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Having the Fiduciary Duty Talk: Model Advice for Corporate Officers (and Other Senior Agents)

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*By Lyman Johnson**

Countless legal materials address the fiduciary duties of corporate directors. These include extensive decisional law, numerous institutes and continuing legal education seminars, several treatises and casebooks, and the well-known Corporate Director's Guidebook *recently released in its fifth edition. By contrast, legal materials on the fiduciary duties of corporate officers—key actors and agents in any company—are quite sparse. Case law is meager and undeveloped, with even such a baseline issue as the applicability of the business judgment rule lacking resolution. Treatises, institutes, and other legal materials frequently lump officer fiduciary duties with those of directors or treat them as an afterthought or, in many instances, overlook the subject altogether. There is no preeminent, standard reference serving as the* "Corporate Officer's Guidebook."

This Article seeks to begin rectifying this glaring gap in legal literature and professional practice. Fiduciary duties, as a vital component of an effective corporate governance system, work on an ex ante *basis—i.e., officers must be advised of such duties beforehand if such duties are to influence conduct. This Article describes the sources of legal material for deriving a succinct exposition of officer fiduciary duties and then provides suggested "model" fiduciary duty advice for lawyers to use in counseling corporate officers and other senior managers.*

I. INTRODUCTION

Countless legal materials address the fiduciary duties of corporate directors. These include extensive decisional law,[1] numerous institutes and continuing legal education seminars,[2] several treatises and casebooks,[3] and the well-known

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1. The Delaware Supreme Court and the Court of Chancery together have, over the years, rendered hundreds of opinions dealing with the duties of corporate directors. *See, e.g.*, Stone v. Ritter, 911 A.2d 362, 370 (Del. 2006) (holding that the director's duty of good faith is an element of the director's duty of loyalty, not an independent fiduciary duty); ATR-Kim Eng Fin. Corp. v. Araneta, C.A. No. 489-N, 2006 WL 3783520, at *15–17 (Del. Ch. Dec. 21, 2006) (finding that director breached his duty of loyalty by stripping corporation of its substantial assets for no consideration), *aff'd*, No. 60, 2007, 2007 WL 1704647 (Del. June 14, 2007) (unpublished table decision).

2. *See, e.g.*, Corporate Board Member, Conferences, http://www.boardmember.com/conferences/ (last visited Oct. 7, 2007) (listing ten director education programs for the years 2007–2008); Seattle University, School of Law, Center on Corporations, Law & Society, The Fifth Annual Directors Training Academy: Adding Value Through Legal, Ethical, and Responsible Corporate Governance, http://www.law.seattleu.edu/ccls/events/directorstraining/2007/brochure.pdf (publicizing conference held on June 15, 2007).

3. All major corporate law casebooks designed for United States law schools and all major corporate law treatises contain materials—to varying extents—on director fiduciary duties. *See, e.g.*, 1 R. FRANKLIN

Corporate Director's Guidebook, recently released in its fifth edition.[4] By contrast, legal materials on the fiduciary duties of corporate officers—key actors and agents in any company—are quite sparse.[5] Case law is meager and undeveloped, with even such a baseline issue as the applicability of the business judgment rule lacking resolution.[6] Treatises, institutes, and other legal materials frequently lump officer fiduciary duties with those of directors or treat them as an afterthought or, in many instances, overlook the subject altogether.[7] There is no preeminent, standard reference serving as the "*Corporate Officer's Guidebook*."

Exacerbating a lack of legal materials, empirical evidence suggests lawyers do not routinely advise corporate officers as to their fiduciary duties.[8] Whether lawyer neglect is the cause, or the effect, of the paucity of legal materials is unknown. Whatever the reason for the oversight, the continuing inattention to officer fiduciary duties, in comparison to the immense attention lavished on the duties of corporate directors, is striking.

This Article seeks to begin rectifying this glaring gap in legal literature and professional practice. Fiduciary duties as a vital component of an effective corporate governance system work on an *ex ante* basis—i.e., officers must be advised of such duties beforehand if such duties are to influence conduct. Officers, moreover, are unlikely to deliberately adhere to fiduciary duties if lawyers do not first counsel them as to the essential contours of those duties. And lawyers in turn are more likely to offer such critical advice if they have dependable and convenient legal material for doing so.

Part II of this Article describes the sources of legal material for deriving a succinct exposition of officer fiduciary duties. Part III provides suggested "model" fiduciary duty advice for lawyers to use in counseling corporate officers and managers. Of course, the proposed advice can and should be modified to take account of various factors noted in Part III. An Appendix reproduces the source material from which the model advice is drawn.

