

Restoring the Balance of Power in Corporate Management: Enforcing an Officer's Duty of Obedience

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The issue of corporate officers' fiduciary duties has been a neglected area of Delaware law for over seventy years. This is surprising given the power and authority that these individuals wield over a corporation's business and affairs. The transgressions that took place at large public corporations such as Enron and WorldCom serve as reminders, even after all these years, of how officer misconduct can dramatically affect a corporation's fortunes. Following the scandals that occurred in corporate America in the beginning of the twenty-first century, as well as those that emerged in the recent financial crisis, there has been a renewed focus in certain quarters on rethinking the officer-centric model of corporate management that has come to exist.

Viewed as an effective means of achieving good corporate governance, much of the discussions surrounding increasing officer accountability pertain to the appropriate model for officer fiduciary duties and the standard of liability for such duties. This article discusses the application to officers of the duty of obedience that exists in agency law and asserts that emphasizing this duty of officers would be an effective step toward restoring the proper balance of power in corporate management. Based on the concept that certain persons are not only subject to the authority and direction of others in an organization's hierarchy, but have an affirmative duty to implement those directions, the duty of obedience exemplifies the relationship between directors and officers contemplated by corporate statutes and case law. Accordingly, this article asserts that focusing on enforcing the fiduciary duty of obedience would advance efforts to distinguish more clearly the governance responsibilities of officers from those of directors as well as increase officer accountability.

I. INTRODUCTION

It is a "basic principle of [Delaware law] that the business and affairs of a corporation shall be managed by the board of directors"¹ and that the officers are

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1. Kaplan v. Peat, Marwick, Mitchell & Co., 540 A.2d 726, 729 (Del. 1988); see Grimes v. Donald, No. 13358, 1995 WL 54441, at *8 (Del. Ch. Jan. 11, 1995) ("A fundamental precept of Delaware corporation law is that it is the board of directors . . . that has ultimate responsibility for the management of the enterprise.").

subject to the authority and control of the board.² However, for the past forty years, some corporate commentators and scholars have taken the position that the relationship between directors and officers, in practice, has been reversed.³ Wielding considerable power and influence over a corporation's business and affairs, officers have replaced directors as the individuals occupying the central role in corporate decision making. Senior executive officers, in particular chief executive officers, have dominated corporate affairs, being referred to as "the boss" and "monarchs."⁴ This shift in the balance of power from the board of directors to officers was highlighted by the upheaval that occurred in corporate America in 2001 and 2002: alleged misconduct by executive officers and lack of managerial accountability were recurring themes in the scandals that took place at corporations such as Enron, Adelphia, Tyco, ImClone, and WorldCom.⁵ And more recently, the financial crisis exposed the officer-dominated model of corporate management that currently exists.⁶

In response to these events, a renewed focus on corporate governance has emerged, with various measures designed to increase officer accountability and director oversight obligations being proposed at the federal and state level. The imposition of fiduciary duties on officers is widely viewed to be one way to achieve this objective. Accordingly, in discussing what the appropriate standard for an officer's fiduciary duties should be, corporate commentators and policymakers have focused on the application of either common law directorial fiduciary duty principles or agency law-based fiduciary duty principles, and in particular the contours of the duties of care and loyalty that exist under each body of law.⁷ What has been overlooked and underutilized, however, is the utility of emphasizing corporate officers' duty of obedience. Based on the concept that one actor in an organization is subservient to the direction and authority of another, the duty of obedience differentiates the roles and responsibilities of officers from those of directors in a way

2. See *Unanue v. Unanue*, No. 204, 2004 WL 5383942, at *15 (Del. Ch. Nov. 9, 2004) ("It is well settled that officers of a corporation serve at the pleasure of the board of directors.").

3. See *infra* notes 53–58 and accompanying text.

4. See *infra* notes 153–54 and accompanying text.

5. See Kathleen F. Brickey, *From Enron to WorldCom and Beyond: Life and Crime After Sarbanes-Oxley*, 81 WASH. U. L.Q. 357, 358 (2003) (discussing corporate misconduct at Enron, WorldCom, and Adelphia and noting that "[t]o date, some ninety corporate owners, executives, and employees have been criminally charged, and the investigations are ongoing"); Lyman P.Q. Johnson & Mark A. Sides, *The Sarbanes-Oxley Act and Fiduciary Duties*, 30 WM. MITCHELL L. REV. 1149, 1219 (2004) ("Much of the recent corporate wrongdoing involves senior officers, many of whom . . . were not members of the board." (footnote omitted)); Joseph E. Murphy, *Can the Scandals Teach Us Anything? Enron, Ethics and Lessons for Lawyers*, BUS. L. TODAY, Jan./Feb. 2003, at 10, 11 (noting that the corporate scandals at Adelphia, Tyco, ImClone and WorldCom did not involve rogue employees, rather high-profile corporate executives played a role); see also *infra* note 147.

6. See, e.g., *Am. Int'l Group, Inc. Consol. Derivative Litig.*, 965 A.2d 763 (Del. Ch. 2009) (addressing claims against directors and officers where stockholder plaintiffs sought to recover funds to make AIG whole for harm it suffered when it was revealed that the corporation's financial statements were materially misleading and overstated the value of the corporation); *In re Citigroup Inc. S'holder Derivative Litig.*, 964 A.2d 106 (Del. Ch. 2009) (addressing claims against directors and officers arising out of corporation's exposure to the subprime lending market as a result of high-risk investments).

7. See *infra* notes 78–89 & 102–10 and accompanying text.

that serves as a step toward restoring the proper model of corporate governance contemplated by corporate statutes and case law.

Historically, officers' fiduciary duties, as distinct from those of directors, have been discussed sparingly in Delaware corporate law.⁸ Mentioned only in dicta and passing references, the exact nature and scope of an officer's fiduciary obligations were left virtually untouched by the Delaware courts and legislature for almost seventy years, despite Delaware's otherwise vast and well-developed body of corporate law. As a result, many corporate scholars and commentators had operated under the assumption that the duties owed by officers were the same as those of directors.⁹ In early 2009, the Delaware Supreme Court in *Gantler v. Stephens* made its first definitive pronouncement on the subject of officer fiduciary duties, holding that corporate officers, *qua* officers, owe fiduciary duties that are the same as those owed by directors.¹⁰ While appearing to satisfy the uncertainty surrounding officer fiduciary duties, the court's opinion has been criticized for failing to address the exact contours of such duties, such as the proper standard for the duty of care and whether the protections of the business judgment rule apply equally to officers and directors.¹¹

Out of the void that had existed in Delaware prior to *Gantler*, two diverging views on officers' fiduciary duties emerged. In 1992, A. Gilchrist Sparks, III and Lawrence A. Hamermesh first proffered their view that officers owe the same fiduciary duties as directors.¹² In contrast, based on their thesis that officers owe fiduciary duties because they are agents of the corporation, Professors Lyman Johnson and David Millon offered a contrary view, claiming that agency law principles should serve as the basis for an officer's fiduciary duties and liability.¹³ At the center of this debate is the duty of care and the standard of liability for conduct in violation of that duty and whether the business judgment rule applies to directors and officers alike. Notably absent from the competing views advanced by these scholars, however, is any in-depth discussion or emphasis on the application of the fiduciary duty of obedience that exists in agency law to officer conduct.¹⁴

8. See Lyman P.Q. Johnson & David Millon, *Recalling Why Corporate Officers Are Fiduciaries*, 46 WM. & MARY L. REV. 1597, 1601 (2005) ("Hardly a week goes by without yet another Delaware decision addressing the subject of director duties. Yet, surprisingly, no Delaware decision has ever clearly articulated the subject of officer duties and judicial standards for reviewing their discharge.").

9. See *id.* at 1600 ("[C]ourts and commentators routinely describe the duties of directors and officers together, and in identical terms."); see, e.g., *In re Walt Disney Co. Derivative Litig.*, No. 15452, 2004 WL 2050138, at *3 (Del. Ch. Sept. 10, 2004); *Copi of Del., Inc. v. Kelly*, No. 14529, 1996 WL 633302, at *5 (Del. Ch. Oct. 25, 1996); *Zirn v. VLI Corp.*, No. 9488, 1989 WL 79963, at *4 (Del. Ch. July 17, 1989); Hillary A. Sale, *Delaware's Good Faith*, 89 CORNELL L. REV. 456, 462 n.28 (2004); DAVID A. DREXLER, LEWIS S. BLACK, JR. & A. GILCHRIST SPARKS, III, 1 DELAWARE CORPORATION LAW AND PRACTICE § 14.02, at 14-5 (Supp. 2008). *But see* Johnson & Millon, *supra* note 8, at 1600-02 (arguing that officers and directors do not have the same fiduciary duties).

10. 965 A.2d 695 (Del. 2009).

11. See *infra* notes 58-61 and accompanying text.

12. See *infra* Part III.A.

13. See *infra* Part III.B.

14. *But see* A. Gilchrist Sparks, III & Lawrence A. Hamermesh, *Common Law Duties of Non-Director Corporate Officers*, 48 BUS. LAW. 215, 234 (1992) (contemplating that, despite the application of the business judgment rule, officers would be exposed to liability where they act outside the scope of their delegated responsibility, i.e., disobediently).

Even Professors Johnson and Millon, who advocate for the application of agency principles, fail to focus on the enforcement of the fiduciary duty of obedience of corporate officers, but instead look to an agent's duty of loyalty and care as a way to achieve better corporate governance.

In choosing to apply common law directorial fiduciary principles to officers, the court in *Gantler* arguably rendered inapplicable agency law-based fiduciary duties, including potentially the duty of obedience. Where, however, the primary goals of corporate governance reform are to increase officer accountability and correct the reversal of the roles of directors and officers in corporate management, focusing on officers' duty of obedience would achieve both. The basis for the duty of obedience is the fiduciary obligation of an agent to obey the instructions and directions of the principal.¹⁵ Thus, this fiduciary duty embodies the proper model of corporate governance, emphasizing that officers are subject to the authority of the board. Enforcing a duty of obedience would also address the lack of accountability that has resulted from the unbalanced relationship that currently exists between directors and senior officers. Under agency law, agents have a duty to obey their principal, regardless of their discretion or their status within the organization's hierarchy.¹⁶ Accordingly, applying these principles to officers, even the chief executive officer of a corporation would have a fiduciary duty to follow the instructions of the board and answer for his or her actions, in particular where those actions diverge from the board's directions. Further, restoring directors to a position of power over officers through the duty of obedience would emphasize the duty of the board to monitor the corporation generally and to oversee the actions of the officers. In particular, focusing on the utility of the duty of obedience as a way to limit the discretion of officers would encourage boards of directors to be more thoughtful and precise in delegating authority to officers and defining their responsibilities. Finally, the duty of obedience would further efforts to distinguish more clearly the governance responsibilities of officers from those of directors, thereby bringing state corporate law in line with recent proposals at the federal level for corporate governance reform. Thus, the focus in restoring the proper model of corporate governance through the imposition of fiduciary duties should include attention to developing and enforcing an officer's duty of obedience.

Part II of this article outlines the history of officer fiduciary duties in Delaware. Until *Gantler*, the only guidance from Delaware courts on this issue stemmed from a summary pronouncement, in dicta, that officers and directors owe fiduciary duties to the corporation and its stockholders.¹⁷ In *Gantler*, however, the question of what fiduciary duties officers owe the corporation and its stockholders was put squarely before the Delaware Supreme Court, thereby allowing it to address the issue.

15. See *infra* Part IV.A.

16. See *id.*

17. See *infra* notes 21–22 & 24–25 and accompanying text.

Part III of this article summarizes the debate, pre-*Gantler*, between corporate commentators regarding whether officers should be held to duties that are the same as, or stricter than, those of directors. Finally, Part IV addresses how the imposition of the agency law-based fiduciary duty of obedience on corporate officers would help to remedy the imbalance in power that exists in corporate management. By requiring that officers obey the directions of the board of directors, the duty of obedience would place the board in a more powerful position vis-à-vis the officers, thereby moving toward restoring directors as the center of corporate management. Part IV also discusses some of the additional benefits that would result from emphasizing corporate officers' fiduciary duty of obedience.

II. BACKGROUND

A. THE HISTORY OF FIDUCIARY DUTIES OF OFFICERS IN DELAWARE

In 1939, the Delaware Supreme Court first articulated the idea that officers of a Delaware corporation owe the same fiduciary duties to the corporation and its stockholders as directors. In *Guth v. Loft*, the court stated, without discussion, that “[c]orporate officers and directors . . . stand in a fiduciary relation to the corporation and its stockholders.”¹⁸ The court in *Guth* was faced with claims that the defendant had usurped an opportunity of the corporation for himself. However, because the defendant was both an officer and director of the corporation, there was no need for the court to address specifically the nature and scope of the defendant’s fiduciary duties *qua* officer. Over forty years later, the Delaware Supreme Court in *Lynch v. Vickers* again mentioned the fiduciary duties of officers. Looking beyond Delaware’s borders, the court noted that “[p]ractically all jurisdictions recognize a fiduciary relationship arising from the directors and officers to their corporation and to the stockholders.”¹⁹ But, as was the case in *Guth*, because an officer’s fiduciary duties were not an issue squarely before the court, the precise nature of these duties was not addressed in any depth.

