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A Comparative Analysis of Corporate Fiduciary Law: Why Delaware Should Look beyond the United States in Formulating a Standard of Care

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COMMENTS

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Corporate internationalization has altered the corporate landscape irreversibly. Specifically, international trading in securities and cross-border corporate ownership, directorship, and management have increased substantially.[1] In 1995 multinational companies invested a record $315 billion outside their own national

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1. *See generally* Richard M. Klapow, *Foreign Investment Company Law in the United* States: *The Need for Change in a Global Securities Market*, 14 BROOK. J. INT'L L. 411 (1988) (citing OECD REPORT, THE COMMITTEE ON FINANCIAL MARKETS INTERNATIONAL TRADE IN SERVICES: SECURITIES (Paris, 1987)); Caroline A.A. Greene, *International Securities Law Enforcement: Recent Advances in Assistance and Cooperation*, 27 VAND. J. TRANSNAT'L L. 635 (1994); Arthur R. Pinto, *The Internationalization of the Hostile Takeover Market: Its Implications for Choice of Law in Corporate and Securities Law*, 16 BROOK. J. INT'L L. 55 (1990). This trend to expand corporate activities internationally is driven by the benefits of risk diversification, the enhanced profitability that international investment frequently offers, and technological improvements and reductions in regulatory constraints. Klapow, *supra*, at 411.

borders; the United States, a massive $96 billion.[2] One-third of the one hundred largest multinational companies, ranked by foreign assets, are U.S. companies.[3] Additionally, U.S. investors increasingly look to Eastern Europe and developing countries for new investment opportunities.[4] Furthermore, American companies, via joint ventures and wholly foreign-owned enterprises on the Chinese mainland, have directly invested more than $15 billion into China over the past six years.[5]

After more than four decades, Eastern European countries have enacted or reenacted corporate and commercial codes.[6] These laws closely follow American and Western European corporate governance models.[7] Similarly, Chinese laws increasingly reflect U.S. corporate law standards.[8] Drafters of the sections of the Russian Civil Code that regulate companies have consciously borrowed elements from the United States' past.[9] Thus, as the world's securities markets systematically are interwoven, the hues of Delaware law increasingly become visible in foreign laws.

With internationalized corporate securities markets in place and with other countries increasingly looking to the United States in formulating their corporate fiduciary standards, the standard of care the Delaware Supreme Court dictates affects Delaware interests in a variety of ways. For example, it affects Delaware interests through the application, in a litigation setting, of Delaware substantive fiduciary law to a foreign corporation, or to a Delaware corporation doing business abroad. Delaware law can apply in a U.S. federal or state court, in a foreign court applying Delaware law through choice of law analysis, or in an arbitration or mediation proceeding where substantive Delaware law controls. Furthermore, if a court's or tribunal's choice of law principles lead it to apply a foreign jurisdiction's laws, and those laws reflect "Delaware fiduciary principles," Delaware fiduciary standards could affect Delaware interests.[10] Additionally, Delaware

2. Fred R. Breakley, *Foreign Investment by Multinationals Grew 40% in 1995, Lifted by Mergers*, WALL ST. J., Sept. 25, 1996, at A2 (citing United Nations Conference on Trade and Development Report). The 40% growth in foreign direct investment, more than twice the rate of world export growth, is, in part, attributable to "[c]ross-border acquisitions in the pharmaceutical, telecommunications, financial-services and entertainment industries," as well as "competitive pressures, new technologies, privatizations of country-owned enterprises and more of an open-door policy toward investments by many countries." *Id.*

3. *Id.*

4. Vassil Breskovski, *Directors' Duty of Care in Eastern Europe*, 29 INT'L LAW. 77 (1995).

5. Note, *Chinese Characteristics in Corporate Clothing: Questions of Fiduciary Duty in China's Company Law*, 80 MINN. L. REV. 503, 504 (1995).

6. Breskovski, *supra* note 4, at 78. State-owned businesses are being transformed into public limited companies as privatization increases in Eastern and Central Europe. *Id.* at 77.

7. *Id.* at 78.

8. *See infra* parts II.A., II.E.

9. Bernard Black & Reinier Kraakman, *A Self-Enforcing Model of Corporate Law*, 109 HARV. L. REV. 1912, 1930 (1996).

10. Delaware's interests at stake often are not visible at first glance. A Delaware citizen with funds in a Delaware-based mutual fund investing in Bulgaria may have an interest in both Bulgaria's and Delaware's fiduciary laws because Bulgarian fiduciary law may reflect Delaware fiduciary principles. *See infra* parts II, III. Should the Delaware investor choose to file a class action arising from

fiduciary standards affect Delaware interests when Delaware investors, in part, choose the country where they will invest based on the corporate fiduciary law protection that country affords shareholders, and where that country's fiduciary law, to some extent, is based on Delaware corporate fiduciary standards.

Delaware corporate fiduciary law, however, reflects neither the globalization of securities markets, nor the impact such globalization has on Delaware citizens.[11] Intended to counteract director inattentivenes and inactivity, Delaware's standard of care derives from established notions of trust law and agency law.[12] Closely tied to duties of loyalty and candor, the Delaware duty of care is, in essence, an ordinary prudent director standard.[13] However, the Delaware duty of care balances against the business judgment rule's principles of judicial deference.

In carving directors' duty of care from the protective shield of the business judgment rule, the Delaware Supreme Court has left the demarcating lines blurred. Consequently, the Delaware Supreme Court has been criticized, in part, for contributing to Delaware's somewhat uncertain and wavering standard of care.[14] Moreover, the duty of care has, in practice, very little effect on corporate governance.[15] While the Delaware Supreme Court offered cautious guidance in its 1985 *Smith v. Van Gorkum*[16] and its *Cede I, II,* and *III* decisions,[17] the Delaware duty of care remains largely ineffective. In this regard, little commentary has focused on the formulation of Delaware's director standard of care in light of internationalized securities markets and how emerging economies look to the United States for guidance in formulating standards of care.

This Comment addresses these concerns as follows. Since comparative analysis of corporate fiduciary law is sketched against the backdrop of conflict of laws issues, Part I briefly outlines the distinctions between procedural and substantive law and overviews the corporation law that might apply to international corporations. Part II offers a comparative analysis of corporate fiduciary duties (in particular, the duty of care) in various countries. First, it analyzes Delaware fiduciary law

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the Bulgarian corporate directors' breach of fiduciary duties as stipulated in Bulgarian law, the Delaware citizen's rights and remedies will be closely linked to the standard of care both Bulgaria and Delaware set forth for corporate directors. *Id.*

11. *See, e.g.*, Paramount Communications, Inc. v. QVC Network Inc., 637 A.2d 34 (Del. 1994); Cede & Co. v. Technicolor, Inc., 634 A.2d 345 (Del. 1993); Jedwab v. MGM Grand Hotels, Inc., 509 A.2d 584 (Del. Ch. 1986); Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986); Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985); Aronson v. Lewis, 473 A.2d 805 (Del. 1984); Weinberger v. UOP, Inc., 457 A.2d 701 (Del. 1983).

12. Henry Ridgely Horsey, *The Duty of Care Component of the Delaware Business Judgment Rule*, 19 DEL. J. CORP. L. 971, 973 (1994).

13. *Id.* at 985 (citing Graham v. Allis-Chalmers Mfg. Co., 188 A.2d 125 (Del. 1963)).

14. *Id.*

15. *Id.* at 977-80.

16. 488 A.2d 858 (Del. 1985).

17. Cede & Co. v. Technicolor, Inc., 542 A.2d 1182 (Del. 1988) (*Cede I*); Cede & Co. v. Technicolor, Inc., 634 A.2d 345 (Del. 1993) (*Cede II*); Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156 (Del. 1995) (*Cede III*).

and traces the business judgment rule, its origins, development, and underlying justifications. It then tracks the duty of care as a corporate fiduciary obligation in Delaware since it was first recognized by a Delaware court. Part II also offers a comparative analysis of the standard of care directors owe to shareholders or corporations in various countries. This country-by-country fiduciary overview provides a rough basis for assessing risk in international investment activities; in negotiating cross-border joint ventures, mergers, and acquisitions; and in choosing remedial actions following international corporate fall-outs. In addition, it benchmarks Delaware's standard of care relative to various other legal systems. The Comment assesses the fiduciary duties corporate directors owe to shareholders and the corporation in Western Europe (the United Kingdom, Germany, and France), Japan, Eastern Europe (Bulgaria, the Czech Republic and the Republic of Slovakia, Hungary, and Poland), the People's Republic of China, and Canada.

In Part III, this Comment argues that the Delaware Supreme Court should reassess the standard of care directors owe to a corporation in light of the internationalization of corporation and securities markets.

I. What Law Will Apply?

A threshold question this Comment addresses is: How will a court decide what law governs the standard of care corporate directors owe to their corporation? More specifically, how will the standard of care set forth in the Delaware Supreme Court come to be applied in a particular forum?

