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MEMORANDUM

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TO: Christopher D. Imlay
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CC: Rick Roderick, Tom Gallagher, Barry Shelley

FROM: David A. Swerdloff
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DATE: May 26, 2017

RE: Response to Questions on Day Pitney March 17, 2017 Memo

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You have asked us to respond to certain questions posed by a Vice Director of American Radio Relay League, Incorporated ("**ARRL**") arising from our March 17, 2017 memorandum to you, along with certain additional questions you have raised. This Memorandum responds to those questions.

BACKGROUND

ARRL is a Connecticut nonstock corporation, and the Connecticut Nonstock Corporation Act, Connecticut General Statutes ("**C.G.S.**") Sections 33-1000 *et seq*. (the "**Act**"), governs its internal affairs, including the election, rights and duties of members of the Board of Directors. Per the Articles of Association of ARRL (the "**Articles**") and the Bylaws of ARRL (the "**Bylaws**"), the Vice Directors of ARRL (the "**Vice Directors**") serve two main purposes: (1) to take the place of a Director of ARRL (a "**Director**") at meetings of the Board of Directors when the Director cannot attend, including the right to speak and vote, and (2) to fill the vacancy caused by the resignation, death or other termination of service of the elected Director.

Our March 17 memo concluded that Connecticut does not expressly permit alternate Directors with the power to act on behalf of a Director in the Director's absence. Connecticut also does not appear to permit Members of a nonstock corporation to elect individuals to fill vacancies on the Board of Directors in advance, except in certain narrow circumstances such as resignation or retirement. We noted that the Act was not entirely clear, however, and arguments could be made that the governance structure at ARRL should be enforceable. Maintaining the current structure raises risks. If the Vice Directors were found by a court to lack the legal authority to fulfill the role delegated to them in the ARRL Articles and Bylaws, that could jeopardize the validity of corporate actions.

ARRL Vice Directors and others have questioned these conclusions. Important points were made, including the effect of the so-called "freedom of contract" clause in the Act, C.G.S. Section 33-1001(a). This section affords corporations broad autonomy to structure and manage their governance, as follows:

> [The Act] shall be so construed as to provide for a general corporate form for the conduct of lawful activities with such variations and modifications from the form so provided as the interested parties may agree upon, subject to the interests of the state and third parties. Whether or not a section of said [Act] contains the words "unless the certificate of incorporation or bylaws otherwise provide", or words of similar import, no provision of a certificate of incorporation or bylaw shall be held invalid on the ground that it is inconsistent with such section unless such section expressly prohibits variations therefrom, or prescribes minimum or maximum numerical requirements, or a substantial interest of the state or third parties is adversely affected thereby.

Questions were also raised about the "grandfathering" provision of the Act. C.G.S. Section 33-1001(b) provides as follows:

> If the certificate of incorporation, in effect on January 1, 1997, of a corporation without capital stock formed under the laws of this state, whether general law or special act, prior to said date, contains any provision contrary to, inconsistent with or in addition to any provision of [the Act], but which provision was permitted to be contained in such certificate pursuant to the provisions of applicable law as in effect prior to January 1, 1997, the provisions contained in such certificate shall govern such corporation and the provisions of said sections shall not be held or construed to alter or affect any provision of the certificate of incorporation of such corporation inconsistent herewith [with certain exceptions not relevant here].

In other words, if the role of Vice Directors was authorized under prior versions of the Connecticut Nonstock Corporation Act, then that role would continue to be authorized under the Act.

Reference was also made to the case of *Steeneck v. University of Bridgeport* (235 Conn. 572, 1995) ("***Steeneck***"), in which the Connecticut Supreme Court analyzed the structure of a board of directors of a Connecticut nonstock corporation and held that a non-voting "Life Trustee" would not be considered a Director for purposes of standing to contest corporate actions.

We have considered the questions raised and here are our conclusions.

DISCUSSION

1. **Voting and Delegation: How is the voting power of Vice Directors negated by the "no delegation by the Director" principle?**

One of the Vice Directors reported that he agreed that Directors cannot grant proxies or otherwise delegate their fiduciary duties under general principles of corporate law. However, he suggested that the authority of Vice Directors to vote in the absence of Directors was derived from the Articles and not from any delegation of duties by the Directors.