Similarly, the Delaware Court of Chancery—widely considered one of the nation’s leading business courts²⁰—until *Gantler*, had never addressed the exact contours of the fiduciary duties of officers. Rather, like the Delaware Supreme Court in *Guth* and *Lynch*, the court of chancery referenced such duties only in passing, and largely in dicta, providing little direction on the issue.²¹ In *Zirn v. VLI Corp.*,

18. 5 A.2d 503, 510 (Del. 1939).

19. *Lynch v. Vickers Energy Corp.*, 429 A.2d 497, 502–03 (Del. 1981) (quoting *Mansfield Hardwood Lumber Co. v. Johnson*, 263 F.2d 748, 754 (5th Cir. 1959)).

20. See, e.g., William H. Rehnquist, *The Prominence of the Delaware Court of Chancery in the State-Federal Joint Venture of Providing Justice*, 48 *Bus. Law.* 351, 354 (1992) (“Corporate lawyers across the United States have praised the expertise of the Court of Chancery, noting that since the turn of the century, it has handed down thousands of opinions interpreting virtually every provision of Delaware’s corporate law statute. No other state court can make such a claim.”).

21. See, e.g., *Copi of Del., Inc. v. Kelly*, No. 14529, 1996 WL 633302, at *5 (Del. Ch. Oct. 25, 1996) (“Officers and directors of a corporation owe a fiduciary duty to shareholders.”); *Zirn v. VLI Corp.*, No. 9488, 1989 WL 79963, at *4 (Del. Ch. July 17, 1989).

for example, the chancery court stated, “Delaware law is clear that a fiduciary duty is owed to the shareholders of a corporation by the officers and directors of the corporation.”²² This is typical of the chancery court’s treatment of the issue pre-*Gantler*; references to similar language appear in a number of chancery court opinions, most of which simply cite the sweeping language from *Guth* as precedential support without any further explication.²³ Perhaps this should not be surprising given that none of the issues in these cases turned on the nature of the fiduciary duty of corporate officers *qua* officers. Thus there was no need—and in fact, no opportunity—for the court to provide further guidance on the topic.²⁴

Aside from the broad language in *Guth* and *Lynch* and dicta in lower court opinions, the Delaware courts left corporate officers and corporate counsel to speculate as to the exact nature of their fiduciary duties and what liability may arise from a breach of those duties.²⁵ Given Delaware’s reputation as a leader in the world of corporate law, this uncertainty has led to much speculation as to why Delaware courts have not provided more guidance as to the fiduciary duties of officers.²⁶

22. 1989 WL 79963, at *4.

23. See, e.g., *In re Walt Disney Co. Derivative Litig.*, No. 15452, 2004 WL 2050138, at *3 (Del. Ch. Sept. 10, 2004).

24. See *In re Tyson Foods, Inc. Consol. S’holder Litig.*, No. 1106-CC, 2007 WL 2351071, at *1 (Del. Ch. Aug. 15, 2007) (“Judicial restraint suggests that a court should limit itself to the case or controversy placed before it and, to the extent practicable, not engage in speculation about phantasmal parties or issues that might one day appear.”).

25. See Sparks & Hamermesh, *supra* note 14, at 215 (“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.”).

In the bankruptcy context, however, courts have recently begun to wade into the muddy waters of officer fiduciary duties. In *Miller v. MacDonald*, a Delaware bankruptcy court indicated that, in its view, liability for the failure of oversight, so-called *Caremark* liability, applied to directors and officers equally. 385 B.R. 576 (Bankr. D. Del. 2008); see also *In re Bridgeport Holdings, Inc.*, 388 B.R. 548 (Bankr. D. Del. 2008) (addressing fiduciary duty claims, including oversight claims, brought against corporate officers). In *Miller*, the trustee in bankruptcy alleged, among other things, that the corporation’s management “became aware of or should have been aware of the malfeasance and misdealing and discrepancies in [the corporation’s] revenues” and failed to take any action to remedy such discrepancies. 385 B.R. at 588. In particular, the trustee claimed that the corporation’s vice president of operations and general counsel had breached his fiduciary duties for “failing to implement any internal monitoring system and/or failing to utilize such system as is required by *Caremark*.” *Id.* at 591. The court rejected the defendant officer’s argument that Delaware law does not recognize *Caremark* duties as applying to corporate officers. Instead, relying in part on the defendant’s role as general counsel and the broad proposition that officers owe fiduciary duties, the *Miller* court denied the defendant officer’s motion to dismiss the oversight claim, stating that “I believe the *Caremark* decision itself suggests that the same test would be applicable to officers.” *Id.* at 592.

26. In their article, Professors Johnson and Millon posit several reasons that may account for the lack of attention to distinguishing officers from directors in analyzing fiduciary duties. See Johnson & Millon, *supra* note 8, at 1609–18. In addition to the Delaware Court of Chancery’s historical lack of personal jurisdiction over officers, Professors Johnson and Millon also assert that the following have contributed to officers’ status as forgotten fiduciaries of the corporation: (1) officer misconduct can be addressed by a board of directors by contractual means; (2) the lack of appreciation by plaintiffs’ attorneys, boards of directors, and judges for the distinctive fiduciary obligations of officers; (3) lawyers do not fully appreciate the fiduciary duties of officers as agents of the corporation because law schools devote less time and attention to agency law principles; and (4) the “cozy” relationship between boards of directors and senior officers. *Id.*

Perhaps the obvious, and therefore most likely, rationale for the absence of such case law is that prior to January 1, 2004, Delaware courts did not have personal jurisdiction over non-resident, non-director officers of Delaware corporations.²⁷ Effective January 1, 2004, the scope of Delaware's long-arm director consent to service statute, 10 *Del. C.* § 3114, was amended to include certain corporate officers.²⁸ This amendment, at least in the opinion of one Delaware Supreme Court justice, would "enable Delaware courts over time to develop a jurisprudence of corporate officer fiduciary duty across a broad spectrum of activities in which public corporations commonly engage."²⁹

This considerable jurisprudence that Justice Jacobs envisioned has not fully materialized in the six years since the amendment to section 3114, even in cases where the Delaware courts could have taken advantage of an opportunity to create law. For example, in *In re Walt Disney Co. Derivative Litigation*, the Delaware Court of Chancery was presented with the opportunity to expand upon the issue of officer fiduciary duties when it was faced with challenges to two defendants' actions taken both in their roles as directors and as officers in connection with the hiring and firing of President Michael Ovitz. But because the plaintiffs in *Disney* had essentially made the same claims against the defendants in their capacities as officers and as directors, the court chose to sidestep the issue of an officer's fiduciary duties, merely declaring that "[t]o date, the fiduciary duties of officers have been assumed to be identical to those of directors."³⁰ Subsequent decisions in the chancery court have relied on the *Disney* court's generalized declaration in support of the proposition originally set forth in *Guth* that an officer owes the same

27. See, e.g., *Gebelein v. Perma-Dry Waterproofing Co.*, No. 6210, 1982 WL 8776 (Del. Ch. Jan. 12, 1982) (holding that the court did not have personal jurisdiction over non-resident, non-director officers by reason of their officer status alone); *Kelly v. McKesson HBOC, Inc.*, No. 99C-09-265WCC, 2002 WL 88939 (Del. Super. Ct. Jan. 17, 2002) (finding that Delaware state courts did not have personal jurisdiction over non-resident executive vice president and chief financial officer of Delaware corporation).

28. 74 Del. Laws 213 (2003). Following the amendment, section 3114(b) provides that:

Every nonresident of this State who . . . accepts election or appointment as an officer of a corporation organized under the laws of this State . . . shall, by such acceptance or by such service, be deemed thereby to have consented to the appointment of the registered agent of such corporation . . . as an agent upon whom service of process may be made in all civil actions or proceedings brought in this State, by or on behalf of, or against such corporation, in which such officer is a necessary or proper party, or in any action or proceeding against such officer for violation of a duty in such capacity, whether or not the person continues to serve as such officer at the time suit is commenced.

DEL. CODE ANN. tit. 10, § 3114(b) (Supp. 2008).

29. Jack B. Jacobs, *The Delaware Supreme Court: Looking to the Future*, M&A LAW., June 2004, at 1, 5.

30. No. 15452, 2004 WL 2050138, at *3 (Del. Ch. Sept. 10, 2004) (citing DREXLER et al., *supra* note 9, § 14.02); see also *In re Walt Disney Co. Derivative Litig.*, 907 A.2d 693, 777 n.588 (Del. Ch. 2005) ("The parties essentially treat both officers and directors as comparable fiduciaries, that is, subject to the same fiduciary duties and standards of substantive review. Thus, for purposes of this case, theories of liability against corporate directors apply equally to corporate officers, making further distinctions unnecessary."); *aff'd*, 906 A.2d 27 (Del. 2006). On appeal, the plaintiffs attempted to argue for a stricter standard against the defendants for their actions taken as officers but the Delaware Supreme Court rejected this argument on procedural grounds. See *Disney*, 906 A.2d at 46 n.38.

fiduciary duties as directors, but have similarly failed to develop this concept any further.³¹

Despite the dicta from Delaware's supreme and chancery courts and opinions coming out of the bankruptcy courts, the nature and scope of corporate officers' fiduciary duties and liability remained unsettled. Commentators on Delaware corporate law seemed to agree that, as a general matter, officers owe fiduciary duties to the corporation and its stockholders.³² Nevertheless, opinions diverged on how to apply this broad proposition. The uncertainty surrounding open issues such as the exact scope of an officer's fiduciary duties and, perhaps more important, whether the protections of the business judgment rule apply to officers, has led to much debate among scholars and practitioners alike.³³

B. *GANTLER V. STEPHENS*

In early 2009, the Delaware Supreme Court settled, at least in part, some of the outstanding questions with respect to officer fiduciary duties. In *Gantler v. Stephens*, stockholders of First Niles Financial, Inc. ("First Niles") filed suit against certain of the corporation's officers and directors, alleging that those individuals breached their fiduciary duties in connection with the rejection of an opportunity to sell the corporation and a subsequent reclassification of the corporation's stock.³⁴ In late 2003, due to a depressed local economy and meager expectations for growth, the

31. See, e.g., *McPadden v. Sidhu*, 964 A.2d 1262, 1275 (Del. Ch. 2008) (stating that "an officer owes to the corporation identical fiduciary duties of care and loyalty as owed by directors" (citing *Disney*, 2004 WL 2050138, at *3)); *Midland Grange No. 27 Patrons of Husbandry v. Walls*, No. 2155-VCN, 2008 WL 616239, at *7 n.32 (Del. Ch. Feb. 28, 2008) ("Thus, regardless of whether the Officer Respondents are properly characterized as 'officers' of the Grange or 'directors' of the Grange, [t]he fiduciary duties an officer owes to the corporation 'have been assumed to be identical to those of directors.'" (quoting *Disney*, 2004 WL 2050138, at *3)); *Ryan v. Gifford*, 935 A.2d 258, 269 (Del. Ch. 2007) ("The fiduciary duties an officer owes to the corporation 'have been assumed to be identical to those of directors.'" (quoting *Disney*, 2004 WL 2050138, at *3)).

32. See DREXLER et al., *supra* note 9, § 14.02, at 14-5 ("With respect to the obligation of officers to their own corporation and its stockholders, there is nothing in any Delaware case which suggests that the fiduciary duty owed is different in the slightest from that owed by directors."); 3 WILLIAM MEADE FLETCHER, *FLETCHER CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS* §§ 837.50, 991 (rev. vol. 2002) ("[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"); Lyman P.Q. Johnson & Robert V. Ricca, (*Not Advising Corporate Officers About Fiduciary Duties*, 42 WAKE FOREST L. REV. 663, 669 (2007) ("What apparently is not controversial, however, is that officers owe fiduciary duties of some sort, at least equivalent to those owed by directors, if not the stricter duties owed under agency law."); Sparks & Hamermesh, *supra* note 14, at 217 ("Nonetheless, most authorities suggest that, as a general proposition, corporate officers owe the corporation the same fiduciary duties as do directors.").

33. See Aaron D. Jones, *Corporate Officer Wrongdoing and the Fiduciary Duties of Corporate Officers Under Delaware Law*, 44 AM. BUS. L.J. 475, 480-83 (2007) (discussing the differing views with respect to the contours of officers' fiduciary duties offered by commentators on Delaware law). Compare Lyman P.Q. Johnson, *Corporate Officers and the Business Judgment Rule*, 60 BUS. LAW. 439 (2005) (asserting that the business judgment rule does not apply to officers), with Lawrence A. Hamermesh & A. Gilchrist Sparks, III, *Corporate Officers and the Business Judgment Rule: A Reply to Professor Johnson*, 60 BUS. LAW. 865 (2005) (contending the business judgment rule does apply to officers).