A. Procedural versus Substantive Law

The law of the forum in common law jurisdictions commonly controls procedural questions while choice-of-law rules select the proper law that serves as the rule of decision for substantive questions.[18] Therefore, the first step in selecting the law to apply is to characterize the issue as substantive or procedural. Within the U.S. federal court system, an issue often must receive such a characterization at least twice.[19] First, a court must decide whether it even needs to consider applying law other than its own.[20] Second, a court must, if the primary rule of

18. Joseph W. Dellapenna, Suing Foreign Governments and Their Corporations 214 (1988). *See generally* Restatement (Second) of Conflict of Laws § 122 (1971), and intro. note to ch. 12 (1971). "Conflict of laws" deals with when and why a certain jurisdiction's courts consider another jurisdiction's prior determination in a case pending before the former jurisdiction's courts. Eugene F. Scoles & Peter Hay, Conflict of Laws 1 (1982). The term "conflict of laws," also referred to as "private international law," is primarily used in the United States, Canada, and England. *Id.* Relating to issues between individuals, conflicts laws do not flow from an international consensus, such as "customary (public) international law." *Id.* Furthermore, two jurisdictions' substantive rules of decision "conflict" when circumstances seem to justify the application of either state's rule. *Id.* at 2. Because conflicts rules are purely domestic in nature, foreign rules will impact the transaction if the domestic conflicts rules point to foreign law. *Id.*

19. Dellapenna, *supra* note 18, at 214.

20. *Id.* (citing A. Robertson, Characterization in Conflicts of Law 135-37 (1940)).

decision refers to some other law, choose the law that will ultimately be used to determine the rights and responsibilities of the parties.[21] The double operation of these concepts results from the use of different concepts of substance and procedure for different purposes.[22] In this vein, "procedure" means nothing more than rules not intended to operate outside the court that created the rules, and "substance" means only a rule that is not "procedural."[23] Therefore, the standard of care corporate directors owe to shareholders probably is "substantive" because it commonly is intended to operate outside the court that created it.

B. CORPORATION LAW IN CHOICE OF LAW ANALYSIS

Parties to a lawsuit or proceeding can choose the law they wish to govern the dispute resolution.[24] Nonetheless, corporate directors' fiduciary duties are governed by what broadly can be termed "corporation law."[25] Under both English law[26] and American law,[27] a company's existence, dissolution, and internal affairs are governed by the law of incorporation.[28] For corporation law and therefore corporate fiduciary duties to apply, an entity first must be legally classified as a corporation.[29]

Absent a valid choice of law by the parties to the suit, legal systems use different

21. *Id.* For a comprehensive illustration, consider cases under the Erie doctrine such as *In re* Cepeda, 233 F. Supp. 465 (S.D.N.Y. 1964).

22. *In re* Cepeda, 233 F. Supp. 465 (S.D.N.Y. 1964); *see* Grant v. McAuliffe, 264 P.2d 944, 948 (Cal. 1953); Guaranty Trust Co. of N.Y. v. York, 326 U.S. 99, 108 (1945); *see also* Peter Western & Jeffrey S. Lehman, *Is There Life for Erie After the Death of Diversity?* 78 MICH. L. REV. 311, 361-63 (1980); John H. Ely, *The Irrepressible Myth of Erie*, 87 HARV. L. REV. 693 (1974). "Procedural" rules relate to functioning of courts themselves; in contrast, "substantive" rules address primary conduct or conduct in nonjudicial contexts. DELLAPENNA, *supra* note 18, at 214; *see* Hanna v. Plumer, 380 U.S. 460, 475 (1965) (Harlan, J., concurring); RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 122 cmt. a (1971). A court or tribunal may determine, in interpreting a statute or precedent, that the law is either substantive, procedural, or both; therefore, no single test is suitable for all choice-of-law purposes. DELLAPENNA, *supra* note 18, at 215.

23. Thus, a judge could justify virtually any particular outcome even if not consciously engaged in such a decision-making process. DELLAPENNA, *supra* note 18, at 414-67.

24. *See* MODEL BUS. CORP. ACT ch. 2 (1984); UCC § 5-108 (1996); RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6, at 188 (1971); Peter Winship, *Formation of International Sales Contracts Under the 1980 Vienna Convention*, 17 INT'L LAW. 1 (1983); P. NORTH, CONTRACT CONFLICTS v, 12, 299 (1982) (discussing choice of law under the EU Convention).

25. *See, e.g.*, Kademian v. Ladish, 792 F.2d 614, 628 (7th Cir. 1986).

26. 2 J.H.C. MORRIS ET AL., THE CONFLICT OF LAWS 725-31 (10th ed. 1980).

27. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 279 (1971).

28. Corporate "nationality" also depends on the place of incorporation. *See, e.g.*, Sumitomo Shoji America, Inc. v. Avagliano, 457 U.S. 176, 183 n.8 (1982).

29. While numerous theories discuss corporations' characteristics, all agree that corporations have group interests distinguishable from the individual interests of its individual members. HARRY G. HENN & JOHN R. ALEXANDER, LAWS OF CORPORATIONS (3d ed. 1983). Under the federal tax code, corporations include associations, joint-stock companies, and insurance companies. I.R.C. § 7701(a)(3) (1996).

factors to determine the law applicable to corporations.[30] For example, early French literature suggested that the law of the place "*d'exploitation*," the place where the corporation has the center of its commercial activity, was the proper choice.[31] This principle is analogous to the American concept of a corporation's principal place of business. French case law increasingly rejected the reference to the law of the place of principal commercial activity and instead adopted the reference to the corporation's "*siège social*" or seat.[32] This rule has been accepted in continental Europe, except in the Netherlands.[33] The "seat" of a corporation is where most of its administration or management is located or takes place. The civil law, however, does not share this logic. Civilians hold that just as "an individual's center of existence is where he lives, a legal entity's center of existence is where its commercial activity is carried on."[34]

Thus, in a civil law country, if absent a valid choice of law clause a corporation is found to have its "seat" or "principal place of business" in a certain jurisdiction, that jurisdiction's laws will apply and a Delaware shareholder's interests will be decided by that jurisdiction's laws. However, in both the United States and England, the law of the place of incorporation controls.

II. Fiduciary Duties

This part considers fiduciary duties in the United States (Delaware), Western Europe[35] (specifically the United Kingdom, Germany, and France), Japan, Eastern Europe (specifically Bulgaria, the Czech Republic and the Republic of Slovakia, Hungary, and Poland), the People's Republic of China, and Canada. The State of Delaware was selected as representative of U.S. fiduciary law.[36]

30. Courts must work within one of three different choice-of-law traditions just within the United States. DELLAPENNA, *supra* note 18, at 228. These are: a rule-centered "vested rights" approach, aimed at coordinating competing sovereignties; a methodology-centered "interest analysis" aimed at coordinating social policies; and a new rule-centered "neoterritorialist" approach, aimed at coordinating the parties' expectations. *Id.* The vested rights system, found in the *First Restatement of Conflicts*, allows courts first to characterize the nature of the suit and then select the jurisdiction under whose law rights of that type "vest"—for example, for torts, the place where the injury occurred. *Id.*

31. SCOLES & HAY, *supra* note 18, at 884.

32. *Id.* (citing BATTIFOL & LAGARDE, 1 DROIT INTERNATIONAL PRIVÉ NO. 193, 230 (7th ed. 1981)).

33. Eric Stein, *Conflict-of-Law Rules by Treaty: Recognition of Companies in a Regional Market*, 68 MICH. L. REV. 1327, 1330-31 (1970).

34. ROBERT A. LEFLAR, AMERICAN CONFLICT LAW 503 (3d ed. 1977) (citing KEGAL, INTERNATIONALES PRIVATRECHT 263 (4th ed. 1977)).

35. This Comment discusses Western European standards of care not to show how United States fiduciary principles shaped Western European standards of care, but rather to place the Delaware standard of care in a Western jurisprudential context.

36. Not only are more than half of the 500 largest industrial firms in the United States incorporated in Delaware, but Delaware's corporation law also serves as an innovator and model for other jurisdictions. Curtis Alva, *Delaware and the Market for Corporate Charters: History and Agency*, 15 DEL. J. CORP. L. 888, 889-90 (1990).

Fiduciary duties are born out of the equitable principles of trust and agency.[37] Fiduciary duties protect the fiduciary relationship against wrongful administration by forbidding disloyalty.[38] However, while the roots and principles of fiduciary law are fairly well established, its exact scope and application in Delaware remain unclear. Therefore, before assessing non-U.S. fiduciary principles and before commenting on the need for Delaware to consider international developments in reassessing its standard of care, this Comment first analyzes Delaware's past and present fiduciary corporate standard of care.

