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Common Law Duties of Non-Director Corporate Officers

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INTRODUCTION

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. This is surprising given the large size of many businesses and the concomitant necessity of delegating managerial responsibilities. Where the issue of officers' liability has been discussed, it is almost invariably in the shadow of directors' conduct. This Article is an effort to distill the law (with particular emphasis on Delaware law) specifically applicable to officers *qua* officers.

Part One briefly defines "officer." Part Two describes the officers' duties to the corporation and to the board of directors. Part Three discusses an officer's duty to inform the board of matters calling for board oversight. Part Four analyzes the application of the business judgment rule to non-director officers.

WHO IS AN OFFICER?

Under Delaware law, *officers* are endowed with their titles and duties from the corporation's bylaws or resolutions of the board of directors.[1] Likewise, those employees and agents whose authority to act for the corporation does not flow directly from the bylaws or the board of directors and whose duties otherwise do not involve such discretion are not endowed

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1. Del. Code Ann. tit. 8, § 142 (1974).

with officer status.[2] Thus, status as an employee or agent is by no means equivalent to status as an officer.[3]

The term "officer" is properly applicable only to those in whom administrative and executive functions have been entrusted,[4] and does not apply to those without judgment or discretion as to corporate matters.[5] Even a director is not ordinarily an officer for the corporation. Accordingly, he or she is not empowered solely by reason of the director status to act alone on behalf of the corporation.[6] An individual expressly designated as an officer by the board of directors should, however, be presumed to be empowered to exercise judgment and discretion as to corporate matters, unless it is shown that the board did not intend to vest such authority.

OFFICERS' DUTIES TO THE CORPORATION AND THE BOARD

GENERAL NATURE OF OFFICERS' DUTIES

For purposes of determining whether fiduciary duties attach, the scope of the term "officer" seems to be a function of responsibilities. A title is not dispositive. For example, a business manager is not necessarily an officer,[7] nor is a vice president for sales necessarily an officer whose ap-

2. *See* Goldman v. Shahmoon, 208 A.2d 492, 493 (Del. Ch. 1965) (*officers* and *agents* are by no means interchangeable terms. "Officers as such are the corporation." An agent is an employee.).

3. *Id.* In *Goldman*, the plaintiff sought to depose the defendant corporation through its comptroller and an alleged managing agent. The plaintiff argued that the comptroller actually performed the functions of a corporate treasurer and that the alleged managing agent was such in light of his charge over the corporation's accounting department. *Id.* at 494. In finding that neither person was an officer, the court noted that neither individual had been shown to possess "general powers to exercise . . . personal judgment and discretion in dealing with the corporate acts complained of." *Id.*; *see also* Cohen v. Miller, 68 A.2d 421, 424 (N.J. Ch. 1949); Hunt v. Stromberg Motor Devices Co., 184 N.W. 459, 461 (Mich. 1921) ("An officer inherently has knowledge, rights and duties not necessarily belonging to a mere employee.").

4. Lethem v. Wilson, 185 A. 642, 643 (Pa. 1936); *see also* Lewis v. LeBaron, 61 Cal. Rptr. 903, 911 (1967) (defendant denied he was corporate officer, but court held he was, noting that "it appears that he executed a recorded deed for the corporation as its secretary," and that "[h]e was certainly [the corporation's] attorney.").

5. Colonial Capital Co. v. General Motors Corp., 29 F.R.D. 514, 517 (D. Conn. 1961) (clerical employee responsible for handling scheduling and shipment of dealers' car orders and for supervision of fleet sales has "no general power to exercise his judgment and discretion in dealing with corporate matters" and thus is not an officer).

6. Jackson v. County Trust Co., 6 A.2d 380, 382 (Md. 1939); Georgia Casualty & Sur. Co. v. Seaboard Sur. Co., 210 F. Supp. 644, 651 (N.D. Ga. 1962); William M. Fletcher, 2 Fletcher Cyc. Corp. § 271 (perm. ed. 1990); 18B Am. Jur. 2d § 1346 (1985).

7. Syracuse Television, Inc. v. Channel 9, Syracuse, Inc., 273 N.Y.S.2d 16, 28 (N.Y. Supr. 1966).

pointment or removal requires board action.[8] Yet officers still have fiduciary duties to the corporation.[9] Many courts and commentators have taken the position that the rights, duties and liabilities of corporate officers and directors vis-a-vis the corporation and its stockholders are coextensive. In many instances, an officer is also a director. In these cases, there may be no need to draw a distinction between the rights, duties, and liabilities of an officer as distinct from those of a director. Perhaps for this reason, there is little case law concerning the obligations to the corporation of an officer *qua* officer.

Nonetheless, most authorities suggest that, as a general proposition, corporate officers owe the corporation the same fiduciary duties as do directors.[10] The fiduciary duties owed by directors to the corporation are well documented[11] and are not within the scope of this Article. One commentator has stated that "with respect to the obligation of officers to their own corporation and its stockholders, there is nothing in any Delaware cases which suggests that the fiduciary duty owed is different in the slightest from that owed by directors."[12] A non-director president owes fiduciary duties, even in a close, family-held corporation.[13] Cases in numerous jurisdictions have held that a corporation's attorney/secretary,[14] vice president,[15] chief operating officer,[16] and president/CEO[17] owe fiduciary duties to the corporation.

The Model Business Corporation Act (MBCA)[18] articulates standards of conduct for corporate officers in a provision separate from, but almost identical to, the provision governing conduct of directors.[19] Section 8.42 provides, in part:

8. Balousek v. Milwaukee Cheese Co., 452 F. Supp. 920, 922 (E.D. Wis. 1978).

9. *Id.*; *Syracuse Television, Inc.*, 273 N.Y.S.2d at 28.

10. *See, e.g.*, William M. Fletcher Cyc. Corp. §§ 838, 846 (perm. ed. 1986); 18B Am. Jur. 2d Corporations § 1689 (1985).

11. *See, e.g.*, David A. Drexler, et al., Delaware Corporation Law and Practice, ¶ 15.02 at 15-2 to 15-5 (perm. ed.); Model Bus. Corp. Act. § 8.30 (3d ed. 1985 & Supp. 1990); Guth v. Loft, Inc., 5 A.2d 503, 510 (Del. 1939); Smith v. Van Gorkum, 488 A.2d 858 (Del. 1985).

12. Drexler, *supra* note 11, ¶ 14.02 at 14-5 to 14-6.

13. *In re* Truco, Inc., 110 B.R. 150, 152 (Bankr. M.D. Pa. 1989) (where non-director president used corporate funds to satisfy personal obligations, "officers and directors stand in a fiduciary relationship to that corporation").

14. Lewis v. LeBaron, 61 Cal. Rptr. 903, 911 (1967) (corporation's attorney/secretary stands in fiduciary relationship both to corporation and its shareholders).

15. Pros v. Mid-America Computer Corp., 491 N.E.2d 851, 856-57 (Ill. Ct. App. 1986) (under Delaware law, vice president, as officer, occupied fiduciary relationship toward corporation).