34. 965 A.2d 695, 699 (Del. 2009).

board of directors of First Niles decided to explore potential strategic opportunities, eventually deciding to put the company up for sale.³⁵ In the sale process, three potential purchasers of First Niles emerged.³⁶ First Niles's board of directors directed its financial advisor and management to conduct due diligence in connection with a possible transaction with two of the three bidders.³⁷ With respect to one of the bidders, members of management had agreed to furnish due diligence materials that had been requested, but failed actually to provide any such materials to the bidder.³⁸ As a result, the bidder withdrew its bid for the company.³⁹ The second bidder also requested due diligence materials and a due diligence session with First Niles.⁴⁰ Initially, management did not provide the requested information and resisted setting up the due diligence session, agreeing to do so only after the bidder withdrew its offer.⁴¹ After receiving a revised offer from the second bidder, the First Niles board voted to reject the offer and consider proceeding with management's privatization plan, which involved a reclassification of First Niles's common stock.⁴² Nine months later, the board voted to amend First Niles's charter to reclassify each outstanding share of common stock held by holders of 300 or fewer shares into one share of preferred stock, which had no voting rights except in the case of a sale of the company, thereby effectively delivering control of the company to management.⁴³ As a result of the reclassification, First Niles would be able to delist its stock and go private.⁴⁴ The reclassification became effective after 57.3 percent of the company's outstanding shares approved the amendment, which included 50.28 percent of the unaffiliated shares voting in favor of the reclassification.⁴⁵

In their complaint, the plaintiff stockholders alleged, among other things, that certain officers of First Niles had sabotaged the sale process by failing to make timely responses to the bidders' due diligence requests, thus causing one of them to withdraw.⁴⁶ The officers' actions, the plaintiffs alleged, were in breach of their fiduciary duties of care and loyalty.⁴⁷ In addressing the claims against Lawrence Safarek, the company's treasurer and vice president, the Delaware Court of Chancery stated, "[A]s an officer, Safarek owed fiduciary duties of loyalty and care to First Niles and its shareholders."⁴⁸ In support of its conclusions, the court reiterated the broad statements made by the Delaware Supreme Court in *Guth* and by

35. *Id.* at 700.

36. *Id.*

37. *Id.*

38. *Id.*

39. *Id.*

40. *Id.* at 701.

41. *Id.*

42. *Id.*

43. *Id.* at 701–02.

44. *Id.* at 701.

45. *Id.* at 703.

46. *Gantler v. Stephens*, No. 2392-VCP, 2008 WL 401124, at *6, *7, *9 n.62 (Del. Ch. Feb. 14, 2008).

47. *Id.* at *5.

48. *Id.* at *7.

the Delaware Court of Chancery in *Disney*.⁴⁹ However, because the court found that the complaint failed to allege sufficient facts from which it could be reasonably inferred that Safarek had acted in bad faith or was grossly negligent, the allegations against the defendant officer were dismissed.⁵⁰

On appeal, the Delaware Supreme Court reversed the lower court's holdings on all counts. In addressing the dismissal of the breach of fiduciary duty claims as to the officer defendants, the court held that:

The Court of Chancery has held, and the parties do not dispute, that corporate officers owe fiduciary duties that are identical to those owed by corporate directors. That issue—whether or not officers owe fiduciary duties identical to those of directors—has been characterized as a matter of first impression for this Court. In the past, we have implied that officers of Delaware corporations, like directors, owe fiduciary duties of care and loyalty, and that the fiduciary duties of officers are the same as those of directors. We now explicitly so hold.⁵¹

Applying this holding to the facts of the case, the court concluded that the plaintiffs had alleged sufficient detail of wrongdoing by the defendant officers to state a claim that they breached their fiduciary duties in their capacity as officers.⁵² The court's holding with respect to the fiduciary duties of non-director officers was the first definitive ruling by it on the issue.

III. THE DEBATE: DIRECTOR DUTIES VS. AGENCY DUTIES

Prior to the court's opinion in *Gantler*, the nature and scope of a corporate officer's fiduciary duties and liabilities were uncertain, having been left essentially untouched in both Delaware case law and corporate statutes.⁵³ As a result of the

49. *Id.* (“Corporate officers and directors . . . stand in a fiduciary relation to the corporation and its stockholders. The fiduciary duties an officer owes to the corporation have been assumed to be identical to those of directors.” (ellipses in original) (internal citations and quotations omitted)).

50. *Id.*

51. *Gantler*, 965 A.2d at 708–09 (footnotes omitted). Since the decision in *Gantler*, the chancery court has reiterated the *Gantler* court's holding. *See, e.g.*, *Hampshire Grp., Ltd. v. Kuttner*, No. 3607-VCS, 2010 WL 2739995, at *11 (Del. Ch. July 12, 2010) (“As a general matter, our Supreme Court has found that the duties of corporate officers are similar to those of corporate directors.” (citing *Gantler*, 965 A.2d at 709)); *ZRII, LLC v. Wellness Acquisition Grp., Inc.*, No. 4374-VCP, 2009 WL 2998169, at *11 (Del. Ch. Sept. 21, 2009).

52. *Gantler*, 965 A.2d at 708–09.

53. *See* Sparks & Hamermesh, *supra* note 14, at 215 (“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.”); Hamermesh & Sparks, *supra* note 33, at 865 (“The relevant legal landscape has changed little since 1992: a few more judges and commentators have weighed in on the subject, but the topic remains relatively unexplored.”); Johnson & Ricca, *supra* note 32, at 665–66 (“Yet there is remarkably little law on the basic substantive question of what the fiduciary duties of corporate officers really are and virtually no theoretical attention to the issue of what those duties should be and why.”); Jones, *supra* note 33, at 475 (noting the “decades of neglect” with respect to the legal obligations of corporate officers); John Mark Zeberkiewicz & Blake Rohrbacher, *Commanding Officers: The Fiduciary Duties of Officers Under Delaware Law*, *INSIGHTS: CORP. & SEC. L. ADVISOR*, June 2008, at 1, 1 (“For most of that time, however, the question whether fiduciary duties attached to non-director officers was of little practical concern, and the nature and scope of the duties of these officers remained unexamined and, as a result, uncertain.”).

void with respect to officer fiduciary duties, diverging views emerged as to what standard should apply to these forgotten fiduciaries. As noted by Professors Lyman Johnson and Robert Ricca, “[s]cholars and lawyers vehemently disagree, to be sure, as to whether officers should be held to duties that are the same as, or stricter than, those of directors, and as to whether the business judgment rule should apply to officers with the same full force with which it applies to directors.”⁵⁴ At the center of this debate is the question of which set of fiduciary principles should govern the conduct of corporate officers—common law directorial fiduciary duties or agency law fiduciary duties.⁵⁵

Even post-*Gantler*, the nature and scope of a corporate officer’s fiduciary duties and liabilities are, in some minds, just as unsettled as the *Guth* court left them. At first blush, the court’s opinion in *Gantler* seemed to resolve the debate—quite simply, officers of Delaware corporations owe “the same” fiduciary duties as directors. In declaring the fiduciary obligations of officers and directors to be the same, the *Gantler* court made reference to the familiar fiduciary duties of care and loyalty.⁵⁶ Thus, it would be reasonable to conclude from the court’s opinion that, going forward, the robust body of law governing the fiduciary duties of directors (and not agency law principles) will similarly govern the fiduciary standards for officers.⁵⁷ Although superficially appealing, the court’s holding has been criticized for failing to answer many of the outstanding questions surrounding the fiduciary duties of officers.⁵⁸ For example, as pointed out in a recent article by Profes-

54. Johnson & Ricca, *supra* note 32, at 669.

55. See *id.* The question of whether the business judgment rule extends to non-director officers is also a hotly contested issue. Compare Sparks & Hamermesh, *supra* note 14, at 229–36, and Hamermesh & Sparks, *supra* note 33, at 865, with Johnson & Millon, *supra* note 8, at 868–76, and Johnson, *supra* note 33, at 440, 452–58. See also Jones, *supra* note 33, at 480–83 (summarizing the debate over the application of the business judgment rule to corporate officers). This question, however, presents a litany of practical and theoretical issues that are beyond the scope of this article.

56. *Gantler*, 965 A.2d at 709.

57. See J. Travis Laster & Steven M. Haas, *Delaware Supreme Court Establishes Clear Rules in Gantler Decision*, INSIGHTS: CORP. & SEC. L. ADVISOR, Mar. 2009, at 2, 5 (stating that the *Gantler* court’s “ruling is the first definitive pronouncement by the Delaware Supreme Court that officers owe the same fiduciary duties as directors”). The position that the fiduciary duties of officers post-*Gantler* are the same as those of directors, as opposed to looking to agency law for the parameters of such duties, is consistent with corporate law outside of Delaware. The Model Business Corporation Act, for example, provides that non-director officers are held to the same standards of conduct that is required of directors. See MODEL BUS. CORP. ACT § 8.42 cmt. (4th ed. 2008) (“Subsection (a) provides that an officer, when performing in such officer’s official capacity, shall meet standards of conduct generally similar to those expected of directors under section 8.30.”). In addition, other states have either included officers in their statutes governing the standard of conduct for directors or adopted a separate statute that defines the standard of conduct for officers similar to that of directors. See ALASKA STAT. § 10.06.483(e), (f) (2009) (separate statute defining standard of officer conduct); KY. REV. STAT. ANN. § 271B.8-420 (LexisNexis 2003) (same); MINN. STAT. ANN. § 302A.361 (West 2004); N.D. CENT. CODE § 10-19.1-60 (2005) (same); 15 PA. CONS. STAT. ANN. §§ 1712(c), 1732(c) (West 1995) (same); COLO. REV. STAT. ANN. § 7-108-401 (West 2006) (added officers to statutes governing standard of conduct for directors); LA. REV. STAT. ANN. §§ 12:91, 12:92(G) (1994) (same); UTAH CODE ANN. § 16-10a-840 (West 2009) (same).

58. See Lyman Johnson & Dennis Garvis, *Are Corporate Officers Advised About Fiduciary Duties?*, 64 BUS. LAW. 1105, 1108 (2009) (discussing the outstanding issues following *Gantler* and stating that “[c]learly the area of officer duties remains murkier than that of director duties”); see also Laster & Haas, *supra* note 57, at 8 (noting the issues that remain after *Gantler*).

sors Johnson and Dennis Garvis, the court's opinion in *Gantler* fails to address "whether and how the business judgment rule applies to officers in Delaware."⁵⁹ In addition, because the court was addressing duty of loyalty issues, the "scope and reach of officer duties of care and good faith," as well as "officer oversight responsibilities," still remain unclear.⁶⁰ Finally, Professors Johnson and Garvis note that the *Gantler* court failed to explain its rationale for holding that the fiduciary duties of directors and officers are equal, which they assert is important given the significant differences in the roles and responsibilities inherent in these two groups of individuals.⁶¹

Perhaps the most prominent debate surrounding the proper definition of officer fiduciary duties, and the applicable standard of liability, comes from a series of articles written by two sets of authors.⁶² Nearly twenty years before the *Gantler* decision, A. Gilchrist Sparks, III and Lawrence A. Hamermesh first wrote on their views of what the fiduciary duties of an officer should entail.⁶³ Relying on the language from *Guth* and its progeny, Sparks and Hamermesh argue that corporate officers' fiduciary duties are no different from those of directors.⁶⁴ They base their position, in part, on pointing out the distinction between corporate officers on the one hand, and the employees and agents of a corporation on the other, including the differences in the authority and discretion with which each is empowered by statute and by the corporation's governing documents.⁶⁵ An alternative view, espoused by Professors Lyman Johnson and David Millon, found its genesis in the inherent distinctions between the roles and responsibilities of a corporation's stockholder-elected directors versus its board-and-management-appointed officers.⁶⁶ In the opinion of Professors Johnson and Millon, officers are fiduciaries because they are agents of a corporation, and thus agency principles, and not traditional director fiduciary duty principles, should govern the treatment of corporate officers.⁶⁷ Professors Johnson and Millon argue that corporate officers should be held to stricter fiduciary duties than directors, and that agency law serves as the proper basis for imposing liability on these individuals.⁶⁸ While the court in *Gantler* arguably settled the debate over the proper standard for

59. Johnson & Garvis, *supra* note 58, at 1108.

60. *Id.* In particular, Professors Johnson and Garvis point out the uncertainty that remains with respect to whether the standard for the duty of care for officers is the ordinary negligence standard or the gross negligence standard. They note, however, that this issue was not before the court in *Gantler* and thus the court did not need to address the issue. *Id.*

61. *Id.*

62. See *In re Walt Disney Co. Derivative Litig.*, 907 A.2d 693, 778 n.588 (Del. Ch. 2005) (noting examples of pertinent literature on the issue of officer fiduciary duties); Jones, *supra* note 33, at 480-81 (discussing the differing views with respect to the contours of officers' fiduciary duties offered by commentators on Delaware law).

63. See Sparks & Hamermesh, *supra* note 14; see also Hamermesh & Sparks, *supra* note 33.

64. See Sparks & Hamermesh, *supra* note 14, at 216-17.

65. See *id.* at 215-16.

66. See Johnson & Millon, *supra* note 8, at 1608.

67. See *id.* at 1608, 1625, 1635-38; Johnson, *supra* note 33, at 464-65.

68. See Johnson & Millon, *supra* note 8, at 1600-03; see also Johnson & Ricca, *supra* note 32, at 669.

officers' fiduciary duties, the writings of these two sets of authors are important to understanding the implications of the court's decision as well as the remaining issues surrounding officer fiduciary duties.

