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Lyman P.Q. Johnson

Washington and Lee University School of Law, johnsonlp@wlu.edu

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Corporate Officers and the Business Judgment Rule

By Lyman P.Q. Johnson*

"[The business judgment rule], which began as a minor exception, is now so dominant a winning argument that the only fun left is trying to prove that [it] ... does not cover absolutely all forms of corporate theft."1

I. INTRODUCTION

Corporate officers stand at the very center of recent business scandals.2 Executive misconduct has led to numerous criminal charges,3 the bringing of Securities and Exchange Commission administrative proceedings,4 and the imposition of substantial new federal responsibilities mandated by the Sarbanes-Oxley Act.5 One sector of society that, historically, has been strangely silent about officer wrongdoing, is state corporate law.6 Even here, however, prominent judges in Dela-

* Robert O. Bentley Professor of Law, Washington and Lee University Law School. The Frances Lewis Law Center provided support for this project. The author wishes to thank Frank Balotti, Larry Hamermesh, and David Millon for their helpful comments, and David Freed, Kevin White, and Christina Bowden for their excellent research assistance.


3. Grant & Nuzum, supra note 2, at Al; Emshwiller et al., supra note 2, at A1; Executives on Trial: Scandal Scorecard, supra note 2, at B1.

4. Grant & Nuzum, supra note 2, at A1; Emshwiller et al., supra note 2, at A1; Executives on Trial: Scandal Scorecard, supra note 2, at B1.


6. A leading treatise on corporate directors and officers summed up the state of the law as follows: "[T]here is little law on the subject of the liability of corporate officers who are not directors." William E. Knepper & Dan A. Bailey, Liability of Corporate Officers and Directors § 1.15, at 1-54 (2003). See R. Franklin Balotti & Jesse A. Finkelstein, The Delaware Law of Corporations and Business Organizations § 4.17, at 4-36 (3d ed. Supp. 2004) ("Few authorities deal with the nature of the obligation owed by officers to the corporation and its stockholders."); see also A. Gilchrist Sparks III & Lawrence A. Hamermesh, Common Law Duties of Non-Director Corporate Officers, 48 BUS. LAW. 215, 215 (1992) (stating "The precise nature of the duties and liabilities of corporate officers who are not directors is a topic that has received little attention from courts and commentators."). Several states have adopted reforms inspired by the federal Sarbanes-Oxley Act. Largely, these reforms address
ware—the leading corporate law state—have remarked that they expect a new focus on litigation against officers. In fact, to accommodate the expected lawsuits, effective January 1, 2004, the Delaware Chancery Court now asserts personal jurisdiction over officers of Delaware corporations.8

Two problems immediately confront the effort to bring fiduciary duty claims against miscreant officers. First, despite a great deal of loose talk that officers are “fiduciaries,”9 such assertions typically fail to supply any conceptual or positive law foundation for that claim. Recently, this author and David Millon have argued that officers owe strong fiduciary duties because, unlike corporate directors, they are agents of the corporation.10 Second, even with a clear theoretical basis for advancing fiduciary duty claims against officers, when sued, those officers will likely invoke, in defense, the generous protection of the business judgment rule.11 This Article argues that the business judgment rule—a cornerstone concept in corporate law—does not and should not be extended to corporate officers in the same broad manner in which it is applied to directors. The argument proceeds along both descriptive and normative lines. Part II begins by noting the frequency with which commentators and courts uncritically assert that the business judgment rule does cover officers as a matter of positive law. That Part then canvasses decisions applying—or purporting to apply—the business judgment rule to officers. The examination reveals a decidedly more mixed picture than is commonly believed. Delaware, for example, has very little law at all on corporate officers, and has yet to hold squarely that the rule applies to officers as well as directors.12 Only one decision in any jurisdiction appears to have adopted the rule in connection with an officer of a publicly-held corporation, and the court went on, moreover, to find the rule inapplicable.13 Furthermore, although many decisions state that the rule applies to officers, several of these cases involved officers who also served as directors. Consequently, it is unclear whether the rule would be


7. See E. Norman Veasey, Corporate Governance and Ethics in the Post-Enron WorldCom Environment, 38 WAKE FOREST L. REV. 839, 851 (2003); William B. Chandler III & Leo E. Strine, Jr., The New Federalism of the American Corporate Governance System: Preliminary Reflections of Two Residents of One Small State, 152 U. PA. L. REV. 953, 1002–03 (2003). Mr. Veasey recently retired as Chief Justice of the Delaware Supreme Court. Mr. Chandler is Chancellor, and Mr. Strine is a Vice Chancellor, on the Delaware Chancery Court.


9. The foundational case on corporate fiduciary duties in Delaware stated: “Corporate officers and directors ... stand in a fiduciary relation to the corporation and its stockholders.” Guth v. Loft, Inc., 5 A.2d 503, 510 (Del. 1939). A leading corporate law treatise puts the matter as follows: “[C]orporate directors and officers occupy a fiduciary capacity. ... To a great extent, the rules governing liability are the same whether the officer sued is a director or some other officer such as the president, vice president, secretary ... .” WILLIAM MEADE FLETCHER, FLETCHER CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS §§ 837.50, 991 (3d ed. 2003 & Supp. 2004).

11. See infra Part II B.
12. See infra notes 30–41 and accompanying text.
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II. COMMENTARY AND CASE LAW

A. COMMENTARY

The prestigious American Law Institute's (ALI's) *Principles of Corporate Governance* apply the business judgment rule to corporate officers on the same terms as it is applied to directors.\(^4\) In support of this position, the commentary states as follows:

\(^4\) 1 PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 4.01(c) (American Law Institute 1994) [hereinafter ALI PRINCIPLES]. Section 4.01 provides, in pertinent part, as follows:
Sound public policy points in the direction of holding officers to the same duty of care and business judgment standards as directors, as does the little case authority that exists on the applicability of the business judgment standard to officers, and the views of most commentators support this position.\textsuperscript{15}

As support for that assertion, the ALI cites the corporate law treatise written by Professor Harry Henn and John Alexander, along with a dictum from a 1971 Delaware Chancery Court decision.\textsuperscript{16} The Henn and Alexander treatise, last updated in 1983, boldly states that the business judgment rule "is no less applicable to officers in the exercise of their authority,"\textsuperscript{17} but cites no supporting decisions. Instead, it refers to the 1975 edition of Fletcher's well known corporate law treatise.\textsuperscript{18} The Fletcher treatise, in turn, states that the rule "generally applies to decisions of executive officers as well as those of directors."\textsuperscript{19} As authority, Fletcher cites two Delaware opinions addressing the subject through dicta,\textsuperscript{20} one of which contains the dictum relied on by the ALI.\textsuperscript{21} As it turns out, then, the views of "most commentators"—to which the ALI referred\textsuperscript{22}—rest on very slender support.

The commentary to the Model Business Corporation Act makes a similar broad statement: "[T]he business judgment rule will normally apply to decisions within an officer's discretionary authority."\textsuperscript{23} No authority is cited for this assertion, however. Experienced corporate law practitioner Charles Hansen also concludes that "as a matter of precedent, and as a matter of sound policy, it seems clear that officers do and should have the protection of the rule."\textsuperscript{24} Mr. Hansen, unlike others, cites several cases,\textsuperscript{25} although, as indicated in sub-Part B below, those cases

\begin{verbatim}
§ 4.01 Duty of Care of Directors and Officers; the Business Judgment Rule
(a) A director or officer has a duty to the corporation to perform the director's or officer's functions in good faith, in a manner that he or she reasonably believes to be in the best interests of the corporation, and with the care that an ordinarily prudent person would reasonably be expected to exercise in a like position and under similar circumstances. This Subsection (a) is subject to the provisions of Subsection (c) (the business judgment rule) where applicable. . . .
(c) A director or officer who makes a business judgment in good faith fulfills the duty under this Section if the director or officer:
(1) is not interested [§ 1.23] in the subject of the business judgment;
(2) is informed with respect to the subject of the business judgment to the extent the director or officer reasonably believes to be appropriate under the circumstances; and
(3) rationally believes that the business judgment is in the best interests of the corporation.
\end{verbatim}

\textit{Id.}\textsuperscript{15} \textit{Id. at} 140.
\textit{Henn \& Alexander, supra note 16, at 663.}
\textit{Id. (citing 3A William Meade Fletcher, Fletcher Cyclopedia of the Law of Private Corporations §§ 1029–39 (1975)).}
\textit{Fletcher, supra note 18, at 38.}
\textit{Id. at} 42 (citing Kelly v. Bell, 266 A.2d 878 (Del. 1970) and Kaplan v. Centex Corp., 284 A.2d 119 (Del. Ch. 1971)).
\textit{284 A.2d 119, 124 (Del. Ch. 1971).}
\textit{See supra note 14.}
\textit{See supra note 14.}
\textit{Id. (Aspen Law & Bus. Sept. 1, 2001).}
\textit{Id. at} 16–17 (citing, among other cases, Para-Med. Leasing, Inc. v. Hangen, 739 P2d 717 (Wash. Ct. App. 1987)).
do not support the rule in nearly as strong a fashion as Hansen contends. Other notable commentators favoring extension of the business judgment rule to corporate officers include Professor Stephen Bainbridge,26 and Professors Lawrence Hamermesh and Gilchrist Sparks.27 Finally, in their exhaustive treatise on the business judgment rule, Dennis Block and co-authors place existing legal authority in proper perspective: "Numerous courts have referred to the business judgment rule as a doctrine protecting directors and officers without distinguishing between the rule's applicability to officers as opposed to directors. There is, however, only sparse case law that specifically addresses this question."28

Existing commentary does not make—or even attempt to make—a very compelling policy case for extending the business judgment rule to officers but, instead, largely recites case law. That case law, it turns out, is actually quite "sparse."29 Does the little law that exists really support the bold claims that so much commentary makes for it?