16. *In re* Black, 787 F.2d 503, 506 (10th Cir. 1986) (under Utah law, corporate officer (chief operating officer) owes fiduciary duty to the corporation and its shareholders).

17. Gregg v. U.S. Indus., Inc., 715 F.2d 1522, 1541 (11th Cir. 1983) (president and CEO's fiduciary obligations to corporation terminate upon being made a mere consultant), *clarified on other grounds*, 721 F.2d 345 (1983), *cert. denied*, 466 U.S. 960 (1984).

18. Model Bus. Corp. Act (3d ed. 1985 & Supp. 1990) [hereinafter MBCA].

19. *Id.* §§ 8.42 (governing officers), 8.30 (governing directors).

> An officer with discretionary authority shall discharge his duties under that authority:
> (1) in good faith;
> (2) with the care an ordinarily prudent person in a like position would exercise under similar circumstances; and
> (3) in a manner he reasonably believes to be in the best interests of the corporation.[20]

Section 8.30 merely substitutes the word director for the words "officer with discretionary authority."[21] The substantial similarity of the duties of officers and directors under these respective provisions supports the view that the legal standard governing their conduct is identical.

SCRUTINY GIVEN TO CONDUCT OF OFFICERS MAY BE MORE STRINGENT THAN THAT GIVEN TO CONDUCT OF DIRECTORS

The official comment to MBCA Section 8.42 suggests that an officer's accessibility to corporate information may subject the officer to a higher standard of scrutiny.[22] Conversely, the standard of scrutiny may be relaxed as the officer's discretion is more closely circumscribed.[23]

The official comment to MBCA Section 8.42 states:

> This section provides that a non-director officer with discretionary authority must meet the same standards of conduct required of directors under section 8.30. But his ability to rely on information, reports, or statements, may, depending upon the circumstances of the particular case, be more limited than in the case of a director in view of the greater obligation he may have to be familiar with the affairs of the corporation. Non-director officers with more limited discretionary authority may be judged by a narrower standard, though every corporate officer or agent owes duties of fidelity, honesty, good faith, and fair dealing to the corporation. The Official Comment to section 8.30 is generally applicable to non-director officers as well as to directors.[24]

The comment states that the duty of loyalty, indicated by the words "fidelity, honesty, good faith, and fair dealing," does not vary with the non-director officer's level of discretion. As to the duty of care, the comment does not necessarily alter the applicable duty of care depending on the amount of discretion or knowledge. Rather, the comment indicates that

20. *Id.* § 8.42.
21. *Id.* § 8.30.
22. *Id.* § 8.42 cmt.
23. *Id.*
24. *Id.* § 8.42 cmt. (citations omitted).

application of the standard of care to facts that demonstrate greater intimacy with corporate affairs may be more likely to result in liability.[25]

It also has been said that the duties of active officers of a corporation who devote all or most of their time to a corporation's business and who receive a salary as officers, are more extensive than those of directors who do not give the corporation daily attendance and who receive little or no salary.[26] This seems to stand for the principle that there should be accountability commensurate with one's actual involvement. Sometimes this approach has resulted in a higher level of liability for non-director officers than for directors.[27]

The Nebraska Supreme Court, in applying a duty to non-director officers that is proportionate to the power of those officers, stated:

> The managerial duty of a corporate officer is of such a degree of legal and practical importance that if he fails to conduct the affairs of his enterprise with the care of a reasonably prudent officer, he becomes liable to his company or its stockholders for negligent mismanagement. His obligation "is increased in the precise degree that his representative character has given him power and control derived from the confidence reposed in him by the stockholders who appointed him their agent."[28]

Therefore, because a president generally is charged with a particularly high degree of corporate familiarity, the resultant liability to the company or its stockholders is more extensive than that of a mere director.[29] The president's duty to avoid (and liability for) losses is measured by the same legal standard as that of a director due to the president's added responsibility and authority.[30] It has been held, however, that "[t]here is an even greater fiduciary duty on one who is both a director and an officer in a company" than that of a non-officer director.[31] While this language implies the application of a higher legal standard, it may simply mean that directors

25. *See id.*

26. William M. Fletcher, 3 Fletcher Cyc. Corp. § 991 (perm. ed. 1986).

27. *See, infra* notes 28-31 and accompanying text.

28. Electronic Dev. Co. v. Robson, 28 N.W.2d 130, 137-38 (Neb. 1947) (quoting Twin-Lick Oil Co. v. Marbury, 91 U.S. 587, 590 (1875)).

29. William M. Fletcher, 3 Fletcher Cyc. Corp. § 1032 (perm. ed. 1986).

30. *Id.*; *see also* Seymour D. Thompson, et al., Commentaries on the Law of Corporations § 1606 (3d ed. 1927) (stating president's responsibility "to be of a higher character than that of directors, who serve without compensation"). In many older cases, the implication is that the difference in compensation between officers and directors affects their relative liabilities. This largely historical distinction aside, knowledge is the stronger basis for the distinction. *See In re* Ozark Restaurant Equip. Co., Inc., 41 B.R. 476, 480 (Bankr. W.D. Ark. 1984).

31. *In re* Ozark Restaurant Equip. Co., Inc., 41 B.R. 476, 480 (Bankr. W.D. Ark. 1984); *see also* Leppaluoto v. Eggleston, 357 P.2d 725, 731 (Wash. 1960) (directors and officers have the same fiduciary duties).

with the same level of knowledge as officers must do more to satisfy their duties than the non-officer directors.

The United States Supreme Court addressed the greater liability of officers who have an active role in the management of the corporation in *Bates v. Dresser.*[32] In *Bates*, a former president and a number of directors were charged with the loss of the corporation's assets through thefts by an employee while they were in control. The Court held that the president owed a different duty to the corporation than that which the directors owed. Whereas the directors were not bound to examine the bank's books and ledger, the president had the deposit ledger in his hands daily and therefore had sufficient notice to prevent the fraud.[33] As a result, the Court determined that only the president was liable to the corporation. The Court seemed to rely on the factual distinction between the defendants' intimacy with the corporation, rather than a different legal standard.[34]

Summing up these authorities, a comment to section 4.01 of the proposed Principles of Corporate Governance of the American Law Institute noted that "it is relatively well settled that officers will be held to the same duty of care and business judgment standards as directors."[35] The comment cautioned, however, that:

> When it comes to application of these formulations, of course, full-time officers will generally be expected to be more familiar with the affairs of a corporation than outside directors. Officers will be expected to be more familiar with business affairs under their direct supervision than officers who do not have such responsibility.[36]

DUTY OF LOYALTY

Officers, like directors, owe a duty of loyalty to the corporation and its stockholders. This duty does not arise solely by virtue of director or officer status; it is a duty owed under general principles of agency law.[37] The duty of loyalty is of general applicability, but most frequently affects officers in the areas of corporate opportunity, competition with the corporation/employer, and use of corporate trade secrets.

