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Safe Harbor for Officer Reliance: Comparing the Approaches of the Model Act and Delaware's General Corporation Law

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SAFE HARBOR FOR OFFICER RELIANCE: COMPARING THE APPROACHES OF THE MODEL BUSINESS CORPORATION ACT AND DELAWARE'S GENERAL CORPORATION LAW

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I

INTRODUCTION

Over the past decade, corporate commentators and policymakers have given increasing attention to the duties of and potential for imposing liability on corporate officers, as distinct from directors. In response, in part, to the alleged corporate malfeasance that led to the events at WorldCom and Enron, the federal government put in place the Sarbanes-Oxley Act in an effort to increase officer accountability and impose legal responsibilities on these individuals.¹ Similarly, post-Enron, regulatory agencies and stock exchanges such as the Securities and Exchange Commission (SEC), the New York Stock Exchange (NYSE), and Nasdaq, adopted procedures designed to promote greater legal accountability not only with respect to officers, but also the directors who are responsible for overseeing the actions of officers.² More recently, and even before the causes and impact of the financial crisis have been fully understood,

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1. See 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.S.) (2005); see also Lyman P.Q. Johnson & Mark A. Sides, *The Sarbanes-Oxley Act and Fiduciary Duties*, 30 WM. MITCHELL L. REV. 1149, 1150 (2004) (discussing regulation of director and officer conduct under the Sarbanes-Oxley Act); Larry Catá Backer, *The Sarbanes-Oxley Act: Federalizing Norms for Officer, Lawyer, and Accountant Behavior*, 76 ST. JOHN'S L. REV. 897, 897 (2002) (discussing the effects of the Sarbanes-Oxley Act following corporate scandals).

2. See Johnson & Sides, *supra* note 1 (discussing steps taken by the SEC, the NYSE, and Nasdaq and the interplay of federal reform with state fiduciary duty law); Hillary A. Sale, *Delaware's Good Faith*, 89 CORNELL L. REV. 456, 456-57 (2004) ("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.").

lawmakers have sought to address the perceived misjudgments and lack of accountability of corporate officers.³ Amid these calls for increased scrutiny and regulation of the behavior of corporate executives, corporate scholars and commentators have been focused on the proper standards by which to judge the fiduciary duties of officers and how to impose liability for the breach of such duties, in particular noting that, until recently, there was a lack of definitive guidance from the Delaware courts on the issue.⁴

The fiduciary duties of officers is addressed, in differing degrees, under Delaware law, the law frequently applied to corporate-governance disputes, and under the Model Business Corporation Act (MBCA). As a general matter, both Delaware law and the MBCA provide that the fiduciary duties of corporate officers are essentially the same as those owed by directors. The MBCA provides for such duties by statute, specifying express conduct requirements of officers.⁵ By contrast, Delaware's approach to fiduciary duties is grounded in common law and contains no such particularized statutory guidance.⁶ While each of these bodies of corporate law impose essentially the same fiduciary obligations on officers and directors, the MBCA and Delaware's corporate statute, the General Corporation Law of the State of Delaware (General Corporation Law), differ in what statutory protections are provided to officers in fulfilling their fiduciary obligations.

In discharging their fiduciary duties, directors under both the MBCA and the General Corporation Law are generally protected from personal liability if, in making business decisions, they reasonably rely on the reports and records of officers, employees, advisors, and experts of the corporation. The statutes diverge, however, in whether this safe harbor should be extended to the officers of a corporation, whether they are non-director officers or directors acting in their capacity as officers. The MBCA provides that officers may be protected when their actions are taken in reliance on the other employees and outside advisors and experts of the corporation, while the reliance protections set forth in the General Corporation Law are available only to directors. This article

3. See *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, 110 n.3 (2009); see, e.g., Shareholder Bill of Rights Act of 2009, S. 1074, 111th Cong. § 2 (2009), available at http://www.schumer.senate.gov/new_website/Bill%20Text%20%20Shareholders%20Bill%20of%20Rights%20Act%20of%202009.pdf.

4. See Lyman Johnson & Dennis Garvis, *Are Corporate Officers Advised About Fiduciary Duties?*, 64 BUS. LAW. 1105, 1106 (2009) ("For all their undoubted significance, however, corporate officers receive scant attention in the world of corporate law."); 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."); A. Gilchrist Sparks III & Lawrence A. Hamermesh, *Common Law Duties of Non-Director Corporate Officers*, 48 BUS. LAW. 215, 215 (1992) ("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.").