II. Sources of Authority for Officer Fiduciary Duties

In thirty-four states there are both statutory and common law sources for officer fiduciary duties.[9] The remaining sixteen states have only common law. The primary

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Balotti & Jesse A. Finkelstein, The Delaware Law of Corporations and Business Organizations § 4.17 (3d ed. 2007).

4. Comm. on Corp. Laws, Section of Bus. Law, Am. Bar Ass'n, Corporate Director's Guidebook (5th ed. 2007).

5. *See* Lyman P.Q. Johnson & David Millon, *Recalling Why Corporate Officers Are Fiduciaries*, 46 Wm. & Mary L. Rev. 1597, 1600–01, 1609–10 (2005).

6. Lyman P.Q. Johnson, *Corporate Officers and the Business Judgment Rule*, 60 Bus. Law. 439 (2005); Lawrence A. Hamermesh & A. Gilchrist Sparks, III, *Corporate Officers and the Business Judgment Rule: A Reply to Professor Johnson*, 60 Bus. Law. 865 (2005).

7. Casebooks and treatises pay little, if any, separate attention to the fiduciary duties of corporate officers. *See* Johnson & Millon, *supra* note 5, at 1600 & n.10, 1609–10 (noting how legal materials generally lump officers and directors together, making no distinctions between them).

8. Lyman P.Q. Johnson & Robert V. Ricca, *(Not) Advising Corporate Officers About Fiduciary Duties*, 42 Wake Forest L. Rev. 663, 669–78 (2007).

9. Model Bus. Corp. Act Ann. § 8.42 (2005) (listing thirty states with statutes based on the Model Act). *See infra* note 16 for a citation to all thirty-four statutes. As noted in footnote 16, two states—Nevada

common law source is the law of agency—officers being agents[10]—and the recent *Restatement (Third) of Agency* ("*Restatement*") is the most authoritative and thorough source of agency law principles.[11] To be sure, on certain points the law of agency in some states may differ from those principles articulated in the *Restatement*, especially until courts and lawyers become more familiar with—and accordingly have occasion to help shape the law to reflect—some of the doctrinal innovations of the *Restatement*. In the area of the fiduciary duties of agents, however, that is unlikely to be the case, inasmuch as core doctrinal precepts appear to enjoy wide acceptance. Of course, given the paucity of case law directly addressing the fiduciary duties of corporate officers, it remains possible that courts, for various policy rationales thought persuasive for senior executives, may temper the way in which traditional agency principles are applied to such persons. Conceptually, however, officers are agents and, absent convincing case law guidance to the contrary, lawyers should counsel them as such. Those sections of the *Restatement* most pertinent to officer fiduciary duties are set forth verbatim in Appendix 1.

In thirty-two of the thirty-four states that have codified officer fiduciary duties, their statutory source derives from section 8.42 of the Model Business Corporation Act, a copy of which is set forth in Appendix 2.[12] Section 8.42, captioned "Standards of Conduct for Officers," was first adopted in 1984.[13] It

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and New York—have statutory standards of conduct for officers but those statutes are not based on the Model Act. Moreover, the statutes of South Dakota and West Virginia appear to be based on the Model Act but for some reason (perhaps oversight) the Annotated Model Act does not list the statutes of those two states.

10. *See* Johnson & Millon, *supra* note 5; Jill Barclift, *Senior Corporate Officers and the Duty of Candor: Do the CEO and CFO Have a Duty To Inform?*, 41 VAL. U. L. REV. 269 (2006).

Although this Article specifically addresses corporate officers, the agency principles drawn on in fashioning advice for officers about their fiduciary duties can apply more broadly in the business organization area. They are pertinent to unincorporated associations, such as in advising managers of limited liability companies and partners of partnerships, inasmuch as those persons are agents, subject, of course, to what the applicable business entity statute and operating agreement or partnership agreement specify on the subject of fiduciary duties. Unless no fiduciary duties whatsoever are owed—see *infra* note 33 for recent scholarship exploring policy concerns about such an extreme arrangement—managers and partners also should be advised of their duties by the business's lawyer, in the same essential manner (if not with the same substantive content) as this Article advocates for corporate officers.

11. RESTATEMENT (THIRD) OF AGENCY (2006). Those sections of the *Restatement* most relevant to agent duties are reproduced in Appendix 1. The Reporter for the *Restatement*, Professor Deborah DeMott, has written articles on agency principles subsequent to her drafting of the *Restatement*. *See* Deborah A. DeMott, *The Discrete Roles of General Counsel*, 74 FORDHAM L. REV. 955 (2005); Deborah A. DeMott, *Inside the Corporate Veil: The Character and Consequences of Executives' Duties*, 19 AUSTL. J. CORP. L. 251 (2006); Deborah A. DeMott, *Disloyal Agents*, 58 ALA. L. REV. 1049 (2007).

