Limiting Directors' Liability

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I. INTRODUCTION

A substantial risk of personal liability is widely believed to be a deterrent to service as a director of a public company, for at least some prospective candidates. 1 In the 1980s, suits against corporations and their directors asserting claims of all sorts multiplied, and some actions led to large judgments or agreements to pay large settlement amounts. 2 Additionally, contrary to many predictions, 3 and to prior trends, in recent years courts have held directors and officers liable in suits challenging, not their loyalty to the corporation, but the competence and care with which they discharged their duties. 4 Thus, the risk of an outcome adverse to individual directors or officers in such litigation has become more real than hypothetical, even when the fiduciaries' decisions are not afflicted with palpable conflicts of interest. The reality of these risks, coupled with other factors, caused underwriters of directors' and officers' ('D & 'O) liability insurance either to withdraw from that segment of the insurance market in the mid-1980s or to enhance their premiums drastically. 5 Additionally, many underwriters of professional liability insurance entered the 1980s with a penchant for "cash flow" underwriting. Under this practice underwriters write policies with premiums that are

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4. See Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985); Hanson Trust PLC v. ML SCM Acquisition, Inc., 781 F.2d 264 (2d. Cir. 1986) (ordering issuance of preliminary injunction against exercise of lock-up option).
5. According to a study done by the executive search firm Heidrick & Struggles, in 1986 on average premiums increased by 506 percent and in 1987 the companies surveyed reported an average premium increase of 219 percent. Only eight percent of the respondents turned to self insurance, however, and four out of five reported they had not reduced coverage. See Corporate Restructuring, Feb. 1988, at 14, col. 2. See also Hilder, Risky Business, Wall. St. J., July 10, 1985, at 1, col. 6.
admittedly inadequate for the risk, but which are based on the high interest rates that their investments earn. The adverse financial consequences of cash flow underwriting were aggravated by the underwriters' belief—in retrospect severely mistaken—that the frequency and severity of claims would remain constant. 6

Prior to these developments, some types of litigation that involved corporate directors as defendants had long been controversial. In particular, derivative suits—actions brought by a representative shareholder plaintiff on behalf of a corporation to assert a claim belonging to the corporation—are perennial objects of criticism. The perennial controversies surrounding derivative litigation are the inevitable consequences of its principal contemporary function. That function is to call to account corporate managers and controlling shareholders who have abused their relationships with corporations to which they owe obligations of fidelity, or who have failed to discharge their obligations of care in the management of corporations' assets. 7 To be sure, these controversies have been enhanced by other characteristics of derivative litigation. A striking feature of derivative litigation in the post-Depression era is the frequency with which the same plaintiffs make their appearance in actions against public companies. 8 The repeat plaintiff phenomenon, coupled with the high settlement rate in such actions, has supported the view in some quarters that, at least in this era, derivative litigation is abusive and socially wasteful. 9 Other observers are more sanguine, noting that frequency of settlement itself is not adverse if the settlements benefit corporations and their


8. Cf. Lewis v. Anderson, 453 A.2d 474, 475 n.1 (Del. Ch. 1982) (disproving thesis that "Harry Lewis" was a "street name" employed by various counsel), aff'd, 477 A.2d 1040 (Del. 1984). A search of the Westlaw data bases for federal courts and regional reporters from 1945 to May 1986 led to 81 entries of judicial opinions in derivative or class actions or other securities actions in which Harry Lewis participated as a plaintiff. But see Lewis v. Black, 74 F.R.D. 1 (E.D.N.Y. 1975) (institution of many lawsuits does not disqualify person from bringing suit or serving as class representative).

9. This in essence is the thesis of the influential Wood Report, which provided ammunition for the imposition of security for expense requirements in derivative suits. See F. Wood, Survey and Report Regarding Stockholders' Derivative Suits (1944).
shareholders. For that matter, that certain persons specialize in being plaintiffs creates no problem if the behavior of these persons in connection with lawsuits is not objectionable.

These developments all lent legitimacy to the possibility of adjusting the law defining directors' liability so that, by reducing directors' risk of liability, directors' litigation risks might become more readily insurable. In 1986 and 1987, a number of states amended their corporation statutes, in a variety of ways, with the goal of reducing a director's risk of personal liability for money damages in litigation challenging the quality of the director's service to the corporation. Relatedly, many states also revised their statutory treatment of indemnification and D & O liability insurance so as to actually reduce or facilitate the reduction of the financial risks to directors and corporate agents that litigation generally poses.

Over half the states now expressly permit the inclusion of provisions that limit or eliminate directors' liability for money damages in corporations' articles or certificates of incorporation, under circumstances specified by a statutory enabling provision. Many states modeled their enabling provisions closely on the Delaware statute, with some variations. Other state statutes instead define a limited set of circumstances under which a director's misfeasance or nonfeasance will make the director liable. A few states permit subject corporations to opt out of the statutory restrictions on liability. In contrast, the Virginia statute imposes a cap on monetary damages for which directors and officers could be liable as a result of certain actions.

The following sections of this article review the technical and policy
issues raised by these statutes and by recent changes in statutes regulating indemnification and D & O insurance. In general it is noteworthy that substantial questions arise as to the interpretation and efficacy of many of these statutes. Relatedly, many of these statutes reflect little effort by their drafters to integrate their import with other sections of the statute that appear pertinent to issues of directors' liability. As a result of these unfortunate deficiencies, the risk exposure of directors and officers to liability is unpredictable. If in fact the goal of these statutory revisions is to enhance the insurability of directors' litigation risks by reducing directors' liability, the uncertain effect of some of these statutes could undercut enhanced insurability. In addition some of these provisions are drafted in a highly detailed style that, perversely enough, makes it difficult to determine precisely the situations to which they do and do not apply. Extreme particularization of this sort runs counter to the conventional wisdom that general corporation statutes should be drafted consistently with a preference for general as opposed to narrow applicability and for prescribing broad standards that apply to more rather than fewer types of transactions. Finally, the clear impetus for enacting the provisions was the perceived crisis in the availability of D & O insurance for directors of public companies. Many statutes, however, apply much more broadly, permitting the reduction of directors' liability in all corporations, including closely-held ones, and, in some states, in relationship to claims that raise issues of the defendant's loyalty to the corporation.