A. DIRECTOR FIDUCIARY DUTIES: SPARKS AND HAMERMESH

In their articles, Sparks and Hamermesh take the position that corporate officers owe fiduciary duties that are the same as those of directors. Sparks and Hamermesh begin their analysis of the duties and liabilities of officers by drawing a distinction between officers and the other employees and agents of a corporation.⁶⁹ Officers, they point out, are given titles and duties in a corporation's bylaws or resolutions of the board of directors.⁷⁰ In addition, officers are entrusted with both administrative and executive functions, and thus are empowered to exercise discretion and judgment with respect to certain corporate matters.⁷¹ By contrast, employees and agents of a corporation do not similarly receive their authority to act for the corporation directly from the bylaws or the board of directors.⁷² Further, this latter group of individuals is rarely found to exercise the type of discretion and authority as those endowed with officer status.⁷³ Thus, Sparks and Hamermesh conclude, "[S]tatus as an employee or agent is by no means equivalent to status as an officer."⁷⁴

Citing the dicta of the Delaware courts that the fiduciary duties of directors and officers are assumed to be identical, as well as cases from other jurisdictions that have held the same, Sparks and Hamermesh assert that such statements are an accurate description of what Delaware law is and should be.⁷⁵ Accordingly, Sparks and Hamermesh take the position that the legal standard governing corporate officers' conduct and liability is the same as that of directors.⁷⁶ As a corollary to this

69. See Sparks & Hamermesh, *supra* note 14, at 215–16.

70. See *id.* at 215; see also DEL. CODE ANN. tit. 8, § 142(a) (2001).

71. Sparks & Hamermesh, *supra* note 14, at 215–16; see also *Grimes v. Donald*, No. 13358, 1995 WL 54441, at *8 (Del. Ch. Jan. 11, 1995) ("Section 141(a) of [the General Corporation Law] expressly permits a board of directors to delegate managerial duties to officers of the corporation, except to the extent that the corporation's certificate of incorporation or bylaws may limit or prohibit such a delegation."), *aff'd*, 673 A.2d 1207 (Del. 1996).

72. Sparks & Hamermesh, *supra* note 14, at 215–16.

73. Sparks and Hamermesh take the position that "[t]he term 'officer' is properly applicable only to those in whom administrative and executive functions have been entrusted, and does not apply to those [(such as employees and agents of the corporation)] without judgment or discretion as to corporate matters." *Id.* at 216 (footnote omitted); see also *Goldman v. Shahmoon*, 208 A.2d 492, 495 (Del. Ch. 1965) (finding individuals not to be officers of the corporation because they had not been shown to possess "general powers to exercise . . . personal judgment and discretion in dealing with the corporate acts complained of").

74. Sparks & Hamermesh, *supra* note 14, at 216; see also *Goldman*, 208 A.2d at 494 (finding that officers and agents are not interchangeable terms: "Officers as such are the corporation. An agent is an employee." (citation omitted)).

75. See Sparks & Hamermesh, *supra* note 14, at 217.

76. Sparks and Hamermesh do acknowledge that, as suggested by the Official Comment to section 8.42 of the Model Business Corporation Act, officers may be subject to more stringent scrutiny than that given to the conduct of directors based on officers' greater familiarity with the affairs of the corporation. See *id.* at 218–19. However, as a general principle, Sparks and Hamermesh view the

view, Sparks and Hamermesh also assert that the business judgment rule should apply equally to directors and officers.⁷⁷

Applying common law directorial fiduciary duties, Sparks and Hamermesh outline the fiduciary duties of a corporate officer. With respect to the duty of loyalty, an officer must act in the best interests of the corporation, and not for any personal interests.⁷⁸ Issues involving an officer's duty of loyalty will frequently arise in the context of usurpation of a corporate opportunity, competition with the corporation, and use of corporate trade secrets.⁷⁹ Sparks and Hamermesh note that the duty of loyalty may apply more rigidly to officers where an officer has usurped (or attempted to usurp) an opportunity that rightfully belongs to the corporation or in situations where an officer competes with the corporation.⁸⁰ Additionally, an officer must refrain from abusing corporate trade secrets and inside information.⁸¹ This aspect of an officer's duty of loyalty arises more by virtue of an officer's access to non-public corporate information as opposed to his or her status as an officer.⁸² Overall, an officer's duty of loyalty as articulated by Sparks and Hamermesh does not differ from the duty articulated by Professors Johnson and Millon. Indeed, as acknowledged by Sparks and Hamermesh, the concepts of the duty of loyalty under Delaware's director fiduciary duty law and agency law mirror each other in many respects.⁸³

Addressing the duty of care, Sparks and Hamermesh contend that an officer owes a duty to exercise due care parallel to the duty owed by directors.⁸⁴ With

fiduciary duties of officers to be the same as those of directors. The American Law Institute takes a similar view that the duties of directors and officers are the same. AM. L. INST., PRINCIPLES OF CORPORATE GOVERNANCE § 4.01 cmt. a, at 140 (1992) (“[I]t is relatively well settled . . . that officers will be held to the same duty of care standards as directors.”); see also DREXLER et al., *supra* note 9, § 14.02, at 14-5; Sale, *supra* note 9, at 462 n.28.

77. See Sparks & Hamermesh, *supra* note 14, at 229–37; Hamermesh & Sparks, *supra* note 33, at 865 (“[W]e ultimately and respectfully disagree with Professor Johnson to the extent that he is urging that the business judgment rule should not extend to non-director officers. We continue to believe that the policy rationales underlying the development and application of the business judgment rule to corporate directors similarly justify application of the rule to non-director officers, at least with respect to their exercise of discretionary delegated authority.”).

78. See Sparks & Hamermesh, *supra* note 14, at 220–21; see also *Guth v. Loft*, 5 A.2d 503, 510 (Del. 1939) (stating that the duty of loyalty “requires an undivided and unselfish loyalty to the corporation”). Under Delaware law, the duty of good faith is considered a subset of the duty of loyalty. See *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006); *Emerald Partners v. Berlin*, No. 9700, 2001 WL 115340, at *25 n.63 (Del. Ch. Feb. 7, 2001), *vacated on other grounds*, 787 A.2d 85 (Del. 2001).

79. See Sparks & Hamermesh, *supra* note 14, at 220–23. Sparks and Hamermesh note that corporate law may parallel general principles of agency law with respect to the duty of loyalty. See *id.* at 222. For instance, the corporate opportunity doctrine has been observed by Delaware courts to be a result of the application of certain agency fiduciary law principles to a particular corporate situation. See *id.* (quoting *Sci. Accessories Corp. v. Summagraphics Corp.*, 425 A.2d 957, 964 (Del. 1980) (“[T]he doctrine of corporate opportunity is but an application of agency fiduciary law in a particular corporate fact setting.”)).

80. See *id.* at 222–24.

81. See *id.* at 224–25.

82. See *id.*

83. See *id.* at 220 (stating that the fiduciary duty of loyalty “does not arise solely by virtue of director or officer status; it is a duty owed under general principles of agency law”).

84. See *id.* at 225. Such duty of care includes, among other things, the obligation to disclose information to the board of directors that is material to its decision making. See *id.* at 226–27.

respect to the standard of review for duty-of-care-based claims, they note that “Delaware case law has long applied a ‘gross negligence’ standard of care to corporate directors.”⁸⁵ Accordingly, the gross negligence standard of liability for breaches of the duty of care likewise applies to officers.⁸⁶ This standard for liability is notably higher than the ordinary negligence standard of liability for breach of the duty of care under agency law, a point with which Professors Johnson and Millon take issue.⁸⁷ In response to Professors Johnson and Millon’s position, Sparks and Hamermesh have given voice to the concern that under an ordinary negligence standard, the potential for negligence-based liability for officers would be totally incongruous with those individuals’ compensation.⁸⁸ Further, because officers do not enjoy the protections from duty-of-care violations that are afforded to directors under exculpatory provisions in a corporation’s certificate of incorporation, their exposure to liability for neglect under the agency standard of the duty of care is great.⁸⁹

B. AGENCY PRINCIPLES: JOHNSON AND MILLON

The basis for Professors Johnson and Millon’s position stems from their thesis that “corporate officers are fiduciaries because they are agents.”⁹⁰ From that foundation, Professors Johnson and Millon assert that agency law fiduciary principles should serve as the groundwork for imposing fiduciary duties on corporate officers.⁹¹ There are three main benefits, they contend, from adopting their agency law thesis as opposed to applying directorial fiduciary duties to officers. First, applying the principal-agent model from agency law would restore the legal model of management of a public corporation contemplated by corporate case law and statutes, with directors delegating to officers, who are acting as agents, the task of managing the corporation.⁹² Second, framing officer fiduciary obligations in terms of agency law would permit courts to impose more demanding fiduciary obligations on officers and, accordingly, scrutinize officer conduct more closely than that of directors.⁹³ Professors Johnson and Millon view this heightened scrutiny as

85. Hamermesh & Sparks, *supra* note 33, at 868; *see, e.g.*, *Smith v. Van Gorkom*, 488 A.2d 858, 873 (Del. 1985); *In re Walt Disney Co. Derivative Litig.*, 907 A.2d 693, 750 (Del. Ch. 2005), *aff’d*, 906 A.2d 27 (Del. 2006).

86. Hamermesh & Sparks, *supra* note 33, at 868.

87. *See* Johnson & Millon, *supra* note 8, at 1633.

88. Hamermesh & Sparks, *supra* note 33, at 871 (“[T]he scope of potential negligence-based liability for officers is enormous in comparison to any but the most generous incentive compensation packages: even at the median \$3 million level, CEO compensation (let alone presumably lesser compensation for more junior officers) is trivially small in relation to corporate harm potentially arising from officer neglect.”).

89. *See id.* at 871.

90. Johnson & Millon, *supra* note 8, at 1601.

91. *Id.* at 1601–02.

92. *Id.* at 1602–03. In addition, Professors Johnson and Millon explain that differentiating the fiduciary duties of officers and directors would also be congruent with efforts at the federal level to impose new responsibilities on directors and officers and recent emphasis on the monitoring of officers. *See id.*

93. *Id.*

an important response to the corporate scandals involving officer wrongdoing.⁹⁴ Finally, the third benefit from the application of agency fiduciary principles would be its theoretical implications, which include (i) building on and reinforcing the growing support for an entity conception of the corporation and corporate relations as opposed to the nexus of contract theory,⁹⁵ and (ii) strengthening the policy perspective that fiduciary duties and liability for officers should be analyzed separately from those of a corporation's outside directors.⁹⁶

Whereas Sparks and Hamermesh begin their analysis by distinguishing officers from other employees of a corporation, Professors Johnson and Millon emphasize the differences between officers and directors. "Contemporary debates over corporate governance ills and reforms have," they note, "in a rather puzzling way, forgotten some basic distinctions between two critical participants in corporate governance: directors and officers."⁹⁷ These distinctions include first, that officers are not elected by the stockholders like directors.⁹⁸ Rather, officers are appointed and removed by or under a grant of authority from the board of directors. Second, while directors are not agents of either the stockholders or the corporation, officers such as the chief executive officer and general counsel are agents of the corporation.⁹⁹ And third, directors are fiduciaries notwithstanding the fact that they are not agents of the corporation or stockholders; however, officers are fiduciaries because of their status as agents.¹⁰⁰

Professors Johnson and Millon argue that officers are agents to their principal—the corporation—and it is out of this relationship that an officer's fiduciary duties arise.¹⁰¹ Accordingly, they rely on agency law principles in describing their view of the fiduciary duties owed by officers. With respect to the duty of loyalty, a corporate officer is required to act solely for the benefit of the corporate principal.¹⁰² This duty includes not acting adversely to the principal, not acting on behalf of a person or entity with interests adverse to the principal, not competing with the principal, not wrongly appropriating a corporate opportunity, and not using or wrongly communicating confidential information.¹⁰³ Professors Johnson and Millon take the view that, similar to the duty of loyalty obligations of directors, an officer's duty may require him or her to "advance the well-being of the company,

94. *See id.* at 1603.

95. *Id.* at 1603–04. Professors Johnson and Millon believe that corporate law is entering an era when the entity conception of the firm will be strengthened. *See id.* Accordingly, positive law, such as agency law, will build on and reinforce that understanding of corporate relationships. *See id.*

96. *Id.* at 1604 ("We believe that, from a policy perspective, the fiduciary duties and liability rules for officers should be analyzed separately from those for outside directors. Contemporary corporate law and fiduciary discourse, however, do not do so, thereby hindering attention to this subject.").

97. *Id.* at 1605.

98. *See id.*

99. *See id.* at 1605–06.

100. *See id.* at 1606–07.

101. *See id.* at 1607 ("That officers are agents, and therefore fiduciaries subject to the control of directors acting on behalf of the corporate principal, can be seen in the basic architecture of governance established by corporate statutes.").

102. *Id.* at 1629.