B. CASE LAW

1. Delaware Law

The Delaware Supreme Court routinely states that the rule covers officers and directors when it recites the rule in actions involving only directors.30 The court, however, has never held that the rule applies to corporate officers acting in that capacity. In a 1970 decision, Kelly v. Bell,31 the Supreme Court, in affirming a Chancery Court decision,32 broadly stated that "the directors or officers were not necessarily liable to the corporation because they honored the commitment, pro-

26. STEPHEN M. BAINBRIDGE, CORPORATION LAW AND ECONOMICS § 6.4, at 285–86 (2002). Professor Bainbridge acknowledges that it is "less well-settled" that officers should get the benefit of the business judgment rule, as compared to directors. Id.

27. See Sparks & Hamermesh, supra note 6, at 230, 237. Mr. Sparks and Professor Hamermesh recite extensive case law in support of their policy position favoring application of the business judgment rule to officers. As developed in sub-Part B, this author believes that today's more abundant decisional law supporting the rule in that context is weaker than Sparks and Hamermesh, writing in 1992, contend.

28. DENNIS J. BLOCK ET AL., THE BUSINESS JUDGMENT RULE: FIDUCIARY DUTIES OF CORPORATE DIRECTORS 97–98 (5th ed. 1998) (emphasis added). The Committee on Corporate Laws of the Section of Business Law has stated that the business judgment rule "in appropriate circumstances should be available to officers." Committee on Corporate Laws, Changes in the Model Business Corporation Act Pertaining to the Standards of Conduct for Officers; Inspection Rights and Notices—Final Adoption, 54 Bus. Law. 1229, 1230 (1999). The Committee goes on, however, to rightly acknowledge the "limited case law" and to describe that law as "muddled" by various factors. Id. These statements are more muted than the statement in the Model Business Corporation Act's Official Comment. See supra note 23 and accompanying text.

29. BLOCK ET AL., supra note 28.

30. See, e.g., Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156, 1162 (Del. 1995); Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 361 (Del. 1993). For Delaware Chancery Court decisions reciting the rule's applicability to corporate officers in dicta, see Sparks & Hamermesh, supra note 6, at 232 & nn. 107–08. For a collection of cases from numerous jurisdictions reciting the rule's applicability to corporate officers in dicta, see Block et al., supra note 28, at 98 n.456 (and 2002 Supp. at 119).


vided they exercised honest business judgment...."\textsuperscript{33} The lower court earlier had stated, "(u)nder the circumstances of this case ... the [business judgment rule] is applicable to the executive officers...."\textsuperscript{34} These statements, however, were made in a case that sought money damages against only the directors, not the officers. Moreover, the case raised a delegation of responsibility issue and, because the directors had not initially approved the challenged transaction but had, nonetheless, later proceeded with it, the case involved director ratification of earlier officer action.\textsuperscript{35} The case most assuredly, however, did not involve a challenge to the independent action of officers \textit{qua} officers properly acting within their official sphere. The \textit{Kelly} case, therefore, contains a broad dictum but little else in support of according business judgment rule protection to corporate officers.

Likewise, \textit{Kaplan v. Centex Corp.},\textsuperscript{36} a 1971 Chancery Court decision citing \textit{Kelly},\textsuperscript{37} states that a decision of executive officers "may" come within the business judgment rule.\textsuperscript{38} Moreover, the Chancellor went on to say the rule "probably" applied at bar, "in the light of subsequent ratification by the board of directors."\textsuperscript{39} In other words, \textit{Kaplan} specifically linked application of the business judgment rule to board action. Furthermore, given what he called "conflicts in the record,"\textsuperscript{40} the Chancellor stated that he preferred to base his conclusions on findings from the record, "and not on the broad cutting edge of the Rule."\textsuperscript{41} Thus, application of the business judgment rule to officers did not supply the ground for decision in the \textit{Kaplan} case.

Recalling that the ALI's \textit{Principles of Corporate Governance} and Fletcher's treatise ultimately relied on these two Delaware decisions as the basis for their strong claims in favor of extending the rule to corporate officers,\textsuperscript{42} those cases turn out to provide rather flimsy backing for that position. Do other decisions applying Delaware law support broad application of the business judgment rule to corporate officers?

Over the past few years, two non-Delaware courts, along with the U.S. District Court for the District of Delaware, have applied Delaware law to conclude that

\textsuperscript{33} \textit{Kelly}, 266 A.2d at 879.  
\textsuperscript{34} \textit{Kelly}, 254 A.2d at 75.  
\textsuperscript{35} This is seen in the Delaware Supreme Court's phrasing: "[T]he directors or officers were not necessarily liable to the corporation because they \textit{honored} the [nonauthorized] commitment...." \textit{Kelly}, 266 A.2d at 879 (emphasis added). Thus, although the board made no initial considered decision that could be the subject of business judgment rule protection, in later electing to honor the commitment, the board at least impliedly ratified the officers' actions, if indeed it did not, at that later time, make its own belated business judgment. The court's statement quoted above (see \textit{supra} text accompanying note 33) goes on specifically to premise upholding the challenged action on the exercise of business judgment, suggesting the Delaware Supreme Court believed the directors' later decision to "honor" the commitment to be such an exercise of judgment.  
\textsuperscript{36} \textit{Kaplan v. Centex Corp.}, 284 A.2d 119 (Del. Ch. 1971).  
\textsuperscript{37} \textit{Id.} at 124.  
\textsuperscript{38} \textit{Id.}  
\textsuperscript{39} \textit{Id.} (emphasis added).  
\textsuperscript{40} \textit{Id.} at 125.  
\textsuperscript{41} \textit{Id.}  
\textsuperscript{42} See \textit{supra} notes 16, 20 and accompanying text.
the business judgment rule does protect corporate officers. A 1997 Minnesota Court of Appeals decision, Potter v. Pohlad, involved an action against three persons who had served as corporate officers, two of whom also had served as directors. Thus, as to the third officer, who was not a director, application of the business judgment rule was squarely at issue. The court, citing the Fletcher treatise for support, held the rule applicable to the corporate officer. The court noted that an officer's responsibilities may be more extensive than those of a director and that the "level" of fiduciary duty owed might be affected by circumstances. The court, moreover, acknowledged that corporate officers were agents and, as such, owed an obligation to disclose material information to the board, but oddly, the court measured performance of that duty by the gross negligence standard applicable in Delaware to directors, not the ordinary negligence standard typically governing agents. Concluding that plaintiff had not offered evidence of gross negligence, the court affirmed summary judgment for the officers. Although Potter applied the business judgment rule to shield a corporate officer on the same basis as directors, the ruling reached that result only by ignoring the fiduciary duty implications of the admitted agency status of the officer. Had the court appreciated that officers are not fiduciaries for the same reason as directors, but owe stricter duties due to their agency status, it might have been more reluctant to grant the officer the same highly deferential business judgment review given directors.

A 2003 decision from the U.S. District Court for the Western District of Washington applied Delaware law and held the business judgment rule applicable to corporate officers. In support, however, the decision relied on cases that utterly fail to uphold that proposition. The cases cited involve only directors, or, in one case, a controlling shareholder. As to the standard of care, the court confusingly articulated two standards. In one place, the court stated that intentional or

44. 560 N.W2d 389.
45. Id. at 391–92.
46. Id. at 395.
47. Id. at 391–92 n.1.
48. Id. at 394.
49. Id. at 395. For another case inexplicably applying a gross negligence standard to a fiduciary duty claim against a corporate officer, see Washington Bancorporation v. Said, 812 F.Supp. 1256, 1270 (D.D.C. 1993).
50. See Johnson & Millon, supra note 10, at 34; RESTATEMENT (SECOND) OF AGENCY § 379 & cmt. (1958) (agents owe duty of ordinary care).
51. Potter, 560 N.W2d at 395.
knowing breaches of due care are needed to overcome the business judgment rule, although in another place, the court ruled that the plaintiff had sufficiently pleaded that the defendants had negligently breached their duties. In any event, the plaintiff alleged self-dealing on the part of the officer, thereby making the rule inapplicable under a well-established exception.

A 2004 decision from the federal court for the District of Delaware, applying Delaware law, extended the business judgment rule to corporate officers and dismissed an action alleging breach of fiduciary duty. The plaintiff alleged that the officers had breached their fiduciary duties (stated to be those of care, loyalty, and good faith) in various ways, including the failure to inform the directors of various problems. The court, citing a Delaware decision pertaining to directors, held that an officer is not responsible for losses that result from a good faith decision. Determining that plaintiff’s allegations of bad faith were only conclusory, the court dismissed the complaint.

Absent from the court’s analysis was any serious attention to the breach of duty of care allegation, liability for which officers, unlike directors, are not exculpated. Even more problematic was the court’s dismissive treatment of the failure of the plaintiff to substantiate her allegation. The court stated that the plaintiff had not explained how that failure violated the officers’ fiduciary duty and had not offered any authority in support. Perhaps the plaintiff did fail in that regard, but such a failure by a corporate officer—who is an agent owing strong fiduciary duties—can readily constitute a breach of fiduciary duty, as, for example, the report by the Enron Bankruptcy Examiner reveals. Acknowledging such a duty would have allowed the federal court to highlight—and differentiate—the governance role of senior officers to report to the board exercising its oversight responsibilities. Instead, the court treated officers the same as directors and gave them broad shelter under the business judgment rule.