II. THE DELAWARE STATUTE AND ITS COUNTERPARTS

A. The Delaware Statute

The Delaware general corporation statute was amended in 1986 to authorize corporations to include language in their certificates of incorporation that eliminates or limits a director's monetary liability for breach of fiduciary duty, subject to specified restrictions and exclusions. For firms already incorporated in Delaware, such a provision could be added to the firm's certificate through a certificate amendment. Section 102(b)(7) of the statute permits "[a] provision eliminating or limiting the personal liability of a director to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director." Under the statute, no such provision may eliminate or limit a director's liability

17. See infra note 22.
(i) for any breach of the director's duty of loyalty to the corporation or its stockholders; (ii) for acts or omissions not in good faith or which involve intentional misconduct or knowing violation of law; (iii) under section 174 . . . ; (iv) for any transaction from which the director derived an improper personal benefit. 19

Section 174 imposes joint and several liability on directors under whose administration a corporation unlawfully pays a dividend or unlawfully purchases or redeems stock. 20 Finally, under section 102(b)(7) no certificate provision may "eliminate or reduce the liability of a director for any act or omission occurring prior to the date when such provision became effective." 21

The limited scope and effect of the certificate provisions authorized by section 102(b)(7) is significant. First, in order to invoke the protection of this section, an existing Delaware corporation must take the affirmative steps necessary to amend its certificate. 22 The provisions authorized by the statute cannot eliminate, limit or reduce directors' duties to the corporation or redefine the acts that constitute breaches of those duties. Additionally, the certificate provision can cover only directors and not officers or other agents of the corporation and can affect only liability arising from acts as a director. Furthermore, the provision will reach only money damages. Other types of remedies—such as injunctions—and other types of defendants are outside the scope of authorized provisions. The statute also defines broadly the types of breaches of fiduciary duty against which such a provision would be ineffective; as a result, only claims that a director breached a fiduciary duty of care, uncomplicated by any breach of the director's duty of loyalty, would be affected by certificate provisions authorized by the statute.

Moreover, section 102(b)(7) does not address claims against third parties who benefit as a consequence of the directors' breach of their duty of care. Consider, for example, a claim that a corporation's directors breached their duty of care in connection with a sale of assets owned by the corporation, so that the purchaser of the assets benefitted by acquiring them for less than their value. 23 Conventional principles of restitution oblige the third party, under some circumstances, to disgorge the

19. Id.
20. Id. § 174.
21. Id. § 102(b)(7).
benefit received. Section 138(2) of the Restatement of Restitution provides that "[a] third person who has colluded with a fiduciary in committing a breach of duty, and who obtained a benefit therefrom, is under a duty of restitution to the beneficiary." For that matter, even an innocent recipient of benefit derived from another's wrongful act is obliged to make restitution to the person from whom the benefit was obtained, unless the innocent recipient gave value for the benefit. Innocent recipients, however, are not liable for gains or profits realized through their subsequent use of the property received; their liability is limited to the immediate benefit realized through the defendant's breach.

Unfortunately, at least for the purposes of this article, the import of these well-established principles for the problems under discussion awaits development in the case law. The limitations on directors' liability permitted by section 102(b)(7) and its counterparts in other states may nurture this development. Obvious issues include defining "collusion" and measuring the benefit received by the third party. A less obvious question is whether an appropriately-drafted certificate provision could ever reduce or eliminate a third party's liability to make restitution for a benefit it derived from directors' breach of duty. If a corporation's shareholders adopt a certificate provision that explicitly reduces or eliminates the restitutary liability of third parties benefitted by any breach by its directors of their duty of care, should the provision be effective? It is noteworthy that most of the rationales given for permitting the reduction of directors' liability are inapplicable to third parties. Directors, but not third parties, run the risk of liability for damages greatly in excess of the economic benefits they receive from serving the corporation. The costs


26. Id. at 224-25.

27. If the plaintiff can establish that the third party knew of the directors' breach, is that showing sufficient to establish collusion? Or is an affirmative contribution to the directors' breach by the third party a requisite for collusion?

These issues can usefully be examined from the perspective of the purchaser of corporate assets described in the example in the text. On the one hand, typically purchasers do not wish to incur obligations to pay more for, or to return, the assets they are negotiating to acquire. On the other hand, typically purchasers do not wish to agree to pay more for assets which the seller is willing to sell for less. When do principles of restitution oblige the prospective purchaser to offer to pay more? Or to inform the seller that, as purchaser, it distrusts the seller's conduct?
of their D & O coverage reflect this risk. The third party's liability, in contrast, is precisely to make restitution for the benefit received. Supporters of liability-reducing provisions also argue that, in their absence, directors are under pressures to behave too cautiously and to avoid risky business ventures. The risk of restitutionary liability borne by third parties may affect their behavior, but less visibly so, and less substantially, given the restitutionary measure of recovery.

Finally, a useful analogy can be drawn to the law of trusts, which is more fully developed on these points. The law of trusts permits and enforces exculpatory provisions in trust instruments that relieve the trustee of personal liability for some forms of breach of trust. But the liability of third parties—typically transferees of trust property—who benefit from the trustee's breach of trust is governed by the circumstances of the transfer and by the transferee's knowledge of the breach.

B. Other States' Statutes

A number of states adopted statutory authorizations for such provisions using language substantially identical to that in the Delaware statute. In other states, the statutory enabling language diverges significantly from the Delaware pattern. Key points of divergence are: (1) the types of plaintiffs and litigation that the certificate provision can reach; (2) the types of potential defendants whose liability the certificate

29. See id. at 249.
30. But see id. § 7.17, Reporter's Note 2, at 269 (analogy to law of trusts is "hardly apposite" in case of publicly held company because law of trusts contemplates true bargaining between settlor and trustee whereas certificates of incorporation of public companies are contracts of adhesion that are read by few shareholders).
31. See Restatement (Second) of Torts § 222 (1959).
32. See id. §§ 284 & 287-93.

The Arkansas authorization is comparable to Delaware in its effect. It contains an additional exception "[f]or any action, omission, transaction or breach of a director's duty creating any third-party liability to any person or entity other than the corporation or stockholder." But, like the Delaware statute, the Arkansas statute authorizes only provisions respecting a director's liability to the corporation or its stockholders. See Ark. Stat. Ann. tit. 4, § 4-27-202(B)(3) (Supp. 1987).
provisions can affect; (3) the types of conduct and claims resulting in liability that cannot be reduced or eliminated; (4) whether any reference is made to statutory standards for directors’ conduct or indemnification of directors; and (5) whether the statute expressly excludes the retroactive application of a certificate provision for events occurring prior to its adoption. Furthermore, effective adoption of an amendment to a corporation’s certificate or articles of incorporation obviously requires that a corporation comply with the amendment procedures that the corporation statute of the corporation’s state of incorporation prescribes. Among the states expressly permitting provisions of the sort under discussion, only Pennsylvania requires that the provision be contained in a bylaw adopted by the corporation’s shareholders, rather than placed in its articles or certificate of incorporation. 34