A. DELAWARE

Within the United States, fiduciary law is state law.[39] In Delaware, the fundamental relationship between a director and the corporation that he or she serves is the fiduciary relationship.[40] Section 141(e) of Delaware's Corporations Code in part codifies a director's fiduciary standard of care.[41] It allows directors, in exercising their duty of care, to rely on certain materials and information:

> A member of the board of directors . . . shall, in the performance of his duties, be fully protected in relying in good faith upon . . . such information . . . presented to the corporation 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.[42]

Drawing upon notions of trust law, the Delaware Supreme Court has held that the board of directors has the ultimate responsibility for managing the business and affairs of a corporation and owes fiduciary duties of care and loyalty to the corporation and its shareholders.[43] Thus, directors are guardians of the sharehold-

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37. Robert B. Robbins, *Fiduciary Duties of Directors of Corporate General Partners to Limited Partnerships*, CA65 A.L.I.-A.B.A. 87 (1996) (citing G. BOGERT, TRUSTS & TRUSTEES § 543 (rev. 2d ed. 1978)).

38. A trustee has a fiduciary duty of undivided loyalty to the beneficiary of a trust to administer the trust "solely in the interest of the beneficiary." *Id.* at 89. Moreover,

> [t]he trustee must exclude all self-interest, as well as the interest of a third party, in his administration of the trust solely for the benefit of the beneficiary. The trustee must not place himself in a position where his own interests or that of another enters into conflict, or may possibly conflict, with the interest of the trust or its beneficiary.

Id.

39. Klapow, *supra* note 1, at 411.

40. Loft, Inc. v. Guth, 2 A.2d 225 (Del. Ch. 1938).

41. DEL. CODE ANN. tit. 8, § 141(e) (1996).

42. *Id.* (emphasis added).

43. Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 179 (Del. 1986). The Delaware Supreme Court drew from what it established in 1939 as a bedrock principle of Delaware corporation law:

> Corporate officers and directors are not permitted to use their position of trust and confidence to further their private interests. While technically not trustees, they stand in a *fiduciary relation* to the corporation and its shareholders. . . . This rule, inveterate and uncompromising in its rigidity, does not rest upon the narrow ground of injury or damage to the corporation resulting from a betrayal of confidence, but upon a broader foundation of a wise public policy that, for the purpose of removing all

ers' property and, therefore, assume special duties and responsibilities by virtue of this relationship. Moreover, American corporate law establishes that the primary, if not the sole, responsibility of corporate directors goes to the shareholder owners.[44] However, although directors' duties are frequently analogized to those of trustees, the nature of directors' duties are tempered in corporation law by the "business judgment rule"—judicial deference to board actions and decisions that fall within the sphere of the board's business judgment. Consequently, absent a showing of culpability, directors or controlling shareholders do not have to sacrifice their own financial interests in an enterprise for the sake of the corporation or its minority shareholders.[45]

1. *The Business Judgment Rule*

The Delaware Supreme Court in 1984 described the business judgment rule as follows:

> It is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company. Absent an abuse of discretion, that judgment will be respected by the courts. The burden is on the party challenging the decision to establish facts rebutting the presumption.[46]

While the presumption component of the business judgment rule procedurally places the burden on the challenging party, the origins of the rule probably relate

> temptation, extinguishes all possibility of profit flowing from a breach of the confidence imposed by fiduciary relation.

Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1280 (Del. 1989) (emphasis added; quoting Guth v. Loft, Inc., 5 A.2d 503, 510 (Del. 1939)).

44. Roger S. Aaron, *Directors' Duties in Corporate Takeovers, Mergers and Acquisitions*, 878 PRAC. L. INST. CORP. L. & PRAC. COURSE HANDBOOK SERIES 289, 295 (quoting Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985)).

45. Jedwab v. MGM Grand Hotels, Inc., 509 A.2d 584 (Del. Ch. 1986). In *Jedwab*, a preferred shareholder brought a class action on behalf of all owners of preferred stock other than the controlling shareholder and the related corporation. *Id.* The defendants argued that there is no broad duty of fidelity owed to preferred stock if that duty is understood to extend beyond the specific contractual terms defining the special rights, preferences, or limitations of the preferred stockholders. *Id.* More specifically, defendants argued from the rule that "preferential rights are contractual in nature and therefore are governed by the express provisions of a company's certificate of incorporation." *Id.* at 593. The court, however, concluded that:

> with respect to matters relating to preferences or limitations that distinguish preferred stock from common, the duty of the corporation and its directors is essentially contractual and the scope of the duty is appropriately defined by reference to the specific words evidencing that contract; where however the right asserted is not to a preference as against the common stock but rather a right shared equally with the common, the existence of such right and the scope of the correlative duty may be measured by equitable as well as legal standards.

Id. at 594.

46. Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) (citations omitted).

back to its substantive context.[47] The rule dates to nineteenth and early twentieth century cases that were based on concepts of judgment, risk, and discretion rather than on a "procedural presumption."[48] However, by the early twentieth century, Delaware had established a procedural interpretation of the rule. Indeed, by 1924, Delaware described the business judgment rule as follows:

> [D]irectors of [a] corporation are clothed with that presumption which the law accords to them. . . . [T]he sale in question must be examined with the presumption in its favor that the directors who negotiated it honestly believed that they were securing terms and conditions which were expedient and for the corporation's best interests.[49]

The business judgment rule is grounded in the essential nature of the corporate form[50]—while directors possess the expertise and experience to manage a corporation, shareholders passively invest capital into the corporation. Therefore, an agency relationship exists between directors and shareholders.[51] Notwithstanding that directors and shareholders have certain incentives to see a company prosper, their interests also at times diverge. Specifically, certain directors might attempt to "appropriate perquisites" for personal use out of a company's resources.[52] In response, shareholders might choose to monitor director behavior by actually observing directors and demanding detailed performance reports,[53] bargain ex ante with directors over a range of possible contingencies,[54] or, perhaps most efficiently, allow directors to operate within the purview of the business judgment rule and fiduciary obligations.

Therefore, the business judgment rule is a judicial response to the need to balance the fiduciary standards imposed on directors when exercising their managerial responsibilities in practical real-world decision making.[55] The rule creates an environment in which capable people are willing to serve as decision makers

47. Jay P. Morgan, *Business Judgment Rule or Relic?*: Cede v. Technicolor *and the Continuing Metamorphosis of Director Duty of Care*, 45 EMORY L.J. 339, 353 (1996); *see also* R. Franklin Balotti & James J. Hanks, Jr., *Rejudging the Business Judgment Rule: Symposium on Corporate Governance*, 48 BUS. LAW. 1337, 1342 (1993).

48. Morgan, *supra* note 47, at 353.

49. Robinson v. Pittsburgh Oil Refining Corp., 126 A. 46, 48 (Del. Ch. 1924); *see also* Cole v. National Cash Credit Ass'n, 156 A. 183 (Del. Ch. 1931).

50. *See generally* Morgan, *supra* note 47, at 342.

51. *Id.*

52. *Id.* at 342. The opportunities for corporate corruption may be greater in developing than in developed countries. *See, e.g.*, Black & Kraakman, *supra* note 9, at 1911, 1961 ("[t]he risk of looting is far higher in emerging than in developed markets"); John Hogarth, *Bribery of Official in Pursuit of Corporate Aims*, 6 CRIM. L. FORUM 557 (1995) (noting corruption in developing countries such as Russia).

53. American shareholders investing in a foreign corporation are not only geographically removed from the corporation's headquarters, but also face language and foreign regulatory barriers in monitoring foreign directors.

54. Likewise, American shareholders cannot easily bargain with foreign directors.

55. Aaron, *supra* note 44, at 303 (1995). As one court stated:

> Because businessmen and women are correctly perceived as possessing skills, information and judgment not possessed by reviewing courts and because there is great social utility in encouraging the allocation of assets and the evaluation and assumption of

without the constant risk of judicial second-guessing and personal liability exposure.[56]

The business judgment rule also is based upon the principle that shareholders, with financial information available in the corporate marketplace, voluntarily invest in corporate stocks notwithstanding the risks involved.[57] Indeed, shareholders, unlike directors, can diversify their investments to reduce risk.[58] If directors are subject to strict standards of judicial review, they may become overcautious in decision making and, consequently, forgo favorable risks.[59] Furthermore, it is impracticable to determine ex post facto the quality of business decisions, other than through a rule of general judicial deference.[60] Consequently, the business judgment rule places the burden on the party challenging the decision to establish that the judgment of a board was an abuse of discretion.[61]

Business judgment judicial review encompasses three elements: a review of the objective financial interests of the board under scrutiny (i.e., independence);[62] a review of the board's subjective motivation (i.e., good faith);[63] and an objective review of the decision-making process (i.e., due care).[64]

If the board is financially interested, or breaches its duties of care or good faith, it bears the burden to establish the entire fairness of the transaction. A director can satisfy the good faith and due care elements if the plaintiff cannot show a prima facie case of bad faith or gross negligence, or if the balance of the evidence does not establish bad faith or gross negligence, even if a prima facie case is made out.[65]

Thus, while directors initially are given the benefit of the doubt that they have acted honestly and with reasonable care, a breach of the duties of care or loyalty could rebut this presumption.[66] Then, directors must prove the intrinsic or entire fairness of the challenged conduct.[67] If they fail to do so, directors are personally

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> economic risk by those with such skill and information, courts have long been reluctant to second-guess such decisions when they appear to have been made in good faith.