103. *Id.* (citing RESTATEMENT (SECOND) OF AGENCY §§ 387–88, 395–96 (1958)).

not simply refrain from harming it.”¹⁰⁴ They note, however, that, unlike directors, officers are not required to maximize the wealth of the corporation in a change of control setting.¹⁰⁵

With respect to the duty of care, Professors Johnson and Millon assert that an agent’s duty of ordinary care, as distinguished from the duty of due care owed by directors, is the proper standard.¹⁰⁶ In support of this point, they highlight the different roles, compensation, responsibilities, and overall position within the corporation occupied by directors and officers.¹⁰⁷ Professors Johnson and Millon also note the slew of corporate scandals as examples of the power and authority that corporate officers wield and the concomitant need to regulate their conduct.¹⁰⁸ Accordingly, they contend that officers should be held to stricter standards than directors, with the applicable standard of culpability for breaches of the duty of care being the ordinary negligence standard applicable to agents, and not the looser gross negligence standard of directors supported by Sparks and Hamermesh.¹⁰⁹ Holding officers to a higher standard of care than directors, coupled with the threat of personal liability for failure to meet that standard, they assert, “may lead to renewed attention to the development of distinctive fiduciary rationales for the liability of officers.”¹¹⁰

IV. IMPROVING CORPORATE GOVERNANCE THROUGH THE DUTY OF OBEDIENCE

As discussed above, much of the debate over the application of director fiduciary principles versus agency fiduciary principles to corporate officers centers on the implications for the duty of care. Sparks and Hamermesh take the view that officers owe a duty of due care akin to that of directors and thus are subject to a gross negligence standard of liability. On the other hand, Professors Johnson and Millon argue in favor of an agent’s duty of ordinary care and accordingly a simple negligence standard of liability as the proper standard to apply to officers. The Delaware Supreme Court’s holding in *Gantler*, however, did not necessarily settle this debate. Because the claims against the officer-defendants were duty of loyalty claims, the court did not have the opportunity or the need to address specifically the contours of a corporate officer’s duty of care.¹¹¹

Absent from the debate regarding the fiduciary duties of officers, however, is any meaningful discussion of the fiduciary duty of obedience that arises under

104. *Id.*

105. *See id.* at 1630.

106. *See id.* at 1630–31 (“By way of contrast, a corporate director owes fewer duties.”). Professors Johnson and Millon’s formulation of the duty of care for officers includes, among other things, the “duty of good conduct” and the “duty to provide information and assist directors in understanding the significance of reported information.” *Id.*

107. *See id.* at 1631.

108. *See id.* at 1602–03.

109. *See id.* at 1631, 1634.

110. *Id.* at 1639.

111. *See supra* note 60 and accompanying text.

agency law. It is somewhat surprising that, in advocating for agency principles to govern officer fiduciary duties, Professors Johnson and Millon fail to emphasize the duty of obedience or address the application of that duty to corporate officers. Additionally, in adopting Sparks and Hamermesh's view, and that of the court in *Gantler*, that director fiduciary duty law serves as the basis for imposing duties on officers, the specific duty of an agent to obey one's principal under agency law gets lost.¹¹² Recent corporate scandals illustrating that it is the officers, and not the directors, that are at the center of managing the business and affairs of the corporation, however, highlight the potential importance of the duty to obey in restoring the balance of power in corporate management. Where the overarching goal in developing officer fiduciary obligations is to reform the actions of corporate officers, an additional means for holding these individuals accountable for their actions is necessary. Indeed, the Model Business Corporation Act, which adopts the position of holding officers to the same fiduciary obligations as those of directors, recognizes the importance of imposing a duty to obey on corporate officers: "Consistent with the principles of agency, which generally govern the conduct of corporate employees, an officer is expected to observe the duties of *obedience* and loyalty and to act with the care that a person in a like position would reasonably exercise under similar circumstances."¹¹³ Embodying the concept that certain persons in an organization's hierarchy are subject to the authority and control of other persons, the duty of obedience emphasizes the relationship between directors and officers contemplated by corporate case law and statutes. Accordingly, focusing on emphasizing an officer's duty of obedience would further efforts to distinguish more clearly the governance responsibilities of officers and directors, thereby reinforcing the proper model of corporate governance.

A. THE DUTY OF OBEDIENCE

Agency law implies three distinct fiduciary duties on agents: the duty of care, the duty of loyalty, and the duty of obedience. The first two of these duties are similar to their corporate law counterparts. To wit, these duties require an agent act with care, competence, and diligence,¹¹⁴ and to subordinate his or her interests to those of the principal.¹¹⁵ The duty of obedience, however, is peculiar to agency

112. Under Delaware law, directors have fiduciary obligations to the corporation and its stockholders, but such fiduciary duties do not arise out of an agency relationship. Thus, directors do not owe an analogous duty of obedience. See *infra* notes 124–28 and accompanying text.

113. See MODEL BUS. CORP. ACT § 8.42 cmt. (4th ed. 2008) (citing RESTATEMENT (SECOND) OF AGENCY § 379(1) (1958)) (emphasis added).

114. See RESTATEMENT (THIRD) OF AGENCY § 8.08 (2006). Notably, in describing the duty of care, competence, and diligence, the *Restatement* categorizes these obligations as "performance" duties, as opposed to its explicit reference to an agent's duty of loyalty as a "fiduciary duty." See *id.* § 8.01, § 8.01 cmt. b, § 8.08(B) reporter's note b; see also Lyman Johnson, *Having the Fiduciary Duty Talk: Model Advice for Corporate Officers (and Other Senior Agents)*, 63 BUS. LAW. 147, 151 (2007).

115. See RESTATEMENT (THIRD) OF AGENCY § 8.01 & cmt. b. Sections 8.02, 8.03, 8.04, and 8.05 of the *Restatement* state an agent's specific duties of loyalty, which include not acquiring material benefits in connection with transactions or other actions undertaken on the principal's behalf (§ 8.02), not dealing with the principal as or on behalf of an adverse party in a transaction that is connected with

law, lacking a clear analog in corporate law. This duty requires that an agent obey all reasonable directions of his or her principal.¹¹⁶

The *Restatement (Third) of the Law of Agency* defines the duty of obedience as the “duty to comply with all lawful instructions received from the principal and persons designated by the principal concerning the agent’s actions on behalf of the principal.”¹¹⁷ The Official Comment to section 8.09 expands upon the duty to obey, stating that an agent must comply with the instructions received from his or her principal regardless of whether he or she believes that not taking such action, or taking other action, would be better for the principal.¹¹⁸ Moreover, regardless of the discretion that an agent has the authority to exercise, or his or her relative position within an organization’s hierarchy, an agent must obey his or her principal.¹¹⁹ Of course, an agent’s duty of obedience is not absolute. Where a principal’s instructions would expose an agent to criminal, civil, or administrative sanctions, for instance, an agent has no duty to comply with such orders.¹²⁰ But when an agent elects not to comply with an instruction, he or she has a duty to inform the principal.¹²¹

While one can imagine several examples of agent malfeasance that would be violative of both the duty of obedience and the duty of loyalty, these duties are distinct under agency law and should not be confused or conflated. As the Official Comment to section 8.9 explains, “[i]n general, when an agent breaches the duties to the principal stated in this section, the agent has not breached duties of loyalty owed to the principal. However, an agent’s breach of the duties stated in this section may be closely coupled with breaches of the agent’s duty of loyalty.”¹²² To illustrate this point, the Restatement provides the following example:

4. P Bank employs A as a loan officer. P Bank gives A substantial discretion to determine whether to make any particular loan. P Bank also tells A not to exceed a limit of \$500,000 in commercial loans to any one customer. A makes a loan on P Bank’s behalf to T in the amount of \$1 million, honestly believing that T is a good credit risk and will be a good source of additional business for P Bank. A believes that P Bank does not intend A’s lending limit to restrict A’s lending authority when A harbors such beliefs about a particular borrower. A is subject to liability to P Bank for loss P Bank suffers as a consequence of A’s loan to T in an amount that greatly exceeds A’s lending

the agency relationship (§ 8.03), refraining from competition with the principal during the agency relationship (§ 8.04), and not using property or confidential information of the principal for his or her own purposes or those of a third party (§ 8.05).

116. See *id.* § 8.09.

117. *Id.* § 8.09(2). The Delaware courts will generally look to the *Restatement* for guidance on agency principles and in analyzing the fiduciary duties of agents. See, e.g., *Triton Constr. Co. v. E. Shore Elec. Servs., Inc.*, No. 3290-VCP, 2009 WL 1387115, at *9 (Del. Ch. May 18, 2009) (citing to the *Restatement* in addressing issues of agency law); *Shock v. Nash*, 732 A.2d 217, 225–26 (Del. 1999) (same); *Sci. Accessories Corp. v. Summagraphics Corp.*, 425 A.2d 957, 962 (Del. 1980) (same).

118. See RESTATEMENT (THIRD) OF AGENCY § 8.09 cmt. c.

119. See *id.*

120. See *id.*

121. See *id.*; see also *id.* § 8.11 cmt. d.

122. *Id.* § 8.09 cmt. c.

limit. A did not comply with P Bank's unambiguous instructions. It is no defense for A that A believed in good faith that P Bank's instructions should be disregarded.¹²³

In this scenario, A, the agent, believed in good faith that the instructions of P Bank, the principal, should be disregarded for the benefit of P Bank. In addition, A did not take the actions contrary to P Bank's instructions for his own personal benefit or the benefit of a competitor of P Bank. As a result, while A has breached his duty of obedience in making a loan to T in an amount that exceeded P Bank's instructions, he has not also breached his duty of loyalty. Thus, as illustrated by this example, under agency law the duty of obedience creates a separate, independent fiduciary obligation.

In contrast to agency law, Delaware corporate fiduciary duty law does not provide for an analogous separate duty of obedience. The absence of a reference to the duty of obedience is unsurprising, however, given that that area of law developed to govern director behavior. Under Delaware law, directors are not agents, as that concept exists under traditional agency law principles, of either the corporation or the stockholders,¹²⁴ and thus their fiduciary obligations exist separate and apart from agency principles. To that end, the Delaware courts have consistently held that directors are not obligated to follow the wishes of the stockholders, even a majority of the stockholders.¹²⁵ Further, as stated by the Delaware Supreme Court,

Directors, in their ordinary course of their service as directors, do not act as agents of the corporation, however. An agent acts under the control of the principal. The board of directors of a corporation is charged with the ultimate responsibility to manage or direct the management of the business and affairs of the corporation. A board of directors, in fulfilling its fiduciary duty, controls the corporation, not *vice versa*.¹²⁶

Accordingly, “[i]t would be an analytical anomaly, therefore, to treat corporate directors as *agents* of the corporation when they are acting as *fiduciaries* of the

123. *Id.*

124. See *infra* notes 126–28 and accompanying text.

125. See, e.g., *Paramount Commc'ns Inc. v. Time Inc.*, Nos. 10866, 10670 & 10935, 1989 WL 79880, at *30 (Del. Ch. July 14, 1989) (“The corporation law does not operate on the theory that directors, in exercising their powers to manage the firm, are obligated to follow the wishes of a majority of shares. In fact, directors, not shareholders, are charged with the duty to manage the firm.”), *aff'd*, 571 A.2d 1140 (Del. 1990); *Am. Int'l Rent A Car, Inc. v. Cross*, No. 7582, 1984 WL 8204, at *3 (Del. Ch. May 9, 1984) (“Nor am I persuaded that it is a per se breach of fiduciary duty for the Board to act in a manner which it may believe is contrary to the wishes of a majority of the company's stockholders.”).

126. *Arnold v. Soc'y for Sav. Bancorp, Inc.*, 678 A.2d 533, 539–40 (Del. 1996) (internal citations omitted); see also *Johnson & Millon*, *supra* note 8, at 1606; *Report of the Task Force of the ABA Section of Business Law Corporate Governance Committee on Delineation of Governance Roles and Responsibilities*, 65 *BUS. LAW.* 107, 115–16 (2009) [hereinafter ABA Report]. (“Contrary to the often-used analogy, directors are not ‘agents’ in a principal-agent relationship with shareholders, since shareholders cannot dictate board actions and directors are obligated to make their own judgments based on the best interests of the corporation and bear the full liability for those judgments.”). The *Restatement* also recognizes that a director is neither an agent of the corporation nor of its stockholders. See *RESTATEMENT (THIRD) OF AGENCY* § 1.01 cmt. f(2) (2006) (“Although a corporation's shareholders elect its directors and may have the right to remove directors once elected, the directors are neither the shareholders' nor the corporation's agents as defined in this section, given the treatment of directors within contemporary corporation law in the United States.”).

stockholders in managing the business and affairs of the corporation.”¹²⁷ Thus, with no principal whose instructions directors must obey, there was not a need for an analogous fiduciary duty of obedience to develop in the director context.¹²⁸

Following *Gantler*, if officers are held to only the same fiduciary standards as directors, because directors do not owe a duty of obedience, an officer duty of obedience would be lost. Thus, absent the judicial or statutory recognition and imposition of the fiduciary duty of obedience, officers would have no such separate fiduciary obligation under Delaware law. However, the institutional function and legal roles within a corporation are not the same for directors and officers.¹²⁹ Statutorily, “the business and affairs of every corporation . . . shall be managed by or under the direction of a board of directors,”¹³⁰ and the board cannot abdicate this duty. By contrast, the powers and duties of officers are fixed in the bylaws or by resolution of the board of directors,¹³¹ and ultimately are subject to the broad discretion and authority of the board.¹³² In fact, in the context of the duty to disclose information to the board, the Delaware courts have found officers to occupy roles similar to those of agents of the corporation.¹³³ Thus, because of the inherent differences in the roles, responsibilities, and authority that directors and officers have within the corporate management structure, recognizing and emphasizing the fiduciary duty of obedience as applicable to corporate officers would be appropriate.