1. Type of plaintiffs and litigation

The enabling language in the Delaware statute authorizes provisions that eliminate or limit a director’s liability, “to the corporation or its stockholders . . . for breach of fiduciary duty as a director.” 35 Under this language, a certificate provision could reduce or eliminate directors’ liability in actions brought by the corporation itself as plaintiff, brought derivatively on the corporation’s behalf, or brought by shareholders asserting claims individually or as a class. If an action alleges claims other than breach of fiduciary duty—such as breach of contract—the authorized provision would presumably be inapplicable. In contrast, the California statute permits only provisions that eliminate or reduce a director’s liability “in an action brought by or in the right of a corporation for breach of a director’s duties to the corporation and its shareholders as set forth in section 309.” 36 Section 309 requires directors to perform their duties in good faith and with the care, including reasonable inquiry, that an ordinarily prudent person in a like position would use in similar circumstances. 37 If the action is not brought by or in the right of the corporation, the liability-reducing provision would not apply. Thus, the California enabling language does not reach actions that shareholders bring singly or as a class which allege that directors breached their duties, including those defined by section 309. This limitation is of practical

34. See 42 PA. CONS. STAT. ANN. § 8364 (Purdon 1987).
35. See supra note 22.
significance in California because California's courts have long recognized that directors owe fiduciary duties directly to the corporation's shareholders as well as to the corporate entity itself.\textsuperscript{38}

South Dakota and North Carolina statutes authorize certificate provisions that extend to a broader range of plaintiffs than does Delaware's statute. The South Dakota statute authorizes a provision "eliminating or limiting the personal liability of a director to the corporation, its shareholders, policy holders or depositors for monetary damages for breach of fiduciary duty as a director."\textsuperscript{39} The inclusion of policyholders and depositors is striking because they are creditors of the corporation and because the statute does not require their consent to the shareholders' amendment of the corporation's articles of incorporation.\textsuperscript{40} It strains credulity to believe that bank depositors or purchasers of insurance policies would be aware of such limitations in the charter of their bank or insurance company. Similarly, the North Carolina statutory language authorizes a provision "limiting or eliminating the personal liability of each director arising out of an action whether by or in the right of the corporation or otherwise for monetary damages for breach of his duty as a director."\textsuperscript{41} On its face, the phrase "or otherwise" appears to embrace actions in which the plaintiff is a creditor of the corporation.

2. Types of defendants

Like the Delaware statute, most states' statutes limit the protective scope of authorized provisions to directors, for claims based on the person's actions or omissions as director. In contrast, the statutory enabling language in Louisiana\textsuperscript{42} and Nevada\textsuperscript{43} permits the inclusion of officers in the provision.

The New Jersey statute permits certificate provisions limiting or eliminating officers' liability for money damages.\textsuperscript{44} The enabling authority for such provisions, however, was enacted in New Jersey with a two year


\textsuperscript{39} S.D. CODIFIED LAWS ANN. § 47-2-58.8 (Supp. 1987).

\textsuperscript{40} See id. §§ 47-2-11, -12 (1983).

\textsuperscript{41} N.C. GEN. STAT. § 55-7(11) (Supp. 1987).


"sunset" provision, so that statutory authority for certificate provisions limiting officers' liability will expire in February 1989 unless the legislature affirmatively acts to renew the authority. The sunset feature does not apply to the statutory authority for provisions limiting or eliminating directors' liability. Presumably, duly-adopted certificate provisions that affect officers' liability would survive the demise of the statutory authorization.

3. Prohibitions on reductions of liability

No state permits universal elimination of directors' liability for all claims, regardless of their basis. Indeed, many states, like Delaware, structure their statute's enabling language so that only claims alleging breach of the directors' duty of care effectively are reached. Nonetheless, state statutes vary significantly in defining the types of liability that cannot be eliminated or reduced. Georgia and North Carolina, in contrast with Delaware, do not generally prohibit the reduction of liability arising from directors' breaches of their duty of loyalty. The Georgia statute prohibits the elimination or reduction of a director's liability for "any appropriation, in violation of his duties, of any business opportunity of the corporation," acts or omissions not in good faith or involving intentional misconduct or a knowing violation of law, illegal distributions to shareholders, and any transaction from which the director derived an improper personal benefit.

Even fewer categories of liability are not susceptible of reduction under the North Carolina statute: "acts or omissions not made in good faith that the director at the time of such breach knew or believed were in conflict with the best interests of the corporation"; liability for illegal distributions; and transactions from which the director derived an improper personal benefit. In the absence of a personal benefit to the director, a director's liability stemming from a transaction in which the director had a conflicting interest (but acted in good faith) can thus be excluded under the North Carolina statute. Furthermore, the statute provides that "improper personal benefit" does not include a director's compensation or other incidental benefit for or on account of his service.

47. See N.C. GEN. STAT. § 55-7(11) (Supp. 1987).
as a director, officer, employee, independent contractor, attorney or consultant of the corporation." 50 Thus, under the North Carolina statute, a certificate provision can effectively insulate a director from liability stemming from the director's receipt of excessive compensation from the corporation, regardless of the capacity in which the director received the compensation. And, as noted above, the North Carolina statute purports to authorize certificate provisions applicable to all types of plaintiffs, including creditors, trustees in bankruptcy and the Internal Revenue Service!

Nonetheless, the practical impact of certificate provisions authorized by the Georgia and North Carolina statutes can be difficult to evaluate. Suppose a director of a bank also serves as a director of a real estate development corporation. If the bank makes loans to the real estate developer, the common director clearly has a conflicting interest with regard to the loan transaction even though the loan is not made to him directly. Indeed, a conflict of interest exists even if the common director does not own a substantial amount of equity in the real estate developer. If the borrower defaults on the loan, and the banking corporation is injured as a result, certificate provisions authorized by the Georgia and North Carolina statutes could reduce or eliminate any liability incurred by the banking corporation's directors, including the director in common with the real estate developer, so long as the director acted in good faith and did not derive an "improper personal benefit" from the transaction. What does this phrase mean? If the common director is paid a commission by the developer (a "loan origination" fee of sorts), surely that is a personal benefit derived from the loan that is "improper" under conventional fiduciary analysis. Suppose that the common director receives from the real estate developer only the same director's fee it pays to all directors. The fee is surely a "personal benefit," but is it an "improper" personal benefit? Suppose the common director neglects to disclose to the corporation's shareholders, and her fellow directors, that she serves the real estate developer as a director and is paid for so doing. Has she acted in "good faith"?

In this connection, it is noteworthy that these provisions in the Georgia and North Carolina statutes omit any reference to pre-existing statutory sections dealing with directors' conflicts of interest 51 and the

50. Id.
consequences of not disclosing them to fellow directors prior to the board’s approval of a transaction in which a director has an adverse interest. In any event, it is difficult to argue, as a general matter, that the fee for serving as a director of the real estate developer is "derived from" the loan transaction.