One aspect of an officer's fiduciary duty of loyalty is the duty not to usurp an opportunity that is rightfully the corporation's. Thus, an officer must refrain from buying for himself that which he was instructed to buy

32. 251 U.S. 524 (1919).
33. *Bates*, 251 U.S. at 530-31.
34. *See id.*
35. American Law Institute, Principles of Corporate Governance: Analysis and Recommendations (Proposed Final Draft, March 31, 1992) at 183.
36. *Id.*
37. Restatement (Second) of Agency § 387-98 (1958).

on behalf of the corporation.[38] The corporate opportunity doctrine extends this principle to usurpation of corporate business opportunities even where the officer has not been instructed to acquire the opportunity for the corporation. In *Guth v. Loft, Inc.*,[39] the seminal corporate opportunity case in Delaware, the Supreme Court of Delaware used far-reaching language regarding the fiduciary duties of officers and directors to the corporation. In *Guth*, the corporation sought to impress a trust upon all shares of Pepsi stock registered in the name of Guth and a company he controlled. Guth, as president and dominant director of Loft, Inc., was found in a derivative suit to have usurped for himself the opportunity to secure a substantial stock interest in Pepsi.

The court, in discussing the duties of both directors and officers, stated:

> Corporate officers and directors are not permitted to use their position of trust and confidence to further their private interests. While technically not trustees, they stand in a fiduciary relation to the corporation and its stockholders. A public policy . . . has established a rule that demands of a corporate officer or director . . . the most scrupulous observance of his duty, not only affirmatively to protect the interests of the corporation committed to his charge, but also to refrain from doing anything that would work injury to the corporation, or to deprive it of a profit or advantage which his skill and ability might properly bring to it. . . . The rule that requires an undivided and unselfish loyalty to the corporation demands that there shall be no conflict between duty and self interest.[40]

The court characterized this corporate opportunity rule as "merely one of the manifestations of the general rule that demands of an officer or director the utmost good faith in his relation to the corporation which he represents."[41]

The impact of *Guth's* broad language is ameliorated by placing the case in its factual context. First, one of the remedies sought by the corporation was the imposition of a trust. In order to impose the trust, the court had to conclude that Guth, while "technically" not a trustee, stood in a fiduciary position. Second, Guth was not just any officer. He was the president and dominant director of Loft. He exercised such a high level of

38. Onslow Wholesale Plumbing & Elec. Supply Inc. v. Fisher, 298 S.E.2d 718, 720 (N.C. 1982), *aff'd*, 302 S.E.2d 632 (N.C. 1983) (defendant, acting as general manager, breached his contractual obligations to follow orders, advice and direction of board, and breached his fiduciary duty to discharge his duties in good faith, when he disobeyed directive from president and chairman of board to purchase stock for the corporation and instead purchased the stock for himself).

39. 5 A.2d 503 (Del. 1939).

40. *Guth*, 5 A.2d at 510.

41. *Id.*

control that the court concluded that Guth was Loft's "master" and that Guth "manifested some of the qualities of a dictator."[42]

An officer's position is not, however, the determining factor in corporate opportunity matters. An officer's duty under the corporate opportunity doctrine does not seem to arise from a duty as an officer *qua* officer but from the general laws of agency which apply to all corporate employees. An example of this is *Science Accessories Corp. v. Summagraphics Corp.*,[43] where the defendants were neither officers nor directors, but were "key employees."[44] The court, following *Guth*, stated that "the doctrine of corporate opportunity is but an application of agency fiduciary law in a particular corporate fact setting."[45]

A fundamental tenet of agency law is that the extent of the agent's duties to the principal is generally determined by the parties' agreement.[46] Corporate law may parallel agency law in this respect, insofar as directors and officers may by contract or charter provision limit or define what conduct the corporate opportunity doctrine will or will not reach.[47] Courts, however, tend to apply duty of loyalty concepts more rigidly to officers than to mere agents. This propensity, when combined with directors' limited ability to alter by contract their liability in the duty of loyalty context and the courts' frequent uniform treatment of directors and officers,[48] demonstrates that a corporate officer may have less leeway than an agent to escape (by agreement) the ordinary strictures of the duty of loyalty.

The duty of loyalty may apply more rigidly to officers than mere employees and agents in situations where officers compete with the corporation. In *Franklin Music Co. v. American Broadcasting Companies, Inc.*,[49] Franklin, the president of Franklin Music Company (FMC), had an employment contract with FMC which contained a covenant not to compete with FMC. The court found that Franklin breached his fiduciary duty to the company by meeting and negotiating, while president of FMC, with a competitor of FMC for future employment and failing to perform certain

42. *Id.* at 512; *see also* Gottlieb v. McKee, 107 A.2d 240 (Del. Ch. 1954) (holding that the text of whether business opportunity comes to corporate officer or director as an individual is whether there is a duty to act in that matter as the corporation's representative).

43. 425 A.2d 957 (Del. 1980).

44. *Science Accessories Corp.*, 425 A.2d at 960-61 & n.5.

45. *Id.* at 964.

46. Restatement (Second) Agency § 376 (1958).

47. *Cf. In re* Tri-Star Pictures Shareholder Litig., Del. Ch., C.A. No. 9477, slip op. at 19-23 (May 5, 1989, revised May 30, 1989) (noting that a charter provision governing the treatment of corporate opportunities might be invalid to the extent it purported to eliminate director liability for breach of the duty of loyalty, in contravention of Del. Code Ann. tit. 8, § 102(b)(7) (1991), but indicating that the provision, which attempted to prescribe a formula for allocating corporate opportunities among the corporation and certain stockholders, might otherwise be valid).

48. *See supra* notes 12-19; *see also infra* notes 50-65 and accompanying text.

49. 616 F.2d 528 (3d Cir. 1980).

business functions at FMC. There also was evidence that Franklin, while he was president of FMC, was discussing the possibility of hiring away other key FMC employees.

The United States Court of Appeals for the Third Circuit concluded that the trial court correctly instructed the jury that "as an officer and director of FMC, Franklin was bound by the strictest duties of honesty and individual loyalty, and could not engage in business conduct detrimental to FMC's best interests."[50] In addition, the court found no fault with the trial court's instruction that the jury could not find a breach of fiduciary duty solely because Franklin sought new employment and failed to disclose that fact to his employer. Rather, the court stated that, for there to be a breach of duty, the jury must find some specific disloyalty or betrayal of FMC's interests during the time when Franklin was president.[51] The court concluded that there was sufficient evidence to support the jury's finding that Franklin breached his fiduciary duty even though he had not breached the covenant not to compete.[52] Thus, *Franklin Music Co.* stands for the proposition that an officer's fiduciary duties may be more strict than those duties imposed by the officer's employment agreement.[53]

Similarly, the Delaware Court of Chancery held in *Craig v. Graphic Arts Studio, Inc.*[54] that "Delaware has adopted the view that a corporate officer or director is entirely free to engage in an independent competitive business, so long as he violates no legal or moral duty with respect to the fiduciary relation that exists between the corporation and himself."[55] The quoted proviso, however, is a significant qualification to the words "entirely free to engage in an independent competitive business." In *Craig*, Ralph N. Craig, the president of Graphic, Inc., acquired 50% ownership of Reproduction Center, Inc., a newly formed competing business in a highly limited market, for his own personal gain without first presenting the opportunity to Graphic. In these circumstances the court, in finding Craig breached his fiduciary duty, stated:

50. *Franklin Music Co.*, 616 F.2d at 533.