56. Id. at *3.
57. Id. at *4.
58. Self-dealing claims implicate the duty of loyalty rather than the duty of care and, consequently, courts abandon business judgment review in favor of a more demanding fairness review. See, e.g., Grobow v. Perot, 539 A.2d 180, 187 (Del. 1988).
60. Id. at *7 (citing Gagliardi v. TriFoods Int’l, Inc., 683 A.2d 1049, 1051 (Del. Ch. 1996)).
61. Id.
62. Id. at *6.
63. Id. at *7.
64. See Johnson & Millon, supra note 10.
A fourth decision applying Delaware law refused to apply the business judgment rule to a corporate officer. In *Platt v. Richardson*, the U.S. District Court for the Middle District of Pennsylvania stated that the business judgment rule "applies only to directors of a corporation and not to officers . . . defendant does not cite a single authority which extends the presumption afforded by the business judgment rule to officers of a corporation and we have found none." The court did not refer to the *Kaplan* or *Kelly* cases and, as a result, certain commentators have criticized *Platt*. Perhaps the court made a strong statement about the lack of authority for extending the business judgment rule to corporate officers when viewed from the vantage point of the year 2005, given an additional sixteen years of cases uncritically repeating dicta from a tiny handful of earlier decisions. Yet, at the time of the *Platt* decision—1989—Delaware had not, and still has not, held the rule applicable to corporate officers. Moreover, hardly any of the other decisions stating that the rule covers officers had yet been decided. At the time it was made, therefore, the statement was not far from accurate in describing the state of the law.

### 2. Non-Delaware Law

Decisions applying law other than Delaware's appear to support application of the business judgment rule to officers, but, in fact, the case law is quite mixed and provides substantially less support for that position than is commonly acknowledged. For example, a 1994 Illinois appellate decision, before criticizing the *Platt* decision as "against the substantial weight of judicial authority from other jurisdictions . . . ", stated unequivocally that a significant number of courts from
other jurisdictions "have clearly articulated that the business judgment rule protects corporate officers as well as corporate directors." 75 The court then cites ten cases. 76 One of these was the Kaplan decision, already discussed, 77 which named only directors as defendants. Two decisions involved claims against corporations. 78 One of these two involved an odd claim against the corporation itself for mismanagement and breach of fiduciary duty; 79 neither of the two actions were against corporate officers. A fourth decision involved only directors as defendants. 80 A fifth decision involved a person who purportedly was the sole shareholder and also both a director and President, but who never actively participated in management, being President in name only. 81 Consequently, the case did not address the issue of whether an officer acting qua officer receives business judgment review. 82 The sixth decision described the defendants as "officers and directors" without indicating whether any were only officers or sued only in their capacity as officers rather than as officers and directors. 83 The decision, therefore, tells us nothing about business judgment rule review for officers as officers. The seventh decision involved a person who was only an officer but the legal significance of his status—as distinguished from that of defendants who were directors—was never explicitly addressed by the court. 84

Only three of the ten decisions cited by the Selcke court squarely applied the business judgment rule to officers. 85 Two of these involved nonpublic companies, 86 one of which—Omnibank of Mantee v. United Southern Bank 87—found after trial that the officer had breached the duty of reasonable care he owed to the corporation as its agent. 88 The court inexplicably asserted that "[t]he duty of care is subject to a well settled common law defense, known as the business judgment

75. Id.
76. Id.
77. See supra notes 36–41 and accompanying text.
79. Massaro, 559 F. Supp. at 1070. The lawsuit is odd because a corporation itself typically does not owe fiduciary duties, rather, it is owed fiduciary duties from directors and officers.
82. The case also stated that only "reasonable" acts were protected by the business judgment rule and that defendant's actions were not reasonable. Id. at 384.
84. Estate of Detwiler v. Offenbecher, 728 F. Supp. 103 (S.D.N.Y. 1989). Sparks and Hamermesh believe the Detwiler court's failure to distinguish among the defendants based on officer versus director status supports application of the business judgment rule to officers. Sparks & Hamermesh, supra note 6, at 236. This author reaches a different conclusion. The court seemed utterly unaware that the liability of corporate officers might stand on a different basis than that of directors. See Johnson & Millon, supra note 10. The court's failure to address the rule's application to a corporate officer more likely reflects an unawareness of the issue rather than its head-on resolution.
87. Omnibank of Mantee, 607 So. 2d 76.
88. Id. at 87.
rule." The court, citing the ALI's codification of the business judgment rule, then applied a lower "rational basis" standard of review to the officer's conduct, concluding he failed that lower standard as well.

The Omnibank case is a wonderful illustration of judicial confusion concerning the interplay between an officer's duty of care as an agent and the business judgment rule. The court rightly determined that a corporate officer is an agent and, as such, is liable to his or her principal for losses caused by the agent's misdeeds. That conclusion should have ended the analysis. Going on, however, to apply the ALI's unsupported position that the business judgment rule applies to officers as well as directors, the court, in effect, abandoned its earlier agency law duty of reasonable care analysis in favor of applying the weaker standard advocated by the ALI. The effect, never acknowledged by the court (or the ALI), is to jettison the well established standard of ordinary care required of officers in their capacity as agents. Applying the business judgment rule to officers in this manner wrongly relieves them of the well settled duty to comply with a negligence standard of care. Applying the rule to directors, on the other hand, is fully consistent with a policy of according directors deference in the exercise of judgment, by means of a gross negligence standard of care. Here we clearly see how failure to distinguish the role of officers from the role of directors in our system of corporate governance leads to a failure to appreciate the different reasons for imposing fiduciary duties on each group, which, in turn, leads to a failure to differentiate between them for purposes of applying the business judgment rule.

Another decision cited by Selcke in support of applying the business judgment rule to corporate officers—the only one involving a public company—acknowledged the business judgment rule but denied defendant's motion to dismiss on the ground that the plaintiff, by alleging recklessness, illegality, and a lack of reasonable care, had overcome the rule. Finally, the tenth case cited by Selcke in support of extending the business judgment rule to officers, stands alone in explicitly applying the business judgment rule to exonerate a corporate officer from liability. That decision, however, like Omnibank, stunningly misapplied the business judgment rule in the officer setting.

Para-Medical Leasing, Inc. v. Hangen represents a complete failure to uphold an officer's fiduciary duty to act with due care by deploying the business judgment rule to nullify that duty. Hangen, the defendant, was a certified public accountant who was hired as interim manager for a small vehicle and equipment leasing

89. Id. at 85.
90. Id. at 84. See supra note 14.
91. Omnibank of Mantee, 607 So. 2d at 84.
92. Id. at 84. See RESTATEMENT (SECOND) OF AGENCY § 379 cmt. a (1958); Johnson & Millon, supra note 10.
93. See supra notes 14–21 and accompanying text.
94. See supra note 92 and accompanying text.
95. See, e.g., Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985).
98. Id.
company. The sole shareholder and sole director gave him a written description of his duties and a four page procedures manual for reference in arranging leases on behalf of the company. Hangen entered into two leases with a business losing money and already in default on an existing lease with Hangen's employer. On one lease, Hangen did not follow the procedures specified in the manual, with the result that he failed to obtain documentation revealing the lessee's poor financial condition. On the other lease, structured as a sale-leaseback, Hangen advanced $22,000 of borrowed money to purchase a vehicle from the financially distressed counterparty. No lease documents were signed and the counter-party defaulted without making any lease payments.

The corporation sued Hangen under Washington law for breaching the fiduciary duty of care he owed under agency law. The court acknowledged the plaintiff's contention that agents owe a duty of ordinary care,99 the same duty set forth in the Restatement (Second) of Agency.100 The court held, however, that, for corporate officers, the business judgment rule overrode the agent's duty of care, stating: "[I]n considering the actions of a corporate officer, however, the business judgment rule rather than the standard of ordinary care applies."101 The plaintiff had strongly urged that no precedent supported application of the rule to corporate officers, pointing out, correctly, that the Fletcher treatise cited only holdings involving directors. The court, however, referred to the Henn and Alexander treatise—which, as noted earlier,102 simply points to Fletcher—and three additional cases involving directors.103 Thus, without any precedent in support, the court thoughtlessly transported the business judgment rule into the officer setting, thereby lowering the well established standard of care applicable to agents and enabling a very incompetent manager to escape liability.

The Hangen decision embodies the danger of cavalierly stating, as does the ALI and other commentary,104 that the business judgment rule applies to corporate officers. That decision, ironically, is one of the very few that even acknowledges, in the context of a claim against an officer, that an agent owes the corporate principal a duty of ordinary care.105 The court, however, undermined that more robust duty by means of the business judgment rule. Applying the business judgment rule to officers in this fashion creates a substantial risk that the longstanding confusion concerning the relationship of that rule to the duty of care now reigning in the director context will be imported into the officer context as well.106

The same judicial "bootstrapping" on miscited authority seen in Selcke is evident in other cases where courts state unequivocally that the business judgment rule applies to officers. Thus, as authority for the position that the business judgment rule applies to corporate officers on the same basis as directors, these decisions

99. Id. at 722.
100. RESTATEMENT (SECOND) OF AGENCY § 379 (1958).
102. See supra note 18 and accompanying text.
104. See supra notes 14-24 and accompanying text.
106. See infra notes 120, 132 and accompanying text.
simply are not well supported. For example, in *FDIC v. Stahl*, the Southern District of Florida court applied the business judgment rule to officers after citing four cases in support. One of the cases, *AmeriFirst Bank v. Bomar*, did indeed state that the business judgment rule applied to officers, but did so in reliance on three cases—the other three cases relied on by *Stahl*—which involved only directors. Moreover, the *Bomar* court ruled that plaintiff's allegations had overcome the rule. Thus, the blanket statement in *Stahl* is based only on the blanket statement in *Bomar*, which, in turn, is based on cases involving only directors.