On the other hand, certificate provisions of the type under discussion do not affect the corporation's ability to avoid transactions in which its directors had conflicting interests. Under the Georgia and North Carolina corporation statutes, unless a quorum of disinterested directors or the corporation's shareholders approve the transaction after full disclosure of the conflict of interest, the transaction is voidable unless its proponents establish that it is fair to the corporation. Thus, a certificate provision reducing or eliminating a director's liability for money damages is not pertinent if the issue is the corporation's ability to avoid the transaction. If the issue is instead the director's liability for damages in the wake of an unfortunate transaction, then the Georgia and North Carolina statutes authorize the reduction of directors' monetary liability even if the directors' conduct affecting the transaction did not meet the statutory standard prescribing conditions to make the transaction enforceable against the corporation. That is, unless the director derived an improper personal benefit from the transaction or failed to act in good faith, he is not financially liable for the transaction's untoward consequences, even if the director failed to disclose a conflicting interest prior to the directors' authorization of the transaction, and even if, as of the time of its adoption, the transaction was not fair to the corporation.

Moreover, the structure of these statutes undercuts an argument that a director's failure to disclose the conflicting interest in itself establishes that the director did not act in good faith. In both statutes, the sections dealing with transactions in which directors had conflicting interests expressly provide for disclosure of the director's conflicting interest as a route through which the transaction may be made enforceable against the corporation. That the director with the conflicting interest "acted in good faith" is not an express criterion. Thus, against this background, an equation of "acting in good faith" with prior disclosure of the director's conflicting interest is difficult to justify. And suppose the director is able to establish that he believed the transaction to be beneficial for the corpo-

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ration. Arguably the director "acted in good faith" despite his failure to disclose a conflicting interest. In short, these statutes create a troubling discontinuity between the standards for directors' liability for the consequences of transactions, and the standards regulating director conduct preceding corporate involvement in transactions. To the extent they undercut incentives for disclosure by directors of conflicting interests, their effect is likely to be unfortunate.\(^{54}\)

The Washington statute likewise defines narrowly the types of liability that cannot be reduced or eliminated through certificate provisions. Washington prohibits the elimination or reduction of liability for acts or omissions that involve knowing violations of law or intentional misconduct, illegal distributions to shareholders, and "for any transaction from which the director will receive a benefit in money, property, or services to which the director is not legally entitled."\(^{55}\) In the absence of personal benefit to the director, that the director did not act in good faith, or that the director had a conflicting interest as to a transaction, would not preclude the elimination or reduction of the director's liability under this statute. Indeed, the Washington statute appears to authorize provisions that exculpate directors who fail to disclose the existence of a conflicting interest, as well as directors who fail to act in good faith. Thus, arguably under this statute a certificate provision could exculpate from liability a director with a conflicting interest in a transaction who neither disclosed the existence of that interest to his fellow directors prior to their approval of the transaction, nor honestly believed the transaction to be beneficial to the corporation.

In contrast, the Tennessee statute does not expressly prohibit the reduction or elimination of liability when the director has received an improper personal benefit from a transaction. Like Delaware, however, Tennessee’s statute prohibits the reduction or elimination of any liability arising from breaches of the director’s duty of loyalty.\(^{56}\)

Finally, under the New York statute, whether a particular director’s liability can be eliminated or limited turns on the outcome of litigation: [no certificate provision shall eliminate or limit] the liability of any director if a judgment or other final adjudication adverse to him establishes that his

\(^{54}\) Cf. Gelb, supra note 12, at 35 (indeterminacy of good faith criterion); see generally Barnard, Curbing Management Conflict of Interest—The Search for an Effective Deterrent, 40 RUTGERS L. REV. 369 (1988) (inadequacy of present deterrents to managerial self-dealing).


\(^{56}\) TENN. CODE ANN. § 48-12-102(b)(3) (Supp. 1987).
acts or omissions were in bad faith or involved intentional misconduct or a knowing violation of law or that he personally gained in fact a financial profit or other advantage to which he was not legally entitled or that he violated the statutory restrictions on distributions to shareholders. 57

Presumably, if the litigation is resolved through settlement without any judgment or final adjudication establishing such matters, the director's liability could be eliminated or limited through the certificate provision. As a practical matter, the structure of the New York statute provides a large disincentive to a plaintiff to settle an action contesting whether a director's conduct met the statutory standards for permissible exculpation.

4. Reference to statutory standards for directors' conduct or indemnification of directors

An obvious technical issue, which regrettably only a few statutes address, is the relationship between authorized provisions that reduce or limit directors' liability and the standards for directors' conduct and liability that are specified by statute, as well as statutory provisions that regulate corporate indemnification of directors. The Delaware corporation statute contains no statutory definition of the standard of conduct with which directors must discharge their duties and thus has no counterpart to California Corporations Code section 309, discussed above. 58

Not surprisingly, the Delaware statutory provision that authorizes the reduction or elimination of directors' liability makes no cross reference to a statutory standard applicable to directors' conduct in office. What is surprising is that a number of states which specify by statute the standards for directors' discharge of their duties neglect to refer to these standards in the additional statutory provision authorizing the reduction or elimination of directors' liability through charter provisions. In the interests of clarity it is desirable that reference be made to such standards in the statutory language authorizing certificate provisions that reduce or eliminate directors' liability for money damages for breach of their duties.

Indeed, Tennessee enacted a new corporation statute, effective in January 1988, that authorizes charter provisions "eliminating or limiting the personal liability of a director to the corporation or its shareholders for

58. See supra text accompanying note 19.
monetary damages for breach of fiduciary duty as a director."\[59\] This section of the statute, however, makes no reference to the section prescribing the standards for directors' discharge of their duties, which concludes with the statement that "[a] director is not liable for any action taken as a director, or any failure to take any action, if he performed the duties of his office in compliance with this section."\[60\] If the statute's drafters intended for charter provisions to reduce or eliminate the liability of a director whose conduct failed to meet the standard specified in the statute, greater clarity would have been achieved by expressly stating so.\[61\]

Several of the statutes that authorize provisions to reduce or eliminate directors' liability omit any cross reference between that section and the statute's regulation of indemnification. Thus, the following questions, among others, may arise: (1) Even if the director, by virtue of an authorized certificate provision, is not liable for money damages in an action, under what circumstances may the corporation indemnify the director for litigation expenses incurred in the defense of the action? (2) If the director makes a monetary contribution to the settlement of the action, may the corporation indemnify the director in that amount? (3) If the director's liability cannot be excluded by an authorized certificate provision, then when will the director's litigation expenses and contribution to any settlement or judgment be indemnifiable by the corporation? An example of useful cross-referencing is a provision in the Georgia treatment of indemnification. This provision explicitly provides that liabilities that cannot be reduced or eliminated through a provision in the corporation's articles cannot be the object of claims to indemnity that were created by a contract or corporate bylaw or a corporate resolution, beyond the statute's own provision for and regulation of indemnification.\[62\] Additional issues in this context raised by the statutory regulation of indemnification are discussed in Section V.

\[59\] TENN. CODE ANN. § 48-12-102(b)(3) (Supp. 1987).
\[60\] Id. § 48-18-301(d).
\[61\] Additional technical questions are raised by the general failure of these statutory authorizations to refer expressly to the statute's general treatment of self-dealing transactions between directors and the companies they serve. A notable exception is Section 10-054(A)(9) of the Revised Statutes of Arizona (Supp. 1987), which excludes from the scope of permissible limitations on liability "[a] violation of § 10-041," which is the statute's general treatment of conflict of interest transactions.