127. *Arnold*, 678 A.2d at 540. In *Unisuper, Ltd. v. News Corp.*, the Delaware Court of Chancery stated that “the board’s power—which is that of an agent’s with regard to its principal—derives from the shareholders, who are the ultimate holders of power under Delaware law.” No. 1699, 2005 WL 3529317, at *6 (Del. Ch. Dec. 20, 2005) (emphasis added). However, as the court clarified in its opinion addressing certification of an interlocutory appeal of its decision, its references to agency law principles were only to “illustrate by analogy the gap filling nature of fiduciary duties.” *Unisuper, Ltd. v. News Corp.*, No. 1699, 2006 WL 207505, at *3 (Del. Ch. Jan. 19, 2006) (“In the Opinion, this Court referred generally to agency law principles to illustrate why the nature and purpose of fiduciary duties is to serve as a shield for shareholders, not as a sword for directors to use against shareholders as a group.”). Accordingly, the statements in *Unisuper* should not be read as supporting the proposition that directors are agents of the corporation.

128. See *Weinstein Enters., Inc. v. Orloff*, 870 A.2d 499, 509 (Del. 2005) (“To impose a duty of obedience on directors, moreover, would conflict with the fundamental point that corporate law assigns ultimate managerial power and responsibility to directors.” (quoting Deborah A. DeMott, *The Mechanisms of Control*, 13 CONN. J. INT’L L. 233, 253 (1999))).

129. See *Johnson & Millon*, *supra* note 8, at 1601.

130. DEL. CODE ANN. tit. 8, § 141(a) (2001) (emphasis added).

131. See *id.* § 142.

132. See R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, 1 THE DELAWARE LAW OF CORPORATIONS & BUSINESS ORGANIZATIONS § 4.10[A] (3d ed. Supp. 2010) (“The term ‘management,’ however, is deemed to encompass ‘supervision, direction and control,’ while ‘the details of the business [may be] delegated to inferior officers, agents and employees.’” (quoting *Canal Capital Corp. v. French*, No. 11764, 1992 WL 159008, at *3 (Del. Ch. July 2, 1992))).

133. See, e.g., *Sci. Accessories Corp. v. Summagraphics Corp.*, 425 A.2d 957, 962 (Del. 1980) (discussing agency principles as applying to officers of a corporation); see also *In re Walt Disney Co. Derivative Litig.*, No. 15452, 2004 WL 2050138, at *4 n.39 (Del. Ch. Sept. 10, 2004) (“Under Delaware law, an agent, such as a CEO, can bind the principal if the third person with whom that agent is dealing reasonably concludes that the agent is acting on behalf of the principal.” (citing *Int’l Boiler Works Co. v. Gen. Waterworks Corp.*, 372 A.2d 176, 177 (Del. 1977))). Commentators on Delaware law have also described officers as agents of the corporation. See BALOTTI & FINKELSTEIN, *supra* note 132, § 4.10[C] (“Officers are the principal agents of the corporation.”); see also *Johnson & Millon*, *supra* note 8, at 1601.

Applying agency law's duty of obedience to corporate officers,¹³⁴ these individuals would be required to comply with all instructions given by their principal or persons designated by their principal. An officer's principal would be the corporation and, as the body that acts for and on behalf of the corporation, the board of directors.¹³⁵ Accordingly, an officer would have a fiduciary duty to obey the directives and instructions of the board of directors. The instructions that an officer would be required to obey could take many forms. Resolutions of the board of directors would likely be the primary source of an officer's instructions; however, a corporation's certificate of incorporation or bylaws may also provide for the duties and responsibilities of an officer.¹³⁶

Recognizing a separate duty of obedience as part of officers' fiduciary duties could be challenged on the grounds that it overlaps with the already established duties of care and loyalty, and is thus duplicative and unnecessary.¹³⁷ While the duty of obedience may run into the domain of the duties of care and loyalty,¹³⁸ the purpose underlying such a duty is distinct from those of the duties of care and loyalty. The duty of obedience emphasizes that in a fiduciary relationship a person is charged with acting for another. As one commentator has summarized, "[t]he root of the fiduciary relationship is this directive from the principal to the

134. Under Delaware law, fiduciary duties are based in common law. See *In re Citigroup Inc. S'holder Derivative Litig.*, 964 A.2d 106, 115 n.6 (Del. Ch. 2009). Accordingly, in order to impose a duty of obedience on officers, the Delaware courts would need to hold that such individuals owe such duty to the corporation and its stockholders.

135. See *AGR Halifax Fund, Inc. v. Fiscina*, 743 A.2d 1188, 1195 (Del. Ch. 1999) ("It is the petitioner's interpretation and harmonization of 8 Del. C. §§ 141(f) and 242(b) that is most faithful to the principle underlying § 141(a), namely, that the board of directors alone is empowered to act on behalf of the corporation"); see also DEL. CODE ANN. tit. 8, § 141(a) (2001).

136. See DEL. CODE ANN. tit. 8, § 142(a) (2001).

137. To take the position that the mere triggering of multiple fiduciary obligations in a certain factual situation would render one of those duties redundant and unnecessary is nonsensical. For example, in the duty of oversight context, directors' failure to monitor has been described as breaches of both the duty of care and the duty of loyalty. See *Stone v. Ritter*, 911 A.2d 362, 370 (Del. 2006) (clarifying that the standard for oversight liability "draws heavily upon the concept of director failure to act in good faith" and implicates the duty of loyalty); *Desimone v. Barrows*, 924 A.2d 908, 935 (Del. Ch. 2007) ("For reasons *Caremark* well explained, to hold directors liable for a failure in monitoring, the directors have to have acted with a state of mind consistent with a conscious decision to breach their *duty of care*." (emphasis added)); *Guttman v. Huang*, 823 A.2d 492, 506 (Del. Ch. 2003) ("[T]he *Caremark* decision is rightly seen as a prod towards the greater exercise of *care* by directors in monitoring their corporations' compliance with legal standards." (emphasis added)); see also *Zeberkiewicz & Rohrbacher*, *supra* note 53, at 5 (citing *In re Caremark Int'l Inc. Derivative Litig.*, 698 A.2d 959, 967 (Del. Ch. 1996)). Likewise, a director's duty of disclosure finds its roots in both the duty of care and the duty of loyalty. See *Malpiede v. Townson*, 780 A.2d 1075, 1086 (Del. 2001) (stating that "the board's fiduciary duty of disclosure . . . is not an independent dut[y] but the application in a specific context of the board's fiduciary duties of care, good faith, and loyalty"); see also *Pfeffer v. Redstone*, 965 A.2d 676, 684 (Del. 2009); *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156, 1163 (Del. 1995). In either of these contexts, no one would assert that either the duty of care or, alternatively, the duty of loyalty, was duplicative and therefore inapplicable.

138. Professor Rob Atkinson has described the duty of obedience as "deeper, broader, and longer" than the duties of care and loyalty and a duty with "greater reach, a writ that runs into the domains of the other two duties." Rob Atkinson, *Obedience as the Foundation of Fiduciary Duty*, 34 J. CORP. L. 43, 48-50 (2008).

fiduciary: Serve the one the principal designates, as the principal designates.”¹³⁹ Further, as the *Restatement* makes clear in describing the duty of obedience, while a breach of that duty may, in certain situations, also be closely coupled with a breach of an agent’s duty of care or loyalty, in general when there occurs a breach of the duty of obedience an agent will not have breached the other duties owed to the principal.¹⁴⁰ There are many situations where an officer could breach his or her duty of obedience without such actions rising to a breach of the duty of care through gross negligence or a willful and interested breach of the duty of loyalty. Looking back to the example discussed above from the Official Comment in the *Restatement*, for instance, an officer may believe in good faith that disregarding the instructions of the board of directors would nonetheless be in the best interests of the corporation. However, acting contrary to those instructions would violate the officer’s duty of obedience. Thus, the interplay of these three fiduciary duties can be more accurately described as the duty of obedience modifying, and not subsumed in, the duties of care and loyalty.

It may be the case, however, that the Delaware courts ultimately determine that the duty of obedience exists not as a separate fiduciary duty, but rather as a component of the duty of loyalty. With respect to the duty of good faith, for example, it was frequently thought that good faith existed as a separate, independent fiduciary duty.¹⁴¹ Nonetheless, the Delaware Supreme Court held that the duty of good faith is not an independent, stand-alone fiduciary duty; rather it is a component of the duty of loyalty.¹⁴² Similar to this analysis of the duty of good faith, it is possible that the Delaware courts could take the same approach in recognizing the duty of obedience.

Finally, courts and lawmakers may be reluctant to emphasize corporate officers’ fiduciary duty of obedience, fearing that a robust duty of obedience would paralyze officers’ decision-making capacity. To that end, opponents of a duty of obedience may assert that such a duty would hinder officers’ flexibility in managing the day-to-day operations of a corporation’s business and responding to market changes by leaving little discretion for these individuals to exercise in performing their jobs. The duty of obedience, however, would not remove all discretion from an officer’s management of the corporation’s business and affairs. The instructions of a board of directors to an officer may be as broad or as narrow as it deems appropriate given the circumstances. The board may, on the one hand, provide its officers with the authority and discretion to respond to market changes as they

139. *Id.* at 48.

140. See *supra* note 122 and accompanying text.

141. See, e.g., *Emerald Partners v. Berlin*, 787 A.2d 85, 90 (Del. 2001) (“The directors of Delaware corporations have a triad of primary fiduciary duties: due care, loyalty, and good faith.” (footnote omitted)); *McMullin v. Beran*, 765 A.2d 910, 918 (Del. 2000) (“The . . . Board owed fiduciary duties of care, loyalty and good faith to all . . . shareholders”); see also *Sale*, *supra* note 9, at 463–64 (discussing the emerging duty of good faith).

142. See *Stone*, 911 A.2d at 370 (“[A]lthough good faith may be described colloquially as part of a ‘triad’ of fiduciary duties that includes the duties of care and loyalty, the obligation to act in good faith does not establish an independent fiduciary duty that stands on the same footing as the duties of care and loyalty.”).

see fit. While on the other hand, to the extent that the board wanted to constrain management's decision making, it could do so through narrowly tailored, explicit directives on how to act.¹⁴³ In this latter situation, using the fiduciary duty of obedience as a restraint on officers' actions in certain situations is a much more flexible alternative than the board attempting to achieve the same result through implementing new bylaw provisions or contractual means.

B. CORPORATE GOVERNANCE IMPLICATIONS: RESTORING THE BALANCE OF POWER

It is undisputed that corporate officers today play a central role in the operations of a corporation. Tasked with managing the day-to-day affairs, the actions of officers can have a profound effect on the success or failure of a business.¹⁴⁴ In particular, senior executive officers wield enormous power in our corporate environment, occupying "recognized positions of immense economic and social influence" and drawing "widespread attention in the larger cultural arena."¹⁴⁵ "Such well-known names as Michael Eisner at the Walt Disney Company, Martha Stewart, formerly at Martha Stewart Living, Dick Grasso, formerly head of the New York Stock Exchange, and Dennis Kozlowski, formerly at Tyco, embody the influence of the modern CEO."¹⁴⁶ The breadth of their power and the impact these officers can have on a corporation is further evidenced by the wave of corporate scandals that occurred in 2001 and 2002, with corporate executives at the center of the problems in Enron, Adelphia, and WorldCom.¹⁴⁷ Even more recently, the alleged misbehavior of corporate officers has been cited as playing a role in the downfall of corporate giants such as Lehman Brothers and Merrill Lynch.¹⁴⁸

143. Regardless of the discretion that an officer has the authority to exercise or his or her relative position within the corporation's management structure, the duty of obedience would require that the officer obey the board's directive. See RESTATEMENT (THIRD) OF AGENCY § 8.09 cmt. c (2006).

144. See Johnson & Garvis, *supra* note 58, at 1106 ("Some companies are successfully navigating the current hard times while others are struggling or collapsing.")

145. See *id.*; Johnson & Millon, *supra* note 8, at 1599. Recently, the Task Force of the ABA Section of Business Law Corporate Governance Committee published a report on the delineation of governance roles and responsibilities in which it noted that "[t]hroughout much of the last century, the professional managers hired to run public companies have wielded significant power in relation to both the board of directors and shareholders." ABA Report, *supra* note 126, at 128; see also Laura Lin, *The Effectiveness of Outside Directors as a Corporate Governance Mechanism: Theories & Evidence*, 90 Nw. U. L. REV. 898, 913-17 (1996).

146. Johnson & Millon, *supra* note 8, at 1599.

147. See *id.* at 1602 ("Agency law illuminates the nature of this director-officer interaction and highlights how dysfunctional boards contributed to recent governance scandals. Corporate interests were left unprotected as officers operated free of any meaningful director supervision."); Sale, *supra* note 9, at 461-62 ("Indeed, some of the recent corporate scandals can be tied to governance failures and the inability—or unwillingness—of officer and director fiduciaries to manage faithfully."); see also *Executives on Trial: Scandal Scorecard*, WALL ST. J., Oct. 3, 2003, at B1 (detailing criminal charges and investigations involving corporate officers); Robert W. Hamilton, *The Crisis in Corporate Governance: 2002 Style*, 40 HOUS. L. REV. 3, 19-34 (2003).

148. See generally Jessica Erickson, *Corporate Misconduct and the Perfect Storm of Shareholder Litigation*, 84 NOTRE DAME L. REV. 75 (2008) (discussing shareholder litigation involving officers of Merrill Lynch named as defendants and their alleged role in misleading the market and other misconduct at the company); see also *supra* note 6.