West Point-Pepperell, Inc. v. J.P. Stevens & Co., 542 A.2d 770, 780 (Del. Ch. 1988).

56. Aaron, *supra* note 44, at 303.

57. Morgan, *supra* note 47, at 349.

58. *See generally* Eugene F. Fama & Michael C. Jensen, *Agency Problems and Residual Claims*, 26 J.L. & ECON. 327 (1983).

59. *See* FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 96-97 (1993).

60. *See* Morgan, *supra* note 47, at 352.

61. Aaron, *supra* note 44, at 66.

62. *In re* RJR Nabisco, Inc. Shareholder Litigation, [1988-1989] Fed. Sec. L. Rep. (CCH) ¶¶ 94,194, at 91,709-10 (Del. Ch. 1989).

63. *Id.*

64. *Id.* However, the duty of care is seldom used to overcome the business judgment rule. *See* Horsey, *supra* note 12, at 977.

65. *In re* RJR Nabisco, Inc., [1988-1989] Fed. Sec. L. Rep. (CCH) ¶¶ 94,194, at 91,709-10.

66. *Van Gorkom*, 488 A.2d at 872.

67. Aaron, *supra* note 44, at 66-67. Recently, the Delaware Supreme Court in Paramount Communication, Inc. v. QVC Network Inc., 637 A.2d 34 (Del. 1993), stipulated that the key features of an enhanced scrutiny, the degree of scrutiny applied during entire fairness review, are as follows:

liable to the corporation or its shareholders for damages proximately caused by such conduct.[68]

2. *The Delaware Duty of Care*

Very rarely have shareholders successfully used directors' fiduciary duties of care to overcome the business judgment rule.[69] While "in the abstract, the duty of care seems to impose a meaningful obligation on directors and officers," in practice the duty of care "has had almost no effect on corporate governance."[70] Thus, in applying the business judgment rule, courts presuppose "that judgment—reasonable diligence—has in fact been exercised."[71] However, some commentators argue that to invoke the business judgment rule in the first instance, "the director must exercise his judgment within the scope of the duty of care—that is, his judgment must have been reasonable and exercised with the care of an ordinarily prudent person."[72]

While Delaware is famous for its sophisticated and developed corporate case law, Delaware courts have only sparsely articulated a director's duty of care.[73] Not until 1963, in *Graham v. Allis-Chalmers Manufacturing Co.*,[74] did Delaware espouse a substantial body of case law[75] imposing on a fiduciary director the

a judicial determination regarding the adequacy of the decision-making process employed by the directors, including the information on which the directors based their decision; and a judicial examination of the reasonableness of the directors' action in light of the circumstances then existing. *Id.* at 45. The *Paramount* court noted that "[a]lthough an enhanced scrutiny test involves a review of the reasonableness of the substantive merits of a board's actions, a court should not ignore the complexity of the directors' task in a sale of control." *Id.* (footnote omitted). The court concluded that "a court applying enhanced judicial scrutiny should be deciding whether the directors made a reasonable decision, not a perfect decision." *Id.*

68. *Van Gorkom*, 488 A.2d at 893.

69. *See* Horsey, *supra* note 12, at 977-80; Krishnan Chittur, *The Corporate Director's Standard of Care: Past, Present, and Future*, 10 DEL. J. CORP. L. 505 (1985) (noting that the business judgment rule historically proved to be a very potent defense for corporate directors against shareholder claims for loss resulting from decisions that went awry); Stuart R. Cohn, *Demise of the Director's Duty of Care: Judicial Avoidance of Standards and Sanctions Through the Business Judgment Rule*, 62 TEX. L. REV. 591, 593 (1983) (finding judicial reluctance to apply diligence standards against well-intentioned, non-self-dealing directors); Joseph W. Bishop, Jr., *Sitting Ducks and Decoy Ducks: New Trends in the Indemnification of Corporate Directors and Officers*, 77 YALE L.J. 1078, 1099 (1968) (finding only four cases of derivative litigation in which disinterested directors breached fiduciary duty of care).

70. George W. Dent, Jr., *The Revolution in Corporate Governance, the Monitoring Board, and the Director's Duty of Care*, 61 B.U. L. REV. 623, 644-45 (1981).

71. Chittur, *supra* note 69, at 505 n.2 (quoting Casey v. Woodruff, 49 N.Y.S.2d 625, 643 (N.Y. 1944)).

72. Dent, *supra* note 70, at 647.

73. Horsey, *supra* note 12, at 981.

74. 188 A.2d 125 (Del. 1963).

75. *See, e.g.*, Briggs v. Spaulding, 141 U.S. 132 (1891); Atherton v. Anderson, 99 F.2d 883 (6th Cir. 1938).

duty to act in an informed manner and with the care of a prudent person.[76] In *Graham*, the Delaware Supreme Court concluded:

> [D]irectors of a corporation in managing the corporate affairs are bound to use that amount of care which ordinarily careful and prudent men would use in similar circumstances. Their duties are those of control, and whether or not by neglect they have made themselves liable for failure to exercise proper control depends on the circumstances and facts. . . .[77]

While *Graham* broke new ground in corporate law by recognizing a director's fiduciary duty of care, "the accomplishment was diminished by the tentative and almost begrudging manner in which the court embraced this new-found duty."[78]

However, in 1971 the Delaware Supreme Court, in *Kaplan v. Centex Corp.*,[79] found an enforceable duty of care component in the business judgment rule. Finding the defendant directors in breach of their duty of care, the court held that the business judgment rule's application "of necessity depends upon a showing that informed directors did, in fact, make a business judgment authorizing the transaction under review."[80] The court concluded that absent evidence that "director judgment was [not] brought to bear with specificity on the transactions," the business judgment rule does not apply.[81]

Drawing upon *Kaplan*[82] and the dicta of *Graham v. Allis-Chalmers Manufacturing Co.*,[83] the Delaware Supreme Court, in *Aronson v. Lewis*,[84] repositioned a director's standard of care in relation to the business judgment rule. The court stated:

> [T]o invoke the rule's protection directors have a duty to inform themselves, prior to making a business decision, of all material information reasonably available to them. Having become so informed, they must then act with requisite care in the discharge

76. *Graham*, 188 A.2d at 130; *see also* Bodell v. General Gas & Electric Corp., 132 A. 442, 447 (Del. Ch. 1926), *aff'd*, 140 A. 264 (Del. 1927) (first Delaware decision enunciating directors' duty to refrain from profiting themselves at expense of their beneficiaries and to save their beneficiaries from loss); Cole v. Nat'l Credit Ass'n, 156 A. 183 (Del. Ch. 1931) (earliest Delaware decision holding that grossly imprudent conduct of otherwise disinterested directors is not protected by business judgment rule).

77. *Graham*, 188 A.2d at 130. *Graham* is believed to represent the first explicit recognition by a Delaware court of directors' duty of care as well as of good faith and loyalty. Horsey, *supra* note 12, at 986–87.

78. Horsey, *supra* note 12, at 988. While numerous state legislatures enacted statutes defining a director's fiduciary standard of care, Delaware, by contrast, left this responsibility to the courts. *Id.* Delaware courts, however, did not refine the disinterested director's duty of care parameters. *See, e.g.*, Meyerson v. El Paso, 246 A.2d 789 (Del. Ch. 1967) (extending business judgment rule to all conduct absent gross and palpable overreaching); Sinclair Oil Co. v. Levien, 280 A.2d 717, 720 (Del. 1971) (extending business judgment rule to any rational business purpose).

79. 284 A.2d 119 (Del. Ch. 1971).

80. *Id.* at 124.

81. *Id.*; *see also* Penn Mart Realty Co. v. Becker, 298 A.2d 349, 351 (Del. Ch. 1972) (holding director in breach of duty of care upon a finding of gross negligence); Gimbel v. Signal Companies, 316 A.2d 599, 610 (Del. Ch. 1972), *aff'd*, 316 A.2d 619 (Del. 1974) (holding director duty of care distinct from, and not merely surrogate of, duty of loyalty).

82. 284 A.2d 119 (Del. Ch. 1971).

83. 188 A.2d 125 (Del. 1963).

