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The Appeal of Nevada: Why Corporations are Heading West

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More and more corporations are moving to Nevada. Is this because of the lack of corporate or franchise taxes associated with incorporating in the state or the lack of state income tax? Likely not (Nevada does not collect franchise taxes but does collect fees associated with yearly filings disclosing a corporation's directors and officers).¹ Rather, the Nevada Supreme Court interpreted/confirmed Nevada Revised Statute (NRS) § 78.138(7) in 2020 holding that per the plain language of the statute, the directors and officers of a Nevada corporation are "not individually liable for damages as a result of an act or failure to act in his or her capacity as a director or officer except under circumstances described."²

Presumption of Good Faith

We start with the plain language of the statute. NRS § 78.138(3) codifies the presumption of good faith of the directors and officers of a Nevada corporation. The directors and officers are also presumed to act on an informed basis with a view to the best interests of the corporation. With certain exceptions, a director or officer is not individually liable for damages because of an act or failure to act in his or her capacity as a director or officer.

Nevada's regime is pro-officer/director because it reduces the risk of a director or officer being held personally liable for acts related to their position. All else being equal, a Nevada corporation is appealing to executives.

Comparison with Delaware's Business Judgment Rule

On its face, Nevada's statute sounds similar to the Delaware Supreme Court's decision in *Stone v. Ritter*.³ There, the Court indicated that, in order to sustain a claim for oversight on the part of the directors, the plaintiff must show "(a) the directors utterly failed to implement any reporting or information system or controls; or (b) having implemented such a system or controls, consciously failed to monitor or oversee its operations thus disabling themselves from being informed of risks or problems requiring their attention. In either case, imposition of liability requires a showing that the directors knew that they were not discharging their fiduciary obligations"⁴ (e.g, gross negligence). In Delaware, pleading facts that indicate grossly negligent behavior of directors or officers of a Delaware corporation is enough to overcome the presumption of good faith inherent in the business judgement rule.

Whereas in Nevada, the Nevada Supreme Court held that gross negligence-based allegations *did not* state an actionable claim against

corporate directors or officers because, based on its plain text, NRS § 78.138(7) applies to all claims of individual liability against directors and officers, precluding the imposition of liability for grossly negligent breaches of fiduciary duties.⁵ Rather, a claimant must establish that the director or officer *had knowledge* that the alleged conduct was wrongful in order to show a knowing violation of law or intentional misconduct pursuant to NRS § 78.138(7)(b).⁶

Relevant Examples

The pro-director/officer regime in Nevada has enticed many Fortune 500 companies to reincorporate from Delaware to Nevada recently. The high-profile case of Twitter (now “X”) leads the list. Additional examples, include reincorporation attempts by Tripadvisor, Inc. and Liberty Tripadvisor Holdings, Inc., which indicated a desire to reincorporate to Nevada in their annual proxy statements. Shareholders filed suit to prevent this reincorporation alleging it would eliminate shareholder rights to sue for a breach of fiduciary duties. However, in February 2024, a Delaware court allowed Tripadvisor, Inc. to reincorporate to Nevada but held the door open for potential shareholder claims for the reduction in minority stockholders' rights under Nevada law.⁷

Applicability to limited liability companies

NRS § 86.298 provides that the only duty attributable to a manager or managing member of a Nevada limited liability company are the implied contractual covenant of good faith and fair dealing, plus any other duties expressly prescribed in the articles of organization or operating agreement.

This is contrary to the Delaware limited liability company regime, which provides that “in the absence of a provision explicitly altering such duties, an LLC's managers and controlling members in a manager-managed LLC owe the traditional fiduciary duties that directors and controlling shareholders in a corporation would.”⁸

In Nevada, by statute there are *no* fiduciary duties assigned to a manager or managing member unless prescribed in the governing documents. Whereas in Delaware, a manager or managing member owes fiduciary duties unless the governing documents contain explicit language altering such duties.⁹

Conclusion

Nevada's presumption of good faith for directors and officers of Nevada corporations means that unlike Delaware, conflict of interest transactions involving a director or officer are not viewed through a heightened scrutiny “entire fairness” lens where the burden of proof is on the defendant to show that the transaction was fair to the corporation and its stockholders. Similarly, Nevada has pro-manager/managing member protections for limited liability companies organized in the state. There is no need to opt out of fiduciary duties like in Delaware.

Nevada's pro-officer/director regime is already making waves and

prompting more companies to reincorporate or reorganize in Nevada. It remains to be seen whether the “race to the bottom” of fiduciary duties will have any negative effects on shareholder or member value solely as a result of such reincorporation.

¹ The lack of franchise fees in Nevada can save a Nevada corporation up to \$200,000 per year (which is Delaware's ceiling on franchise fees).

² Chur v. Eighth Judicial Dist. Court of Nev., 136 Nev. 68, 458 P.3d 336 (2020).

³ 911 A.2d 362,

⁴ Stone v. Ritter, 911 A.2d 362 (Del. 2006).

⁵ See Chur.

⁶ See Chur.

⁷ Palkon v. Maffei, No. 2023-0449-JTL, 2024 Del. Ch. LEXIS 48 (Del. Ch. Feb. 20, 2024)

⁸ Kelly v. Blum, C.A. No. 4516-VCP (Del. Ch. Feb. 24, 2010).

⁹ NRS 86.298

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