12. *See* Appendix 2 & *supra* note 16. Delaware, the leading corporate law state, has no general statutory standards of conduct for officers or directors. However, Delaware does have a statute dealing with conflict of interest transactions between a corporation and any of its officers or directors. DEL. CODE tit. 8, § 144 (2007) (citations to the Delaware Code are to the official online version at http://www.delcode.delaware.gov/ (last accessed Sept. 27, 2007)). Also, to be eligible for indemnification by the corporation, an officer must have acted "in good faith and in a manner the person reasonably believed to be in or not opposed to the best interests of the corporation." DEL CODE tit. 8, § 145(a), (b) (2007). This Article does not specifically address corporate statutes dealing with conflict of interest transactions involving, or indemnification statutes covering, corporate officers. Such statutes do require certain specified conduct of officers. Adherence to the model advice set forth in Part III substantially enhances the likelihood that officers will meet the required standard of conduct prescribed in those sorts of statutes.

13. *See* MODEL BUS. CORP. ACT § 8.42 (2005).

was most recently amended in 2005 to add the current subsection (b),[14] which imposes a disclosure obligation on officers in certain far-ranging situations. The latest version has not been adopted by any state,[15] but earlier versions have been adopted, either verbatim or with some variation, in thirty-two states.[16]

States deviating from later versions of section 8.42 of the Model Act have done so in a variety of ways. For example, Minnesota and North Dakota continue to require that officers act with the care of an "ordinarily prudent person"[17]—the original, possibly stricter, standard of care language from 1984.[18] Also, Georgia has omitted the Model Act requirement that an officer act in what he or she reasonably believes to be the corporation's best interests and also has deleted subsection (c), which permits an officer to rely on various persons.[19] Other states have altered the standard in yet additional ways.[20] Consequently, the statutory standard for the specific state in which the company is incorporated must be carefully examined.

The statutory standards of conduct and the *Restatement* differ in how they formulate officer duties. First, unlike section 8.42,[21] the *Restatement* does not expressly impose on agents a duty to act in good faith except when seeking a principal's consent to, and when acting in conjunction with, a conflict of interest transaction. Second, section 8.42 contains an explicit right to rely on others,[22] including other

14. Comm. on Corp. Laws, Section of Bus. Law, Am. Bar Ass'n, *Changes in the Model Business Corporation Act—Amendments Relating to Chapters 1, 7, 8 and 14*, 60 BUS. LAW. 943, 951 (2005).

15. The statement in the text is based on a survey of statutes which were in effect as of August 1, 2007.

16. ALA. CODE § 10–2B-8.42 (1999); ALASKA STAT. §§ 10.06.483(e), (f) (2004); ARIZ. REV. STAT. ANN. § 10-842 (2004); ARK. CODE ANN. § 4-27-842 (2001); COLO. REV. STAT. §§ 7-108-401, 402 (2007); CONN. GEN. STAT. ANN. § 33-765 (West 2005); GA. CODE ANN. § 14-2-842 (2003); HAW. REV. STAT. ANN. § 414-233 (LexisNexis 2004); IDAHO CODE ANN. § 30-1-842 (2005); IOWA CODE ANN. § 490.842 (West 1999 & Supp. 2007); KY. REV. STAT. ANN. § 271B.8-420 (West 2006); LA. REV. STAT. ANN. § 12:91 (1994 & Supp. 2007); ME. REV. STAT. ANN. tit. 13-C, § 843 (2005); MASS. GEN. LAWS ch. 156B, § 65 (2004); MICH. COMP. LAWS ANN. § 450.1541(a) (West 2002); MINN. STAT. § 302A.361 (2006); MISS. CODE ANN. § 79-4-8.42 (2001); MONT. CODE ANN. § 35-1-443 (2005); NEB. REV. STAT. § 21-2099 (1997); N.H. REV. STAT. ANN. § 293-A:8.42 (1999); N.C. GEN. STAT. ANN. § 55-8-42 (West 2005); N.D. CENT. CODE § 10-19.1-60 (2005); OR. REV. STAT. § 60.377 (2005); 15 PA. CONS. STAT. ANN. §§ 1712(c), 1732(c) (West 1995); S.C. CODE ANN. § 33-8-420 (2006); S.D. CODIFIED LAWS § 47-1A-842 (2007) (citation to the South Dakota Code is to the official online version at http://legis.state.sd.us/statutes/StatutesQuickFind.aspx (last accessed Sept. 27, 2007)); TENN. CODE ANN. §§ 48-18-403, 48-18-601 (2002); TEX. BUS. CORP. ACT art. 2.42 (2007) (citation to the Texas Business Corporation Act is to the official online version at http://tlo2.tlc.state.tx.us/statutes/ba.toc.htm (last accessed Sept. 27, 2007)); UTAH CODE ANN. § 16-10a-840 (2005); WASH. REV. CODE ANN. § 23B.08.420 (West 1994); W. VA. CODE ANN. § 31D-8-842 (LexisNexis 2003); WYO. STAT. ANN. § 17-16-842 (2007).