84. 473 A.2d 805 (Del. 1984).

of their duties. While the Delaware cases use a variety of terms to describe the applicable standard of care, our analysis satisfies us that under the business judgment rule director liability is predicated upon concepts of gross negligence.[85]

In 1985, in *Smith v. Van Gorkom,*[86] the Delaware Supreme Court refined (or some would argue "redefined") a director's standard of care in light of the business judgment rule. In a controversial opinion,[87] the court found the directors of Trans Union Corporation liable for failing to exercise care during the corporation's merger negotiations.[88] The court applied a gross negligence standard and held that the Trans Union directors were uninformed and, consequently, did not satisfy their duty of care to ensure business judgment rule protection.[89] The court stated:

> The directors (1) did not adequately inform themselves as to Van Gorkom's role . . . in establishing the . . . purchase price; (2) were uninformed as to the intrinsic value of the Company; and (3) given these circumstances . . . were grossly negligent in approving the "sale" of the Company upon two hours' consideration, without prior notice, and without the exigency of a crisis. . . .[90]

Rather than substitute its own judgment for that of the board, the court reviewed the process by which the board reached the decision and noted the board's lack of preparation and deliberation.[91] Notwithstanding the court's firm duty-of-care language, the opinion has been rationalized as based on "exceptional facts."[92]

Recently, the Delaware Supreme Court refined the duty of care in separate opinions all involving the same case, namely *Cede & Co. v. Technicolor, Inc.*[93] *Cede* involved a cash-out merger where the dissenting shareholders sued the directors for, among other claims, breach of fiduciary duty. In 1993, in the second appeal to the Delaware Supreme Court (*Cede II*),[94] the court held that Delaware had never put forth, for purposes of rebutting the business judgment

85. *Id.* at 812.

86. 488 A.2d 858 (Del. 1985).

87. *See, e.g.*, R. Link Newcomb, *The Limitation of Directors' Liability: A Proposal for Legislative Reform*, 66 TEX. L. REV. 411, 419 (1987). Shortly after *Van Gorkom*, Delaware enacted a statute that provides, in part, that a Delaware corporation's articles may contain:

> A provision eliminating or limiting the personal liability of a director to the corporation or its stockholders for monetary damages for breach of a fiduciary duty as a director, provided that such provision shall not eliminate or limit the liability of a director: (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 a knowing violation of law. . . .

DEL. CODE ANN. tit. 8, § 102(b)(7) (1995).

88. *Van Gorkom*, 488 A.2d at 864.

89. *Id.* at 893.

90. *Id.* at 874.

91. *Id.* at 874–80.

92. *See, e.g.*, Newcomb, *supra* note 87, at 419.

93. Cede & Co. v. Technicolor, Inc., 542 A.2d 1182 (Del. 1988) (*Cede I*); Cede & Co. v. Technicolor, Inc., 634 A.2d 345 (Del. 1993) (*Cede II*); Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156 (Del. 1995) (*Cede III*).

94. 634 A.2d 345 (Del. 1993).

rule, a requirement that the plaintiffs prove not only a breach of duty of care, but also the underlying injury.[95] Finding that the plaintiffs successfully rebutted the business judgment rule, the court stated:

> To inject a requirement of proof of injury into the [business judgment] rule's formulation for burden shifting purposes is to lose sight of the underlying purpose of the rule. Burden shifting does not create per se liability on the part of the directors; rather, it is a procedure by which Delaware courts of equity determine under what standard of review director liability is to be judged. To require proof of injury as a component of the proof necessary to rebut the business judgment presumption would be to convert the burden shifting process from a threshold determination of the appropriate standard of review to a dispositive adjudication on the merits.[96]

Therefore, it took the Delaware Supreme Court no less than three decades, since it first recognized a director's duty of care in *Graham v. Allis-Chalmers Manufacturing Co.*,[97] to resolve that injury is not needed to rebut successfully the business judgment rule's presumption.[98]

In 1995 the *Cede III* court affirmed the Chancery Court's subsequent finding of entire fairness in the cash-out merger.[99] The court concluded that the defendant directors' "undisputed lack of care in making a market check," a flaw in the approval process, did not preclude a finding of entire fairness.[100] The court noted that the defendant directors:

> [H]ad carefully focused on whether the . . . bid offered the best price available in a sale of the company; had considered whether to shop the company and the risks that course would entail; possessed a substantial amount of prior knowledge pertinent to the decision to sell; and relied on the reports of [its chief executive officer and board chairman], Goldman Sachs and its outside legal counsel.[101]

While the Delaware Supreme Court has wrestled with the duty of care, it has left the breach of that duty a largely ineffective cause of action. In sum, the court has stipulated that to rebut the business judgment rule's presumptions, a litigant must show that a director was grossly negligent.[102] A showing of injury, however, is not required.[103] And while directors may exhibit an "undisputed lack of care" in executing some of their obligations, the directors can still prevail under an entire fairness review.[104] Thus, a plaintiff must make a considerable showing of gross negligence to shift the heavy burden of the business judgment rule. But

95. *Id.* at 370.
96. *Id.* at 371.
97. 188 A.2d 125 (Del. 1963).
98. While this progress was certainly laudable, the court's continued reluctance to embrace the duty of care was also evident.
99. *Cede III*, 663 A.2d 1156 (Del. 1995).
100. *Id.* at 1175.
101. *Id.*
102. *Van Gorkom*, 488 A.2d at 893; *Aronson*, 473 A.2d at 812.
103. *Cede II*, 634 A.2d at 371.
104. *Cede III*, 663 A.2d at 1175.

even if the plaintiff makes such a showing, the plaintiff may still fail under an entire fairness review.

In forging a director's standard of care, the Delaware Supreme Court has not yet considered the effects of corporate internationalization on Delaware's citizens. To evaluate Delaware's standard of care relative to other countries' standards, this Comment now overviews several countries' standards of care and, where appropriate, compares and contrasts them to Delaware's standard of care.

B. Western Europe

1. *An Overview of European Regulation*

Before addressing directors' fiduciary obligations in specific European countries, this Comment overviews the regulation of corporate directors in Europe generally.

A dual system, analogous to that existing in the United States, increasingly regulates director conduct in Europe.[105] As the state of incorporation provides the basic law governing corporations in the United States, so too is the basic law governing European corporations that of the country of incorporation.[106]

Because a jurisdiction's de facto standard of care depends on both substantive law and procedural rules, it is very difficult to evaluate meaningfully which jurisdiction's law sets the highest standard for corporate directors.[107] Nonetheless, the strictest substantive provisions of law in Western Europe are found in France and Germany, followed by the United Kingdom.[108] The regulation of director conduct in numerous European Community (EC) Member States, such as Spain and Greece, however, is considerably less developed.[109] This lack of regulation is partially due to the fact that hostile takeovers have been rather rare until recently in most EC countries.[110]

Notwithstanding the different stages of development of European countries' corporation and fiduciary law, legal harmonization throughout Europe appears probable.[111] However, the European Union Draft Fifth Directive and proposals for European cooperation do not articulate a standard for skill and care for corporate

105. David J. Berger, *The Second Common Market: Development of a Unified Standard for Reviewing the Actions of Target Directors in the United States and the European Community*, 9 INT'L TAX & BUS. LAW. 1 (1991).

106. David J. Berger, *Exporting the Twin Towers: The Development of a Transnational Business Judgment Rule*, 9 ST. LOUIS U. PUB. L. REV. 169, 172–78 (1990); *see also* David J. Berger, *The European Markets Try to Coordinate, Unify Conflicting Merger Law*, NAT'L L.J., Nov. 6, 1989, at S14.

107. Breskovski, *supra* note 4, at 80.

108. *Id.* at 81.

109. Berger, *supra* note 106, at 1.

110. One study suggests that the first successful hostile takeover in West Germany was the Flick Brothers' acquisition of Fedmuehle-Nobel in 1989. *See* Julian Franks & Golin Mayer, *Capital Markets and Corporate Control: A Study of France, Germany and the UK*, 10 ECON. POL'Y 189 (1990).

111. Breskovski, *supra* note 4, at 81.

directors.[112] Furthermore, recently enacted Eastern European codes closely copy existing provisions of the European Union (EU) regulations.[113] Consequently, the issue confronting Eastern European countries that are Member States of the EU is whether they should passively await development of director duty of care case law through jurisprudence, or expedite codification through directives.[114] Accordingly, some commentators suggest that Eastern European countries should look to U.S. duty of care case law in formulating guidelines for their own director standard of care.[115]

2. *The United Kingdom*

The United Kingdom imposes on directors a slightly less demanding standard of care than does Delaware. Indeed, the United Kingdom's subjective common law duty of care[116] has been said to "give directors a remarkable freedom to run companies incompetently."[117] Directors in the performance of their duties need not exhibit "a greater degree of skill and care than may reasonably be expected from . . . person[s] of [their] knowledge and experience."[118] In addition, directors are required to attend those meetings they reasonably can, but are not obligated to give continuous attention to the affairs of the company.[119] Directors may, however, be required to give continuous attention to the affairs of the company pursuant to the terms of their service contracts.[120] Furthermore, directors may trust officials to perform their duties honestly, provided the directors have no grounds for suspi-

112. *Id.*
113. *Id.*
114. *Id.*
115. *Id.*
116. Directors' duties of skill and care lie in nineteenth century Courts of Chancery's treatment of directors as "trustees" or "quasi-trustees." Vanessa Finch, *Company Directors: Who Cares About Skill and Care?* 55 MOD. L. REV. 179, 200 (1992). Directors' duties of care are not strictly formed from either the common law or principles of professionalism, and the duty of care's formulation did not heed the differences in law and practice that differentiate directors and trustees. *Id.* Rather, directors were long treated as well-intentioned amateurs free from liability for anything short of negligence. *Id.* However, some commentators suggest that courts may now, in light of employment contracts, apply a higher standard to full-time executives. A.J. Boyle, *Draft Fifth Directive: Implications for Directors' Duties, Board Structure and Employee Participation*, 13 COMPANY LAW. NO. 1, at 6 (1992).
117. Finch, *supra* note 116, at 179.
118. Boyle, *supra* note 116, at 6 (citing *In re* City Equitable Fire Ins. Co. Ltd., 1925 Ch. 407, 428 (Eng. C.A.)). The court stated that:

> A director is not bound to give continuous attention to the affairs of the company of his company [sic]. His duties are of an intermittent nature to be performed at periodical board meetings, and at meetings of any committee of the board in which he happens to be placed. He is not, however, bound to attend such meetings though he ought to attend whenever in the circumstances, he is reasonably able to do so.