5. Retroactive effect

Under the Delaware statute, a director's liability arising from an act or omission that occurred prior to the date upon which the corporation effectively adopted the provision reducing or eliminating directors' liability cannot be affected by the provision.\(^{63}\) Although most states' statutes contain a comparable express exclusion, the Texas statute does not.\(^{64}\) If shareholders, under this statute, adopt a general provision that purports to relieve directors from liability arising from prior acts or omissions, the shareholders would not necessarily have notice of any particular acts or omissions that might have given rise to liability. If the shareholders lacked such notice, it is not likely that their adoption of the general provision will be effective in releasing the directors from liability for prior undisclosed acts or omissions. How can shareholders release a claim on behalf of the corporation or themselves if they do not know what the claim consists of? In short, persuading shareholders to adopt such a provision is not likely to be an effective end run around the disclosure requisite to an effective ratification of prior acts by the corporation's directors.

III. STATUTORY STANDARDS FOR DIRECTORS' LIABILITY

In contrast to the enabling legislation in Delaware and its counterparts elsewhere, some states, in 1986 and 1987, adopted statutes that specified the circumstances under which a director's breach would result in personal liability. The statutes were to reduce the effective risk to directors. The approaches taken by these statutes vary considerably, and some of the provisions are afflicted with technical difficulties.

The 1987 amendments to the Florida statute probably raise the largest number of technical questions, due to the drafters' proclivity for differentiated treatment of liability depending on the plaintiff's identity. Section 607.1545 of the Florida Corporation Act, added in 1987, provides that a director shall not be personally liable for money damages, "to the corporation or any other person for any statement, vote, decision, or failure to act, regarding corporate management or policy" unless the director breached or failed to perform his duties and that breach or failure fits within one of five enumerated categories.\(^{65}\) The first three of these are of general applicability. They are: (1) a violation of criminal law, "unless

\(^{63}\) DEL. CODE ANN. tit. 8, § 102(b)(7) (Michie Supp. 1986).
\(^{64}\) See TEX. BUS. CORP. ACT ANN. art. 7.06(B) (Vernon Supp. 1988).
the director had reasonable cause to believe his conduct was lawful or had no reasonable cause to believe his conduct was unlawful”; (2) a transaction from which the director directly or indirectly derived an improper personal benefit; and (3) an illegal distribution to shareholders. If the action is brought by the corporation itself, or in its right, or in the right of a shareholder, then the fourth category applies: “conscious disregard for the best interest of the corporation, or willful misconduct.” If the action is brought by a plaintiff other than a shareholder or the corporation or a shareholder suing on behalf of the corporation, the fifth category is applicable: “recklessness or an act or omission which was committed in bad faith or with malicious purpose or in a manner exhibiting wanton and willful disregard of human rights, safety, or property.”

A separate subsection of section 607.1645, as it happens, contains a narrow definition of “recklessness,” discussed below.

Moreover, a subsequent section of the statute defines “improper personal benefit” in a fashion that may raise insurmountable technical obstacles to its interpretation. The section, however, appears designed to preclude the argument that a director has derived an “improper personal benefit” from a transaction if a majority of the corporation’s disinterested directors, after disclosure to them of the nature of the personal benefit, approved or ratified the transaction. None of the Florida statutory provisions state whether they apply only to claims arising after their effective date. Further complicating the analysis is the omission from these 1987 statutory amendments of any reference to the statute’s pre-existing section requiring directors to perform their duties in good faith and with that degree of care which an ordinarily prudent person would deploy

66. Id. § (1)(b)(4).

67. Note that this provision on its face applies to actions brought by “any other person,” other than the corporation itself or its shareholders. Id. § (1)(b)(5).

68. Fla. Stat. Ann. § 607.1645(2) (West Supp. 1988). This subsection defines “recklessness” as an action or omission “in conscious disregard of a risk” known or so obvious it should have been known to the director, “as to make it highly probable that harm would follow from such action or omission.” Under this standard, the magnitude of the risk, that is its propensity to result in harm, is a component of what the director “consciously” disregards.

69. See Id. § 607.165. One difficulty is that subsection (1)(a) is constructed grammatically to resist successful parsing. It provides: “[A] director is deemed not to have derived an improper personal benefit ... [i]n an action other than a derivative suit regarding a decision by the director regarding a decision by the director to approve, reject, or otherwise affect the outcome of an offer to purchase the stock of... the corporation....” To what actions does this subsection apply? All non-derivative actions? All non-derivative actions as well as all derivative actions, other than derivative actions concerning director’s decisions regarding offers to purchase the corporation’s shares?

70. Id. § 607.165(1)(a).
under similar circumstances.\textsuperscript{71}

Given their structure and scope, the Florida provisions raise a number of perplexing questions. Suppose the director of a bank knows, or should know, that its officers are making loans to their close associates on terms more favorable than the terms upon which the bank makes loans available to non-insiders. If the bank subsequently fails, and an action is brought on behalf of its creditors, depositors or the depositors' insurer, the director's liability should presumably be assessed under the "recklessness" standard described above, unless the loan transactions were illegal or conferred a direct or indirect personal benefit on the director. Under the statute's definition of "reckless" behavior, the director's action (in approving the loans) or omission (in failing to object to them) is not culpable unless the director proceeded "in conscious disregard" of a risk known or so obvious that it should have been known to the director. Additionally, under the statutory definition the director's conduct is not reckless unless the risk was known to be, or obviously was, one that made it "highly probably that harm would follow" from the director's act or omission. Thus, in the example under discussion, the director's conduct is not reckless unless the hapless bank is so unfortunate as to have only insider loans or default-prone borrowers in its loan portfolio, or unless a particular loan can be identified which itself made the bank's failure highly probable, or perhaps unless the particular loan was known to bear a "highly probable" risk of default. Further, unless the director has actual knowledge of the loans, the "conscious disregard" test is impossible to apply.