Nevada and New York also have statutory standards of conduct for officers that differ from the Model Act. The Nevada statute essentially requires only that the officer act in good faith and "with a view to the interests of the corporation." NEV. REV. STAT. ANN. § 78.138 (LexisNexis 1994 & Supp. 2005). The New York statute requires good faith and the care that an ordinarily prudent person would use. N.Y. BUS. CORP. LAW § 715(h) (Consol. 2003).

17. MINN. STAT. ANN. § 302A.361 (2006); N.D. CENT. CODE § 10-19.1-60 (2005). New York, although not a Model Act state, also imposes this requirement. N.Y. BUS. CORP. LAW § 715(h) (Consol. 2003).

18. *See* MODEL BUS. CORP. ACT § 8.42 (1984).

19. *Compare* GA. CODE ANN. § 14–2-842 (2003), *with* MODEL BUS. CORP. ACT § 8.42 (2005).

20. *See* MODEL BUS. CORP. ACT ANN. § 8.42 (2005).

21. *See* Appendix 2, MODEL BUS. CORP. ACT § 8.42 (2005).

22. *See id.*

employees, unlike the *Restatement*, probably because the latter addresses agents generally, not just corporate officers. Moreover, officers under the *Restatement* are likely to have an implicit right to rely, at least in certain situations, as part of their duties of care and competence.[23]

Third, neither section 8.42 itself nor the Official Comment to that section ever uses the term "fiduciary" to describe officer duties, whereas the *Restatement* states explicitly that an agent's duty of loyalty is a "fiduciary duty."[24] Interestingly, however, the *Restatement* describes the agent's duties of care, competence, and diligence as "performance" duties,[25] deliberately avoiding the descriptor of "fiduciary," while noting, however, that other sources do refer to such duties as fiduciary in nature.[26] Also, the *Restatement* establishes as the standard applicable to the duties of care, competence, and diligence that level of conduct "normally exercised by agents in similar circumstances."[27] Section 8.42, however, specifies only a standard of care, without using the terms "competence" or "diligence," and establishes as the applicable standard "the care that a person in a like position would reasonably exercise under similar circumstances."[28]

Finally, the *Restatement* states that a "general or broad" advance release of an agent from the agent's "general fiduciary obligation to the principal [i.e., the duty of loyalty] is not likely to be enforceable."[29] As to the duties of care, competence, and diligence, however, the *Restatement* states that a "contract may, in appropriate circumstances, raise or lower the standard" applicable to those duties and that such duties can be "contractually shaped," but it does not indicate whether they can be eliminated altogether.[30] By way of contrast, the Official Comment to Model Act section 8.42 states that an officer's disclosure obligations may not be negated by agreement but their scope under subsection (b)(1) "may be shaped."[31] The issue of how far employment agreements may go in limiting the fiduciary duties of officers or in reducing (eliminating?) officers' monetary liability for breach, or both, is likely to receive significant attention in the years ahead as lawyers increasingly appreciate the current open-ended nature of officer liability. This issue of the degree to which fiduciary duties are "mandatory," rather than being subject

23. *See* Appendix 1, RESTATEMENT (THIRD) OF AGENCY § 8.08 (2006).

24. *See id.* § 8.01. Model Business Corporation Act § 8.42, modeled on the director standard of conduct found in Model Act § 8.30, is probably essentially a duty of care provision. *See* MODEL BUS. CORP. ACT ANN. § 8.30 cmt. (2005) ("This standard of conduct is often characterized as a duty of care.").

25. *See* RESTATEMENT (THIRD) OF AGENCY § 8.01 cmt. b (2006); *id.* § 8.08(b) reporter's note b.

26. *See id.* § 8.08(b) reporter's note b. Although the term "prudence" is less widely used today than in years past, the duty of care included, historically, the obligation of "prudence." *See supra* notes 17–18 and accompanying text. Prudence is an ancient moral virtue involving deliberation and judgment that, when exercised on behalf of another, would seem to be "fiduciary" in character. *See* Joseph F. Johnston, Jr., *Natural Law and the Fiduciary Duties of Business Managers*, *in* BUSINESS AND RELIGION: A CLASH OF CIVILIZATIONS? 279, 289–90 (Nicholas Capaldi ed., 2005).