5. See MODEL BUS. CORP. ACT § 8.42 (2008).

6. See *Gantler v. Stephens*, 965 A.2d 695, 708–09 (Del. 2009).

discusses the differing approaches of the MBCA and the General Corporation Law and the considerations underlying the extension of a reliance safe harbor to officers.

II

FIDUCIARY DUTIES OF OFFICERS

A. Officer Fiduciary Duties Under the MBCA

Under the MBCA, a corporation may have such officers as are described in its bylaws or as are appointed by the board of directors in accordance with the bylaws.⁷ With respect to the fiduciary obligations of these individuals, section 8.42 of the MBCA sets forth a comprehensive statement of the expected standards of officer conduct, which are generally the same as those imposed on directors of a corporation. Specifically, an officer has a duty to act “(1) in good faith; (2) with the care that a person in a like position would reasonably exercise under similar circumstances; and (3) in a manner the officer reasonably believes to be in the best interests of the corporation.”⁸ In addition to imposing director-like standards of conduct, the MBCA also introduces concepts from agency law, adding a duty of obedience to the fiduciary duties of care and loyalty owed by an officer.⁹

Further, while implicit in the broad standards of conduct provided for in section 8.42(a), and in part in response to the upheavals involving public corporations such as Enron, the MBCA was amended in 2005 to address an officer’s duties with respect to disclosure of information to the board of directors. The amendment, set forth in section 8.42(b), provides that an officer’s duty of disclosure includes the obligation (1) to inform superior corporate authorities, such as a superior officer to whom the officer reports, the board of directors, or a committee of the board, of any material information that is within the scope of the officer’s functional responsibilities, and (2) to inform the relevant superior corporate authority or another appropriate person of material violations of law or material breaches of duty to the corporation by an officer, employee, or agent, that the officer believes have occurred or are likely to occur.¹⁰ The rationale underlying the addition of section 8.42(b) was that, by specifically setting forth certain reporting requirements as part of officers’ fiduciary duties, the type of wrongdoings that were uncovered only after the fact in Enron-type situations could potentially be mitigated or avoided.

7. See MODEL BUS. CORP. ACT § 8.40(a) (2008).

8. *Id.* § 8.42(a).

9. See *id.* § 8.42 cmt. at 8-346.

10. *Id.* § 8.42(b).

B. Officer Fiduciary Duties Under Delaware Law

In contrast to the MBCA, Delaware law does not impose fiduciary duties on officers by statute. Rather, the nature and contours of Delaware fiduciary duties arise out of common law.¹¹ But while Delaware law contains a well-developed set of standards, both in case law and statute, to govern the conduct of corporate directors, the law pertaining to the fiduciary obligations of officers, by comparison, is sparse.¹² In the seminal 1939 case of *Guth v. Loft*, the Delaware Supreme Court first articulated the broad proposition that officers owe fiduciary duties to the corporation and its stockholders.¹³ Over forty years later, the Delaware Supreme Court again mentioned the concept of an officer's fiduciary duties when it noted that "[p]ractically all jurisdictions recognize a fiduciary relationship arising from the directors and officers to their corporation and to the stockholders"¹⁴ Subsequent decisions in the Delaware Court of Chancery relied on the Delaware Supreme Court's generalized declaration in *Guth* in stating generally that an officer owes the same fiduciary duties as directors, but failed to develop this concept any further.¹⁵

Accordingly, based on the Delaware Supreme Court's statements in *Guth*, courts and commentators had, until recently, operated under the assumption that the duties owed by corporate officers were the same as those of directors.¹⁶

11. See *In re Citigroup Inc. S'holder Derivative Litig.*, 964 A.2d 106, 114 n.6 (Del. Ch. 2009) ("Delaware fiduciary duties are based in common law and have been carefully crafted to define the responsibilities of directors and managers, as fiduciaries, to the corporation."). With respect to a corporation's officers, Delaware law does provide statutorily that "[e]very corporation organized under this chapter shall have such officers with such titles and duties as shall be stated in the bylaws or in a resolution of the board of directors" DEL. CODE ANN. tit. 8, § 142(a) (2010).

12. See *Johnson & Garvis*, *supra* note 4, at 1106 n.6.

13. *Guth v. Loft*, 5 A.2d 503, 510 (Del. 1939) (stating that "[c]orporate officers and directors . . . stand in a fiduciary relation to the corporation and its stockholders").

14. *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)). The Delaware Court of Chancery had also only addressed the issue of officer fiduciary duties in dicta, stating that officers and directors each owe fiduciary duties, without further expanding on that proposition. 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) ("Delaware law is clear that a fiduciary duty is owed to the shareholders of a corporation by the officers and directors of the corporation . . .").