Id.
119. *Id.*; *see also* DIRECTORS' DUTIES AND RESPONSIBILITIES IN THE EUROPEAN COMMUNITY, A COUNTRY BY COUNTRY GUIDE 204 (Alex Roney ed., 1992) [hereinafter DIRECTORS' DUTIES]; ROBERT PENNINGTON, COMPANY LAW 676-78 (5th ed. 1985); Finch, *supra* note 116, at 179.
120. *See* DIRECTORS' DUTIES, *supra* note 119.

cion and the duties are allocated properly.[121] Directors may be found negligent if they engage in dishonest behavior, fail to detect or prevent fraudulent behavior, or carelessly misjudge business decisions.[122] Because directors are endowed with different degrees of experience and care, the prevailing opinion is that a subjective duty of care is the only realistic duty that can be imposed on directors.[123] The United Kingdom relieves negligent directors of liability where they acted " 'honestly and reasonably' and, in all the circumstances, 'ought fairly to be excused for the negligence, default, [and] breach of duty'."[124]

The wrongful trading section of the United Kingdom's Insolvency Act, however, imposes a more rigorous standard of care on directors. Once directors become aware of the approaching insolvency, their actions are judged according to both subjective and objective criteria.[125] Directors must convince the court that upon becoming aware of an approaching insolvency, they took every step to minimize potential loss to the company. Furthermore, directors' actions and conclusions are evaluated against those of reasonably diligent persons with the general knowledge, skill, and experience expected of persons carrying out the same functions as directors.[126]

Therefore, the United Kingdom, like Delaware, evaluates director conduct in fulfilling the duty of care according to a reasonable person standard. Nevertheless, the United Kingdom evaluates director conduct from a forgiving subjective standard, in contrast to Delaware, which conducts a slightly more rigorous objective review. The wrongful trading section of the United Kingdom's Insolvency Act, however, more closely approaches Delaware's duty of care. United Kingdom insolvency review, like Delaware duty of care review, involves an objective rather than only a subjective standard. Moreover, as U.K. directors, upon becoming aware of an approaching insolvency, have to minimize potential loss to the company, so Delaware directors, in a transaction involving a sale of a company, have to ensure that the price offered is the highest value reasonably available under the circumstances.[127]

3. *Germany*

Germany exacts a more testing duty of care than do the United Kingdom and Delaware. A civil law country with laws founded upon Roman principles,[128]

121. Breskovski, *supra* note 4, at 77.
122. Boyle, *supra* note 116, at 6.
123. *Id.*
124. Finch, *supra* note 116, at 201.
125. DIRECTORS' DUTIES, *supra* note 119.
126. *Id.*
127. *See, e.g.*, Mills Acquisition Co. v. MacMillan, Inc., 493 A.2d 946 (Del. 1985).
128. *See generally* NIGEL FOSTER, GERMAN LEGAL SYSTEM & LAWS 1 (2d ed. 1996). Although vast differences existed between German and English legal systems at the turn of the century, these systems are now moving closer together as a result of the increasing importance of case law in Germany, the consolidation of statutes in the United Kingdom, and the membership of both countries to the EC. *Id.*

Germany's rigorous duty of care[129] is, in essence, an objective orderly and prudent business manager standard.[130] More particularly, directors must apply the same degree of care as must persons in responsible positions of authority as managers of others' finances.[131] Thus, directors' individual abilities are not considered, and unfitness or inexperience does not qualify as an excuse. Moreover, directors and managers are jointly and severally liable for damages arising from their breach of their duty of care.[132]

In addition, directors and managers bear the burden to show that they have not breached their duty of due care.[133] Under the strict German standard, any negligence, no matter how slight, can give rise to damages.[134] Shareholders' subsequent ratification of directors' actions will waive directors' liability if shareholders were correctly informed.[135] However, ratification following a breach of duty does not relieve the directors from liability.[136]

While Germany, like Delaware, sets an objective standard of review for a director's conduct, Germany imposes a far higher standard of care than does Delaware. First, German directors are not protected by the business judgment rule, but rather, bear the burden to show they did not breach their duty of care. Delaware directors, in contrast, are guarded by the business judgment rule, which places the initial burden on the plaintiff to show gross negligence in a duty of care case. Furthermore, Delaware directors benefit from Delaware's judicial reluctance to find duty of care violations. In Delaware, directors could escape damages notwithstanding their "undisputed lack of care in making a market check"[137] or a flaw in the approval process, while in Germany, the slightest finding of negligence could give rise to damages. Therefore, a director's duty

129. Company law in Germany is governed by the Commercial Code (Handelsgesetzbuch), elements of the Civil Code, and statutes on distinct business forms such as the Joint Stock Corporation Act (Aktiengesetz or AktG) and the Limited Liability Companies Act (Gesetz betreffend die Gesellschaften mit beschränkter Haftung). *Id.* at 318, 328.

130. *See* sections 93 and 116 of the Aktiengesellschaften [AG] [Law on Stock Corporations], translated in *Commercial Laws of West Germany, in* 24 COMMERCIAL LAWS OF THE WORLD (1990); *see also* Bernard Grossfeld, *Management and Control of Marketable Share Companies, in* 14 INTERNATIONAL ENCYCLOPEDIA OF COMPARATIVE LAW, BUSINESS AND PRIVATE ORGANIZATIONS 4-113 (Alfred Canard ed., 1971).

131. AG, *supra* note 130, § 93(1).

132. *Id.* § 93(2).

133. *See id.*

134. Section 93, para. 2, of the AG stipulates the circumstances under which directors are specially liable if they deviate from the provisions of the AG. *Id.* These include paying investments, interest, or dividends to shareholders; issuing shares prior to the full payment of the nominal value or of the higher issue value; dividing up company property; making payments after the inability to pay has been discovered or involvement in debt has been indicated; granting credit; and issuing delivery shares in the case of conditional increases in capital beyond the purpose established or prior to the complete payment of equivalent value. *Id.* para. 3.

135. *Id.* para. 4.

136. Breskovski, *supra* note 4, at 90.

137. Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156, 1175 (Del. 1995).

of care in Germany is not only procedurally higher than in Delaware, but also substantively more exacting.

4. *France*

Like Germany, France imposes a significantly higher standard of care on directors than does Delaware.

French corporate fiduciary law is based, in part, on French corporation structures. Companies can be managed under one of two distinct management structures: a board of directors *(conseil d'administration)*, or an executive board *(directoire)* and a supervisory board *(conseil de surveillance)*.[138]

The duty of *bons pères de famille* (good fathers of families)[139] extends to French directors. A director must refrain from taking any action contrary to the corporation's best interests and may not foster personal interests while acting in the corporation's name.[140] Furthermore, a director must comply with statutory and board-imposed limitations on powers.[141] In sum, "every fault causing damage is a source of liability."[142]

The board of directors can, subject to the limits of the corporate purpose and to powers expressly reserved to shareholder meetings, act in all circumstances on behalf of the corporation.

A company president is liable for all acts of deputies and for court-imposed duties of control and supervision over board activities of directors.[143] Thus, a company president has the considerable duty expressly to disapprove the board's decision in order to escape joint liability.[144]

France's duty of *bons pères de famille*, prohibiting any action contrary to the corporation's best interests and in a director's personal interest, again exceeds Delaware's lenient duty of care. Furthermore, France's standard of care, lacking Delaware's protective business judgment rule, ranks among the most exacting standards in Western Europe.

C. JAPAN

Unlike under the French and German standards of care, shareholders probably are better protected by the Delaware standard of care than the Japanese standard of

138. JEAN-PIERRE LE GALL & PAUL MOREL, FRENCH COMPANY LAW 98-115 (2d ed. 1992).

139. Breskovski, *supra* note 4, at 90.

140. LE GALL & MOREL, *supra* note 138, at 106 (citing art. L 98 at 1).

141. *Id.* at 123.