27. *See* Appendix 1, RESTATEMENT (THIRD) OF AGENCY § 8.08 (2006).

28. *See* Appendix 2, MODEL BUS. CORP. ACT § 8.42 (2005).

29. *See* RESTATEMENT (THIRD) OF AGENCY § 8.06 cmt. b (2006).

30. *See* RESTATEMENT (THIRD) OF AGENCY § 8.08 cmt. b (2006).

31. *See* MODEL BUS. CORP. ACT ANN. § 8.42 cmt. (2005).

to contractual change, will undoubtedly arise in the corporate setting,[32] just as it already has arisen, albeit in somewhat different form, in the unincorporated business entity setting.[33]

Due to these and other possible differences in formulation, the exact interrelationship between the requirements of the *Restatement* and section 8.42 is not completely clear,[34] though each source is mindful of the other. The Comment to section 8.08 of the *Restatement* expressly refers to section 8.42 as establishing standards of conduct for corporate officers.[35] And the Official Comment to Model Act section 8.42 explicitly cites the *Restatement (Second) of Agency* on an agent's duties of obedience, loyalty, and care, and suggests that such agency principles govern the conduct of corporate employees and officers.[36] For purposes of counseling officers *ex ante*, it is probably best to regard the duties specified in both section 8.42 (as modified in certain states) and the *Restatement* as fully applicable, without worrying about identified differences or possible overlap between these two sources. Consequently, as part of a preventive risk reduction strategy, the generic advice formulated in Part III draws on both sources as wholly applicable to corporate officers.[37] It bears emphasizing as well that the fiduciary duties described below pertain to any lawyer serving as a corporate officer by, for example, holding the position of "Chief Legal Officer."

III. Model Fiduciary Duty Advice for Officers

Corporate activity today is heavily regulated. Securities, environmental, antitrust, employment, and criminal laws—to mention just a few—all bear on a company's business affairs. Consequently, corporate officers may need to

32. Aaron D. Jones, *Corporate Officer Wrongdoing and the Fiduciary Duties of Corporate Officers Under Delaware Law*, 44 Am. Bus. L.J. 475 (2007) (arguing for limits on the ability of officers to alter their fiduciary duties contractually).

33. Several recent articles thoroughly describe and analyze the policy concerns of broadly permitting a contractual "opt-out" of fiduciary duties in the unincorporated business association context. Carter G. Bishop, *A Good Faith Revival of Duty of Care Liability in Business Organization Law*, 41 Tulsa L. Rev. 477 (2006); Reza Dibadj, *The Misguided Transformation of Loyalty into Contract*, 41 Tulsa L. Rev. 451 (2006); Robert W. Hillman, *Closely-Held Firms and the Common Law of Fiduciary Duty: What Explains the Enduring Qualities of a Punctilio*, 41 Tulsa L. Rev. 441 (2006); Mark J. Loewenstein, *Fiduciary Duties and Unincorporated Business Entities: In Defense of the "Manifestly Unreasonable" Standard*, 41 Tulsa L. Rev. 411 (2006).

Contractual opt-outs of fiduciary duties are problematic enough when a person (such as a stockholder) acts in his or her own behalf to permit a fiduciary (such as a director) to be (somewhat) free of fiduciary constraints. It is more problematic yet when a person who is a fiduciary (e.g., a corporate director) acts on behalf of a party to whom he or she owes fiduciary duties, to permit yet another fiduciary (e.g., a corporate officer) to be (somewhat) free of fiduciary duties. *See* Johnson & Millon, *supra* note 5, at 1641. Thus, it may be more problematic to carve back an agent's duties in the latter setting than in the former.

34. Johnson & Millon, *supra* note 5, at 1631–34.

35. *See* Restatement (Third) of Agency § 8.08 cmt. b (2006).

36. *See* Model Bus. Corp. Act Ann. § 8.42 cmt. (2005).

37. The proposed advice is based on the latest (2005) version of section 8.42. Although that version has yet to be adopted by any state, the disclosure obligations it imposes on a company's officers are sound and serve the company's interests. Moreover, section 8.11 of the *Restatement* mandates disclosure in certain instances as well, although it is probably narrower in scope than the latest version

be advised as to how a host of regulatory regimes might affect a company's operations. Many of these matters are, or should be, addressed in a company's well-drawn code of conduct or code of ethics.[38] But the fiduciary duties imposed on corporate officers by state law overarch *all* officer functions—they are broadly-worded standards, not narrow rules, and they are pervasive and unremitting in reach.[39]

For this reason, officers should be regularly advised as to their fiduciary duties. This is best done when (or shortly after) they are first hired and periodically thereafter. They should also be reminded of those duties at the outset of significant events, such as, for example, when engaging in acquisitions, divestitures, substantial financings, or financial restructurings, and when contemplating major contracts or projects of any kind.