This detailed, and admittedly critical, review of decisional law is not meant to suggest that an established principle of law cannot be extended into another context. Our common law system allows growth by operating in just that fashion. It is to insist, however, that if a principle is extended solely on the basis of precedent, then the precedent should accurately support the proposition for which it is cited. Even today, however, judicial authority for extending the business judgment rule to corporate officers remains quite "sparse." Without persuasive precedent, a compelling policy case for expanding the principle should be made. In asserting that the business judgment rule applies to officers, however, that is virtually never done, either by courts or commentators.

Importantly, many of the courts that do apply what they call the business judgment rule tend to be vigilant both in deploying the rule as an adjunct to the duty of due care (rather than, as in *Omnibank* and *Hangen*, a substitute for that duty) and in predicking the rule on an officer first fulfilling that duty as measured by a negligence, not gross negligence, standard. For example, in *Resolution Trust Corp. v. Gladstone*, the court applied the business judgment rule to a corporate officer. The court, however, noted that the rule only protected officers who had acted with due care, which the court described as a standard of "ordinary care." In other words, the business judgment rule was not wrongly used, as in *Hangen* and *Omnibank*, to nullify an officer's duty of care; rather, the exercise of due care was a precondition to application of the rule.

108. *Id.* at 1570 n.8.
113. This is Dennis Block's apt description. See supra note 28 and accompanying text.
114. Many jurisdictions outside Delaware do this with respect to directors as well. See, e.g., *FDIC v. Stahl*, 89 F.3d 1510, 1517 (11th Cir. 1996) (applying Florida law); *FDIC v. Wheat*, 970 F.2d 124, 130 n.13 (5th Cir. 1992) (applying Texas law); *Schein*, 491 F.2d at 18 (applying Florida law).
116. *Id.* at 369.
117. *Id.*
Circuit decision relied on by the Selcke court, McDonnell v. American Leduc Petroleums, Ltd.\textsuperscript{118} In fact, Selcke itself acknowledges, in the director setting, that the protection of the business judgment rule might be surmounted through proving a lack of due care by means of negligence.\textsuperscript{119} In actually applying the business judgment rule to corporate officers, therefore, these courts require full compliance with the officer's duty of care and protect—as they should—only noncareless mistakes of business judgment.

Essentially, that same result can be achieved without invoking the business judgment rule at all. The judicial inquiry should focus pointedly on whether the officer did or did not fulfill the duty of due care. If the duty was fulfilled, the inquiry is over and the plaintiff loses; if the duty was not fulfilled, the liability inquiry is over and the plaintiff wins whatever damages were caused by breach of the duty.\textsuperscript{120} Unless the business judgment rule is wrongly being used to lower or nullify the standard of care owed by an officer—an improper use as seen in Omnibank and Hangen—its sole function is to preclude courts from resolving the due care issue by means of evaluating, in hindsight, the overall substantive wisdom of the business decision. Under no circumstances, however, should courts be engaged in such substantive "second-guessing" in their fiduciary duty analysis.

An example of a decision that rightly focused on the issue of due care in this manner is Shields v. Cape Fox Corp.\textsuperscript{121} There, a manager was held liable for breaching the ordinary care (negligence) standard of agency law without also applying the business judgment rule, even though the rule was applied to directors.\textsuperscript{122} In another case, involving a nonprofit organization, Brown v. United Cerebral Palsy, Inc.,\textsuperscript{123} the New Jersey Superior Court held that a manager—the Executive Director—would be liable to her employer under agency principles if she were negligent.\textsuperscript{124} Although not expressly invoking the business judgment rule, the court recognized that some agents exercise judgmental discretion. Consequently, the court sought to differentiate mistakes of judgment from negligence.\textsuperscript{125} Although the court, in this author's view, wrongly injected a substantive component into its definition of negligence by defining it as conduct no "reasonable person" would engage in,\textsuperscript{126} rather than as conduct that, from a decision making process standpoint was faulty, the distinction drawn by the court rightly suggests that a person

\textsuperscript{118} McDonnell v. Am. Leduc Petroleums, Ltd. 491 F.2d 380, 384 (2d Cir. 1974) (noting that under California law, "The business judgment rule protects only reasonable acts of a director or officer.").


\textsuperscript{120} For a similar argument that due care, not the business judgment rule, should be the focal point in the analysis of director fiduciary duty, see Lyman Johnson, The Modest Business Judgment Rule, 55 Bus. Law. 625 (2000).

\textsuperscript{121} Shields v. Cape Fox Corp., 42 P.3d 1083 (Alaska 2002).

\textsuperscript{122} Id.


\textsuperscript{124} Id. at 852.

\textsuperscript{125} Id.

\textsuperscript{126} Id.
could act in a reasonable manner and yet make the wrong decision. Such a person should incur no liability.

The Brown decision, with the modification noted above, suggests a way to harmonize the agent's fiduciary duty of ordinary care with the need to protect agents—including corporate officers—from liability for decisions that turn out poorly but were not negligently made. It is not the province of the business judgment rule to excuse an officer from the obligation to exercise ordinary care; its true function is to prohibit retrospectively using a judgment's poor outcome to conclude that due care was not exercised. This distinction captures as well the Second Restatement of Agency's reconciliation of the agent's fiduciary duty of care with the agent's understandable need to exercise discretion. The Restatement states that an agent with discretion is "under a duty to act competently and carefully and for a mistake in judgment resulting from a failure to have the standard knowledge or to use the standard care, he is subject to liability to the principal."127 Judgments made carefully, on the other hand, do not create liability, however they turn out.

In sum, both commentary and case law greatly overstate the extent of decisional law support for according business judgment rule protection to officers on the same broad basis as directors. The policy case for that position remains unexamined because courts and commentators rarely develop it. Part III outlines the policy arguments customarily offered in favor of affording directors favorable business judgment rule protection and Part IV assesses the applicability of those rationales to corporate officers.

III. POLICY RATIONALES FOR THE BUSINESS JUDGMENT RULE

The case law in support of applying the business judgment rule to corporate officers is less substantial than commonly thought. Moreover, most decisions applying the rule are relatively new; most of them were decided in the last fifteen years. It seems appropriate, therefore, to ask whether the rule can be supported on policy grounds. This first requires a brief summary of the business judgment rule and identification of the key policy rationales for deploying the rule in the director context. These appear, respectively, in "A" and "B" below.

A. BACKGROUND

The business judgment rule is the cornerstone concept in the judicial review of corporate conduct. Courts have addressed the business judgment rule on countless occasions.128 Practicing lawyers frequently assess the business judgment rule's parameters.127

127. RESTATEMENT (SECOND) OF AGENT § 379 cmt. c (emphasis added). See also infra notes 198–199.
rule's elements and reach,\textsuperscript{129} and scholars regularly analyze its underpinnings.\textsuperscript{130} Although broadly applicable to the judicial review of board conduct, the deferential protection of the rule is not applied as strictly in some settings—e.g., in the judicial review of a board's response to a hostile tender offer or in reviewing a special litigation committee's decision to terminate derivative litigation. For all the attention lavished on the rule, however, Henry Manne's statement about the rule remains as true in 2005 as when first made in 1967: the business judgment rule is "one of the least understood concepts in the entire corporate field."\textsuperscript{131}

There exists, to be sure, deep-rooted disagreement about the basic purpose and thrust of the business judgment rule. Much of this disagreement probably stems from profound differences of opinion concerning the rule's proper relationship to the director duty of care,\textsuperscript{132} and, hence, differences as to the degree of deference that courts, applying the rule, should accord director judgments. Notwithstanding a wide range of views on the precise contours and underpinnings of the rule, however, certain core statements about the rule are widely accepted. For example, the rule has both a procedural dimension and substantive force; thus, in Delaware, the rule, procedurally, is described as a "presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company."\textsuperscript{133} From this simple statement—and later case law elaboration\textsuperscript{134}—several undisputed points about the Delaware rule emerge. The rule applies to directors;\textsuperscript{135} the rule applies to directors when they act collectively, that is, as a board or as a committee of the board;\textsuperscript{136} the rule applies only to considered


\textsuperscript{132} See, e.g., Bainbridge, supra note 130; Cohn, supra note 130; Johnson, supra note 130.

\textsuperscript{133} Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984), overruled on other grounds, Brehm v. Eisner, 746 A.2d 244 (Del. 2000).

\textsuperscript{134} A useful statement of the rule's elements is found in Brehm, 746 A.2d at 264 n.66.

\textsuperscript{135} Id.; Aronson, 473 A.2d at 812.