51. *Id.*

52. *Id.* The facts as recited in *Franklin Music Co.* strongly supported liability, and facilitated a finding of breach of fiduciary duty. The court found that Franklin was motivated by personal hostility, that he reduced his attention to FMC at a critical time, and that he timed his departure so as to cause the corporation the maximum financial distress. *Id.* at 532-33.

53. In a case challenging officers' competition similar to *Franklin Music Co.*, the Minnesota Court of Appeals indicated that the officers had a "higher duty" than mere employees. Blackburn, Nickels & Smith, Inc. v. Erickson, 366 N.W.2d 640, 645 (Minn. Ct. App. 1985); *see also* Maryland Metals Inc. v. Metzner, 382 A.2d 564, 568 (Md. 1978) (corporate officer or other high-echelon employee is barred from actively competing with his employer during tenure of employment, even in the absence of a covenant so providing).

54. 166 A.2d 444 (Del. Ch. 1960).

55. *Craig*, 166 A.2d at 445.

> The only reasonable inference that can be drawn is that the growth of Reproduction [Center, Inc.] had to be in part at the expense of Graphic's business. It is contrary to human nature to suppose that [Craig], while continuing to run Graphic's business with knowledge that in time he was leaving and going with 'his' own company, would be diligent in seeking to further the business of Graphic. While he was a small shareholder in Graphic and Graphic Arts it is clear that his real interest was in the future of Reproduction. Thus, there was a real conflict between Graphic's interest and plaintiff's interest up until the date of his discharge.[56]

Officers also have duties to refrain from abusing corporate trade secrets and inside information.[57] A full treatment of employee rights and duties in respect of corporate proprietary information and intellectual property in general, or insider securities trading in particular, is well beyond the scope of this article. The following discussion illustrates, however, the application to corporate officers of principles generally applicable to employees and to employees with management authority.

With respect to trade secrets and patents, one's position in the management hierarchy is a factor in determining whether there is a duty owed. For example, in *B.F. Goodrich Co. v. Wohlgemuth*,[58] the court enjoined a former department manager/top executive—albeit not an officer—from disclosing trade secrets to Goodrich's competitor. The defendant possessed trade secrets of Goodrich, and the court found that "any revelation of them to a Goodrich competitor is in equity a breach of faith and reprehensible to a court of equity."[59] In *Fairchild Engine & Airplane Corp. v. Cox*,[60] the defendant threatened to disclose trade secrets to a competitor. The court, stressing the defendant's position as an officer and director and his concomitant duty of fidelity, held that the defendant had a duty not to disclose trade secrets.[61] As one commentator has stated, any employee who flagrantly misuses confidential information may be liable in trade secret cases, but as the employee's status approaches the executive level, a standard of simple unethical activity or lack of good faith imperceptibly replaces a court's reliance on more extreme misconduct.[62]

Common law duties in the "insider trading" context arise by virtue of access to information, not officer status. In *Brophy v. Cities Service Co.*,[63]

56. *Id.* at 446.
57. *See infra* notes 58-65 and accompying text.
58. 192 N.E.2d 99 (Ohio Ct. App. 1963).
59. *B.F. Goodrich Co.*, 192 N.E.2d at 104.
60. 50 N.Y.S.2d 643 (N.Y. 1944).
61. *Fairchild Engine*, 50 N.Y.S.2d at 655-56.
62. Leslie W. Jacobs, *Business Ethics and the Law: Obligations of a Corporate Executive*, 28 Bus. Law. 1063, 1069 (1973).
63. 70 A.2d 5 (Del. Ch. 1949).

the court illustrated common law "insider trading" principles as they apply to officers and directors as follows:

> [I]n the absence of special circumstances, corporate officers and directors may purchase and sell its capital stock at will, without any liability to the corporation. Ordinarily, an employee has the same rights. But if for some reason the corporation secretly intends to purchase large blocks of its capital stock in the market, and an employee acquires that knowledge in the course of his employment, the application of general [fiduciary] principles would seem to require the conclusion that he cannot use that information for his own personal gain.[64]

Thus, the distinction between officer and employee is not relevant in these circumstances *per se*; rather, the duty of loyalty arises when any employee obtains the non-public information. Indeed, courts have been more inclined to find that officers, as distinct from mere employees, acquire non-public corporate information by virtue of their greater access to a presumably wider range of corporate activities.[65]

DUTY OF CARE

As with cases involving directors, there are few cases involving claims of breach by an officer of the duty of care. The few existing cases hold that officers, like directors, owe the corporation and its stockholders a duty to exercise due care parallel to the duty owed by directors.[66] As with the duty of loyalty, this duty of care has a counterpart in the general law of agency, under which an agent, "unless otherwise agreed . . . [must] act with standard care and with the skill which is standard in the locality for

64. *Brophy*, 70 A.2d at 8; *see also* Diamond v. Oreamuno, 248 N.E.2d 910 (N.Y. 1969) (A person who acquires special knowledge or information by virtue of a confidential or fiduciary relationship with another is not free to exploit that knowledge or information for his or her own personal benefit but must account to his or her principal for any profits derived therefrom.).

65. This inclination underlies the "group pleading presumption" adopted by some courts in securities fraud cases. *See, e.g.*, Wool v. Tandem Computers, Inc., 818 F.2d 1433, 1440 (9th Cir. 1987). Although it does not encompass every officer of a corporation with far-flung offices and divisions, the group pleading presumption dispenses with particularized pleading of knowing participation in corporate disclosure failure as to officers and executives involved in the day-to-day management of those parts of the corporation involved in the fraud. *Id.* The underlying assumption is that "officers involved in the day-to-day management of a corporation must be aware of the internal operations of a corporation." Xoma Corp. Secr. Litig., [1991-1992 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,491, at 92,160 (N.D. Cal. 1991); *see also* Smith v. Network Equip. Technologies, Inc., [1990-1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 95,659 (N.D. Cal. 1990).

66. *See* Bates v. Dresser, 251 U.S. 524 (1919); *see also* MBCA, *supra* note 18, § 8.42; Electronic Dev. Co. v. Robson, 28 N.W.2d 130, 137 (Neb. 1947); William M. Fletcher, 3A Fletcher Cyc. Corp. § 1032 (perm. ed. 1986).

the kind of which he is employed to perform and, in addition, exercise any special skill he has."[67]

In *Keck Enterprises, Inc. v. Braunschweiger,*[68] the court held that the same duty of care required of a corporate president applied to officers.[69] Referring to a defendant who was neither a director nor a majority shareholder, the court stated that "[i]t was Braunschweiger's duty as president of the corporation to exercise such care, skill and diligence in transacting the corporate business as might be expected in his own affairs."[70] One court—perhaps driven by a broadly worded statute—propounded a high level of duty of care, holding that "[a]ny action by a corporate officer which diminishes the value of that asset would be a breach of fiduciary duty for which the officer should be held liable."[71] There is nearly strict liability, moreover, where dishonesty exists. An officer's knowledge and acquiescence in another's dishonest activities to the detriment of the corporation constitutes, as a matter of law, a breach of his fiduciary duty to the corporation.[72]

DUTY TO INFORM THE BOARD

While there is no Delaware case specifically stating that a senior officer has a duty to inform the corporation's board of directors, such a duty can be inferred from the statutory requirement that the corporation be managed by or under the direction of the board of directors[73] and that a director "shall, in the performance of his duties, be fully protected in relying in good faith . . . upon such information, opinions, reports or statements presented to the corporation by any of the corporation's officers."[74] Indeed, in a large public corporation, a board of directors could not function without the information provided to it by senior officers.