It is a daunting interpersonal challenge for a lawyer to provide fiduciary duty advice at appropriate times and in a suitable manner, while avoiding the appearance of being a legal "scold." Especially for in-house counsel—who likely regard themselves as business managers and "team players" as well as lawyers—this can involve some awkwardness. At the same time, to discharge their own legal and professional obligations[40]—which are owed to the company, not the officers—lawyers must effectively communicate to officers the essential contours of their fiduciary obligations.

What follows is intended to be a useful resource for corporate lawyers and law professors. It is not meant to be a verbatim script or formula to be uncritically adopted. It is, rather, meant to be more of a template, one effort to succinctly but fully convey the essential gist of officer duties. The prose style is deliberately a bit more conversational in tone, while also maintaining an inevitable seriousness. It will, of course, require tailoring to reflect possible state law differences noted above, as well as the lawyer's own communication style and relationship to the particular officer being advised, and to best meet the client company's specific circumstances and unique needs. The advice might also be modified somewhat to take account of differing functional responsibilities or levels of seniority by, for example, using illustrations suitable for particular groups or persons but not others.

Without question, the advice could simply be written up and delivered to corporate officers, possibly as a key part of the company's code of conduct. At least

of section 8.42. *See* Appendix 1, RESTATEMENT (THIRD) OF AGENCY § 8.11 (2006). The duty of a trustee to provide information also is an important related subject today. *See* Thomas P. Gallanis, *The Trustees Duty to Inform*, 85 N.C. L. REV. 1595 (2007).

38. Section 406 of the Sarbanes-Oxley Act requires a public company to disclose whether it has adopted a code of ethics for senior financial officers and to disclose in public filings if its code of ethics changes or if any waivers from the code are granted by the company. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, § 406, 116 Stat. 745, 789–90 (codified at 15 U.S.C. § 7264 (Supp. V 2005)). It is now customary for public companies to include a wide range of matters in their codes of ethics and to make them applicable to a significant number, if not all, of their employees.

39. *Cf.* Malone v. Brincat, 722 A.2d 5, 10 (Del. 1998) (describing director duties as "unremitting").

40. Johnson & Ricca, *supra* note 8, at 681–84 & nn. 87–105 (describing professional responsibility of lawyers to advise officers).

at the hiring stage, and perhaps occasionally thereafter, however, the advice may carry greater weight if delivered in person, as frequently is done when advising directors. Perhaps, for example, this could be done, initially, as part of an orientation session and, later, at a periodic "update" event. It should also be made very clear that the lawyer giving the advice represents the company, not the individual officer. It is worth underscoring yet again that the advice set forth below applies to those lawyers who themselves serve as corporate officers. One aspect of this is seen in the obligation of all officers—including legal counsel—to use their special skills and knowledge to carry out their responsibilities. Such skills and knowledge are likely to be taken into account in determining whether an officer has acted with appropriate care and diligence.

- As an officer of [Company X], you are a fiduciary. This means you owe a legal duty to act loyally for the company's benefit. When carrying out your responsibilities, you must always seek to advance what you reasonably believe to be the company's best interests, and you must place the company's well-being above your own personal interests or those of anyone else.
- You also owe the company a duty to always act in good faith. This means you should act with an honest purpose. It also means you must not deliberately disregard your responsibilities and that you must not intentionally violate any laws.
- You are not to ask for or receive any significant benefits from any third party in connection with actions you take on behalf of the company, including gifts or business opportunities, unless you obtain approval from the board of directors. This is true even if you think doing so will not harm the company. While employed by the company, you must never act on behalf of someone doing business, or proposing to do business, with the company.
- You may not compete with the company in any of its business endeavors or assist any of its competitors unless you obtain approval from the board of directors. You must not use the company's property for your own or anyone else's purposes. You must not use or communicate the company's confidential information for your own purposes or those of anyone else.
- You must not enter into a business transaction with the company unless you obtain approval from the board of directors. If you wish to propose such a transaction, or if any relative or business or professional affiliate of yours wishes to do so, you must contact [specify] before taking any actions involving the company on such a proposal.
- In addition to owing the company a duty of loyalty and good faith, you also owe a duty to act with due care, competence, and diligence. You must always act with the care that is reasonable for someone in your position under similar circumstances. You must use your special skills and knowledge in carrying out your responsibilities. You must follow lawful instructions or other direction you receive from the board or from an officer senior to you to whom you report.