15. 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"); *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.'") (alteration in original) (quoting *In re The Walt Disney Co. Derivative Litig.*, No. 15452, 2004 WL 2050138, at *3 (Del. Ch. Sept. 10, 2004)); *Ryan v. Gifford*, 935 A.2d 258, 269 (Del. Ch. 2007) (same); *In re The Walt Disney Co. Derivative Litig.*, No. 15452, 2004 WL 2050138, at *3 (Del. Ch. Sept. 10, 2004) (citations omitted) ("To date, the fiduciary duties of officers have been assumed to be identical to those of directors.").

16. See *Johnson & Millon*, *supra* note 4, at 1600 ("[C]ourts and commentators routinely describe the duties of directors and officers together, and in identical terms."); *Sparks & Hamermesh*, *supra* note 4, at 217 ("Nonetheless, most authorities suggest that, as a general proposition, corporate officers owe

In early 2009, the Delaware Supreme Court in *Gantler v. Stephens* confirmed this assumption by explicitly holding that corporate officers' fiduciary duties are the same as those owed by directors:

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.¹⁷

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.¹⁸ Thus, under Delaware law, officers owe the same fiduciary duties to the corporation and its stockholders as directors.

III

SAFE HARBOR OF RELIANCE

In connection with directors' discharge of their fiduciary duties, several protections have developed over the years in both the MBCA and Delaware law to limit directors' potential liability in carrying out their duties and decisionmaking. One such protection available to directors is a safe harbor that applies when directors act, or choose not to act, in reliance on the records of the corporation, the reports and opinions of officers and employees of the corporation, or the advice of outside experts and advisors. Both the MBCA and the General Corporation Law provide that directors will generally be protected in reasonably relying on these resources and individuals in fulfilling their fiduciary obligations. However, the statutes differ in whether this protection is available to officers as well.

the corporation the same fiduciary duties as do directors."); *see, e.g., In re Walt Disney*, 2004 WL 2050138, at *3; *Copi of Del., Inc.*, 1996 WL 633302, at *5; *Zirn*, 1989 WL 79963, at *4; *Sale*, *supra* note 2, at 462 n.28. *But see* *Johnson & Millon*, *supra* note 4, at 1600–01 (arguing that officers and directors do not have the same fiduciary duties).

17. *Gantler v. Stephens*, 965 A.2d 695, 708–09 (Del. 2009) (internal citation omitted); *see also* Megan W. Shaner, *Restoring the Balance of Power in Corporate Management: Enforcing an Officer's Duty of Obedience*, 66 BUS. LAW. 127 (2010) (discussing the history of Delaware officers' fiduciary duties and issues surrounding such duties post-*Gantler*). In the bankruptcy context, Delaware courts have begun to address the nature and contours of an officer's fiduciary duties. *See, e.g., In re Bridgeport Holdings, Inc.*, 388 B.R. 548, 559 (Bankr. D. Del. 2008) (addressing fiduciary duty claims, including oversight claims, brought against corporate officers); *Miller v. MacDonald*, 385 B.R. 576, 591 (Bankr. D. Del. 2008) (stating that, in the court's view, liability for the failure of oversight, so-called *Caremark* liability, applied to directors and officers equally).

18. *Gantler*, 965 A.2d at 708–09.

A. Reliance Under the MBCA

Section 8.30 of the MBCA sets forth the general standards of conduct for directors of a corporation. Included in the standards of conduct are provisions giving directors the ability to rely on reports, statements, opinions, or other information as well as the corporation's officers or employees, outside advisors, or a committee of the board of directors in discharging their duties.¹⁹ In relying on the reports and other information of the corporation, a director must still comply with the general standard of care, which includes assessing the reliability and competence of the source of information upon which the director intends to rely.²⁰ In addition, in relying on the corporation's officers or employees or other individuals such as outside advisors, a director must similarly make a determination with respect to the reliability and competence of the source.²¹ However, when a director does not otherwise have knowledge that would make reliance unwarranted, he or she will be protected in relying on information, opinions, reports, or statements of the officers, advisors, or experts of the corporation in meeting the standards of conduct expected of directors under the MBCA.