67. Restatement (Second) of Agency § 379(1) (1958); *see* Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985) ("Representation of the financial interests of others imposes on a director an affirmative duty to protect those interests and to proceed with a critical eye in assessing information. . . .").

68. 108 F. Supp. 925 (S.D. Cal. 1952).

69. *Keck Enters., Inc.*, 108 F. Supp. at 927.

70. *Id.*

71. Fausett v. American Resources Management Corp., 542 F. Supp. 1234, 1241 (D. Utah 1982); *see also* Westland Capitol Corp. v. Lucht Eng'g Inc., 308 N.W.2d 709, 715 (Minn. 1981) (under statute imposing fiduciary duty upon officers, a president/director sued in his capacity as president was liable because he caused the corporation to breach a loan agreement and thereby lose money).

72. Wooddale, Inc. v. Fidelity & Deposit Co. of Maryland, 378 F.2d 627, 634 (8th Cir. 1967).

73. *See* Del. Code Ann. tit. 8, § 141(a) (1974).

74. *Id.* § 141(c).

Under agency principles, an agent has a duty to inform its principal of material matters relevant to the agency.[75] In *Science Accessories Corp. v. Summagraphics Corp.*,[76] the Delaware Supreme Court held corporate key employees to such a standard. The court stated that an "agent [has] a duty to disclose information relevant to the affairs of the agency entrusted to him" and that "[t]hese principles of limitation of agency law carry over into the field of corporate employment so as to apply not only to officers and directors but also to key employees."[77]

An officer has a duty to disclose to the board of directors fraud or wrongdoing of which the officer has knowledge. In *Bennett v. Propp*,[78] the Delaware Supreme Court imposed liability on an officer for failing to inform a board of a material problem within the board's decision-making purview. There, Sadacca, the chief executive officer of Noma Lites, Inc., was found to have breached his fiduciary duty by acting on his own to cause the corporation to repurchase a large block of Noma stock for the purpose of maintaining himself and the other directors in office.[79] The non-officer directors who ratified the purchase transaction after the fact were exonerated on the ground that they had been confronted with a *fait accompli*.[80] On the other hand, the court did not exonerate Ward, the president of Noma:

> Ward's prior knowledge of these purchases is sufficient to deprive him of the benefit of the exception. He was the president of the corporation. He had enough time before the following Monday to consult with his fellow officers and directors, to consult counsel, and to take steps to make some arrangements with the brokers beneficial to Noma. As president, he could surely have called a directors' meeting. He did nothing. Apparently he did not even inquire of Sadacca how many shares Sadacca had bought, how much had been paid for them, or how Sadacca expected to finance the purchases. One gets the impression from the record that he was entirely subservient to Sadacca.
>
> We think that his knowledge of the purchases, his silence and failure to act, coupled with his vote on the resolution, constituted a course of conduct amounting to approval of and participation in Sadacca's

75. The Restatement (Second) of Agency states:

> § 381 Duty to Give Information
> Unless otherwise agreed, an agent is subject to a duty to use reasonable efforts to give his principal information which is relevant to affairs entrusted to him and which, as the agent has notice, the principal would desire to have and which can be communicated without violating a superior duty to a third person.

76. 425 A.2d 957 (Del. 1980).
77. *Science Accessories Corp.*, 425 A.2d at 962.
78. 187 A.2d 405 (Del. 1962).
79. *Bennett*, 187 A.2d at 411.
80. *Id.* at 411-12.

> wrongful acts. This is not to hold Ward guilty of negligence as counsel seem to think the Vice Chancellor did. It is to hold that his actions made him jointly and severally liable with Sadacca for the tort of using corporate funds to maintain control.[81]

From this language, it is clear that at least one important factor in the court's decision to hold Ward liable for Sadacca's unauthorized acts was his failure promptly to call a meeting of directors to permit the board to take appropriate action. Similarly, in *Globe Woolen Co. v. Utica Gas & Electric Co.*,[82] the court stated:

> The trustee is free to stand aloof, while others act, if all is equitable and fair. He cannot rid himself of the duty to warn and to denounce, if there is improvidence or oppression, either apparent on the surface, or lurking beneath the surface, but visible to his practiced eye.[83]

Some authorities suggest there is a duty to inform directors of situations calling for oversight attention, even where the behavior is not dishonest or inequitable. In *First National Bank of Tucker v. Hall*,[84] a breach of duty suit against a bank officer, the Court of Appeals of Georgia held that "contrary to her responsibilities as an officer, [she] failed to inform the members of the board of directors of . . . actions by other officers which she knew or should have known were contrary to bank policies or in its best interest."[85] The officer would thus have a duty to inform the board of actions by other officers that a reasonable officer would believe were not in a corporation's best interest.

Finally, liability for failure to disclose fraudulent activity to the board does not require personal benefit on the part of the non-disclosing officer. As Professor Ballantine states in his treatise on corporation law:[86]

> A director of a corporation cannot remain silent, when he knows that a fraud is being attempted against the corporation and ultimately against its shareholders. It is his duty to acquaint the other officers of the corporation with the facts and to use every effort to prevent the consummation of the fraud. If he permits by passive acquiescence any part of the assets of the corporation to be fraudulently diverted

81. *Id.* at 411; *see also* Smith v. Van Gorkom, 488 A.2d 858, 898-99 (Del. 1985) (Delaware Supreme Court invited consideration of whether outside directors not involved in planning or negotiation of a merger should be exonerated by reason of director-officers' failure to fully involve them in the process in a timely manner).

82. 121 N.E. 378, 380 (N.Y. 1918).

83. *Globe Woolen Co.*, 121 N.E. at 380; *see also* Wooddale, Inc. v. Fidelity & Deposit Co. of Maryland, 378 F.2d 627, 634 (8th Cir. 1967). ("Knowledge and acquiescence by an officer in his or another's dishonest activities in any other capacity to the detriment of the corporation constitutes, as a matter of law, a breach of his fiduciary duty to the corporation.").

84. 238 S.E.2d 284 (Ga. Ct. App. 1977).

85. *Hall*, 238 S.E.2d at 284.

86. Henry W. Ballantine, Ballantine on Corporations § 78 (rev. ed. 1946).

> or secret profits to be obtained he is guilty of a neglect of duty to the corporation for which he is liable in damages, notwithstanding the fact that he did not profit financially thereby.[87]

Delaware's adoption in 1986 of its director liability protection statute[88] provides a positive incentive for a director who is also an officer to inform the board of material matters and have important decisions approved by the board. The statute permits a corporation to include in its certificate of incorporation a provision eliminating or limiting the personal liability of *directors* to the corporation or its stockholders for, *inter alia*, breaches of the duty of care.[89] No such protection is provided to officers.[90] Thus, a director who is also an officer arguably will be protected from such liability if an action is authorized by the board, but will not be protected if the director acts alone in his or her capacity as an officer to take the same action.