Additionally, unless the director received a personal benefit from the transaction, actions brought directly against the director herself by the corporation are subject to the "conscious disregard" or "wilful misconduct" standard. If the director has a conflicting interest in a particular transaction, but receives no personal benefit from it, the corporation cannot recover unless the director acted with "conscious disregard" of its best interests. This standard applies awkwardly, at best, to many situations. Suppose the director neglects to disclose his conflicting interest to fellow directors prior to their approval of the problematic transaction. Does the failure to disclose alone constitute "wilful misconduct" or "conscious disregard" of the corporation's best interests? Or does it con-

\textsuperscript{71} See id. § 607.111(4) (West 1976). Subsection (7) provides that "[a] person who performs his duties in compliance with this section shall have no liability by reason of being or having been a director of the corporation."
stitute bad faith? Finally, like the provisions in the North Carolina and Georgia statutes discussed above, these amendments to the Florida statute make no reference to the statute's pre-existing treatment of director conflicts of interest.72

Unlike the Florida statute, the Ohio statute integrated the 1986 amendments into a pre-existing section specifying directors' duties to the corporation. As amended, section 1701.59(B) of the General Corporation Law requires a director to perform his duties in good faith, in a manner "he reasonably believes to be in or not opposed to the best interests of the corporation, and with the care that an ordinary prudent person in a like position would use under similar circumstances."73 In any action brought against a director, the plaintiff must prove "by clear and convincing evidence," that the director violated his statutory duties.74 As written, the "clear and convincing" standard would apply to all actions against directors, including actions brought by creditors and actions contesting transactions in which a director had a conflicting interest. Under a separate subsection of the statute, a director is liable for money damages, "only if it is proved by clear and convincing evidence . . . that his action or failure to act involved an act or omission undertaken with deliberate intent to cause injury to the corporation or undertaken with reckless disregard for the best interests of the corporation."75 The applicability of the restriction on directors' liability for money damages is limited. It does not apply to actions involving illegal distributions or loans to officers, directors, or shareholders made other than in the usual course of business.76 Nor does it limit the relief available under the general statutory regulation of transactions between the corporation and its directors or officers.77 Additionally, a corporation may opt out of this limitation on directors' liability for money damages through a provision in its articles or bylaws.78

Under the Ohio statute, none of these restrictions on directors' liability (including the "clear and convincing" standard) applies to a director of a corporation whose shares are not publicly traded, if that director votes for or assents to any action taken by the corporation's directors that "in

72. See id. § 607.124.
73. OHIO REV. CODE ANN. § 1701.59(B) (Anderson Supp. 1987).
74. Id. § 1701.59(C).
75. Id. § 1701.59(D).
76. See id. § 1701.95.
77. See id. § 1701.60.
78. See id. § 1701.59(D).
connection with a change in control of the corporation, directly results in
the holder or holders of a majority of the outstanding shares of the cor-
poration receiving a greater consideration for their shares than other
shareholders." Otherwise, by implication, the restrictions on directors' liabil-
ity appear to apply. Why, one wonders, is this exception applicable
only to actions against directors of corporations whose shares are not
publicly traded? If preferential treatment of majority shareholders is in-
jurious to minority shareholders, the injury seems no less if the corpo-
ration's shares are publicly traded.

Wisconsin, like Ohio, amended its corporation statute to define nar-
willy the circumstances under which directors could be held liable for
money damages. Like Ohio, Wisconsin expressly permits corporations
to opt out from the limitation. In contrast with the Ohio statute, which
applies to all actions contesting directors' discharge of their duties as di-
rectors, the Wisconsin provision applies more narrowly. It provides
that "a director is not liable to the corporation, its shareholders, or any
person asserting rights on behalf of the corporation or its sharehold-
ers." In such litigation, the director is not liable for any monetary lia-
ibility unless the plaintiff proves that the director's breach or failure to
perform constituted (1) "[a] wilful failure to deal fairly with the corpo-
ration or its shareholders in connection with a matter in which the director
has a material conflict of interest"; (2) a violation of criminal law, unless
the director had reasonable cause to believe his conduct lawful or had no
reasonable cause to believe it unlawful; (3) a transaction from which the
director derived an improper personal benefit; or (4) wilful misconduct.
Like the Ohio limitation, the Wisconsin limitation does not apply to ille-
gal distributions to shareholders or to insider loans. Unlike Ohio, Wis-
consin imposes no special burden of proof on plaintiffs litigating against
directors. A corporation may opt out of the Wisconsin limitation
through a certificate provision.

Indiana, Missouri and New York have revised their corporation stat-
utes to reduce directors' risk of liability, although these revisions are
troublesome in somewhat different respects. The Indiana amendment
provides that a director is not liable for any action taken as a director or

79. Id. § 1701.59(F).
80. See id. § 1701.59(B), (C), (D) & (F)(1).
82. Id. § 180.307(1)(a)-(d).
83. See id. § 180.307(3).

http://openscholarship.wustl.edu/law_lawreview/vol66/iss2/4
any failure to take action unless the director breached or failed to perform the duties of a director that the statute prescribes, and, "[t]he breach or failure to perform constitutes willful misconduct or recklessness." Note that this standard applies even to actions against a director involving transactions in which the director had a conflicting interest, and applies regardless of the identity of the plaintiff.

The Missouri and New York amendments expand the criteria that directors may properly take into account in evaluating proposals to acquire the company that they serve as directors. Under the Missouri statute, in evaluating an acquisition proposal, directors exercising their business judgment “may consider” a number of factors provided for in the statute. The stated factors include “[s]ocial, legal and economic effects on employees, suppliers, customers and others having similar relationships with the corporation, and the communities in which the corporation conducts its businesses.” The stated factors, however, are not exclusive. In contrast, the New York statute provides that in this context “a director shall be entitled to consider, without limitation, both the long-term and short-term interests of the corporation and its shareholders.” Both of these provisions are by their terms merely permissive, and thus do not appear to impose on the directors a duty or obligation to consider the stated criteria.