The MBCA affords similar protection to officers with respect to their reliance upon the records and reports of the corporation or other employees, advisors, and experts. Section 8.42(c) of the MBCA provides that

[i]n discharging his or her duties, an officer who does not have knowledge that makes reliance unwarranted is entitled to rely on . . . (2) information, opinions, reports or statements, including financial statements and other financial data, prepared or presented by one or more employees of the corporation whom the officer reasonably believes to be reliable and competent in the matters presented or by legal counsel, public accountants, or other persons retained by the corporation as to matters involving skills or expertise the officer reasonably believes are matters (i) within the particular person's professional or expert competence or (ii) as to which the particular person merits confidence.²²

Accordingly, an officer will be protected in relying on any other employee of the corporation and the reports and records prepared and presented by such person, if the officer has a reasonable belief that such employee is reliable and competent in the matters he or she presented.²³ When an officer is relying on an

19. See MODEL BUS. CORP. ACT § 8.30(e)–(f) (2008).

20. See *id.* § 8.30 cmt. 5.

21. See *id.* § 8.30 cmt. 6.

22. *Id.* § 8.42(c).

23. See *id.* The Official Comment to section 8.42 of the MBCA makes reference to the Official Comment to section 8.30 in describing an officer's ability to rely on the reports of employees or outside advisors or experts. See *id.* § 8.42 cmt. at 8-348. The Official Comment to section 8.30 of the MBCA describes how to determine whether a person is "reliable" or "competent." See *id.* § 8.30 cmt. 6. In determining whether a person is "reliable," an officer can consider "the individual's background experience and scope of responsibility within the corporation in gauging the individual's familiarity and knowledge respecting the subject matter and . . . the individual's record and reputation for honesty, care and ability in discharging responsibilities which he or she undertakes." *Id.* In determining whether a person is "competent" an officer can consider the same factors as he or she would consider with

advisor or expert retained by the corporation, the officer must reasonably believe that the matters presented by such advisor or expert are within that person's professional or expert competence or are matters on which the particular advisor or expert merits confidence.²⁴ The MBCA's concept of "expert competence" encompasses a much broader variety of qualifications than other corporate statutes, because the MBCA does not limit a person's expert competence to the qualification under the Securities Act of 1933. Rather, an officer may rely on an outside advisor even when "skills or expertise of a technical nature is not a prerequisite, or whe[n] the person's professional or expert competence has not been established, so long as the director reasonably believes the person merits confidence."²⁵ While section 8.42 of the MBCA provides reliance protection to officers similar to that extended to directors under section 8.30, the Official Comment to the MBCA cautions that an officer's ability to rely on others may be more limited in certain circumstances based on his or her familiarity with the corporation's business and affairs.²⁶

B. Reliance Under the General Corporation Law

The Delaware analog to sections 8.30(e) and 8.30(f) of the MBCA is found in section 141(e) of the General Corporation Law. Recognizing that boards of directors, in discharging their duties, frequently must rely on both internal reports from management and external reports from experts, the Delaware legislature adopted section 2041 of the Revised Code of Delaware of 1935, the precursor to section 141(e), to provide that a director of a corporation

shall in the performance of his duties be fully protected in relying in good faith upon . . . reports made to the corporation by any of its officials or by an independent certified public accountant, or by an appraiser selected with reasonable care by the Board of Directors . . .²⁷

The provisions of original section 2041 remained over the years, and in 1987, the legislature modernized the statute, which had by then been reclassified as section 141(e), "to broaden the language to encompass specifically all categories of outside experts and to bring reports by non-officer employees within its ambit."²⁸

respect to reliability of a person. In addition, if a person's expertise is relevant to the decision, an officer should consider the technical skills or knowledge of the person as well. *Id.*

24. *Id.* § 8.42(c). In evaluating the expertise of an outside advisor to the corporation, an officer may take into account a wide variety of qualifications, including where the officer reasonably believes that the person merits confidence, even in the absence of establishing the person's professional or expert competence. *See id.* § 8.30 cmt. 6.

25. *See* MODEL BUS. CORP. ACT § 8.30 cmt. 6 (2008).

26. *See id.* § 8.42 cmt. at 8-348.

27. *See* 44 Del. Laws 423 (1943).

28. *See* DAVID A. DREXLER ET AL., 1 DELAWARE CORPORATION LAW AND PRACTICE § 15.06[2] at 15-45 (Supp. 2009); *see also* S. 93, 134th Gen. Assemb., 1st Sess. (Del. 1987) (official commentary) (stating that the purpose of the amendment was "to clarify that directors may rely in good faith upon all corporate records, reports of employees and committees of the board and the

In its current form, section 141(e) “fully protect[s]” directors who, in carrying out their duties, rely in good faith on certain corporate information and individuals that have been selected with reasonable care. Specifically, section 141(e) provides:

A member of the board of directors, or a member of any committee designated by the board of directors, shall, in the performance of such member's duties, be fully protected in relying in good faith upon the records of the corporation and upon such information, opinions, reports or statements presented to the corporation by any of the corporation's officers or employees, or committees of the board of directors, or by any other person as to matters the member reasonably believes are within such other person's professional or expert competence and who has been selected with reasonable care by or on behalf of the corporation.²⁹

Thus, in discharging their duty to be informed in making decisions on behalf of the corporation, directors, by statute, have no additional duty to research or verify independently that the corporate reports or the underlying data upon which they rely are accurate.