APPLICABILITY OF THE BUSINESS JUDGMENT RULE

The business judgment rule (the Rule), a well-known legal doctrine, has long afforded corporate directors, and the actions they approve, substantial protection from close judicial scrutiny. While the Rule has been articulated in various ways, the Delaware Supreme Court has concisely described it as "a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the corporation."[91] The court recognized that, under the Rule, "[a]bsent an abuse of discretion, that judgment will be respected by the courts."[92] Under Delaware law, only conduct susceptible to characterization as "gross negligence," as distinct from conduct involving only ordinary lack of care, may be a basis for holding directors personally liable for the consequences of their decisions.[93]

The Rule has been applied primarily in the context of director conduct. Myriad authorities apply the Rule where the defendants are both officers and directors—and most of these cases state that the Rule applies to de-

87. *Id.* at 202.
88. Del. Code Ann. tit. 8, § 102(b)(7) (1974).
89. *Id.*
90. *Id.* In six states, however, the statutes comparable to § 102(b)(7) include officers: Louisiana, La. Rev. Stat. Ann. § 12:24(c)(4) (1969); Maryland, Md. Code Ann. Corps. & Ass'ns § 2-405.2(a) (1985); Nevada, Nev. Rev. Stat. § 78.037(1) (1991); New Hampshire, N.H. Rev. Stat. Ann. § 293-A:54(I) (1987); New Jersey, N.J. Rev. Stat. § 14A:2-7(3) (1969); and Virginia, Va. Code Ann. § 13.1-692.1 (Michie 1989). *See generally* James J. Hanks, Jr., *Evaluating Recent State Legislation on Director and Officer Liability Limitation and Indemnification*, 43 Bus. Law. 1207 (1988).
91. Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984).
92. *Id.*
93. *See id.*

cisions of "officers and/or directors." Few cases, however, show the extent of the Rule's applicability to decisions of non-director officers.

The history of the Rule has been well-discussed elsewhere.[94] The rationales for the Rule, as stated by one commentator, are:

1. to "encourage competent individuals to assume directorships,"
2. to "provide directors the broad discretion they need" in formulating company policy,
3. to "keep courts from undertaking corporate decision-making," and
4. to "ensure that the directors rather than shareholders run the corporation.[95]

In short, the Rule is designed to give wide latitude to the Board in its handling of corporate affairs.[96] If the Rule does not apply, a particular transaction will be scrutinized in a breach of fiduciary duty suit to determine the fairness of the action to the shareholders.[97] The Rule "is primarily a tool of judicial review and only indirectly a standard of conduct for corporate management."[98]

In light of the extensive delegation of managerial authority by boards of directors,[99] the rationales for the Rule, although typically phrased with reference to directors, should also apply to officers to whom the board's discretionary authority is delegated, at least where the officer is discharging such authority. Nevertheless, two fairly recent cases demonstrate that this view is not universally accepted.

With little or no analysis, and in complete disregard of contrary authority, a federal court in Pennsylvania in *Platt v. Richardson*,[100] purporting to apply Delaware law, ruled flatly that "[t]he business judgment rule applies only to directors of a corporation and not to officers."[101] Perhaps even more notable in this regard is the California case of *Gaillard v. Natomas Co.*[102] *Gaillard* was a suit against both inside and outside directors alleging breach of fiduciary duty in the creation of "golden parachute" benefits. The defendants raised the Rule as a defense. The court applied the Rule to the outside directors, who were not officers, but held that the inside directors were not entitled to the Rule's presumption. The court,

94. *See, e.g.*, Dennis J. Block, et al., The Business Judgment Rule: Fiduciary Duties of Corporate Directors 4-8 (3d ed. 1989).

95. *Id.*

96. *See* Cramer v. General Tel. & Elec. Corp., 582 F.2d 259, 274 (3d Cir. 1978).

97. *See* Smith v. Van Gorkom, 488 A.2d 858, 893 (Del. 1985); Shamrock Holdings, Inc. v. Polaroid Corp., 559 A.2d 257, 271 (Del. Ch. 1989).

98. Moran v. Household Int'l, Inc., 490 A.2d 1059, 1076 (Del. Ch. 1985), *aff'd*, 500 A.2d 1346 (Del. 1985).

99. *See infra* notes 117-19 and accompanying text.

100. [1989-1990 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 94,786 (M.D. Pa. 1989).

101. *Pratt*, [1989-1990 Transfer Binder] Fed. Sec. L. Rep. (CCH) at 94,231.

102. 256 Cal. Rptr. 702 (Cal. App. 1st Dist. 1989).

in denying the Rule's protection based upon the capacity in which the inside directors acted, analyzed the California statute governing the duties of directors,[103] and stated:

> In securing the payment of these benefits to themselves, they were not "perform[ing] the duties of the director" as specified in [California Corporations Code] § 309, but were acting as officer employees of the corporation. The judicial deference afforded under the Rule, therefore, should not apply. As stated by Marsh in his discussion of § 309, "[section 309(a)] does not relate to officers of the corporation, but only to directors. . . . [A]n officer-director might be liable for a particular conduct because of his capacity as an officer, whereas the other directors would not."[104]

The inside directors did not vote on the golden parachute provisions; rather, their role had been to create and present the compensation agreement proposals to the board. Compensation agreements were included in a tentative merger agreement proposed by the defendant officers to the compensation committee of outside directors. In holding that these officers were not entitled to the presumption of the Rule in connection with merger negotiations, it is likely that the court relied primarily on the fact that the defendants were acting as officers, rather than voting as directors.

103. Cal. Corp. Code § 309 (West 1990). Section 309 provides as follows:

> (a) A director shall perform the duties of a director, including duties as a member of any committee of the board upon which the director may serve, in good faith, in a manner such director believes to be in the best interests of the corporation and its shareholders and with such care, including reasonable inquiry, as an ordinarily prudent person in a like position would use under similar circumstances.
> (b) In performing the duties of a director, a director shall be entitled to rely on information, opinions, reports or statements, including financial statements and other financial data, in each case prepared or presented by any of the following:
> (1) One or more officers or employees of the corporation to whom the director believes to be reliable and competent in the matters presented.
> (2) Counsel, independent accountants or other persons as to matters which the director believes to be within such person's professional or expert competence.
> (3) A committee of the board upon which the director does not serve, as to matters within its designated authority, which committee the director believes to merit confidence, so long as, in any such case, the director acts in good faith, after reasonable inquiry when the need therefor is indicated by the circumstances and without knowledge that would cause such reliance to be unwarranted.
> (c) A person who performs the duties of a director in accordance with subdivisions (a) and (b) shall have no liability based upon any alleged failure to discharge the person's obligations as a director.

Id.

104. *Gaillard*, 256 Cal. Rptr. at 711.