Although narrower in scope, the Missouri and New York provisions resemble in other respects statutory provisions in Ohio and Minnesota which articulate a variety of interests and factors that directors may appropriately take into account in discharging their duties to the corporation. Under the Minnesota statute, a director “may, in considering the best interests of the corporation,” in discharging the duties of a director “consider the interests of the corporation’s employees, customers, suppliers and creditors, the economy of the state and nation, community and societal considerations, and the long-term as well as the short-term interests of the corporation and its shareholders.” Although the Minnesota statute concludes that directors may consider the possibility that these interests will best be served if the corporation continues to be independ-

86. N.Y. BUS. CORP. LAW § 717(b) (McKinney Supp. 1988).
88. N.Y. BUS. CORP. LAW § 717(b) (McKinney Supp. 1988).
ent, the statute is not limited in its effect to directors' consideration of acquisition proposals. Likewise, although the Ohio statute mentions "continued independence of the corporation" as a factor directors may appropriately consider, it permits directors to take into account the panoply of interests endorsed by the Minnesota statute in the context of all decisions made by the directors, not only those responsive to acquisition proposals. 90 Thus, three of these statutes—Minnesota, Missouri and Ohio—expressly permit directors to consider—and by implication to act with reference to—interests other than those of the corporation itself and its shareholders. Taken at face value, these statutes endorse a stunning departure from the fiduciary constraints applicable to directors' decisions. In sharp contrast, the Delaware Supreme Court held in Revlon, Inc. v. MacAndrews & Forbes Holding, Inc. 91 that when a company is for sale, the board's sole duty is to maximize its sale value for the stockholders' benefit. 92 By enlarging the range of interests directors may consider (when a company is "for sale" and in other contexts as well) these statutes may well vitiate the strength of fiduciary accountability. Once loyalty to the interests of the corporation and its shareholders is treated as merely another "factor" directors may consider, fiduciary obligation is effectively trivialized.

IV. STATUTORY CAPS ON LIABILITY

Directors' liability for money damages may also be reduced through the imposition, by statute, of a maximum amount for which directors may be held liable for specified types of claims. Key issues concerning liability caps are the types of claims (and the types of potential plaintiffs) reached by the cap and the ability of shareholders of any particular corporation to opt into or out of the cap. The reporters for the ALI corporate governance project have proposed that corporations be permitted in their certificates of incorporation to establish a ceiling on officers' and directors' liability for breaches of their duty of care to the corporation, or to limit or preclude directors' liability for damages altogether. The ceiling amount would be related to the amount of compensation that the

91. 506 A.2d 173 (Del. 1986).
92. Id. at 182; accord Edelman v. Fruehauf Corp., 798 F.2d 882, 886-87 (6th Cir. 1986) (applying Michigan law).
The Virginia Stock Corporation Act was amended in 1987 to impose a specific cap on monetary damages recoverable from officers and directors "in any proceeding brought by or in the right of a corporation or brought by or on behalf of the shareholders of the corporation."94 The cap applicable to derivative or shareholder litigation is, for any single transaction, occurrence or course of conduct, the lesser of (1) the monetary amount specified in the corporation’s articles or in a bylaw adopted by its shareholders; or (2) the greater of (a) $100,000 or (b) the cash compensation received by the officer or director in the twelve months preceding the action or omission at issue.95 Note that the formula in the Virginia statute is structured to permit a corporation to specify an amount less than $100,000 or the cash compensation amount, but not a greater amount. Thus, "opting out" of the cap is not possible. In this respect, the Virginia statute differs from the ALI proposal discussed above, which requires "opting in" through the adoption of a charter provision, as well as the Delaware-pattern statutes, which merely authorize the adoption of charter provisions to "reduce or eliminate" directors’ liability. And the Virginia cap provisions apply to officers as well as directors. Under the Virginia statute, the cap does not apply if the officer or director engaged in willful misconduct, a knowing violation of the criminal law or of any federal or state securities law.96 But, in contrast to charter provisions that the Delaware statute authorizes, the Virginia cap presumably applies to actions alleging self-dealing by the director or officer and to circumstances in which the director or officer did not act in good faith, unless the director’s or officer’s behavior constituted "willful misconduct."97

V. INDEMNIFICATION AND INSURANCE

Directors, like other defendants, bear certain financial risks created by litigation even if no final judgment ever finds them liable. These risks include incurring expenses for defending against the action and agreeing

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95. Id. § 13.1-692.1(A).
96. Id. § 13.1-692.1(B).
to pay settlement amounts even if the suit never reaches the point of final judgment on the merits. Corporation statutes regulate the corporation's ability to reduce the financial consequences of litigation for its directors, employers and agents by indemnifying them against judgment and settlement amounts, and the expenses of defense, and by paying their litigation expenses as the expenses are incurred. In 1986 and 1987, a number of states amended their statutory regulations of indemnification, in a variety of ways. These changes affected the availability of indemnification to corporate directors, employees and agents.

The most significant of these changes have the effect of enabling more persons' claims for indemnification to be presented as mandatory claims on the corporation, so that the issue is not the corporation's discretionary right to indemnify but its obligation to do so. This shift is of evident value to prospective indemnitees because it provides some insulation against a change in the identity of the persons in control of the corporation. True, corporations are occasionally reported to resist paying mandatory claims for indemnification,98 but such claimants at least have legally cognizable rights created by contract or statute.

Most corporation statutes have long-standing provisions mandating that a corporation indemnify its directors, employees and agents for their litigation expenses if they are successful in defending against the action.99 In Minnesota, and more recently in North Dakota and Wisconsin, essentially all indemnification pursuant to the statute is mandatory if the claimant's conduct fits within the statutory requisites.100 For example, under the Wisconsin statute, subject to contrary provision in the corporation's articles, the corporation is obliged to indemnify an officer or director to the extent he is successful on the merits or otherwise in a proceeding;101 additionally, the corporation must indemnify against liability that a director or officer incurs in a proceeding brought against him by virtue of his position with the corporation, unless his breach or failure to perform fits within any of four categories of conduct.102 These four

99. See, e.g., DEL. CODE ANN., tit. 8, § 145(c)(1979) (success “on the merits or otherwise”); REV. MODEL BUS. CORP. ACT § 8.52 (“wholly successful, on the merits or otherwise”); CAL. CORP. CODE § 317(d)(West 1977) (indemnification of expenses mandatory to the extent the agent has been “successful on the merits”).
102. See id.
categories are: "wilful failure to deal fairly with the corporation or its shareholders in a matter in which the director or officer has a material conflict of interest"; a violation of criminal law unless the defendant lacked reasonable cause to believe his conduct unlawful; a transaction from which the defendant deprived an improper personal benefit; and wilful misconduct.\textsuperscript{103} In Wisconsin, like Minnesota and North Dakota, although the scope of mandatory indemnification is subject to contrary provision in the corporation’s articles or bylaws, the fact that the statute itself creates such a presumption is significant given the affirmative steps required to opt out of the statutory pattern.