Accordingly, under section 141(e), in appropriate circumstances, directors are entitled to place great reliance on the records of the corporation and the reports of experts. This protection, however, is not without limits. In order to secure the protections of section 141(e), a director must (1) be relying in good faith, (2) have a reasonable belief in the professional or expert competence of the person presenting the report, and (3) have selected such person with reasonable care.³⁰ Further, directors cannot rely exclusively on experts' collective experience and expertise to demonstrate an informed decision; they are only “entitled to good faith, not blind, reliance” on expert advice.³¹ To that end, directors are duty-bound to make a “reasonable inquiry” into any reports submitted to the board.³²

Unlike the MBCA, the General Corporation Law does not extend the protections in section 141(e) to officers. As a result, officers of Delaware corporations do not, at least statutorily, receive any safe harbor protection

written or oral advice or opinions of any professionals and experts who are selected with reasonable care and are reasonably believed to be acting within the scope of their expertise”).

29. DEL. CODE ANN. tit. 8, § 141(e) (2010); *see also In re Citigroup Inc. S'holder Derivative Litig.*, 964 A.2d 106, 132 (Del. Ch. 2009) (“[D]irectors of Delaware corporations are fully protected in relying in good faith on the reports of officers and experts.”); *Crescent/Mach I Partners, L.P. v. Turner*, 846 A.2d 963, 985 (Del. Ch. 2000) (“Section 141(e) of Delaware's corporation law provides that directors are protected from a breach of the duty of care ‘when the directors reasonably believe the information upon which they rely has been presented by an expert “selected with reasonable care” and is within that person's “professional or expert competence.”’”) (quoting *In re Cheyenne Software, Inc.*, No. 14941, 1996 WL 652765, at *2 (Del. Ch. Nov. 7, 1996)). For a discussion of the history of section 141(e) and the Delaware courts' application of the statute, *see* Thomas A. Uebler, *Reinterpreting Section 141(e) of Delaware's General Corporation Law: Why Interested Directors Should be “Fully Protected” in Relying on Expert Advice*, 65 BUS. LAW. 1023 (2010) (discussing Delaware case law where section 141(e) provides directors with a defense to liability in duty of care cases and asserting that section 141(e), by its express terms, should also provide a defense to liability in certain duty of loyalty cases).

30. *See* DEL. CODE ANN. tit. 8, § 141(e) (2010).

31. *See* *Smith v. Van Gorkom*, 488 A.2d 858, 875, 880 (Del. 1985).

32. *See id.* at 875.

when they rely in good faith on the corporate records and reports and the advice of experts to the corporation in carrying out their fiduciary duties.

IV

CONSIDERATIONS IN EXTENDING RELIANCE PROTECTION TO OFFICERS

The board of directors of a corporation is tasked with the ultimate responsibility for the management of a corporation.³³ However, given the size and complexity of many modern corporations, actual operational control by the board of directors, itself, is frequently not feasible. Recognizing this reality, the MBCA and the General Corporation Law provide the board with the ability to delegate certain powers and responsibilities to the chief executive officer, chief financial officer, and other executive officers of the corporation.³⁴ The primary functions of management of the corporation generally are delegated to these senior executive officers. In turn, those members of senior management may then delegate to other officers, employees, and agents of the corporation certain responsibilities with respect to the day to day operations of the corporation.³⁵ For example, the chief financial officer of a large public corporation may delegate responsibility for compiling the comprehensive financial statements and conducting the audits of the corporation's various business segments to other senior financial officers or senior audit officers who will then report back to the chief financial officer. This delegation further down the management hierarchy is often necessary for a large public corporation to be able to run effectively and efficiently. The MBCA acknowledges the reality of the

33. See MODEL BUS. CORP. ACT § 8.01(b) (2008); DEL. CODE ANN. tit. 8, § 141(a) (2010); *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) (2010)).