142. Director liability can arise in three main areas: failure of the directors to respect statutory law; failure to respect articles of association, notably restrictions placed on director's accounts, and failure to deal properly with employees to ensure correct company management; and negligent, irregular, and improper company management. CODE COMMERCIAL [C. COM.] art. 244, 249 (Fr.), *translated in* 8 COMMERCIAL LAWS OF THE WORLD: FRANCE (1992). Furthermore, directors can also be liable under general tort law provisions. *See* Breskovski, *supra* note 4, at 90.

143. Breskovski, *supra* note 4, at 90.

144. Grossfeld, *supra* note 130, at 4-115, 116.

care.[145] The main source of law governing transactions in Japan is the Commercial Code.[146] Chapter IV of the Code applies to the internal governance of stock companies.[147] Defining the relationship between a director and the company as one of trust (in Japanese *inin*, often translated as "mandate"),[148] the Code provides that the "trustee's (or 'mandatary's') duty is to manage the affairs entrusted to him 'with the care of a good manager.' "[149] Furthermore, the Code, in article 266-3, provides that directors in breach of their duties through "gross negligence" or "bad faith" are jointly and severally liable for damages to third persons.[150]

In addition to the duty of care, the Commercial Code stipulates explicit duties that relate to directors' duty of care. Specifically, directors have a duty to obey all applicable laws, ordinances, and company articles; a duty to perform their duties faithfully on behalf of the corporation; and a duty to obtain approval of either the directors or shareholders if conflicts of interest arise.[151]

However, notwithstanding the Commercial Code's clear substantive duty of care language, shareholders in Japanese corporations do not enjoy the maximum protection the Code offers. Specifically, Japanese administrative agencies inter-

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145. *See generally* M. Evan Corcoran, *Foreign Investment and Corporate Control in Japan: T. Boone Pickens and Acquiring Control Through Share Ownership*, 22 LAW & POL'Y INT'L BUS. 333, 336 (1991). A shareholders' rights comparison in industrialized countries, evaluating disclosure of corporate information, ease with which shareholders can introduce resolutions, shareholder voting rights, shareholder notification of meetings, and shareholder proxy votes, rated Japan a feeble 48 points where the United States was the standard with 100 points. *Id.* at n.22 (citing S. DAVIS, SHAREHOLDER RIGHTS ABROAD: A HANDBOOK FOR THE GLOBAL INVESTOR 25 (1989)). Nonetheless, the Japanese Commercial Code affords some rights to shareholders depending on the percentage of shares held and the length of time that the shares have been held. *See* Corcoran, *supra*, at 339. The most important right afforded to shareholders is the right to vote, and while different classes of stock are permitted by the Japanese Commercial Code, virtually all stock in Japan carries voting rights. *Id.*

146. SHŌHŌ (Commercial Code), Law No. 48 of 1899 (Japan), *translated in* DOING BUSINESS IN JAPAN app. 5A (Z. Kitagawa ed., 1990). The Code provides a framework for the governance of Japanese corporations. It also covers the acquisition of Japanese companies through the purchase of shares and controls actions by corporate directors aimed at defeating attempted takeovers. *Id.* arts. 210, 241(3). The Code, as originally adopted, was primarily modeled after the German Commercial Code (Handelsgesetzbuch) of 1897. HIROSHI ODA, JAPANESE LAW 261 (1992). However, the Code was amended in 1938 after the Geneva Convention and again, based on U.S. antitrust and securities laws, in 1947 and 1950. *Id.* at 262. The Code underwent further major amendments in 1974, 1981, and 1991. *Id.* at 262-63.

147. *See generally* SHŌHŌ, *supra* note 146, ch. IV.

148. KENNETH L. PORT, COMPARATIVE LAW: LAW AND THE LEGAL PROCESS IN JAPAN 341 (1996).

149. *Id.*; *see also* MINPŌ (Civil Code), Law No. 89 of 1896 (Japan) art. 644, *translated in* EHS LAW BULLETIN SERIES FA 1 (1988). Article 265 requires board approval of transactions between a director and the corporation. *Id.* art. 265. Further, directors must address any reasonable question submitted in advance at a shareholders' meeting. Although foreign shareholders could thus question corporate practices at such meetings, directors are able to evade questions by shareholders in practice. *See* T. Boones Pickens, *The Japan We Have to Say "No" To*, HOUSTON CHRON., July 8, 1990, at 1F, 5F (explaining how Japanese management refused to answer Pickens' questions at a shareholders' meeting).

150. PORT, *supra* note 148, at 341.

151. SHŌHŌ, *supra* note 146, art. 254-3.

preting and applying the Code provide only modest shareholder protection, while Japanese courts offer few shareholder safeguards.[152]

Closely tied to the substantive standard of care enunciated in the Commercial Code and its Japanese enforcement is the way Japanese corporations operate. In contrast to U.S. practice, a Japanese board of directors frequently exercises the management authority that typically, in the United States, is vested in corporate officers.[153] Furthermore, unlike the majority of their U.S. counterparts, Japanese directors are bound to the corporation and its employees by a moral element that may be as important as the duties imposed by the Code.[154] Larger Japanese companies frequently guarantee lifetime employment, and directors evaluate the consequences of corporate decisions by the welfare of the employees.[155]

Moreover, in the context of bids for control, some commentators have suggested that because directors typically are lifetime employees and rarely major shareholders, they may subordinate the interests of shareholders to the needs of employees.[156] In addition, Japanese directors are permitted broad discretion in circumstances that in the United States could lead to shareholder litigation.[157] For instance, the Commercial Code allows directors of Japanese firms to issue shares during a takeover attempt to dilute a would-be aquiror's stake in the company.[158] Although this tactic may present a duty of loyalty problem in the United States, in that it damages shareholders' financial interests, diluting a

152. H. LEIGH FFRENCH, INTERNATIONAL LAW OF TAKE-OVERS AND MERGERS: ASIA, AUSTRALIA, AND OCEANIA 3-4 (1986) (addressing the lack of development of case law in the area of shareholders' rights including the traditional preference for nonlitigious dispute resolution and Japan's unitary, or nonfederal, system of governance); *see also* Masayoshi Kanabayashi & Marcus Brauchli, *Japan Shareholder Debate Erupts as Two Firms Join to Fend Off Suitor*, WALL ST. J., July 19, 1989, at A10.

153. While Japanese directors often exercise management control, Japanese shareholders remain fairly silent with respect to managing Japanese companies. Kanabayashi & Brauchli, *supra* note 152. Specifically, the Code offers some protections similar to those of U.S. corporate law, yet the composition of the body of shareholders in Japan makes it unlikely that shareholder proposals opposed by management will be adopted. S. DAVIS, SHAREHOLDER RIGHTS ABROAD: A HANDBOOK FOR THE GLOBAL INVESTOR 25 (1989). This result occurs because the controlling block of stock of many Japanese corporations is held by corporate shareholders that are often not inclined to sell shares on the open market because of their special relationship to the company. *See* Corcoran, *supra* note 145, at 338. As this group of related shareholders is concerned with intercompany stability and cooperation within the group, it is unlikely that a sufficient number of these shareholders would approve the acquisition of any company within the group. *Id.*

154. Corcoran, *supra* note 145, at 3.

155. U.S. EMBASSY IN JAPAN, UPDATE OF INVESTMENT CLIMATE STATEMENT AND INVESTMENT DATA: JAPAN 13 (Feb. 24, 1988).

156. *See* FFRENCH, *supra* note 152, at 23. Stock in large Japanese firms is held in big voting blocks with institutional investors often owning more than 20% of a firm's stock. PORT, *supra* note 148, at 322-23 (1996). In America, in comparison, the largest five shareholders rarely together control 5% of a large firm's stock. *Id.*

157. Corcoran, *supra* note 145, at 322-23 (citing Toshira Nishimura, *M & A Law in Japan: Rules of the Unplayed Game*, MERGERS & ACQUISITIONS, Winter 1983).

158. *See Lifting a Barrier or Two*, ECONOMIST, Aug. 12, 1989, at 68.

would-be acquiror's stake may also protect the corporation from outside influence.[159]

At first glance, the Commercial Code's substantive "good manager" standard appears analogous to Delaware's ordinary prudent person standard. Furthermore, Japan and Delaware have similar enforcement practices for a director's duty of care: Japanese courts and administrative authorities do not offer extensive shareholder protection and Delaware courts are reluctant to recognize duty of care actions. Shareholders in a Delaware corporation, unlike shareholders in a Japanese corporation, generally are not concerned about directors' favoring employee interests over the corporation's interests. However, shareholders in a Delaware corporation also do not benefit from the moral obligation directors in a Japanese corporation have to the corporation itself.