The same shift toward mandatory indemnification is reflected in several states’ enactment of amendments which expressly make the statutory regulation of indemnification non-exclusive of the provision of additional rights to indemnification created by contract or by a corporation’s charter or bylaws. These statutes permit the creation of enforceable rights to indemnification. In some instances, a person with a contract right to indemnification may not have a claim to mandatory indemnification under the statute because he has not met the statutory criterion for mandatory indemnification. Thus, statutes permitting the creation of additional rights to indemnification enable corporations to opt into mandatory obligations to indemnify. These statutory specifications of non-exclusivity vary in whether they expressly impose limits on the corporation’s ability freely to create additional rights. For example, under the Iowa statute such additional rights may not be created on behalf of defendants in actions brought by or in the right of the corporation itself. Indemnification with respect to such actions is limited to the standards and procedures specified in the indemnification statute itself.\textsuperscript{104} Moreover, under the Iowa statute the corporation may not create additional rights to indemnification for those circumstances in which a statute bars the corporation from reducing or eliminating a director’s liability for money damages through a provision in its articles.\textsuperscript{105} A comparable limitation on the corporation’s ability to create additional rights to indemnity is imposed by statute in Georgia,\textsuperscript{106} Washington,\textsuperscript{107} and New

\textsuperscript{103} See id.
\textsuperscript{104} See IOWA CODE ANN. § 496A.4A(2) & (7) (West Supp. 1987).
\textsuperscript{105} Id. § 496A.4A(7).
\textsuperscript{106} See GA. CODE ANN. § 14-2-156(f) (Supp. 1987).
By contrast, in some states, the statutory authorization for the creation of "additional" rights to indemnification states no express exclusions, or permits indemnification when the director's liability could not be reduced or eliminated through a charter provision. In such states, the ability of a court to impose constraints derived from public policy on extra-statutory rights to indemnity may readily become an issue. The long-standing provision in the Delaware statute authorizing "additional" rights has conventionally been understood to be subject to an implicit exclusion, on public policy grounds, of categorical obligations to indemnify that bind the corporation independent of the merits of the particular claimant's conduct. Courts interpreting Massachusetts law, however, have been reluctant to acknowledge the existence of a residual judicial prerogative to invalidate particular rights to indemnity in light of the sweeping and unqualified language used by the legislature.

The statutory authorizations for "additional" rights to indemnification also differ in their treatment of the corporation's ability to create rights to indemnification with respect to litigation arising from the claimant's conduct in some capacity other than his official capacity with the corporation. For example, section 145 of the Delaware statute expressly states

110. See, e.g., N.Y. Bus. Corp. Law § 402(b)(1) (McKinney Supp. 1988) (prohibiting provision reducing or eliminating director's liability if final adjudication establishes director acted in bad faith, or director's act or omission involved intentional misconduct or knowing violation of law, or director received financial profit or other advantage to which director was not legally entitled) and § 721 (no indemnification may be made on behalf of director or officer if final adjudication establishes acts were committed in bad faith, or were the result of active and deliberate dishonesty and were material to the cause of action adjudicated, or the director or officer received a financial profit or other advantage to which he was not legally entitled); N.C. Gen. Stat. § 55-7(11) (Supp. 1987) (directors' liability may not be reduced or eliminated by charter provision if director's acts or omissions not in good faith, or believed not to be in corporation's best interests, or director derived an improper personal benefit from transaction) and § 55-19 (corporation may not indemnify against liability or litigation expense if claimant's activities were known or believed by him at the time they were undertaken to be clearly in conflict with corporation's best interests).
that indemnification and advancement of expenses provided by or granted pursuant to the statute "shall not be deemed exclusive of any other rights" of the claimant "both as to action in his official capacity and as to action in another capacity while holding such office." Thus, under this statute, and others with comparable provisions, the corporation's ability to create rights to indemnity for acts undertaken in the claimant's "unofficial" capacity is limited to acts occurring while the claimant held his official position as a director, officer, employee or agent. Claims arising from acts committed prior to the person's assumption of "official capacity" could not be encompassed by the right to indemnification. In contrast, the North Carolina statute by implication imposes a stricter limit on the corporation's ability to create rights to indemnity for the consequences of actions undertaken in a capacity other than the person's official capacity with the corporation. Under that statute, the corporation expressly has power to create rights to indemnity for "any person who, at the request of the corporation, is or was serving as a director, officer, employee, or agent of another corporation, partnership, joint venture, trust or other enterprise or as a trustee or administrator under an employee benefit plan." Finally, some states' authorizations for the creation of "additional" rights to indemnity place neither of these limitations on the corporation's ability to create such rights.

A number of state statutes now expressly authorize or mandate, under stated circumstances, the indemnification of amounts paid to settle derivative litigation or, under some circumstances, amounts paid in final

Because the settlement amounts and final judgments in such an action are usually paid to the corporation itself, permitting indemnification is circular. Moreover, some states have amended their statutory regulation of indemnification for such actions to minimize the number of situations in which a court must approve the corporation's determination that a claimant meets the statutory standard for indemnification. Under the Louisiana statute, as amended in 1986, judicial approval is required for the indemnification of claimants adjudged liable, after the exhaustion of all appeals, for wilful or intentional misconduct in actions brought by or in the right of the corporation. In the absence of such a final determination of liability, the corporation's directors, its shareholders or independent legal counsel may make the determination that a claimant meets the standard for indemnification. In contrast, the Delaware statute requires judicial approval for indemnification in a broader range of cases. Section 145(b) of the Delaware statute requires judicial approval when the claimant has been adjudged liable to the corporation, regardless of the grounds for such liability. Finally, a number of statutes now expressly authorize the use of self-insurance or other alternatives to the purchase of D & O insurance from a third party insurance underwriter regardless of whether the corporation itself would have power directly to indemnify against the claims covered by the policy.

VI. CONCLUSION

The statutory revisions discussed in this article have been characterized as legislative responses that attempt to solve crises in directors' liability and in the availability of D & O insurance. In a number of respects, however, some of these solutions have overtaken the crises that legitimated their enactment. True, no single state has enacted a combi-

121. See DEL. CODE ANN. tit 8, § 145(b) (Supp. 1986).
nation of the least appealing features of these statutes, but one ought not be entirely sanguine that all states will successfully resist appeals to do so. At present, some states permit charter provisions that reduce or eliminate directors' liability in actions brought by creditors; others permit these provisions to reduce or eliminate the liability of officers as well as directors. In one state the charter provision could operate retroactively;\footnote{123} and in several states directors' liability could be reduced or eliminated even if an action raises serious questions as to the director's loyalty.\footnote{124} Some states have effectively trivialized directors' fiduciary obligation by defining fidelity to the interests of the corporation's shareholders as merely one in a laundry list of "factors" or "interests" the directors may consider. Some states permit—or even mandate—the circular process of corporate indemnification of settlement amounts or judgment amounts paid in derivative litigation. Finally, and wholly apart from the substantive effect of these statutes, some raise perplexing issues of interpretation. In some cases, "back to the drafting board" has much to recommend it as a future course of action.

\footnote{124} See text accompanying notes 46-57 \textit{supra}.