34. See MODEL BUS. CORP. ACT § 8.01(b) & cmt. at 8-5 (2008); DEL. CODE ANN. tit. 8, § 141(a) (2010); see also AM. LAW INST., PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 3.01 cmt. a (1994) (citation omitted) ("It is generally recognized that the board of directors is not expected to operate the business. Even under statutes providing that the business and affairs shall be 'managed' by the board of directors, it is recognized that actual operation is a function of management. The responsibility of the board is limited to overseeing such operation[s]"); *Grimes v. Donald*, No. 13358, 1995 WL 54441, at *8 (Del. Ch. Jan. 11, 1995) ("[G]iven the large, complex organizations through which modern, multi-function business corporations often operate, the law recognizes that corporate boards, comprised as they traditionally have been of persons dedicating less than all of their attention to that role, cannot themselves manage the operations of the firm, but may satisfy their obligations by thoughtfully appointing officers, establishing or approving goals and plans and monitoring performance. . . . Thus Section 141(a) of [the] DGCL 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). Delegation by the board of directors is not limited or restricted to senior executive officers; however, practically speaking, based on the corporate management hierarchy at many corporations, most delegation and directives from the board will go to these senior officers.

35. See MODEL BUS. CORP. ACT § 8.01 cmt. at 8-5 (2008) ("[I]n many other corporations, the business and affairs are managed 'under the direction, and subject to the oversight, of the board of directors, since operational management is delegated to executive officers and other professional managers.'").

management of the corporate entity and that the delegation, and subsequent reliance, by officers and directors alike is a practice that frequently takes place and is of practical necessity for the modern corporation to function.³⁶ The MBCA thus addresses the implications of officers' delegation and reliance on other persons in discharging their duties to the corporation. By providing officers with protection when they reasonably rely on the information, opinions, reports, or statements of other employees or outside advisors and experts of the corporation, the MBCA's provisions encourage proper delegation, oversight, and reliance by officers. Further, providing officers with a safe harbor in reasonably relying on other individuals encourages officers to take advantage of all of the resources available to them in order to be fully informed and to fulfill properly their fiduciary obligations.

The MBCA's approach finds support not only in practice, but also in policy. For instance, one of the policy considerations underlying the reliance safe harbor afforded to directors is that, given the complex situations and business issues boards must address, in order to meet their fiduciary obligations to be fully informed, directors often must rely on lawyers, financial advisors, economists, and other specialized experts to advise them. By offering protection to directors when they properly rely on the statements, opinions, and reports of outside advisors and experts, reliance statutes encourage directors to seek the appropriate advice to be fully informed in taking action and making decisions on behalf of the corporation. Indeed, the Delaware courts have recognized that "[d]irectors of Delaware corporations quite properly delegate responsibility to qualified experts in a host of circumstances."³⁷ Moreover, as one corporate commentator has put it, "[e]xpert consultation inspired by a perceived need to know on the part of the board is obviously constructive and indispensable."³⁸ Officers are likewise faced with complex business decisions and issues that they may not have the knowledge or industry-specific experience to fully understand. For example, while an officer such as the chief executive officer has a more intimate knowledge of the business and greater access to the records and day to day operations of the corporation than a director, the chief executive officer does not necessarily have thorough knowledge and expertise with respect to *all* aspects and areas of the corporation's business. As a result, the chief executive officer may not be able to make a fully informed decision or recommendation

36. See *id.* § 8.42(c)(1); see also R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, 1 THE DELAWARE LAW OF CORPORATIONS & BUSINESS ORGANIZATIONS § 4.15[B], at 4-114 (3d ed. Supp. 2010) ("Protected reliance on officers' reports, when those reports are facially credible, is a practical necessity for a board of directors to function.").

37. *Ash v. McCall*, No. 17132, 2000 WL 1370341, at *9 (Del. Ch. Sept. 15, 2000); see also *McMullen v. Beran*, No. 16493, 1999 WL 1135146, at *4 n.21 (Del. Ch. Dec. 1, 1999) ("Delaware law recognizes the appropriateness of directors relying on the advice of experts when specialized judgment is required as part of a business judgment."); *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1134, 1142 (Del. Ch. 1994), *aff'd*, 663 A.2d 1156 (Del. 1995) (stating that relying on an experienced advisor is not only allowed, but is "evidence [of] good faith and the overall fairness of the process").