\textsuperscript{136} Aronson, 473 A.2d at 812-13. See also R. Franklin Balotti & Joseph Hinsey IV, Director Care, Conduct, and Liability: The Model Business Corporation Act Solution, 56 Bus. Law. 35, 56 (2000) ("the business judgment rule applies both to the decision and to the decision-maker, whereas [a statutory section] addresses only the individual liability of a director.").
director judgments, not to unconsidered inaction;\textsuperscript{137} directors must be independent and disinterested as to the matter acted upon;\textsuperscript{138} directors must act with due care and in good faith;\textsuperscript{139} the due care inquiry is process-oriented and due care is measured by a standard of gross negligence, not simple negligence;\textsuperscript{140} the burden of proof is on the party challenging the board's decision to establish facts rebutting the presumption in favor of upholding the decision.\textsuperscript{141} Unless a plaintiff succeeds in rebutting the rule, the court will not substitute its views for those of the board if the latter's decision can be "attributed to any rational business purpose."\textsuperscript{142} This last point reflects the well known substantive deference shown by courts to board decisions. As a result of this "hands off" approach, plaintiffs rarely win duty of care cases.\textsuperscript{143}

\textbf{B. POLICY RATIONALES FOR DEFERENCE TO DIRECTORS}

Several policy rationales are said to underlie the business judgment rule.\textsuperscript{144} Although expressed in various ways, these rationales fall into three broad categories.\textsuperscript{145} These are as follows: encouraging directors to serve and take risks;\textsuperscript{146} avoiding judicial encroachment into business decisions; and preserving the board's central decision making role in corporate governance. These rationales will each be briefly described.

\textbf{1. Encouraging Directors to Serve and Take Risks}

Courts recognize that competent directors can make decisions that in hindsight were improvident.\textsuperscript{147} If those decisions result in a company losing a significant amount of money, a legal rule holding directors too readily liable for the loss will deter persons from serving as directors. Consequently, a legal rule—i.e., the business judgment rule—that makes it difficult to hold directors personally liable for

\textsuperscript{137} Aronson, 473 A.2d at 813 ("the business judgment rule operates only in the context of director action. Technically speaking, it has no role where directors have either abdicated their functions, or absent a conscious decision, failed to act.") (citation omitted).

\textsuperscript{138} Brehm, 746 A.2d at 264 n.66.

\textsuperscript{139} Id.

\textsuperscript{140} Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 364 n.31 (Del. 1993); Smith v. Van Gorkom, 488 A.2d 858, 873 (Del. 1985).

\textsuperscript{141} Aronson, 473 A.2d at 812.

\textsuperscript{142} Brehm, 746 A.2d at 264 nn.65 & 66.

\textsuperscript{143} See ALI PRINCIPLES, supra note 14, § 4.01 cmt. h, at 155. Only forty or so twentieth century cases had reached appellate review as of 1992. Id.

\textsuperscript{144} See supra notes 129–130 (reciting policy rationales).

\textsuperscript{145} But see Gevirtz, supra note 130, at 304–21 (describing four categories); Davis, supra note 130 (describing five categories).

\textsuperscript{146} Many courts apparently differentiate the factor of encouraging persons to serve as directors from the factor of encouraging persons to take risks while directors. See BLOCK ET AL., supra note 28, at 12–14. This author treats the two factors together because they raise the same policy issue and because the aim of sound policy should be the attainment of right action while a director, not merely inducing someone to become a director.

\textsuperscript{147} See BLOCK ET AL., supra note 28, at 12 & n.49 (collecting authority).
improvident decisions "encourages competent individuals to become directors who otherwise might decline for fear of personal liability."148

Once directors are willing to serve, they must be induced to make those business decisions stockholders desire. Given limited liability for corporate debts and the ability to alleviate risk through diversifying their portfolio of stock holdings,149 stockholders may prefer that directors take more risks than directors themselves prefer, especially given that directors, holding relatively small amounts of stock, will capture little of the eventual payoff. A judicial standard of review that too severely imposes liability on directors for unwise decisions may exacerbate this tendency toward "sub-optimal risk acceptance"150 and deter directors from pursuing potentially lucrative, but risky, endeavors. To more closely align director attitudes toward risk with stockholder preferences, the business judgment rule is designed to accord directors substantial latitude in their business decision making.151 Delaware courts implement this philosophy by refusing to assess the substantive soundness of director judgments and by holding directors only to a gross negligence standard of care.

2. Avoiding Judicial Encroachment into Business Decisions

Judges are public officials, not business people. This leads some commentators to advocate that judges adopt a highly deferential approach in reviewing director actions: "Courts . . . do not possess the experience, expertise, or information necessary to make complicated business decisions."152 Courts are quick to adopt this rationale, asserting that they are not business experts,153 are ill-equipped to second-guess business judgments,154 and lack an intangible "sense" of the specific circumstances confronting a business.155

At a deeper level, several considerations support this posture of judicial restraint. First, courts worry about "hindsight bias," the tendency to "assign an erroneously high probability of occurrence to a probabilistic event simply because

149. Bainbridge, supra note 130, at 112.
152. Daniel R. Fischel, The Corporate Governance Movement, 35 VAND. L. REV. 1259, 1288 (1982). See also Balotti & Hanks, supra note 129, at 1341–42 (suggesting it is unwise to "risk . . . permitting or requiring . . . courts to become, in effect, appellate boards of directors.")
154. Auerbach v. Bennett, 393 N.E.2d 994, 1000 (N.Y. 1979) (noting that the business judgment rule is grounded, in part, on the "prudent recognition that courts are ill equipped and infrequently called on to evaluate what are and must be essentially business judgments."). See generally BLOCK ET AL., supra note 28, at 15–17 (collecting authority).
155. Branson, supra note 130, at 637.
it ended up occurring.” The deference of the business judgment rule properly quells the temptation to overlook the fact that the “entrepreneur’s function is to encounter risks and to confront uncertainty, and a reasoned decision at the time made may seem a wild hunch viewed years later against a background of perfect knowledge.” Second, directors who make faulty decisions already face the risk of sanction, both from stockholders who may vote them out of office and from the corrective, competitive pressure of product, labor, and capital markets; judges do not face these sanctions for faulty decisions. Recognizing that other legal and market mechanisms hold directors, but not judges, to account, courts defer to director decisions. Finally, drawing on the insights of behavioral economics, Professor Bainbridge argues that, like all decision makers candidly acknowledging their own cognitive limitations and information asymmetries, judges sensibly respond to these challenges by choosing—as their decision making strategy—a policy of deferring to director judgments. Together, these three considerations produce the judicial modesty that forms the essence of this second rationale for the rule.

3. Preserving the Board’s Governance Role

Courts frequently link the business judgment rule to that section of the corporate statute providing that the business and affairs of a corporation are to be managed by or under the direction of its board. By limiting judicial review, “the business judgment rule preserves the statutory scheme of centralizing authority in the board of directors.” Conversely, too readily giving stockholders the ability to challenge director decisions may serve to “transfer ultimate decision-making authority from the board to any shareholder who is willing to sign a complaint.” Thus, a judicial policy of deference toward board action preserves director au-

156. Bainbridge, supra note 130, at 114 (footnote omitted). See generally id. at 114–15.
161. Bainbridge, supra note 130, at 118–20. Bainbridge, however, does not believe this a complete explanation of the business judgment rule. Id.
This honors the corporate governance arrangement designed by the legislature.

It is not the purpose of this Article to develop at great length or critically assess these customary rationales for applying the business judgment rule to directors. That has been done before. The aim, rather, has been to identify the conventional justifications for judicial deference to directors in order to frame the central concern of this Article: do these rationales, or any of them, support application of the business judgment rule to officers?

IV. THE BUSINESS JUDGMENT RULE AND OFFICERS

This section first evaluates whether the standard business judgment rule rationales apply, in whole or in part, to officers. It then provides an overall assessment, concluding that policy considerations do not support application of the rule to corporate officers. It also suggests how directors, stockholders, and state legislatures might respond.

A. POLICY RATIONALES FOR DEFERENCE APPLIED TO OFFICERS

1. Encouraging Officers to Serve and Take Risks

Stockholders desire competent officers willing to serve in that capacity as much as—perhaps more than—they desire competent directors. Moreover, stockholders seek the same optimizing stance toward risky corporate investment opportunities from officers as they do from directors. Must officers receive the protection of the business judgment rule to induce them both to serve and act appropriately once in office, as is the supposed case for directors? For several reasons, this is a doubtful claim.

First, directors are said to need liability protection to induce risk taking because their relatively small stockholdings and lack of incentive compensation give them little of the “upside” gains on investment projects. In other words, the “risk/reward” ratio is highly unfavorable—they perceive too much risk for the expected reward. By way of contrast, executive compensation—at least in the United States—is, or at least is designed to be, highly incentivized. Professors Brian Cheffins and Randall Thomas report on the results of a 2001 worldwide remu-

165. See In re Fuqua Indus., Inc. Sholder Litig., No. CIV A. 11974, 1997 WL 257460, at *12 (Del. Ch. May 13, 1997) (“[T]he board, not the Court, is in the best position to manage the corporation’s affairs.”).

166. Many corporate law scholars are critical of the business judgment rule. Professor Gevurtz, for example, advocates abolishing it. Gevurtz, supra note 130, at 305–12. Professor Bainbridge and this author would not abolish the rule but each would, in different ways, prefer that the rule be used to shelter director decisions from substantive review by courts. See generally Bainbridge, supra note 130; Johnson, supra note 130.