California's codified standard of care for directors does not include officers.[105] Thus, the standard of care for officers is left to the courts. The *Gaillard* court held that the non-inclusion of officers in the codification of the Rule precluded courts' application of the Rule to officers, as if the Rule's codification constituted its exclusive source.[106]

Authorities in other jurisdictions, however, convincingly support application of the Rule to actions taken by corporate officers within their delegated discretionary authority. Delaware law is somewhat underdeveloped in this regard, but a number of cases suggest that decisions of officers should be governed by the Rule. Vice Chancellor Hartnett, of the Delaware Court of Chancery, in a string of four opinions between 1980 and 1983, used the following identical language, even though in none of the cases was an officer *qua* officer a defendant: "The business judgment rule is a presumption that a rational business decision of the officers or directors of a corporation is proper unless there exists facts which remove the decision from the protection of the rule."[107] The fact that none of these cases involved decisions where a non-director officer was a defendant, as well as the verbatim repetition of the language used in *Schreiber v. Pennzoil Co.*,[108] suggests that Vice Chancellor Hartnett's unambiguous language may be mere *dicta*.

A more precise discussion of the Delaware law is found in *Kaplan v. Centex Corp.*,[109] in which the court stated:

> [T]he decision of executive officers may also come within the [business judgment] Rule. It probably does here, in the absence of any divided loyalty and in the light of subsequent ratification by the board of directors. But in view of the state of affairs and the conflicts in the

105. The California Committee on Corporate Laws concluded that:

> [I]t was not appropriate in connection with a revision of Section 35 to deal with those officers who were not also directors of the corporation. Although a non-director officer may have a duty of care similar to that of a director as set forth in Section 35, his ability to rely on factual information, reports or statements may, depending upon the circumstances of the particular case, be more limited than in the case of a director in view of the greater obligation he may have to be familiar with the affairs of the corporation.

Cal. Corp. Code § 309 cmt. (West 1990) (quoting Report of Committee on Corporate Laws, *Changes in the Model Bus. Corp. Act*, 29 Bus. Law. 947, 953 (1974)). The current MBCA codifies standards of conduct for both officers and directors, in separate but nearly identical provisions. *See supra* text accompanying notes 24-25.

106. *Gaillard*, 256 Cal. Rpt. at 710-11.

107. Schreiber v. Pennzoil Co., 419 A.2d 952, 956 (Del. Ch. 1980); Haber v. Bell, 465 A.2d 353, 357 (Del. Ch. 1983); Lewis v. Aronson, 466 A.2d 375, 381 (Del. Ch. 1983), *rev'd on other grounds*, 473 A.2d 805 (Del. 1984) (demand futility); Pogostin v. Rice, No. 6235 (Del. Ch. August 12, 1983), *aff'd*, 480 A.2d 619 (Del. 1984).

108. 419 A.2d 952 (Del. Ch. 1980).

109. 284 A.2d 119 (Del. Ch. 1971).

> record, I prefer to base my conclusions on findings from the record, and not on the broad cutting edge of the Rule.[110]

If the applicability of the Rule to officers was on the "cutting edge" in 1971, the blade may be just as sharp now after twenty years of non-use. As the *Gaillard* and *Platt* cases reflect, the issue still surfaces.

In *Kelly v. Bell*,[111] the case upon which the *Kaplan* court relied to conclude that the Rule may apply to decisions of officers, shareholders of U.S. Steel brought a derivative action against all directors of the corporation. In order to assist the passage of a bill in the Pennsylvania General Assembly eliminating the power of local authorities to tax the value of machinery in real property assessments, U.S. Steel and five other companies made similar commitments to the local county board of commissioners. U.S. Steel's commitment, contained in a letter from U.S. Steel's executive vice president, stated that the corporation would continue to pay tax on existing machinery but not on any new machinery installed subsequently. The commitment by U.S. Steel was considered and approved by six officers, three of whom were also directors. Board approval for the commitment was not sought, however, and most of the directors were unaware of the commitment until after suit was filed. While all the directors were named as defendants, none of the non-director officers were, although all were involved in the payments. The court stated:

> At first blush it may seem surprising that approval of the commitment and the payments was not up to the Board. But, in my judgment, absence of such a request points up Steel's vast operations, not the carelessness or indifference of its management. . . . In short I am persuaded that the magnitude of Steel's operations requires substantial delegation. And that is as permissible in law as it is necessary in fact. . . . I cannot find from the record that the non-participating directors either knew of the commitment or that they should have known about it. And I cannot say that the broad managerial delegation adopted by Steel as a business judgment is wrong as a matter of law because it permitted management to do what was done here.[112]

Thus, the court concluded that the defendant directors were "not precluded from relying on the business judgment rule."[113] Narrowly read, *Kelly* stands for the proposition that U.S. Steel's board was permitted to rely on the business judgment rule for a non-board decision as part of the board's legitimate delegation of authority. The problem with this analysis

110. *Kaplan*, 284 A.2d at 124-25 (citation omitted).
111. 254 A.2d 62 (Del. Ch. 1969), *aff'd*, 266 A.2d 878 (Del. 1970).
112. *Kelly*, 254 A.2d at 72 (citation omitted).
113. *Id.*

is that there was no affirmative delegation. One commentator has stated that, because of the Board's failure to act, *Kelly* did not involve the Rule.[114]

Insofar as *Kelly* involved directors, that comment appears well taken. On appeal, however, the Delaware Supreme Court seemed to go a bit further, suggesting that the business judgment rule may apply to the decision of the officers, not just the delegation decision by the board.[115] The court stated: "The directors or officers were not necessarily liable to the corporation because they honored the commitment, provided they exercised honest business judgment in doing so" and "these acts are governed by the 'business judgment' rule."[116]

The *Kelly* opinions suggest that the policies relating to delegation may also suggest the possible application of the business judgment rule to officers. In Delaware, the decision to delegate is itself protected by the Rule. In *Rosenblatt v. Getty Oil Co.*,[117] the Delaware Supreme Court followed the lower court's holding in *Kelly* that the Rule protected the U.S. Steel board's decision to delegate responsibility[118] and concluded:

> An informed decision to delegate a task is as much an exercise of business judgment as any other. The realities of modern corporate life are such that directors cannot be expected to manage the day-to-day activities of a company. This is recognized by the provisions of 8 Del. C. § 141(a) that the business and affairs of a Delaware corporation are managed "by or under the direction" of its board. In setting its agenda as to the matters in which it will be directly involved, and those it will delegate, a board's decisions . . . are entitled to equal consideration as exercises of business judgment.[119]

While there are no cases directly on point, the concept of an officer as the repository of delegated management authority by the board suggests that the availability of a business judgment rule defense may only be available to a corporate officer when that officer is operating within the scope of the delegated authority. Accordingly, a corporate vice president charged

114. S. Samuel Arsht, *Fiduciary Responsibilities of Directors, Officers and Key Employees*, 4 Del. J. Corp. L. 652, 659 n.23 (1979).

115. Kelly v. Bell, 266 A.2d 878 (1970).

116. *Id.* at 879.

117. 493 A.2d 929 (Del. 1985).

118. *Rosenblatt*, 493 A.2d at 943.