38. Bayless Manning, *The Business Judgment Rule and the Director's Duty of Attention: Time for Reality*, 39 BUS. LAW. 1477, 1487 (1984).

to the board on his or her own, in particular when doing so would require specialized knowledge or judgment. Accordingly, an officer may, and in many cases should, turn to outside legal, financial, and other advisors to assist in providing reports and other information so that the officer can be fully informed in discharging his or her duties. Extending a safe harbor to officers when they properly rely on experts reinforces the appropriate actions by officers to be fully informed in making business decisions and reporting to and advising the board of directors.

Although the foregoing reasons can be cited in support of extending the statutory reliance protections afforded to directors to officers, there are also inherent differences in the roles and responsibilities of directors and officers in managing a corporation, which suggest that, consistent with the General Corporation Law's approach, these protections should not be extended to officers. Even though the fiduciary duties of directors and officers have been found to be the same, the functions and roles of directors and officers within the corporation are fundamentally different.³⁹ Directors are charged with overseeing the management of the corporation,⁴⁰ while officers are charged with running the day to day operations and reporting back to the board.⁴¹ Accordingly, with greater access to the books and records of the corporation and a more intimate knowledge of the business and affairs of the corporation, one of the primary functions of officers is to be fully informed with respect to the corporate enterprise and to report to the board. Under Delaware law, for example, corporate commentators have inferred a duty to inform the board of directors based upon the statutorily mandated information exchange that must take place between officers and directors for a corporation to function.⁴² Furthermore, section 141(a) of the General Corporation Law provides that "[t]he business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors . . ."⁴³ Thus, section 141(a) impliedly requires officers in charge of the corporation's day to day operations to be informed so as to be able to convey sufficient information to the members of the board of directors to enable them to direct the management of the corporation appropriately. In addition, the Delaware Court of Chancery has commented specifically on an officer's duty of disclosure to the board. The court has recognized that there is little question that "in certain circumstances an officer of a Delaware corporation has a duty to speak without being asked to do so."⁴⁴

39. See Johnson & Millon, *supra* note 4, at 1601 (asserting that the institutional function and legal roles within the corporation are not the same for directors and officers).

40. See DEL. CODE ANN. tit. 8, § 141(a).

41. See Jana Master Fund, Ltd. v. CNET Networks, Inc., 954 A.2d 335, 340 (Del. Ch. 2008) (stating that officers "have the far more onerous task of operating the company each day").

42. See Sparks & Hamermesh, *supra* note 4, at 226.

43. DEL. CODE ANN. tit. 8, § 141(a).

44. Greco v. Columbia/HCA Healthcare Corp., No. 16801, 1999 WL 1261446, at *9 (Del. Ch. Feb. 12, 1999).

These informational and disclosure requirements and duties of officers are further evidenced by statutory provisions such as section 141(e) of the General Corporation Law and section 8.30(d)–(f) of the MBCA, both of which protect *directors* from personal liability resulting from corporate action taken in reliance on information provided by *officers*.⁴⁵ The assumption underlying the safe harbor provided by these statutes is that the officers are the persons with the most intimate knowledge and best access to information regarding the corporation and its business.⁴⁶ Accordingly, lawmakers have decided that directors may properly rely on these individuals in discharging their duty to be informed in making decisions and be protected in doing so. Because directors are entitled to such protection, officers should arguably be held to a strict standard of care and requirement to be fully informed. As a result, allowing officers, in turn, to receive a similar safe harbor in relying on other individuals in meeting their standard of care and duty to be informed would undermine the rationale underlying the statutory protections provided to directors.

Finally, in evaluating the merits of the differing approaches of the MBCA and General Corporation Law, one should keep in mind that the protections afforded to officers under the MBCA only address the nature and quality of information upon which an officer is entitled to rely. The benefit that officers receive under section 8.42(c) of the MBCA is that they are not required to research or verify independently that the corporate reports or the underlying data or individuals upon which or whom they rely are accurate. These statutes do not, however, obviate the need for officers to inform themselves fully of the relevant information and details of an issue.⁴⁷ Rather, only reasonable good faith reliance is protected. As provided in section 8.42(c) of the MBCA, officers are only entitled to rely on employees, outside advisors, and experts if the officer “reasonably believes [such individuals] to be reliable and competent.”⁴⁸ Moreover, the MBCA also recognizes that

[a]n officer’s ability to rely on others in meeting the standards [of conduct required under the MBCA] may be more limited, depending upon the circumstances of the particular case, than the measure and scope of reliance permitted a director . . . in view

45. See DEL. CODE ANN. tit. 8, § 141(a); MODEL BUS. CORP. ACT § 8.30(d)–(f).

46. See BALOTTI & FINKELSTEIN, *supra* note 36, § 4.15[B] (“Management is often the best-informed source of the business of the company and the opportunities that might confront it. Thus, a director relying in good faith on such reports should be entitled to the full protection of the business judgment rule.”); see also *In re Toys “R” Us, Inc. S’holder Litig.*, 877 A.2d 975, 1003 (Del. Ch. 2005) (describing officers as the “members with the best capacity to help management craft and implement a sound business plan”).