As noted in our March 17 memo, there is little authority on the ability of a corporation, stock or nonstock, to authorize alternates to act on behalf of duly elected Directors. It is just not common practice. We believe the better analysis would conclude that alternate Directors are not permitted for the same reasons that Directors cannot grant proxies or delegate their fiduciary duties. Only the elected Directors have the statutory duties of a Director—the duties to act in good faith, with due care and in what is reasonably believed to be in the best interest of the corporation—and the potential statutory liability for breach of those duties. Vice Directors may be granted those rights in the organization documents, but they are not addressed in the statute. See C.G.S. Section 33-1104.

The "freedom of contract" provision is relevant here. An argument can be made that the role of Vice Directors does not adversely affect a substantial interest of the state or third parties and therefore should be permitted. In particular, insofar as the Vice Directors have been elected under the same rules as the Directors, and the Vice Directors are made subject to the same fiduciary duties as Directors under ARRL's organization documents (although we understand that some Vice Directors have resisted becoming subject to those duties), it would be difficult to argue that the state or Members of ARRL are adversely affected by the Vice Director structure.

We would disagree. The state and the Members have a strong interest in having the Director elected by his or her regional constituents to represent their interests. The Directors were presumably elected after disclosure of their backgrounds and their views and perhaps after a contested election. We would be troubled by a structure in which two individuals essentially shared a board seat, each with the ability to act in the absence of the other. What would happen if the individuals had different approaches to ARRL's business? The elected Director would be at risk of having his views overridden if he missed a Board meeting and the Vice Director cast a vote contrary to the wishes of the elected Director. This may be less tolerable than the situation in which a Director attempts to grant a proxy, which is prohibited under corporate law as an inappropriate delegation of duties, because the Vice Director may take actions that contradict those that the Director would deem in good faith to be in the best interests of the corporation.

We continue to find the grant of authority to Vice Directors to vote in the absence of the elected Director to be contrary to the Act and to corporate law principles. The Board of Directors is granted the general duty and responsibility of the Board of Directors to manage the activities,

property and affairs of the corporation. See C.G.S. Section 33-1080. In our opinion, these duties and responsibilities are non-delegable and personal to the elected Directors.

2. **Succession: Must ARRL eliminate any automatic succession provision in the Articles and Bylaws? Can a Vice Director be given preference when a vacancy arises on the Board of Directors?**

We concluded in our March 17 memo that filling a vacancy on the Board prior to the date of vacancy is permitted only with respect to vacancies occurring "at a specific later date," such as a future resignation by a Board member who intends to move to a different territory or to retire mid-term. See C.G.S. Section 1091(c). In light of this specific language, we doubted that Vice Directors could be granted automatic succession rights when the date of a future vacancy is not "a specific later date."

A Vice Director has noted that the introductory clause to C.G.S. Section 1091(a) on vacancies begins, "Unless the Certificate of Incorporation provides otherwise…" This can be interpreted to allow methods of filling vacancies by means other than election by the Board or the Members, the Vice Director suggested, so long as the provision is set forth in the certificate of incorporation. See C.G.S. Section 1091(a). ARRL has set forth the succession rights of Vice Directors in Article 5 of the Articles, which are the same as a certificate of incorporation for these purposes, so the Vice Director suggests that the automatic succession of Vice Directors is authorized.

While this is a fair argument, we do not believe it applies. C.G.S. Section 1091(c) is a specific provision on how to fill vacancies arising at a later date, while C.G.S. Section 1091(a) is a broad provision setting forth mechanics on the procedure for filling Board vacancies generally. It is a rule of statutory construction that specific provisions cannot be overridden by more general clauses. Accordingly, we believe the specific rule on vacancies arising at a later date, as set forth in C.G.S. Section 1091(c), would likely preclude filling future vacancies occurring at an undetermined date with Vice Directors.

The Act contemplates the affirmative action of either the Members or the Directors to fill a vacancy on a Board "if a vacancy occurs." See C.G.S. Section 33-1091(a). This suggests that the vote for a replacement Director cannot occur prior to the vacancy. While this section begins, "[u]nless the certificate of incorporation provides otherwise…" that language may have been intended to restrict the authority of the Directors or certain Members to fill vacancies, rather than allowing successor Directors to be determined in advance of the vacancy.

While we do not believe the succession rules on vacancies are consistent with the Act, we cannot advise ARRL that it is mandatory to change its rules on vacancies. In light of the freedom of contract and grandfathering provisions of the Act, a court may find the ARRL structure authorized and enforceable. This is not a black-and-white area, as we said in our March 17 memo. The only way to obtain a definitive answer to the issue would be to begin a legal action in the Connecticut courts to obtain a declaratory judgment that the provisions were or were not enforceable.