- It is important for you to know that you must report certain matters to others in the company. This includes any business information within your sphere of responsibility that you know, or have reason to believe, to be either significant to the person to whom you report or that that person would wish to have, so that he or she can effectively perform his or her job.[41] It also includes any information you have concerning actual or probable material violations of law, or breach of duty by any employee or agent of the company, that you believe has already occurred or is about to occur. Any such past or imminent violation of law or duty should be immediately reported to [specify]. Information, or a violation of law or duty, can be significant or material either because of the dollar amount involved or because of its serious nature.
- Perhaps the best way to recall your fiduciary duties in a shorthand fashion is simply to remember that you owe a duty of loyalty to act in the best interests of the company and a duty of reasonable care when acting on its behalf.
- If you have any questions about what I said, or if any question ever arises in your mind as to what these duties entail, please contact me [or specify] and we can speak further.

There are several reasons why lawyers should advise corporate officers as to their fiduciary duties.[42] Only three will be briefly mentioned here. First, in the years ahead it is quite likely that the conduct of corporate officers will be judicially evaluated more frequently for adherence to applicable fiduciary duties.[43] For the good of the company's and the officer's own interests, officers should be made aware of the basic thrust of their duties before they act, not simply upon being sued. In short, it is an integral part of an officer's legal and cultural "literacy" to more clearly understand what his or her fiduciary obligations encompass. Second, the author believes that persons who, in strong language, are told by a respected figure, such as legal counsel, that they owe a special responsibility to protect and advance the interests of others are more likely to refrain from negative conduct, and engage in positive conduct, than are people who believe they can solely advance their own interests. To advise someone that he or she must be "loyal" to the interests of the larger enterprise in carefully discharging his or her business responsibilities is likely to lead the listener both to consciously desire to act at a higher level and, possibly, actually to perform at a higher level.

The absence of such moral-sounding language, by way of contrast, may lead an actor (such as an officer) to believe that he or she largely may (and perhaps should) act out of self-interested motives. The inaction of lawyers on this matter

41. Note that the reporting obligation under section 8.11 of the *Restatement* is formulated somewhat differently than the obligation under section 8.42 of the Model Act. The proposed advice combines the two formulations.

42. For a discussion of these reasons, see Johnson & Ricca, *supra* note 8, at 681–91.

43. In 2004, Delaware amended its jurisdictional statute to assert jurisdiction over officers who are not also directors. *See* DEL. CODE tit. 10, § 3114(b) (2007).

may itself be sending a negative signal to officers and thereby reinforcing an unhealthy norm of self-interest.

Moreover, by advising officers of their fiduciary duties the lawyer is not telling the officer what to do. Rather, when lawyers clearly and regularly impart to officers that they owe duties of care and loyalty, these social-legal norms will help officers reflectively assess, and possibly alter, their own conduct. This is not a substitute for the lawyer, in appropriate settings, bringing to bear his or her own judgment as to the propriety of a transaction or course of conduct. It does, however, supplement the view of the lawyer and avoids unhealthy client efforts to wholly shift responsibility to the lawyer to legally "pass" on or "bless" the matter. Officers are made aware that with respect to any and all aspects of their conduct they must always satisfy *themselves* that they have fully discharged their fiduciary duties to the company.

Third, a conversation between company counsel and a new officer about fiduciary duties—and other matters as well—can put a human face on legal advice while also serving to habituate officers to consult lawyers at the very outset of significant matters. This enhances the ability of lawyers to work with business managers to prevent problems and reduce company risk, to the good of all concerned.

APPENDIX 1
[Restatement (Third) of Agency (2006)]

Chapter 8

DUTIES OF AGENT AND PRINCIPAL TO EACH OTHER

TOPIC 1. AGENT'S DUTIES TO PRINCIPAL

TITLE A. GENERAL FIDUCIARY PRINCIPLE

§ 8.01 General Fiduciary Principle

An agent has a fiduciary duty to act loyally for the principal's benefit in all matters connected with the agency relationship.

TITLE B. DUTIES OF LOYALTY

§ 8.02 Material Benefit Arising Out of Position

An agent has a duty not to acquire a material benefit from a third party in connection with transactions conducted or other actions taken on behalf of the principal or otherwise through the agent's use of the agent's position.

§ 8.03 Acting as or on Behalf of an Adverse Party

An agent has a duty not to deal with the principal as or on behalf of an adverse party in a transaction connected with the agency relationship.

§ 8.04 Competition

Throughout the duration of an agency relationship, an agent has a duty to refrain from competing with the principal and from taking action on behalf of or otherwise assisting the principal's competitors. During that time, an agent may take action, not otherwise wrongful, to prepare for competition following termination of the agency relationship.

