vote consists of 51% of the shares. W. Va. Code §31D-1-1 *et seq.* Several of the cases cited above include family owned

corporations and none of them found anything akin to Petitioner's "co-majority shareholder" theory. Respondent does not own 51% of the stock of the corporation, and therefore, he is not in a position to control earnings retention or distribution.

What Petitioner seems to be implying is that the Respondent and his fellow shareholder are or have been colluding to deprive Petitioner of funds. There is no evidence in the record to support this implication. On the contrary, the shareholders have acted in good faith at all times, as demonstrated by their immediate instruction to the corporation's officers to issue shares of the corporation to Petitioner/wife when the Family Court announced its decision that she was entitled to one-half ($\frac{1}{2}$) of the Respondent/husband's shares⁷.

Finally, it bears observing that the Petitioner is asking the Court to create new law that would have a significant negative effect on business growth and development in West Virginia. Corporations would have difficulty finding investors for West Virginia businesses and in obtaining credit because they would no longer be able to use retained earnings. Lending institutions would suffer because they would lose collateral on

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Subsequent to the Petitioner/wife's receipt of 45 shares, constituting half of Respondent/husband's shares, she assigned 10% of those shares to her counsel's legal corporation, an ineligible S-shareholder, in payment for past and future legal services. Such action, until undone by the Circuit Court's order, would have resulted in substantial taxes to the shareholders. Was this good faith?

current loans and would not be able to make as many loans in the future due to lack of collateral. Shareholders would suffer because their shares would diminish in value. Adopting Petitioner's position would cause grave injury to closely-held companies. Those companies are part of the lifeblood of the West Virginia economy. Viewed through a wider lens, there are compelling public policy reasons to uphold the Circuit Court's ruling that the retained earnings of the corporation are not marital property.

CONCLUSION

The Respondent respectfully urges this Court to affirm the well-reasoned and legally correct decision of the Circuit Court of Gilmer County, which upheld the parties' Agreement Respecting Marital Rights and reversed the Family Court's ruling distributing a portion of retained earnings of a closely-held corporation to the Petitioner/wife, and to grant him such other and further relief as may be merited in this case.

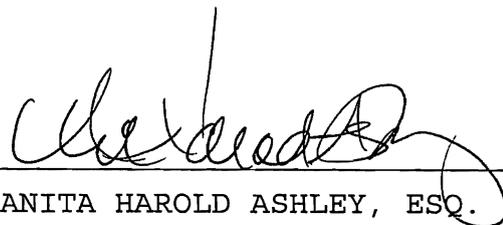


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CERTIFICATE OF SERVICE

I, Anita Harold Ashley, counsel for respondent Douglas Shane Morris do hereby certify that I have served a true copy of the foregoing Brief of Respondent Douglas Shane Morris upon the petitioner by mailing the same, postage prepaid, to her counsel of record, James Wilson Douglas, at his address of record, P. O. Box 425, Sutton, West Virginia 26601, on this 15 day of October, 2013.



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