In response to another question, when a vacancy is filled by the Board, it would be entirely appropriate to consider the Vice Director from the territorial division as the successor Director. The Vice Director may be the best informed candidate and may have broad support among the Members who elected him or her. The Board would exercise its business judgment in determining the appropriate successor.

3. **Risks and Liabilities: What are the potential risks in allowing Vice Directors to vote in the absence of Directors?**

There are two principal risks in allowing Vice Directors to vote in the absence of the elected Directors.

- The first risk is with respect to the presence of a quorum. If the quorum depends upon the presence of Vice Directors, and if it is later determined that the Vice Directors lacked the authority to fill in as Directors, then no quorum would have been present at the particular meeting. Actions taken without a quorum would not be binding on the corporation.

- The second risk is with respect to matters approved by the Board. If the vote of a Vice Director were required to approve a corporate action, as in a split vote of eight to seven, then again, the action may not be binding on the corporation.

In either of the above scenarios, a Member of ARRL, a Director, ARRL itself or the Connecticut Attorney General could bring a lawsuit to challenge the validity of the adopted action. See C.G.S. Section 33-1038(b). In that event, a court might enjoin or set aside the act in question and award damages for loss. See C.G.S. Section 33-1038(c).

We do not see any risk of the corporation being dissolved or losing its right to conduct business. Grounds for judicial dissolution are limited to matters like illegal, oppressive or fraudulent conduct or misapplication or waste of corporate assets. See C.G.S. Section 33-1187.

We also do not see any increased risk of personal liability for the Directors or Vice Directors. So long as the Directors and Vice Directors are otherwise meeting the statutory standards of conduct for directors and the fiduciary duties set forth in the Articles, Bylaws and in the common law, a good-faith attempt to act in accordance with the Articles and Bylaws should not result in liability. Nevertheless, we continue to recommend appropriate amendments to the ARRL Articles and Bylaws to limit the liability of Directors.

4. **Statutory Authority. Where, if at all, does the Act indicate a multi-level concept of "Directors" is prohibited?**

While the concept of an alternate director like an ARRL Vice Director is nowhere authorized in the Act, we were asked whether any provisions expressly prohibited the role. There are no express prohibitions on designating Vice Directors with the authority to vote in the absence of a

Director. However, several provisions imply that Vice Directors were not contemplated and may be prohibited under the Act:

- The Act does not authorize classes of Directors with different voting or governance powers. This is in contrast to provisions of the Act which expressly contemplate multiple classes of Members with distinct voting rights. See C.G.S. Sections 33-1026(b)(2)(B), 33-1057(b), 33-1083(a).

- As noted in our March 17 memorandum, the Act expressly contemplates alternate members of committees of the Board. See C.G.S. Section 33-1101(g). There is no corresponding provision in the Act that contemplates alternate Members for the Board of Directors itself.

5. Classification: Are Vice Directors a separate class of Directors?

A Vice Director has alleged that the Vice Directors are actually Directors with limited powers. We do not understand this distinction. The Articles and Bylaws are clear that the Directors and Vice Directors of ARRL are two distinct groups. The Directors are charged with the management of ARRL. The Vice Directors have no duties, other than filling in for the Director from their territorial division in the Director's absence and assuming the Director's seat upon a vacancy. The Vice Directors are not Directors with limited powers. They are alternates with the authority under the Articles and Bylaws to assume the full role of the Directors upon a vacancy, temporary or permanent. In that role, they are no different from the Directors granted the authority under C.G.S. Section 1101(g) of the Act to serve as alternate members of committees of the Board—the only reference to alternate Directors in the Act.

6. Grandfathering: To the extent the Articles and Bylaws regarding Vice Directors were adopted prior to the adoption of the Act, would the provisions be "grandfathered" under prior versions of the Act?

The Act provides for "grandfathering" of provisions in certificates of incorporation adopted prior to January 1, 1997, if those provisions were permitted under the applicable earlier version of the Act. The position of Vice Director was added to the Articles in 1951.

We have reviewed the Connecticut Nonstock Corporation Act as it existed in both 1951 and in 1996, immediately prior to the effective time of the current Act. Neither version expressly contemplates alternate Directors. While the 1951 version of the Act is quite limited in scope and contains little guidance, the 1996 version of the Act is generally similar to the current statutory scheme. Neither version lends support to the creation of an alternative group of Vice Directors who can be substituted for the Directors in the absence of the Director at a Board meeting or who can automatically fill a vacancy on the Board.