Indeed, many recent examples of officer malfeasance can be attributed largely to the role reversal now common in modern corporate management. Originally tasked with the management of the business and affairs of the corporation,¹⁴⁹ the directors of a corporation are intended to be at the top of the management hierarchy. Recognizing that in many large corporations the board of directors cannot manage the operations of the firm itself, the board may delegate certain powers and responsibilities to the officers.¹⁵⁰ Regardless of their ability to delegate, however, the board remains the body with the ultimate responsibility to—and accountability for—management of the business and affairs of the corporation.¹⁵¹ Accordingly, it is “a basic tenet of our corporate governance system” that the board of directors should manage the business and affairs of the corporation, with officers subject to the control of the board.¹⁵²

Nevertheless, corporate scholars and policymakers alike have recognized that in reality it is the officers, and not the directors, who sit atop the corporate management hierarchy. As William H. Donaldson, Chairman of the U.S. Securities and Exchange Commission (“SEC”), summarized at the 2003 Economic Policy Conference, “[o]ver the past decade or more, at too many companies, the chief executive position has steadily increased in power and influence. In some cases, the CEO has become more of a monarch than a manager.”¹⁵³ Describing an “overly cozy relationship” that has come to exist between boards of directors and senior officers, Professors Johnson and Millon assert that directors feel indebted to senior management, even regarding such individuals as the “boss.”¹⁵⁴ Thus, it appears that the relationship and balance of power between directors and officers that is contemplated by corporate statutes and case law has become the opposite of what was intended.

The creeping authority and influence of corporate officers is not novel. In fact, almost forty years ago a study by Professor Myles Mace supported the belief that of-

149. See DEL. CODE ANN. tit. 8, § 141(a) (2001); *McMullin v. Beran*, 765 A.2d 910, 916 (Del. 2000) (“One of the fundamental principles of the Delaware General Corporation Law statute is that the business affairs of a corporation are managed by or under the direction of its board of directors.” (citing DEL. CODE ANN. tit. 8, § 141(a))).

150. See *Grimes v. Donald*, No. 13358, 1995 WL 54441, at *8 (Del. Ch. Jan. 11, 1995), *aff’d*, 673 A.2d 1207 (Del. 1996).

151. See *In re Walt Disney Co. Derivative Litig.*, 907 A.2d 693, 761 n.490 (Del. Ch. 2005) (“A fundamental precept of Delaware corporation law is that it is the board of directors . . . that has ultimate responsibility for the management of the enterprise.” (quoting *Chapin v. Benwood Found., Inc.*, 402 A.2d 1205, 1211 (Del. Ch. 1979) (internal citation omitted))), *aff’d*, 906 A.2d 37 (Del. 2006); *Grimes*, 1995 WL 54441, at *9.

152. See *Jones*, *supra* note 33, at 495; see also *Johnson & Millon*, *supra* note 8, at 1614.

153. William H. Donaldson, Chairman, U.S. Sec. & Exch. Comm’n, Remarks at the 2003 Economic Policy Conference of the National Association for Business Economics (Mar. 24, 2003) (transcript available at <http://www.sec.gov/news/speech/spch032403whd.htm>); see also *Excerpts from Report by Greenspan at Senate*, N.Y. TIMES, July 17, 2002, at C8 (“Our vast and highly liquid financial markets enable large institutional shareholders to sell their shares when they perceive inadequacies of corporate governance, rather than fix them. This has placed de facto control in the hands of the chief executive officer.”).

154. *Johnson & Millon*, *supra* note 8, at 1613–14; see also *Sale*, *supra* note 9, at 459 (“Yet, in today’s world, directors play less of a role in establishing corporate norms than their officer counterparts.”).

ficers, and not directors, played the central role in corporate affairs.¹⁵⁵ A later study conducted in the late 1980s by Professors Jay Lorsch and Elizabeth MacIver suggested Professor Mace's analysis underestimated the centrality of directors;¹⁵⁶ however, those findings did not necessarily mean that executive officers still did not have substantial influence over corporate affairs.¹⁵⁷ Rather, it remains a widely held belief that the modern board of directors has been "relegated to an advisory and legitimizing function that is substantially different from the role of policymaker and guardian of shareholder and public interest contemplated by the law of corporations."¹⁵⁸

In response to the actions of corporate officers, the SEC, the New York Stock Exchange (the "NYSE"), and Nasdaq have taken steps to put in place greater legal accountability not only with respect to officers, but also addressing the directors that should be overseeing those individuals.¹⁵⁹ Recognizing that officers are integral to the success and failure of corporations, federal securities law was amended by the Sarbanes-Oxley Act,¹⁶⁰ which, among other things, imposes legal responsibilities on corporate officers. Federal regulation of public corporations through laws such as the Sarbanes-Oxley Act and the rules promulgated thereunder have established a system of regulation and liability that applies to officers. These current federal regulatory reforms have been aimed directly at fixing the "longstanding reversal of control problem made possible not because of defects unique to the basic architecture of corporate governance, but rather due to problems inherent in the dynamics of [director-officer] relationships."¹⁶¹ Similarly, post-Enron, regulatory agencies such as the NYSE and Nasdaq adopted procedures to achieve greater accountability of officers and directors, in particular with respect to director oversight of officers.¹⁶² And more recently, even before the exact causes of the financial

155. MYLES L. MACE, *DIRECTORS: MYTH AND REALITY* 72–85, 190–94 (1971); see also Myles L. Mace, *The President and the Board of Directors*, HARV. BUS. REV., Mar.–Apr. 1972, at 37 (describing the interactions of corporate directors and presidents).

156. See JAY W. LORSCH & ELIZABETH MACIVER, *PAWNS OR POTENTATES: THE REALITY OF AMERICA'S CORPORATE BOARDS* 75–96 (1989).

157. See Robert W. Hamilton, *Corporate Governance in America 1950–2000: Major Changes but Uncertain Benefits*, 25 J. CORP. L. 349, 363–64 (2000).

158. Arthur J. Goldberg, *Debate on Outside Directors*, N.Y. TIMES, Oct. 29, 1972, § 3, at 1; see also ALFRED F. CONRAD, *CORPORATIONS IN PERSPECTIVE* 349–50 (1976) ("[Directors] do not supervise and control executives; rather, they are supervised and controlled by the executives."); Johnson & Millon, *supra* note 8, at 1614–17; *supra* notes 144–47, 153–54 and accompanying text.

159. See *infra* notes 160–63 and accompanying text.

160. Public Company Accounting Reform and Investor Protection Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified in scattered sections of 11, 15, 18, 28, and 29 U.S.C.); see also Larry Catá Backer, *The Sarbanes-Oxley Act: Federalizing Norms for Officer, Lawyer, and Accountant Behavior*, 76 ST. JOHN'S L. REV. 897 (2002) (discussing the effects of the Sarbanes-Oxley Act following corporate scandals).

161. Johnson & Millon, *supra* note 8, at 1615; see *id.* at 1614–15 ("This stunning, de facto 'reversal of control,' to use sociologist Harrison White's phrase, is the key animating force in recent congressional, SEC, NYSE, and Nasdaq governance reforms.")

162. See Johnson & Sides, *supra* note 5 (discussing regulation of director and officer conduct under the Sarbanes-Oxley Act and steps taken by the SEC, the NYSE, and Nasdaq and the interplay of federal reform with state fiduciary duty law); Sale, *supra* note 9, at 456 ("In the post-Enron era, there has been considerable discussion about what went wrong at Enron and elsewhere and how to fix it. Congress passes the Sarbanes-Oxley Act, the New York Stock Exchange adopted new corporate regulations introducing new checks and balances, and other self-regulatory organizations followed suit.")

crisis that began in 2008 have been determined and fully understood, lawmakers have been proposing a broad range of corporate governance-related reforms.¹⁶³

Stockholder activists and institutional investors have likewise recognized the officer-centric pattern of power occurring in corporate America. This reversal in the balance of power is readily apparent where the chief executive officer also serves as the chairman of the board of directors.¹⁶⁴ In an effort to create a board that is independent from senior management, stockholder proposals requiring the separation of the chief executive officer and the chairman of the board of directors have been on the rise.¹⁶⁵ Vineeta Anand, chief research analyst at the AFL-CIO, has stated that the increase in such proposals evidences the recognition among institutional investors that having an independent chairman of the board is a “fundamental corporate governance practice.”¹⁶⁶ In addition, these proposals have been receiving steadily increasing support from stockholders, averaging support of only 24.8 percent of the votes cast in 2007, to garnering average support of 36.3 percent of the votes cast in 2009.¹⁶⁷ Not surprisingly, lawmakers and regulators have also weighed in on the issue. The SEC approved new proxy disclosure rules for the 2010 proxy season requiring a reporting corporation to disclose its specific leadership structure and explain why its structure is appropriate in the circumstances, including disclosure of whether and why the corporation has chosen to combine or separate the principal executive officer and the board chairman positions.¹⁶⁸ In adopting the amendments, the SEC noted that

163. See ABA Report, *supra* note 126, at 110 & n.3 (describing reforms that have been proposed or adopted in response to the recent financial crisis).

164. See Johnson & Millon, *supra* note 8, at 1617 (“One salient manifestation of control reversal is the widespread United States practice of the CEO also serving as chair of the board of directors. Under this peculiar arrangement, the chief agent to be monitored also serves as the most influential person in the body designed to monitor that agent.”).

165. See U.S. Preview: *Board Issues*, RISKMETRICS GROUP (Feb. 11, 2010), http://www.riskmetrics.com/system/files/private/US_Preview-Board_Issues.pdf [hereinafter *Board Issues*] (reporting that as of February 1, 2010, there were forty stockholder proposals on the issue of having the chairman of the board be independent from management). In 2009, there were thirty-one stockholder proposals on the issue of an independent chair whereas for the 2010 proxy season thus far there are already forty such proposals pending. See *id.*; *RiskMetrics Group Postseason Report*, RISKMETRICS GROUP (Oct. 2009), http://www.riskmetrics.com/system/files/private/2009_PSR_Public_final.pdf [hereinafter *Postseason Report*].

166. *Board Issues*, *supra* note 165, at 1; see also *id.* (“‘Each year, [proposals for an independent chair] ha[ve] gained a little more support as investors are coming around to the idea that boards need independent leadership,’ said John Keenan, a strategic analyst with the American Federation of State, County, and Municipal Employees (AFSCME) . . .”).

167. See *Postseason Report*, *supra* note 165, at 4–5 (“Shareholder resolutions seeking independent board chairs at U.S. firms continued to receive greater approval; the proposals averaged 36.3 percent support, an increase of 6.5 percentage points over 2008.”). In 2009, four stockholder proposals requiring an independent chairman of the board received a majority of the votes cast. See *Board Issues*, *supra* note 165, at 1. Notably, one of those proposals was a binding resolution at Bank of America, which received 50.3 percent of the votes in favor of the proposal, and resulted in then-CEO Kenneth Lewis resigning from his position as chairman. See David Milenberg & Linda Shen, *Bank of America Strips CEO Lewis of Chairman’s Job (Update2)*, BLOOMBERG (Apr. 29, 2009), <http://www.bloomberg.com/apps/news?pid=20601087&sid=ak7trcanESiA>.

168. See Corporate Governance, 17 C.F.R. § 229.407 (2010); see also Proxy Disclosure Enhancements, Securities Act Release No. 33-9089, 74 Fed. Reg. 68334, 68345 (Dec. 23, 2009) (to be codified at 17 C.F.R. pts. 229, 239, 240, 249 & 274) (stating that “the amendments were designed to provide shareholders with disclosure of, and the reasons for, the leadership structure of a company’s

“one important aspect of a company’s corporate governance practices is its board’s leadership structure.”¹⁶⁹

In response to the role reversal that has occurred in corporate management, corporate scholars and policymakers have called for corporate reform and a movement back toward enforcing the proper relationship between directors and officers, with the directors at the center of corporate governance. And “[t]he imposition of fiduciary duties on corporate decision-makers . . . is widely thought to be one way to achieve better corporate governance.”¹⁷⁰ To that end, Professors Johnson and Millon contend that applying the stricter agency law-based duty of care to corporate officers is the proper means of putting directors in “a more powerful position in relation to corporate officers.”¹⁷¹ However, recognizing and enforcing an officer’s duty of obedience would also be a means of achieving that goal.

The duty of obedience would require that an officer comply with all lawful instructions he or she receives from the board of directors (or persons designated by the board of directors). This fiduciary duty emphasizes the role of the board as the party wielding the ultimate power and authority over the business and affairs of the corporation. Additionally, the duty of obedience would reinforce the corporate management hierarchy and distinguish the roles of directors and officers by underscoring the fact that officers serve subject to the control, and at the direction of, the board.¹⁷² Accordingly, emphasizing the fiduciary duty of obedience owed by officers directly addresses what the proper balance of power in corporate management should be.

board concerning the principal executive officer, the board chairman position and, where applicable, the lead independent director position”). Senator Charles Schumer’s 2009 Shareholder Bill of Rights included, among other things, a mandate for the separation of the chairman of the board of directors and chief executive officer as well as requiring the chairman to be an independent director, but he ultimately backed away from that provision after an outcry in corporate circles. See S. 1074, 111th Cong. (2009), available at http://www.schumer.senate.gov/new_website/Bill%20Text%20-%20Shareholders%20Bill%20of%20Rights%20Act%20of%202009.pdf; see also Stephen M. Bainbridge, *Schumer’s Shareholder Bill of Rights: Separating the CEO and CoB*, PROFESSORBAINBRIDGE.COM (May 14, 2009, 11:20 AM), <http://www.professorbainbridge.com/professorbainbridgecom/2009/05/schumers-shareholder-bill-of-rights-separating-the-ceo-and-cob.html>; *Board Issues*, *supra* note 165, at 1–2.