The study, they report, found that much of an American CEO’s compensation “is variable in nature, in the sense that they only benefit if their company meets or exceeds prescribed targets.” In particular, the annual bonus of a U.S. CEO averaged fifty-six percent of salary, although other variable compensation (e.g., stock options and bonus plans with multi-year targets) constituted 161 percent of salary. The pattern seemed to hold for other executives as well, the study finding, for example, that for human resources directors’ variable pay with a long term aspect amounted to sixty-six percent of base salary. Overall, executive officers receive higher absolute levels of pay than do directors, and a significant portion of that pay is—or at least is designed to be—based on performance. In short, officers, unlike directors, stand to reap substantial rewards for taking appropriate risks. Thus, even if the risk element in the risk/reward ratio is the same as for directors, the reward element is quite different, thereby substantially altering how an officer—in comparison to a director—makes this calculation.

Second, it is commonly observed that officers—more so than directors—have risks inherent to their substantial firm specific human capital that cannot be reduced by diversification, thus making officers adverse to taking risks stockholders desire. This argument suggests officers will “play it safe” to protect their jobs. Without more evidence to support such a wholesale claim, this does not seem to be an accurate description of modern executive conduct. To begin with, the widespread pattern of incentive compensation noted above is designed to counteract risk-adverse conduct. Moreover, “playing it safe” suggests that the typical executive lacks ambition, preferring simply to hold onto his or her job at a lower level of pay than to “take a chance” in hopes of advancing upward in the corporate hierarchy and receiving far more in pay and perks. For executives who climb to the top of the corporate ladder, it is unlikely that they either have “play it safe” personality types or that they have successfully navigated their way up

169. Id. at 156–57.
170. Id. Interestingly, a 1993 change in federal tax law permitting a corporation to deduct more than $1 million for an executive’s compensation only if the additional compensation was “performance related” did little to slow increases in executive pay and had only a moderate impact on the balance between performance-related pay and salary. Id. at 170.
171. Id. at 157.
172. Id.
174. For a critique of executive compensation practices in U.S. companies as not being sufficiently performance based, see generally LUCIAN ARYE BEBCHUK & JESSE M. FRIED, PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION (Harvard University Press 2004). Care must be taken that executive pay arrangements are, in practice, truly performance based and that they are not designed to “over-incentivize” officers in a way that tempts them to act imprudently or, worse, commit fraud.
175. See Bainbridge, supra note 130, at 113.
176. Id.
that ladder by means of a “play it safe” approach to business.\textsuperscript{177} Nor is “playing it safe” a cultural norm that is at all lauded in entrepreneurial circles or a norm that very many corporate cultures in the United States highly value and seek to encourage and reinforce.\textsuperscript{178} Additionally, in order to receive more pay via stock price appreciation, officers must convince investors of good prospects for increased future earnings; to be credible, this, in turn, requires innovation and a willingness to take risks.

Furthermore, beyond individual motivation and corporate norms, the argument suggests that a “play it safe” strategy can prevail, notwithstanding that, in a competitive, tournament-like labor market, other executives may defect from that strategy and take risks and succeed. Their success will put pressure on the “play it safe” executives to alter their ways or fail, and will make the risk taking executive comparatively more attractive in the labor market. Indeed, the “safe player” may be out of a job, because a strategy of “protecting” firm specific capital requires, as it turns out, that an executive continue to meet (or exceed) the ongoing challenges of competitors.

Another flaw in the “firm specific” capital argument is the suggestion that simply because a great deal of an executive’s wealth, in both absolute and relative terms, may be tied up in company stock, the person is not otherwise wealthy. Over the years (and decades) it takes to reach the pinnacle of corporate positions, many executives are likely to have acquired significant wealth and to have moved, at least partially, to diversify their holdings. Consequently, the fact that, at a particular time, a senior executive is heavily invested in one company does not mean the executive is not, from a broader wealth perspective, far more diversified.

Third, apart from the fact that officers receive significantly greater rewards from a corporation than do directors, they also should face greater risks. Officers work for the company full time, possess extensive knowledge and skill concerning company affairs, have access to considerably more and better information than directors, enjoy high company and social status, and exercise great influence over the lives of many people—both inside and outside the corporation. They should be held to the same standard of care as are all other persons who serve as agents of companies—a duty of ordinary care.\textsuperscript{179} If that standard of care is thought to be too onerous to induce people to work, then apparently none of us would work, whether in professions, trades, manufacturing, or other jobs where ordinary care is the conventional standard of conduct. It seems unlikely, or at least it has not been plausibly established, that corporate officers at even the highest echelons would be less willing than other persons to pursue their livelihoods unless they were given assurances of facing a lower liability risk. There is certainly no evidence

\textsuperscript{177} For an insightful treatment of how people with egocentric tendencies are valued in hyper-competitive knowledge and service-based firms, see generally Donald C. Langevoort, \textit{The Organizational Psychology of Hyper-Competition: Corporate Irresponsibility and the Lessons of Enron}, 70 Geo. Wash. L. Rev. 968 (2002).

\textsuperscript{178} \textit{Id.}

\textsuperscript{179} \textit{Restatement (Second) of Agency} § 379 (1958). \textit{See also} Johnson & Millon, \textit{supra} note 10.
that people are staying away from, or resigning, high-level corporate positions now that the Sarbanes-Oxley Act imposes more onerous demands on executives. In short, the claim that people will not serve as officers or take appropriate risks unless the standard of care is reduced below the norm for all other employees and agents is, so far, empirically unsupported and, overall, a highly dubious claim.

What this line of argument with respect to officers does reveal is that it is not wholly the business judgment rule that protects directors from liability risk. Rather, in Delaware and states like it, it is a very weak duty of care that permits directors to deviate from the standard of ordinary care as long as they are not grossly negligent. Not discouraging the pursuit of prudent risks is one thing; permitting carelessness in identifying, gathering information on, and assessing those risks in the context of a business decision, is another. Moreover, even if directors fail that generous liability standard, they are not personally liable for ensuing damages due to widespread statutory exculpation. These havens from liability, however, are not the doing of the business judgment rule which, properly understood, simply protects directors against liability for decisions that, though carefully made, were, as it later turns out, mistakes.

Applying this to officers, we see that, as agents, they, unlike directors, should be held to the customary standard of ordinary care. Moreover, in Delaware, stockholders cannot exculpate officers from personal liability for carelessness. This is the default legal background against which officers choose to serve. Yet, they neither refrain from serving or taking risks because of it, nor should these existing liability rules—harsher than for directors—be curtailed through broadly extending to officers the strong Delaware version of the business judgment rule currently applied to directors. The first rationale does not support expanding the rule to cover officers.

180. There are anecdotal reports that it is harder to recruit directors as a result of Sarbanes-Oxley, just as there were reports, after the infamous decision of Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985), that companies were having trouble recruiting high quality directors. Edward Rock & Michael Wachter, Dangerous Liaisons: Corporate Law, Trust Law, and Interdoctrinal Legal Transplants, 96 Nw. U. L. Rev. 651, 659 (2002). Top executive positions, by contrast, apparently are not lacking for applicants.


182. The standard of care for directors when making business judgments is gross negligence. Van Gorkom, 488 A.2d at 873.


184. See generally Johnson, supra note 120. See infra notes 198–199.

185. See supra note 179 and accompanying text.

2. Avoiding Judicial Encroachment into Business Decisions

The rationale that "judges are not business experts"\textsuperscript{187} would seem to carry equal—if not greater—weight for officers as for directors. Officers devote more time to company business than do directors;\textsuperscript{188} they possess greater information and expertise about the business, and they are involved with far more of the operational details of the business than are directors. Courts might more easily imagine themselves in the position of directors—who devote relatively little time to the business and act only episodically\textsuperscript{189}—than in the shoes of senior executives with a deep understanding of the ongoing inner workings and external challenges of a large company.\textsuperscript{190}

Moreover, as to the three deeper considerations underlying this rationale,\textsuperscript{191} most seem applicable to officers. The risk of judicial hindsight bias still applies.\textsuperscript{192} Furthermore, although officers who make faulty decisions may not face ouster from stockholders, they do face the risk of removal from office by directors,\textsuperscript{193} a risk that in recent years has greatly escalated. They—and the companies they work for—also confront the punishing competitive pressures of product, labor, and capital markets.\textsuperscript{194} Finally, awareness of their own cognitive limitations and informational disadvantage may lead judges to adopt—as a decision making strategy—a policy of deference to corporate decision makers.\textsuperscript{195}

The key question on this last point, however, is to which decision maker should the court defer? If the board of directors and the senior officer, whose decision is challenged, by, say, a stockholder, agree that the company should not pursue the claim of wrongdoing, the court may equivocate and simply say it defers to “management” in dismissing the claim. Or, the court may say it is deferring to the judgment of the board, because the board supports dismissal. Where, however, it is the board itself that is pursuing a claim of wrongdoing against an officer, the court must squarely decide whether it will defer to the judgment of the board in

\textsuperscript{187} Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919) (stating "judges are not business experts").


\textsuperscript{189} Id.

\textsuperscript{190} Professor Bainbridge, building on former Delaware Supreme Court Chief Justice Veasey’s observation that courts are very reluctant to interfere with decisions involving “enterprise” issues, believes courts should more readily defer to “operational” decisions than to judgments involving structural matters. Bainbridge, supra note 130, at 129. See E. Norman Veasey, The Defining Tension in Corporate Governance in America, 52 BUS. LAW. 393, 394 (1997). This would seem to mean, overall, greater deference to officer-level rather than director-level decisions.

\textsuperscript{191} See supra notes 156–161 and accompanying text.

\textsuperscript{192} See supra notes 156–161.

\textsuperscript{193} Officers may be removed from office at any time, with or without cause, by the board of directors. 2 MODEL BUS. CORP. ACT ANN. § 8.43(b) (2000–02).