119. *Id.* The board of directors may not, however, delegate "those duties which lay at the heart of management of the corporation." Chapin v. Benwood Foundation, Inc., 402 A.2d 1205, 1210 (Del Ch. 1979); *see also* Lehrman v. Cohen, 222 A.2d 800, 808 (Del. 1966); Adams v. Clearance Corp., 121 A.2d 302, 305-06 (Del. 1956); Clarke Memorial College v. Monaghan Land Co., 257 A.2d 234, 241 (Del. Ch. 1969); Abercrombie v. Davies, 123 A.2d 893, 898 (Del. Ch. 1956). Indeed, certain fundamental directorial functions, such as determining the value of the property acquired as consideration for the issuance of stock, may not be delegated as a matter of law. Field v. Carlisle Corp., 68 A.2d 817, 820 (Del. Ch. 1949).

with public relations duties may not be entitled to the Rule's presumptions of due care were he or she to make a financial decision properly within the sphere of the treasurer's activities. As a result, officers face a dual risk. Liability may attach if the officer is adjudged in hindsight to have acted outside the scope of his or her delegated authority or to have failed to act on a matter that was not within his or her expected areas of responsibility. Boards of directors must be careful to assure that delegations of authority in the bylaws, board resolutions and other documents assigning corporate responsibilities accurately reflect the duties of particular officers.

Most recent authority emanating from jurisdictions other than Delaware also suggest that non-director officers are entitled to the benefits of the Rule, thus relegating *Platt* and *Gaillard* to a distinct minority position. In *Massaro v. Vernitron Corp.*,[120] a federal court applying Delaware law held the business judgment rule applies to corporate officers.[121] The *Massaro* court held that where there was no evidence of bad faith, fraud, gross overreaching, or abuse of discretion, no cause of action existed against corporate officers for breach of fiduciary duty or corporate mismanagement.[122]

In *Para-Medical Leasing, Inc. v. Hangen*,[123] the corporation sued its interim manager for negligent mismanagement. The corporation argued that the Rule applied only to directors of corporations and not to temporary officers. The court cited Washington case law interpreting the Rule as immunizing management generally from liability.[124] The court applied the Rule to a non-director officer based upon cases holding that the Rule applied to defendants who were both directors and officers, reinforcing the interpretation that those director-and-officer cases are actually intended to apply the Rule to officers *or* directors.[125]

In *AmeriFirst Bank v. Bomar*,[126] Hattler, the bank's senior lending officer, and Cole, the chief financial officer of the bank's service corporation subsidiary, were sued along with other defendants for breach of fiduciary duty. Hattler and his co-defendants argued that the Rule shielded them from the allegations of breach of fiduciary duty, negligence, breach of the

120. 559 F. Supp. 1068, 1080-81 (D. Mass. 1983).
121. *Massaro*, 559 F. Supp. at 1080-81 (citing Guth v. Loft, 5 A.2d 503 (Del. 1989), discussed *supra* text accompanying notes 39-42, and Singer v. Magnavox, 380 A.2d 969 (Del. 1977)).
122. *Id.*
123. 739 P.2d 717 (Wash. App. 1987).
124. *See* Nursing Home Bldg. Corp. v. Deltort, 535 P.2d 137 (Wash. Ct. App. 1975).
125. *Para-Medical Leasing, Inc.*, 739 P.2d at 721.
126. 757 F. Supp. 1365 (S.D. Fla. 1991).

duty of loyalty, and other claims. The court expressly recited the business judgment rule as applying to both officers and directors.[127]

Similarly, in *Detwiler v. Offenbacher*,[128] a federal court in New York applied the Rule to a defendant vice president/secretary/treasurer in the same fashion it was applied to the co-defendants, a director and corporate counsel.[129] The claims in *Detwiler* included allegations of breaches of fiduciary duty arising out of events surrounding the sale of a corporation. The applicability of the Rule to the three defendants was challenged on the basis of self-interest. In holding that there was insufficient self-interest to bar application of the Rule, the court treated all three defendants under the same standard of liability.[130] In addressing the defendants' good faith, the court did not distinguish between the non-director officer and the other defendants.[131]

CONCLUSION

Fiduciary duties attach to an officer if he or she is endowed by the board of directors or the bylaws with discretionary power to manage corporate affairs. The duty of care attaches by virtue of one's position as an officer. That duty clearly includes, among other things, an obligation to inform the board of directors of material developments within the board's decision-making purview that come to an officer's attention. Though articulations of the legal standard differ, liability under the duty of care appears to be largely a function of the officer's familiarity with corporate affairs. Thus, liability under the duty of care is usually greater for officers than directors, and for officer-directors than non-officer directors. While some courts have held that officers, or officer-directors, have a greater fiduciary duty than directors, their reasoning for such a standard is largely unsupported.

In addition, the duty of loyalty attaches to officers as well as employees. In fact, it has been stated that a somewhat higher degree of the duty

127. *AmeriFirst Bank*, 757 F. Supp. at 1376; *see also In re* Western World Funding, Inc., 52 B.R. 743, 770 (Bankr. D. Nev. 1985) (applying the business judgment rule to a non-director corporate vice president as well as director/officer co-defendants, but finding a breach of fiduciary duty due to "failure to exercise informed judgment" when defendants were found to have failed to maintain records, to prepare proper financial statements, to monitor financial progress of the debtor companies, to make appropriate inquiries into the purposes for which the investors' monies were being used, and to have caused funds to be transferred into another corporation without assurances of the safety of such investments).

128. 728 F. Supp. 103 (S.D.N.Y. 1989).

129. *Detwiler*, 728 F. Supp. at 149.

130. *Id.*

131. *Id.* at 150; *see also* Unertl v. Bezanson, 414 N.W.2d 321, 324-25 (Iowa 1987) (where corporate creditors sued officers and directors, including the non-director president, for both negligent mismanagement and fraud purposes, no distinction was made between directors and officers).

applies to officers than ordinary employees. A particularly strong formulation is that officers must refrain from doing anything of a self-dealing nature that would cause loss to the corporation.

The business judgment rule is almost universally applied to officers. The Rule's policy of not second-guessing management is imperiled, however, if the Rule's application is withheld from non-director officers. If the officer is deprived of the Rule's protection for delegable decisions, then the corporation has surrendered part of its freedom from judicial interference. The Rule's protection of a board's delegation decision is rendered moot if courts are permitted to interfere with corporate management by subjecting the officer to greater scrutiny. The operation of the Rule should coexist with delegation law, lest courts give with one hand—protecting delegation decisions—while taking with the other by subjecting non-director officers to more liability.

In light of the foregoing, certain practical steps can be taken to minimize the risk of officer liability. Steps should be taken to assure that the scope of authority delegated to particular officers is clearly stated in terms neither too broad nor too narrow. Furthermore, a clear understanding must be developed as to the types of occurrences that are deemed sufficiently material to be reported to the board for possible action. Finally, all officers should be made aware that their fiduciary duty of care includes that of alerting the board (or a superior officer) of any activity within the board's decision-making purview, whether inside or outside their sphere of delegated authority, which comes to the officer's attention and appears to affect materially the corporation's best interest.