169. Proxy Disclosure Enhancements, 74 Fed. Reg. at 68345.

170. Johnson & Ricca, *supra* note 32, at 665; see also *In re Citigroup Inc. S’holder Derivative Litig.*, 964 A.2d 106, 115 n.6 (Del. Ch. 2009) (“In defining [fiduciary duties], the courts balance specific policy considerations such as the need to keep directors and officers accountable to shareholders and the degree to which the threat of personal liability may discourage beneficial risk taking.”). As summarized by then-Chairman of the Federal Reserve Board Alan Greenspan, “[t]he state of corporate governance to a very large extent reflects the character of the CEO, and . . . this is a very difficult issue to address. Although we may not be able to change the character of corporate officers, we can change behavior through incentives and penalties. That, in my judgment, could dramatically improve the state of corporate governance.” *Conduct of Monetary Policy: Hearing Before the H. Comm. on Financial Servs.*, 107th Cong. 60 (2002) (statement of Alan Greenspan, Chairman, Federal Reserve Board).

171. Johnson & Millon, *supra* note 8, at 1627.

172. See *id.* at 1602 (“[P]roviding a conceptual basis both to ground officer fiduciary obligations and to distinguish director and officer functions can substantially enhance the larger project of restoring to reality the legal model of director-officer relations within the public corporation. In this model, directors delegate to officers, acting as agents, the role of managing the business and affairs of the corporation.”).

The duty of obedience also furthers efforts to improve corporate governance by making officers more accountable to the corporation and its stockholders. In addition to their duties of care and loyalty, officers would be subject to a third fiduciary obligation that would require them to serve the board of directors as the board of directors directs. Moreover, the duty of obedience can also operate so as to amplify the duties of care and loyalty that an officer owes to the corporation, thereby holding officers to a stricter standard for their actions. This result would occur in instances where the board of directors gives an officer a specific directive. Giving specific, as opposed to more general, discretionary, instructions to an officer would, as one scholar has described it, “ratchet[] up . . . the duty of either care or loyalty from the default level to the optional level, from what the law infers as the principal’s preference to what the principal actually specifies.”¹⁷³

The corporations that engaged in subprime lending, which ultimately left them exposed to massive losses in the past few years, serve as a good example of how the duty of obedience can enhance an officer’s duty of care and loyalty.¹⁷⁴ In one scenario, a board of directors of a global financial services company with businesses that provide a broad range of financial services to consumers and businesses instructs members of its senior management to investigate additional ways that the corporation should invest its assets. After investigating different options, management recommends that the corporation create and invest in structured investment vehicles (“SIVs”). The corporation decides to adopt management’s recommendation and authorizes management to create SIVs by borrowing cash (by selling commercial paper) and then using those proceeds to purchase loans.¹⁷⁵ Management decides to invest the corporation’s SIVs in subprime mortgages because of the higher returns promised by such investments. The mortgages that management invested the corporation’s SIVs in, however, were riskier assets such as home equity loans and not the low-risk assets traditionally used by SIVs. As a result, the corporation is exposed to problems in the subprime market that arise from the housing market crash, and their SIVs are unable to pay their investors. Because the SIVs can no longer meet their cash needs by attracting new investors, the corporation has to sell its assets at fire sale prices, thereby incurring large losses. The officers who were tasked with investigating and investing assets for the corporation did not necessarily, however, breach their fiduciary duties of care and loyalty in recommending the SIVs and making the investments in subprime mortgages. Recommending and investing in a high-risk investment does not necessarily mean that the officers failed to be adequately informed or acted with gross

173. Atkinson, *supra* note 138, at 60.

174. This example is based on the facts in *In re Citigroup Inc. Shareholder Derivative Litigation*, 964 A.2d 106 (Del. Ch. 2009), in which the court of chancery addressed stockholder claims that the actions of current and former directors and officers of Citigroup breached their fiduciary duties by failing to protect adequately the corporation from exposure to the subprime lending market.

175. As a result, the SIVs are selling short-term debt and buying longer-term, higher yielding assets.

negligence in making their decisions and thus violated their duty of care.¹⁷⁶ Nor does the exposure to the subprime market and subsequent losses in the sale of the SIVs mean that the officers acted in a self-interested manner or in bad faith in making the investment decision, and thus violated their duty of loyalty.¹⁷⁷ Accordingly, even if it is later determined that the board would have preferred management to invest the SIVs in a lower risk investment, because the board did not specifically state such a preference, the officers' decision to invest in the riskier subprime mortgages would not result in a breach of their fiduciary duties.

In a second scenario, after considering the officers' recommendation to create and invest the corporation's assets in SIVs, the board of directors instructs the officers to have the SIVs invested in the low-risk assets traditionally used by the SIVs, and not in the riskier home equity loans. Despite the board's instructions, the officers, believing that the riskier investment's promise of high returns will be better in the long run for the corporation and will in turn result in larger performance-based compensation for the officers, invest the SIVs in the subprime mortgages. In contrast to the first scenario, in this second situation, the board of directors has issued a specific directive to the officers. In terms of the duty of care, the board's specific instructions to have the SIVs invested in lower risk assets has removed the ability of the officers to exercise discretion and choose the speculative home mortgage investment. As a result of the board's directive, the subsequent investment in the high-risk home mortgages by the officers, even if they thought such investment would be more beneficial to the corporation, cannot be seen as a decision made with due care. And in terms of the duty of loyalty, because the officers decided expressly to disregard the board's instructions in favor of the riskier, but potentially higher returning, investment in the subprime market, which higher returns would lead to higher personal gains for the officers in terms of bonuses and other forms of performance-based compensation, such actions could not be said to have been made in good faith and for the benefit of the corporation. As a result, in this latter scenario, not only does the board's greater specificity implicate a breach of the duty of obedience, the officers' fiduciary obligation to follow the board's instructions has also resulted in a higher standard of care and loyalty that must be met. This is because in this second situation, a court is not left to infer what the board's preference might have been, as it would have had to do in the first scenario in order to find a breach of fiduciary duty. Rather, the board has made clear its preference and the officers have a fiduciary obligation to obey it.¹⁷⁸

176. See *Citigroup*, 964 A.2d at 122 ("What should be understood . . . is that compliance with a director's duty of care can never appropriately be judicially determined by reference to *the content of the board decision* that leads to a corporate loss, apart from consideration of the good faith or rationality of the process employed.").

177. See *Gagliardi v. TriFoods Int'l, Inc.*, 683 A.2d 1049, 1051 (Del. Ch. 1996) ("The business outcome of an investment project that is unaffected by director self-interest or bad faith, cannot itself be an occasion for directors liability." (footnote omitted)); see also *Citigroup*, 964 A.2d at 130 n.72.

178. See *Atkinson*, *supra* note 138, at 60 ("Either way, as a question of care or of loyalty, the principal's greater specificity implicates the duty of obedience. Once a principal's will is embodied in a specified purpose, the agent must obey it.").

Accordingly, emphasizing the duty of obedience of officers would be a step toward “revitalizing the centrality of directors in corporate governance and making senior officers more accountable.”¹⁷⁹

There are other additional benefits that can be gained from recognizing a duty of obedience as part of an officer’s fiduciary obligations. First, emphasizing officers’ duty of obedience can serve to encourage greater oversight and thoughtfulness in the board’s delegation of its authority to these individuals. “A legitimate criticism of corporate governance for much of the last century was that boards were unduly passive and deferential to the professional managers to whom they delegated authority for the daily operations of the company.”¹⁸⁰ However, emphasis by the courts and lawmakers on an officer’s duty of obedience can function to encourage boards of directors (ideally guided by legal counsel) to be more thoughtful and precise in defining their delegation of authority and responsibilities to officers. In order for the duty of obedience to be effective in regulating the actions of officers, meaningful input from the board in its delegation to officers is required. As the two scenarios described above illustrate, through the duty of obedience, the board of directors may use its authority in delegating to define officers’ responsibilities and authority in ways that, in conjunction with the duty of obedience, usefully limit their discretion. Closely circumscribing the authority and responsibilities of officers can lead to less opportunity for officers to act against the board’s wishes or not in the best interests of the corporation. Boards of directors will not, however, be able to anticipate every instance of officer misconduct such that they could limit an officer’s discretion to prevent such acts. Nor can boards of directors prevent extreme instances of officer malfeasance such as that alleged to have taken place at Enron and WorldCom. Nonetheless, the utility of emphasizing the duty of obedience of officers would still further efforts to make officers more accountable for their actions and boards of directors more conscious in their delegation to, and oversight of, these individuals.

A second benefit of recognizing and emphasizing officers’ duty of obedience is that it would bring state corporate law in line with federal law. While Delaware state law has, until recently, remained silent as to the exact scope and nature of officers’ fiduciary duties, federal law has taken steps to address the role of corporate officers.¹⁸¹ And because “federal law has begun to step into this void, Delaware judges have expressed concern that Delaware must articulate its own theory of officer fiduciary law or risk abdicating the entire field to federal law.”¹⁸² Focusing

179. Johnson & Millon, *supra* note 8, at 1627.

180. ABA Report, *supra* note 126, at 128.

181. See Robert B. Thompson & Hillary A. Sale, *Securities Fraud as Corporate Governance: Reflections Upon Federalism*, 56 VAND. L. REV. 864, 886 (2003) (“State law actually says very little affirmatively about what officers are supposed to do (in contrast to the relatively well-developed roles of directors and shareholders). [Conversely,] Congress expressed its clear intent, through the Sarbanes-Oxley Act, to regulate the conduct of officers, in the context of the duties of care, loyalty, and good faith.”).

182. Jones, *supra* note 33, at 477; see Sale, *supra* note 9, at 459 & n.19 (“[U]nless Delaware wants to cede corporate law and regulation to the federal government, it must act.” (citing E. Norman Veasey, *State-Federal Tension in Corporate Governance and the Professional Responsibilities of Advisors*, 28 J. CORP. L. 441, 443 (2003))).

on enforcing the duty of obedience of officers serves as one way of differentiating the roles, responsibilities, and fiduciary duties of directors and officers that would be consistent with recent efforts by Congress and the SEC. Those efforts include (i) imposing responsibilities on directors in an effort to emphasize board oversight of corporate management and (ii) imposing new legal duties on corporate officers in an effort to increase accountability.¹⁸³ Further, future efforts by Congress and the SEC to place additional and different responsibilities on senior officers and boards of directors “can be seen as supplementing, rather than displacing, existing state-law-based fiduciary duties of officers.”¹⁸⁴

V. CONCLUSION

The actions of corporate officers have received renewed attention in recent years as a result of corporate misconduct at companies such as Enron and Adelphia and the fall of Lehman Brothers and Merrill Lynch during the recent financial crisis. Recognizing that it is the officers, and not the directors, who hold a position of power and control over the business and affairs of a corporation, scholars and policymakers have called for corporate governance reform in an effort to restore the proper balance of power in corporate management. The imposition of fiduciary duties on officers is widely thought to be one way to achieve this better governance. Until recently, however, the issue of an officer’s fiduciary duties had only been addressed by the Delaware courts in passing references and dicta. In early 2009, the Delaware Supreme Court in *Gantler v. Stephens* appeared to resolve this issue by holding that officers of Delaware corporations owe the same fiduciary duties to the corporation and its stockholders as directors. While taking the first step to define the fiduciary obligations of these individuals, the court’s decision has been criticized for failing to address many of the issues still surrounding the duties of officers.

One way to achieve the goal of better corporate governance using fiduciary duties is through agency law’s fiduciary duty of obedience. Emphasizing the fiduciary obligation of officers to obey the board of directors, in addition to the fiduciary duty framework that the *Gantler* court established, would be an effective way to restore directors to a position of authority and control over officers. The duty of obedience would obligate officers to obey the instructions and directions of the board, thus emphasizing the roles of these individuals in corporate management contemplated in corporate statutes and case law. In addition, imposing a duty of obedience would lead to greater accountability both at the board level, in encouraging directors to be more thoughtful and precise in delegating authority and responsibilities to management of the corporation, and at the officer level, in requiring officers to follow the directions of the board. Not only would

183. See Sale, *supra* note 9, at 476; see also Roberta S. Karmel, *Realizing the Dream of William O. Douglas—The Securities and Exchange Commission Takes Charge of Corporate Governance*, 30 DEL. J. CORP. L. 79 (2005).

184. Johnson & Millon, *supra* note 8, at 1603.

recognizing the duty of obedience impose an additional fiduciary obligation on officers that they must comply with, in some situations the duty of obedience would operate also to require a stricter standard of the duties of care and loyalty, thereby making officers more accountable for their actions. Moreover, imposing a duty of obedience on officers would be consistent with recent federal reform efforts to distinguish more clearly the governance responsibilities of officers from those of directors.

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Restoring the Balance of Power in Corporate Management: Enforcing an Officer's Duty of Obedience

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