\textsuperscript{194} One court specifically cited this rationale for according business judgment rule protection to a corporate officer. Rosenfeld v. Metals Selling Corp., 643 A.2d 1253, 1262 (Conn. 1994). See supra note 159.

\textsuperscript{195} See supra note 161 and accompanying text.
advancing the claim or to the judgment of the officer seeking its dismissal.\textsuperscript{196} Consideration of this factor takes us into the heart of the all-critical third rationale, however, which will be fully addressed later.

Overall, when the various considerations underlying the second rationale are examined, a strong case can be made that the rationale supports judicial deference to officer decisions. Perhaps, given officer responsibility for complex operational issues having a less discrete character than board decisions, courts may be highly uncertain of their competence to evaluate officer conduct and, hence, may be even more deferential than they are to director level decisions.\textsuperscript{197} Again, however, as with the first rationale, we must differentiate deference to the substantive soundness of the judgment itself from rightful insistence that officers fully discharge their duty of ordinary care in preparing for, making, and carrying out the business decision. The business judgment rule rightly precludes inquiry into the former;\textsuperscript{198} the officer's duty of due care demands inquiry into the latter.\textsuperscript{199}

3. Preserving the Board's Governance Role

The rationale that directors—not judges—possess statutory authority to oversee corporate affairs does not support applying the business judgment rule to officers. It does, however, support deference to director decisions about pursuing (or not pursuing) fiduciary duty claims against officers. The Delaware Supreme Court has expressly linked director control over corporate litigation to the stat-

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\item[196.] Where the court defers to the business judgment of the board in pressing the claim, the board must still prove its underlying claim that the officer breached a fiduciary duty. The procedural effect of not granting an officer the broad protection of the rule is that a board seeking to press a claim would not face the high burden of overcoming a pretrial motion to dismiss grounded solely on the strong presumption of propriety the rule accords.
\item[197.] See supra note 190. On the other hand, the Enron Bankruptcy Examiner concluded that "the roles and responsibilities of officers present a different context in which to apply ... [standards of conduct] and may subject officer conduct to a higher degree of scrutiny than that given to director conduct." In re Enron Corp., Case No. 01-16034 (AJG) (Bankr. S.D.N.Y.), Third Interim Report of Neil Batson, Court-Appointed Examiner, app. B, at 8 (June 30, 2003).
\item[198.] Judge Winter's precise phrasing of what the business judgment rule does frequently is overlooked: "[l]iability is rarely imposed upon corporate directors or officers simply for bad judgment and this reluctance to impose liability for unsuccessful business decisions has been doctrinally labelled [sic] the business judgment rule." Joy v. North, 692 F.2d 880, 885 (2d Cir. 1982) (emphasis added). Judge Winter rightly limited the rule to protecting only against liability for judgments that were unsuccessful. He did not excuse directors or officers from exercising due care. See infra note 199.
\item[199.] The Delaware Supreme Court made it very clear in 1984 that the protection of the business judgment rule—precluding inquiry into the soundness of a business judgment—was dependent on directors discharging their duty of care: "[T]o invoke the rule's protection directors have a duty to inform themselves, prior to making a business decision, of all material information reasonably available to them. Having become so informed, they must then act with requisite care in the discharge of their duties." Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984). The comment to \textit{Restatement (Second) of Agency} § 379 (1958) also makes clear that an agent exercising discretion to make a judgment must act with care and competence: "In the use of this discretion [the agent] is under a duty to act competently and carefully and for a mistake in judgment resulting from a failure to have the standard knowledge or to use the standard care, [the agent] is subject to liability to the principal." Id. § 379 cmt. C.
\end{enumerate}
\end{footnotesize}
utory grant of authority: "Directors of Delaware corporations derive their managerial decision making power ... to initiate, or refrain from entering, litigation, from 8 Del. C. § 141(a)." This places the locus of authority over litigation with directors, not officers. This means that directors, upon learning of fiduciary wrongdoing by a corporate officer, must investigate and decide whether to pursue a claim by means of litigation, or to resolve it through imposing an intra-firm sanction or by reaching a negotiated settlement. In making that decision, only independent, disinterested directors can act on the matter and they must discharge their own fiduciary duty to act with due care and in good faith. Here too, incidentally, we see that just as the business judgment rule is not applied in reviewing conduct by self-interested directors, officers—with their deeper, more lucrative company connections—are more likely than directors to fall outside coverage of the rule anyway, due to their financial self-interestedness in the decisions they make.

If directors make a considered business judgment to pursue a breach of fiduciary duty claim against an officer, the rationale of honoring director discretion means that officer conduct should not be deferred to under the auspices of the business judgment rule but, instead, should be scrutinized in accordance with the underlying standard of ordinary care applicable to officers. In this setting, the board has made a considered judgment that it is in the corporation's best interests to pursue a claim that the officer breached his or her duty to the corporation. As representative of the corporation's interests, the board's judgment to pursue the claim should be judicially respected. For a court to broadly shelter a corporate officer's conduct from judicial review under the applicable standard of care by using the business judgment rule to deflect an assessment of officer misconduct serves to undermine the board's decision to hold its agent to the relevant standard and violates the third rationale underlying the business judgment rule. This is precisely the grievous mistake made in the Hangen decision. That case involved an action brought in the corporation's name by its sole stockholder and director against a manager. After rightly acknowledging that, as an agent, the manager owed a duty of ordinary care, the court did not condition application of the rule on discharging the duty of care. Rather, the court wrongly applied the business judgment rule to avoid holding the manager to the applicable care standard. This confuses the function of these two notions—it is not the purpose of the business judgment rule to excuse an officer from the duty to exercise due

201. Brehm v. Eisner, 746 A.2d 244, 264 n.66 (Del. 2000); Aronson, 473 A.2d at 812 (noting that only disinterested directors acting with due care receive protection of the business judgment rule).
202. If the business judgment rule only precluded inquiry into the substantive soundness of an officer's decision—as this author has argued should be the case, for directors as well, see Johnson, supra note 120—rather than serving, as it does in Delaware for directors, to lower the standard of care, this would not be such a problem.
204. Id. at 722.
205. See supra notes 198–199 and accompanying text.
206. Hangen, 739 P2d at 722.
care; its true function is to prohibit retrospectively using a judgment’s poor outcome to conclude that due care was not exercised. The court, however, by inappropriately deferring to the manager’s carelessly-entered business decision, refused to give proper deference to the director’s judgment to attempt to hold the manager accountable for breaching his fiduciary duty of care.\textsuperscript{207} This violates, rather than honors, the third rationale for the rule; namely, that directors (not courts or officers) oversee corporate affairs, including litigation against wrongdoers. Yet, the \textit{Hangen} decision is cited approvingly by courts and commentators.\textsuperscript{208}

If directors elect not to bring an action against a wrongdoer, stockholders, of course, may seek to initiate a derivation action. This will bring the matter within the rules governing derivative litigation,\textsuperscript{209} which essentially pit the views of stockholders—who wish to pursue the claim of officer wrongdoing—against the views of directors—who, in this setting, wish not to initiate or to dismiss the claim.\textsuperscript{210} Assuming disinterested, independent directors fulfill their own fiduciary duties to act with due care and in good faith, their decision not to pursue the claim should judicially be respected by the court, under the third rationale, as a proper exercise of director business judgment.\textsuperscript{211}

Refusing to apply the business judgment rule to officers in a way that too broadly shields officers from their obligation to act with due care and loyalty does not mean directors will routinely use litigation to pursue remedies for officer breaches of duty. In fact, such litigation may remain relatively scarce. It does, however, accord directors considerable leverage in their dealings with officers, leverage that may go beyond the bargained-for terms of an employment agreement. Although tightly written employment contracts can make it very difficult to terminate senior officers “for cause,”\textsuperscript{212} breaches of fiduciary duty, unless contracted around, create liability independently of contract.\textsuperscript{213} Therefore, improper behavior not permitting termination “for cause,” may, nonetheless, constitute a fiduciary duty breach according the corporate principal various noncontractual remedies. These,

\textsuperscript{207} See id.
\textsuperscript{208} See Sparks & Hamermesh, \textit{supra} note 6, at 235; \textit{supra} note 97 and accompanying text.
\textsuperscript{209} See Tooley v. Donaldson, Lufkin & Jenrette, Inc., 845 A.2d 1031 (Del. 2004) (distinguishing derivative from direct claims). In a derivative claim, generally stockholders must first make demand on directors. See Rales v. Blash and, 634 A.2d 927, 933–34 (Del. 1992) (utilizing the test for demand futility where board made no business judgment); Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) (utilizing the test for demand futility where the board made a business judgment).
\textsuperscript{210} See, e.g., In re Walt Disney Co. Deriv. Litig., 825 A.2d 275 (Del. Ch. 2003) (denying motions to dismiss derivative action against directors and former president).
\textsuperscript{211} See, e.g., Brehm v. Eisner, 746 A.2d 244, 257 (Del. 2000).
\textsuperscript{212} Joann S. Lublin, \textit{Windfalls Are Common in Ousters Over Alleged Ethics Violations}, \textit{Wall St. J.}, Nov. 25, 2003, at B8. Professors Stewart Schwab and Randall Thomas found that the most common grounds for “just cause” termination of a CEO, based on their review of 375 employment agreements, were moral turpitude (72.27%), willful misconduct (69.07%), failure to perform duties (57.87%), and fiduciary breach (50.67%). \textit{Stewart J. Schwab & Randall S. Thomas, What Do CEO’s Bargain For?: An Empirical Study of Key Legal Components of CEO Employment Contracts} 25 (Vanderbilt University Law School Law & Economics Working Paper No. 04-12, Apr. 2004).
in turn, may alter the balance of power in favor of the board in fashioning an appropriate intra-firm sanction or advantageous severance arrangement.\textsuperscript{214}

\section*{B. Assessment}

Although the second rationale underlying the business judgment rule might warrant extending the rule to officers, the first and third rationales do not. Perhaps other factors uniquely supporting application of the rule to officers exist, but they have not been identified. A strong policy case for applying the rule to officers therefore has not yet been made. What about the matter of stockholder preferences on this topic? Courts and commentators are quick to speculate as to investor preferences for a high threshold for imposing director liability. Professor Bainbridge regards the business judgment rule as a default rule stockholders prefer, but focuses on what they desire in relation to directors,\textsuperscript{215} not officers.