47. See MODEL BUS. CORP. ACT § 8.30 cmt. 5–6 (2008); see *cf.* *Smith v. Van Gorkom*, 488 A.2d 858, 874 (Del. 1985); *In re The Walt Disney Co. Derivative Litig.*, 907 A.2d 693, 770 n.550 (Del. Ch. 2005) (“The role of experts under § 141(e) is to assist the board’s decision making—not supplant it.”).

48. MODEL BUS. CORP. ACT § 8.42(c)(1)–(2) (2008); see *cf.* *Cantor v. Perelman*, 235 F. Supp. 2d 377, 387–88 (D. Del. 2002); *Ash v. McCall*, No. 17132, 2000 WL 1370341, at *9 (Del. Ch. Sept. 15, 2000); *Grubb v. Bagley*, No. 13882-NC, 1998 WL 92224, at *2 (Del. Ch. Feb. 15, 1998) (“The statute affords a defense only if the board acted reasonably and in good faith.”).

of the greater obligation the officer may have to be familiar with the affairs of the corporation.⁴⁹

Thus, for officers such as the chief financial officer, who have specialized expertise and acumen in certain matters or a more intimate knowledge of specific aspects of the corporation's business, the ability to be protected in relying on reports and records of others in discharging his or her duties may be more closely circumscribed.

V

CONCLUSION

Under both the MBCA and Delaware law, directors and officers owe essentially the same fiduciary duties to a corporation and its stockholders. While officers have the same fiduciary obligations as directors, they do not always benefit from the same statutory protections that directors may receive.⁵⁰ One such statutory protection is the safe harbor afforded to directors when they reasonably rely on the books and records of the corporation, or the reports, statements, and presentations of the officers, advisors, and experts of the corporation. The MBCA and the General Corporation Law take two different approaches to whether the reliance safe harbor that directors receive should be similarly available to officers. The MBCA, recognizing the reality and practicality of the delegation, and accordingly reliance, that takes place in managing a corporation, extends a reliance safe harbor to officers. By contrast, based on the inherent differences in the roles and responsibilities that directors and officers occupy in corporate management, the approach of the General Corporation Law is not to extend a statutory reliance safe harbor to officers. While this article only discusses the narrow issue of whether officers should receive a safe harbor when they rely on other individuals and resources, the fiduciary duties and standards of liability applicable to officers is a prominent topic for corporate commentators and policymakers. As a result, the broader

49. MODEL BUS. CORP. ACT § 8.42 cmt. at 8-348 (2008). The Delaware courts have indicated that they may take into account the specialized skills of a particular individual in concluding whether that individual has met his or her fiduciary obligations. See *In re Emerging Commc'ns, Inc. S'holders Litig.*, No. 16415, 2004 WL 1305745, at *39-40 (Del. Ch. May 3, 2004). Accordingly, an officer's specialized knowledge or expertise may limit such officer's ability to be protected in relying on the reports and opinions of advisors and experts.

50. For example, under both the MBCA and the General Corporation Law, the ability to exculpate for monetary breaches of fiduciary duty is limited to directors. See DEL. CODE ANN. tit 8, § 102(b)(7) (2010) (providing exculpation for "the personal liability of a *director* to the corporation or its stockholders") (emphasis added); MODEL BUS. CORP. ACT § 2.02(b)(4) (2008) (providing exculpation for "the liability of a *director* to the corporation or its shareholders") (emphasis added); see also *Gantler v. Stephens*, 965 A.2d 695, 709 n.37 (Del. 2009) (noting that the protections in section 102(b)(7) do not extend to officers); *McPadden v. Sidhu*, 964 A.2d 1262, 1275 (Del. Ch. 2008) (same). Commentators have also noted the greater exposure faced by non-director officers when subject to the same fiduciary duties as directors. See, e.g., Johnson & Garvis, *supra* note 4, at 1107 n.9; Johnson & Millon, *supra* note 4, at 1639; John Mark Zeberkiewicz & Blake Rohrbacher, *Commanding Officers: The Fiduciary Duties of Officers under Delaware Law*, INSIGHTS, June 2008, at 2, 7 n.36.

issue of whether corporate officers should receive the same, if any, statutory protections as directors, is an important one.