

Legal alternatives to an illegal practice; the use of proxies by Directors

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A recent article by Michael Schulman, Esq. outlined some of the pitfalls that can befall directors when they use a proxy in lieu of actual attendance and personal voting at board meetings. This author agrees with the conclusions reached by Mr. Schulman in that article. Thus, not only will this article provide additional reasons against the use of proxies by directors but, additionally, it will provide valid, and lawful, alternatives for directors when they will not be able to attend a particular meeting.

A developer in creating a common interest community can use various legal entities.¹ The most common form of an entity, however, is the nonprofit corporation formed under Chapter 82 of the Nevada Revised Statutes (“NRS”). The general concepts discussed in this article apply equally to other entity types, but this article will focus on nonprofit corporations. The principles also apply equally for proxies as with powers of attorney. In fact, a proxy is nothing more than a special purpose power of attorney.

Nobody disputes that a director, whether appointed or elected, has a fiduciary relationship with the members being represented. In defining persons who have a fiduciary relationship, and thus a fiduciary duty, Merriam-Webster’s Dictionary of Law uses corporate directors as a prime example. Examples of directors’ fiduciary duties include the duty to act honestly and in a manner consistent with the best interest of those represented, and the duty to act in good faith to fulfill the obligations imposed upon him or her. In short, a fiduciary relationship is where one party places special trust, confidence, and reliance on the fiduciary to act for the benefit of that party or parties. Thus, a director has an obligation to act for the benefit of the corporation and not for personal gain.

These concepts have been codified in the Nevada statutes. NRS 82.221 states that: “Directors and officers shall exercise their powers in good faith and with a view to the interest of the corporation.” NRS 116.3103(1) also specifically states that “the officers and members of the executive board are fiduciaries.” Under Nevada law the articles or bylaws must set forth the number of directors and specify how the number of directors can be modified.² Furthermore, Nevada statutes require that if the number of directors necessary to constitute a quorum and/or to pass resolutions is anything other than a simple majority, such must be specified as well.³

In addition to the general nonprofit corporation statutes, the Legislature has supplemented those statutes when dealing with common interest communities in NRS Chapter 116. There is a very critical difference in how a quorum for business is determined for membership meetings as opposed to executive board meetings. NRS 116.3109(1) allows for all those present “*in person or by proxy*” to be counted toward the minimum number of necessary members for membership meetings. Compare that statute with NRS 116.3109(3) that only

allows those persons entitled to vote that are “*present at the beginning of the meeting*” to qualify toward the quorum for directors’ meetings.

If directors are able to give their proxy to another director to act in their place, such actions defeat the very purpose of requiring a specified number of directors be elected or requiring a specified number of directors be present to constitute a quorum.

While no Nevada statute affirmatively states that one director cannot give another director his proxy, such a statute is not needed. There is a legal concept in law regarding statutory interpretation that in essence is the concept of prohibition by omission. In other words, if the legislature provides certain rights to specified classes of persons, other persons that are not included do not have those rights. In this case, the Nevada legislature has specified that members and delegates may use proxies but, omitted directors. In addition to NRS 116.3109 above, NRS 82.281(4) states:

Unless otherwise provided in the articles or bylaw, the consent or approval of *delegates or members may be by proxy or attorney*, but all such proxies and powers of attorney must be in writing.

Likewise, NRS 82.321(1) provides in pertinent part:

At any *meeting of the members* of any corporation, *any member* may designate another person or persons *to act as a proxy or proxies*.

Since several statutes provide that members and delegates may utilize proxies, but none authorize directors to do so, by omission directors do not have that option.

Remember that the job of a director is to participate in the decision making process and then vote his or her conscience and independent judgment as what is best for the corporation. By giving your vote by proxy to another, it is impossible to fulfill your job and constitutes malfeasance of office. In addition to the other pitfalls that have been discussed, the use of proxies could be adjudged by a court that those directors were not exercising their powers in good faith and could constitute grounds for the appointment of a receiver.⁴

Perhaps more important than detailing all of the problems associated with the use of directors’ proxies; in today’s society, there is really no reason for directors to use proxies. There are viable, and legal, options available depending on the circumstances involved. There are really only two situations where the consideration of proxies should even be involved. Those where the director has a planned absence and will not be able to attend in person, and those where a particular project will require extensive involvement that all directors cannot commit to. For other situations, if a member cannot participate as a director, resignation may be appropriate.

With the worldwide availability of telecommunications, including cell phones, the first

option to be considered would be that provided for in NRS 82.271. That statute provides that *unless restricted* by the articles or bylaws, directors may participate in a meeting by telephone or other means, so long as all persons participating can hear each other. Thus, a simple speaker telephone and conference calling can put all directors together for purposes of the meeting regardless of where in the world individual directors may be at the moment. More importantly, NRS 82.271(3) specifically states that when a director participates in a meeting by this method, his or her participation “*constitutes presence in person*”.⁵ Thus, the quorum requirement for director meetings required by NRS 116.3109(3) can be met through the use of telephone conferencing so long as sufficient directors are involved at the beginning of the meeting. The failure to hold meetings due to a lack of directors being “physically” present can be avoided in this fashion.

Another option is available when there is a particular project that will require too much time for all directors to participate. That is the appointment of a committee of the board. The only requirement is that at least one member of the committee also be a member of the board of directors. Caution should be exercised, however, in the use of committees so as not to abrogate the director’s fiduciary duty. Also, since there are specific limitations on what a committee may or may not do, before appointing a committee, directors need to carefully read NRS 82.206. Additionally, before creating a committee of the board, both the directors and the association’s counsel should review the governing documents to see if there are any limitations on the use of committees beyond those in the statute.

While proxies, or powers of attorney, are not appropriate, nor legal in this author’s opinion for board of directors, as a practical matter, there is really no reason to even consider such with the use of telephone conferences and committees.