Existing legal arrangements might more or less reflect stockholder preferences (or less strongly, reflect what stockholders will minimally tolerate). If this is true of liability rules bearing on directors, it is likewise true for officer liability rules. Therefore, we can infer that stockholders prefer (or tolerate) existing default rules for corporate officers. These rules are clear, if often wrongly described.

Currently, the standard of care applicable to officers is that of ordinary care or negligence.\textsuperscript{216} Currently too, we have seen that there is very little solid case law authority in favor of granting generous business judgment rule protection to officers,\textsuperscript{217} and no compelling policy basis for doing so. Consequently, although perhaps not acted on in a way that has produced much authoritative case law, the better view as to the current default rule for officer liability is that the business judgment rule does not apply to officers in the same broad fashion it has been applied by Delaware courts to protect directors. Of course, we do not really know (as opposed to just imagining) whether stockholders prefer this legal state of affairs, though it is hard to believe most investors wish to hold officers to a standard of care below what they expect from all other people (except directors) who act on their behalf, such as doctors, lawyers, stock brokers, automobile drivers, etc. Moreover, if they disfavor the current liability rule as too strong, they can seek to “contract around” the rule. They can do this in at least two ways.

First, directors, as representatives of the stockholders, can, \textit{ex ante}, enter employment agreements with officers modifying their fiduciary duty of care to a weaker standard, say, to a gross negligence standard or, though less likely, elimi-

\textsuperscript{214} Lublin, \textit{supra} note 212 (describing the backlash against paying severance compensation to departing executives who engaged in wrongdoing). Although Professors Schwab and Thomas found that only about half of their sample employment contracts allowed a “just cause” termination for breach of fiduciary duty, \textit{supra} note 212, failure to perform duties would still subject the CEO to various common law remedies, whether or not it constituted “cause” for termination. Moreover, although Professors Schwab and Randall found that “poor performance” was not included as cause for termination in most CEO contracts, \textit{supra} note 212, such conduct would likely constitute breach of an agent’s fiduciary duty of ordinary care.

\textsuperscript{215} Bainbridge, \textit{supra} note 130, at 83 n.22.

\textsuperscript{216} See \textit{supra} note 179 and accompanying text.

\textsuperscript{217} See \textit{supra} Part II.
nating the duty altogether. 218 Alternatively, directors could leave the duty intact but agree to eliminate (or place a cap on) the money damages that could be recovered from an officer for breaching the duty of care, similar to what stockholders may do for directors in a company's certificate of incorporation. 219 If directors will not do this on their own initiative, stockholders may request that they do so or, under SEC proxy rules, 220 submit a stockholder proposal for action (even if nonbinding) at the annual meeting. The fact that there is no great clamoring for any of these actions might suggest that stockholders believe the current liability regime is working well. One problem with this position, however, is that, as this Article has shown, most legal authorities state that officers face only the same liability risks as directors, when, in fact, a correct understanding of existing legal authority reveals they actually face (and should face) greater risk. This suggests that, because other nonlegal but socially powerful mechanisms seem to be impeding corporate lawsuits against officers—such as settlements or director reluctance (for whatever reason, perhaps the same reason they overpay officers) even to initiate action—stockholders may prefer the current arrangement along with the more lax liability scheme that the law is wrongly said to adopt, rather than the stricter positive law regime that, on the books at least, actually prevails. Whatever is the case, however, the point remains that if stockholders want to alter what they understand to be the current arrangement, they can communicate that desire to directors.

Second, states wishing to give stockholders better voice on this issue could follow the lead of Virginia and allow stockholders, through a provision in the articles of incorporation, to eliminate, or place a cap on, officer liability for wrongdoing as well as director liability for wrongdoing. 221 Absent express stockholder

218. For an expression of concern about allowing one fiduciary—the board of directors—to freely exculpate another group of fiduciaries—senior officers—see Johnson & Millon, supra note 10.

219. See Del. Code Ann. tit. 8, § 102(b)(7) (2001) (permitting stockholders to exculpate directors from liability for money damages for breaching duty of care). It is surprising to this author that more lawyers for executives do not seek to negotiate fiduciary duty issues in the employment agreement, for the purpose of lowering the standard of care or reducing the liability exposure, or both. Instead, they focus on the termination provisions, ignoring the fact that fiduciary duty claims arise independently of contract, but can be, within limits, contractually modified.

220. SEC Rule 14a-8 permits stockholders to submit proposals for inclusion in the board's proxy materials sent to all stockholders. 17 C.F.R. § 240.14a-8 (2004).


Limitation on liability of officers and directors; exception.—

A. In any proceeding brought by or in the right of a corporation or brought by or on behalf of shareholders of the corporation, the damages assessed against an officer or director arising out of a single transaction, occurrence or course of conduct shall not exceed the lesser of:

1. The monetary amount, including the elimination of liability, specified in the articles of incorporation or, if approved by the shareholders, in the bylaws as a limitation on or elimination of the liability of the officer or director; or

2. The greater of (i) $100,000 or (ii) the amount of cash compensation received by the officer or director from the corporation during the twelve months immediately preceding the act or omission for which liability was imposed.

B. The liability of an officer or director shall not be limited as provided in this section if the officer or director engaged in willful misconduct or a knowing violation of the criminal law or
action, Virginia's statute sets officer and director liability at the greater of $100,000 or the amount of cash compensation received by the wrongdoer during the twelve months preceding the wrongful act or omission. The ALI, moreover, allows stockholders to limit, but not eliminate, officer liability for wrongdoing to the amount of an officer's annual compensation. Losing a year's pay that one thought had already been earned, can be a potent reminder that officers owe fiduciary duties. At the same time, a limitation on damages spares officers the draconian exposure to monetary claims that could induce a decision maker to be, if only at the margin, overly risk adverse.

Another buffer against excessive exposure to personal liability for officers is the fact that any recovery is likely to come from the Directors' and Officers' ("D&O") liability insurance policy purchased by the corporation. Thus, the corporation, upon the board (or shareholders, in some instances) making a decision to pursue such a claim, would sue the officer for breach of duty, and the officer would be covered under a "Side A" (or nonindemnifiable loss) insurance policy purchased with corporate funds specifically for director and officer (not corporate) protection. Perhaps the existence of third party coverage somewhat undercuts the healthy deterrent effect of liability. On the other hand, it does provide a source for recovery by the corporation and may be a sensible way for the corporation to induce in officers a desirable propensity to engage in riskier conduct by reducing the risk element in the risk/reward assessment.

If the latter occurs, this weakens the force of the argument—already weak, in this author’s view—that officers, like directors, will not serve or act appropriately if they face the risk of severe liability. Perhaps a middle ground is to find a way for officers to continue to face some liability—perhaps for retained coverage (the deductible) on the policy—payment of which might be high enough to sting but not so high as to deter desired conduct. Currently, however, it appears that most “Side A” policies have no deductible, but provide coverage from the first dollar of exposure.

...
A final hurdle to recovery of damages against an officer is the element of causation. Any breach of fiduciary duty claim against an officer—whether or not damages have been capped by contract or by statute—requires that the plaintiff establish that the wrongdoing is the cause of damage to the corporation. In the complex world of commerce, where many factors may intervene to alter a corporation's financial well being, proving that officer negligence caused damage can be a daunting obstacle to overcome.

V. CONCLUSION

Case law support for extending broad business judgment rule protection to officers is far weaker than commentators and courts acknowledge or appreciate. The policy case, likewise, fails to stand up, at least based on the standard rationales underlying the rule's application to directors. This means that corporate officers—like other agents—face potential liability for damages caused by breaching the duty of ordinary care they owe the corporation. The decision to pursue or relinquish the corporation's claim generally belongs to the directors, whose decision to pursue the claim should be accorded deference by the courts.

Liability rules certainly are not the only—or maybe even the most important—factor shaping the behavior of corporate officers. Professional, reputational, moral, and cultural considerations, along with well designed incentives and well functioning market constraints, can play key roles in leading most officers to desire to perform well. Nonetheless, just as criminal and administrative law sanctions increasingly are used to punish and deter corporate officers in this era of corporate scandal, so too the prospect of civil liability for breaching fiduciary duties can serve a useful purpose. Too often, corporate officers and their advisors may believe that employment agreements establish the outer limits of executive legal responsibilities. Just as criminal law sanctions today are reminding many officers that society at large expects certain minimal behavior from them, the prospect of exposure to civil liability can remind officers that stockholders and directors likewise expect adherence to basic fiduciary standards, without undeserved refuge in the business judgment rule.

230. See supra note 2.