Under the 1996 version of the Act, the Board has the right to manage the corporation's activities, property and affairs, subject to fiduciary duties. See C.G.S. Section 33-447 (repealed 1/1/97). As in the current Act, reference to alternate Directors is made solely in the section on

committees, not with respect to the Board itself. See C.G.S. Section 33-452 (repealed 1/1/97). A Director serves until his or her successor has been elected and qualified, unless the Director was earlier removed from office. See C.G.S. Section 33-448(h) (repealed 1/1/97). A Director ceases to hold office only upon death, resignation or removal. See C.G.S. Section 33-448(h) (repealed 1/1/97). Accordingly, a Vice Director cannot fill a "temporary vacancy" on the Board because no vacancy has actually occurred under the 1996 Act until a Director's death, resignation or removal.

The 1996 version also specifies how vacancies on a Board of Directors are to be filled. Generally the Members or, in certain circumstances, the Directors themselves can fill the vacancy. See C.G.S. Section 33-451(d) (repealed 1/1/97). This section suggests that a vacancy must first occur on the Board, and then an affirmative action must be taken by the Members or Directors to fill that vacancy. There is no provision for designating the successor Director in advance.

For these reasons, we do not believe the prior versions of the Act offer stronger support than the current Act for (i) allowing Vice Directors to vote in the temporary absence of the Director from a meeting or (ii) succeeding to the role of Director upon a vacancy in the Director's position during the term of a Director.

7. The Connecticut Supreme Court Case: Is *Steeneck v. University of Bridgeport* relevant?

We are familiar with the Connecticut Supreme Court's decision in *Steeneck v. University of Bridgeport* (235 Conn. 572, 1995). We do not believe the case supports the argument that nonstock corporations are free to structure a Board with Vice Directors who can act in the absence of Directors.

In *Steeneck*, a nonstock Connecticut corporation had three classes of trustees: "term trustees," "life trustees" and "honorary trustees." Only the term trustees were counted in determining a quorum, and only the term trustees could vote on Board action, hold office or serve as Members or chairpersons of the standing and executive committees. Otherwise, the life trustees and honorary trustees had "all the privileges of a Trustee" under the corporation's bylaws. They could attend Board meetings and participate in Board deliberations.

A life trustee challenged the actions of the corporation in court. The Connecticut Supreme Court held that the life trustee could not bring the lawsuit because she was not a "director" under the Nonstock Corporation Act then in effect and did not have standing. The court held:

> We agree…that a life trustee is not a director for purposes of the Act…. Ultimately, the question to be determining the status of one who claims to be a director under the Act is whether that person is intended to have a significant managerial role in the corporation's affairs.

Steeneck at 581, 583. The Vice Directors do not have a significant managerial role in ARRL's affairs. They are on "standby," attending and potentially participating in meetings (as did the life trustee in *Steeneck*), but having no right with respect to management unless their Directors are absent. In addition, the court held that, in order to be deemed a Director, a party outside the "traditional management framework" would be required to demonstrate that his or her position carried the ability, in some substantial sense, to direct the corporation's operation and future. *Steeneck* at 583, 584. Vice Directors do not have that ability.

The court noted the freedom of contract language in the Act that allowed corporations to deviate from "the simple, traditional framework it recognizes for corporate management." Corporations could "create positions that possessed some but not all of the attributes traditionally associated with directorship." *Steeneck* at 582. However, because she lacked voting and other managerial rights, she was not properly considered a "director."[1]

We do not regard this case as relevant to ARRL. Many nonstock corporations have Honorary Directors, Life Directors, Directors Emeritus, advisory boards and similar advisory positions. These are acceptable and common, in part because they do not grant the right to vote. The problem with the ARRL structure is that the Vice Directors have voting rights in the absence of Directors, not that they are permitted to attend meetings or access Board information.

CONCLUSION

We hope these comments are responsive to the questions raised. These are complex questions, and the answers are not as clear as we would like. Nevertheless, we note that corporate actions that relied on the presence or votes of Vice Directors could be questioned. We would be glad to discuss these matters further with you and answer any additional questions you may have.

[1] The court noted in a footnote as follows:

> We need not decide in this case, as the defendants urge, whether the unqualified right to vote on board action is an essential attribute of directorship. Although we recognize that it is an ordinary incident of that status and the ordinary means by which to exercise authority, we also recognize that the Act has application to a great variety of nonstock corporations, and so we do not foreclose the possibility that any organization governed by the Act may present a unique situation in which voting rights have less significance for director status than is ordinarily the case.

This is dictum and does not establish any legal precedent or, for that matter, address the role of alternate Directors or Vice Directors like those at ARRL.