§ 8.05 Use of Principal's Property; Use of Confidential Information

An agent has a duty

(1) not to use property of the principal for the agent's own purposes or those of a third party; and

(2) not to use or communicate confidential information of the principal for the agent's own purposes or those of a third party.

§ 8.06 Principal's Consent

(1) Conduct by an agent that would otherwise constitute a breach of duty as stated in §§ 8.01, 8.02, 8.03, 8.04, and 8.05 does not constitute a breach of duty if the principal consents to the conduct, provided that

(a) in obtaining the principal's consent, the agent

(i) acts in good faith,

(ii) discloses all material facts that the agent knows, has reason to know, or should know would reasonably affect the principal's judgment unless the principal has manifested that such facts are already known by the principal or that the principal does not wish to know them, and

(iii) otherwise deals fairly with the principal; and

(b) the principal's consent concerns either a specific act or transaction, or acts or transactions of a specified type that could reasonably be expected to occur in the ordinary course of the agency relationship.

(2) An agent who acts for more than one principal in a transaction between or among them has a duty

(a) to deal in good faith with each principal,

(b) to disclose to each principal

(i) the fact that the agent acts for the other principal or principals, and

(ii) all other facts that the agent knows, has reason to know, or should know would reasonably affect the principal's judgment unless the principal has manifested that such facts are already known by the principal or that the principal does not wish to know them, and

(c) otherwise to deal fairly with each principal.

TITLE C. DUTIES OF PERFORMANCE

§ 8.07 Duty Created by Contract

An agent has a duty to act in accordance with the express and implied terms of any contract between the agent and the principal.

§ 8.08 Duties of Care, Competence, and Diligence

Subject to any agreement with the principal, an agent has a duty to the principal to act with the care, competence, and diligence normally exercised by agents in similar circumstances. Special skills or knowledge possessed by an agent are circumstances to be taken into account in determining whether the agent acted with due care and diligence. If an agent claims to possess special skills or knowledge, the agent has a duty to the principal to act with the care, competence, and diligence normally exercised by agents with such skills or knowledge.

§ 8.09 Duty to Act Only Within Scope of Actual Authority and to Comply with Principal's Lawful Instructions

(1) An agent has a duty to take action only within the scope of the agent's actual authority.

(2) An agent has a duty to comply with all lawful instructions received from the principal and persons designated by the principal concerning the agent's actions on behalf of the principal.

§ 8.10 Duty of Good Conduct

An agent has a duty, within the scope of the agency relationship, to act reasonably and to refrain from conduct that is likely to damage the principal's enterprise.

§ 8.11 Duty to Provide Information

An agent has a duty to use reasonable effort to provide the principal with facts that the agent knows, has reason to know, or should know when

(1) subject to any manifestation by the principal, the agent knows or has reason to know that the principal would wish to have the facts or the facts are material to the agent's duties to the principal; and
(2) the facts can be provided to the principal without violating a superior duty owed by the agent to another person.

APPENDIX 2

[Model Business Corporation Act § 8.42 (2005)]

§ 8.42 Standards of Conduct for Officers

(a) An officer, when performing in such capacity, has the duty to act:
  (1) in good faith;
  (2) with the care that a person in a like position would reasonably exercise under similar circumstances; and
  (3) in a manner the officer reasonably believes to be in the best interests of the corporation.

(b) The duty of an officer includes the obligation:
  (1) to inform the superior officer to whom, or the board of directors or the committee thereof to which, the officer reports of information about the affairs of the corporation known to the officer, within the scope of the officer's functions, and known to the officer to be material to such superior officer, board or committee; and
  (2) to inform his or her superior officer, or another appropriate person within the corporation, or the board of directors, or a committee thereof, of any actual or probable material violation of law involving the corporation or material breach of duty to the corporation by an officer, employee, or agent of the corporation, that the officer believes has occurred or is likely to occur.

(c) In discharging his or her duties, an officer who does not have knowledge that makes reliance unwarranted is entitled to rely on:
  (1) the performance of properly delegated responsibilities by one or more employees of the corporation whom the officer reasonably believes to be reliable and competent in performing the responsibilities delegated; or
  (2) information, opinions, reports or statements, including financial statements and other financial data, prepared or presented by one or more employees of the corporation whom the officer reasonably believes to be reliable and competent in the matters presented or by legal counsel, public accountants, or other persons retained by the corporation as to matters involving skills or expertise the officer reasonably believes are matters (i) within the particular person's professional or expert competence or (ii) as to which the particular person merits confidence.

(d) An officer shall not be liable to the corporation or its shareholders for any decision to take or not to take action, or any failure to take any

action, as an officer, if the duties of the office are performed in compliance with this section. Whether an officer who does not comply with this section shall have liability will depend in such instance on applicable law, including those principles of section 8.31 that have relevance.