D. Eastern Europe

Bulgaria, the Czech Republic and the Republic of Slovakia, Hungary, and Poland recently have enacted corporate and commercial laws that closely follow American and Western European models.[160]

1. *Bulgaria*

Bulgarian corporations are largely governed by the Bulgarian Law on Commerce. The Law on Commerce does not, in the context of a public limited company, contain any distinct provision delineating a director's standard of care.[161] Nevertheless, members of the "management board" or board of directors are jointly liable for any "damages caused guiltily to the company."[162] Additionally, board members have to insure against their possible liability by depositing security, in the form of stocks or bonds, in an amount specified at a general meeting. This amount may not be less than the board members' remuneration for a three-month period.[163] However, a board member is not liable if the court concludes that the board member has no fault connected with the damage.[164]

Thus, while the still-developing Bulgarian Law on Commerce does not specifically address a director's duty of care, it does address a board member's "fault." In formulating a standard of care, Bulgaria is likely to look to the United States.[165]

159. Corcoran, *supra* note 145, at 338.

160. *See* Breskovski, *supra* note 4, at 79.

161. *Id.* at 93.

162. Bulgaria: Turgovski Zakon [Law on Commerce], Durzhaven Vestnik N. art. 240(1), (2) (1991), *translated in* 1 Central and Eastern European Legal Materials (Vratislav Pechota ed., 1993).

163. *Id.* (citing art. 240(1)).

164. *Id.*

165. Breskovsky, *supra* note 4, at 81.

2. *The Czech Republic and the Republic of Slovakia*

The Czech Republic and the Republic of Slovakia, like Bulgaria, are in the process of developing their corporation laws. Corporate control in public limited companies is vested in a three-tiered system: shareholders (specifically, through a general assembly), a board of directors, and a supervisory or oversight council.[166]

Although corporate fiduciary law is as yet only emerging, directors are bound by a duty to exercise "appropriate care" in fulfilling their obligations.[167] Additionally, directors must maintain confidentiality of information and facts if disclosure to third parties could cause corporate harm.[168] Thus, while a duty of care exists, corporate fiduciary law is cursory at best and, consequently, cannot effectively be compared with Delaware.

3. *Hungary*

Hungarian corporate fiduciary law, also not yet well developed, nonetheless spells out that a director "shall be obliged to act with the care generally expected from persons in such positions."[169] A director that breaches this duty of care is liable pursuant to Hungary's general civil law.[170]

More specifically, directors have responsibilities that relate to the duty of care. Such responsibilities include directing the working organization of the company, exercising the employers' rights, and drafting balance sheets and distribution proposals.[171] While directors can be jointly and severally liable, a director who objects to a decision and reports the objection either to the supervisory board or to the general meeting of shareholders will be relieved of liability.[172]

4. *Poland*

Modern Poland is a reconstruction of territories formerly under the rule of three countries with vastly different legal systems: Austria, Russia, and Germany.[173] Poland's legal system, including its corporate fiduciary law, therefore reflects both its socialist past and its future as part of the EU. Indeed, the Association

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166. *Id.* at 82.

167. Obchodni Zakonik [Czechoslovak Commercial Code of 1991] § 194(5), *translated in* 2 DAVID E. BIRENBAUM, BUSINESS VENTURES IN EASTERN EUROPE AND RUSSIA (2d ed. 1992).

168. *Id.*

169. Breskovsky, *supra* note 4, at 94 (quoting Torveny a Gazdasagi Tarsasagokrol [Act VI of 1988 on Business Organizations], *translated in* 3 HUNGARIAN RULES OF LAW IN FORCE NO. 3-4, art. 32(1) (Feb. 1-15, 1992)).

170. *Id.*

171. KLARA OPPENHEIN & JENNY POWER, HUNGARIAN BUSINESS LAW 19 (1990).

172. *See* Breskovski, *supra* note 4, at 94 (quoting Torveny a Gazdasagi Tarsasagokrol, *supra* note 169); Gyula Gayuer, *Changes in Hungarian Corporate Law*, DE DROIT DES AFFAIRES INTERNATIONALES 526 (1990).

173. *See generally* Bogudar Kordawiewicz & Marek Wierzbowski, *Polish Civil and Commercial Law*, *in* LEGAL REFORM IN POST-COMMUNIST EUROPE 163, 163-64 (Stanislaw Frankowski et al. eds., 1995).

Agreement signed in Brussels in December 1991 obligates Poland to harmonize Polish law with EU legislation.[174]

Poland's standard of care requires directors to execute their duties with the "diligence of a conscientious merchant."[175] However, it is not clear whether the standard of review is subjective or objective.[176] Nonetheless, directors are jointly and severally liable for breaches of their duty of care.

Polish law provides that a joint stock company governance structure consists of the general meeting of shareholders, the management board, and the supervisory board or audit commission.[177] The function of the members of the supervisory board is defined as the " 'exercise of permanent (constant) supervision over company activities encompassing all branches of the enterprise.' "[178]

A director's duties include several specific requirements related to the duty of care. Directors must examine the balance sheet and profit-and-loss accounts, the company's books and documents (to determine that such books and documents are consistent with the actual condition of the company), and the management's reports regarding profits and losses, and submit an annual report to shareholders describing the results of these examinations.[179]

E. People's Republic of China

The development of the People's Republic of China's law, including its corporate fiduciary law, mirrors Chinese economic reforms.[180] Thus, Chinese law retains principles of its past:

> Even allowing for recent developments in China that are tending to blur the rigid outlines of the earlier Soviet economic models, it remains true that since the mid-1950's the major sectors of the industrial and commercial economy, as well as the financial institutions which serve them, have been and are dominated by state enterprises, that is, enterprises under the ownership of the whole people.[181]

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174. The European Agreement, establishing an association between the European Communities on the one hand and the Republic of Poland on the other, was signed in Brussels on December 16, 1996. *Id.* at 169 (citing Dziennik Ustaw [Dz.U.] (Journal of Laws) No. 11, item 38 (1992)).

175. Breskovski, *supra* note 4, at 94.

176. *Id.* (quoting Decree of the President of the Republic, June 27, 1934, Dz.U. (1934) 57/502, amended by Dz.U. (1946) 57/321, (1950) 34/312, (1964) 16/94, (1969) 13/95, (1988) 41/326, (1990) 17/98, art. 290).

177. *Id.* at 84 (citing William Sievers & Andre Spark, *Directors' Duties in Selected Markets: Poland*, 8 Int'l Company & Com. L. Rev. 311 (Aug. 1993)); Birenbaum, *supra* note 167. If the initial capital exceeds five billion zlotys (US$290,000), the corporation has to have a supervisory board, and the latter cannot be replaced by an audit board. Breskovski, *supra* note 4, at 84.

178. Breskovski, *supra* note 4, at 84 (quoting Decree of the President of the Republic, June 27, 1934, Dz.U. (1934) 57/502, amended by Dz.U. (1946) 57/321, (1950) 34/312, (1964) 16/94, (1969) 13/95, (1988) 41/326, (1990) 17/98, art. 382).

179. *Id.* (citing Commercial Code of Poland, art. 382(2)).

180. Kuei-Kuo, Business Law of China 6 (1993).

181. *Id.* at 8-9 (citing Weng, Introduction to Chinese Law 130-34 (1987)).

China adopted its Corporation Law in 1993, modeling it on American and other Western corporation codes.[182] In so doing, China has pursued a distinct mission to meld the organizational structure of Western capitalist business into a political and economic regime that maintains socialist principles and goals.[183]

Under Chinese law, every corporation must have a board of directors generally elected by the shareholders for terms of up to three years.[184] The board then selects managers.[185] Chinese law also creates a "supervisory committee" that oversees the board of directors and assures that the board pursues the policies fixed by the shareholders.[186]

Both directors and supervisors owe fiduciary duties to the corporation and are subject to liabilities for breach. Specifically, directors and supervisors must, analogously to American duties of loyalty, good faith, and care, fulfill their duties "sincerely and diligently."[187] Furthermore, directors must obey administrative rules and company regulations and are responsible for damages if a breach damages the corporation.[188]

Although China does not expressly delineate a director standard of care, the Corporation Law stipulates shareholder rights that may indirectly affect the degree of care directors exercise. Granting shareholders extensive powers, the Corporation Law provides that a "shareholders' meeting is the most powerful authority."[189] Furthermore, the Corporation Law allows the shareholder with the most equity to call and preside over the first shareholders' meeting;[190] permits shareholders to elect and dismiss directors and members of the supervisory committee and set salaries at these meetings; and empowers shareholders to inspect financial records, to issue additional shares, and to vote on mergers, dissolutions, and

182. Robert C. Art & Minkang Gu, *China Incorporated: The First Corporation Law of the People's Republic of China*, 20 YALE J. INT'L L. 273, 274-75 (1995). The primary purposes of the law are: to restructure state-owned enterprises' organization and management; to combat inefficiency; to lessen the state's role in managing business; and to stimulate competition. The state will, however, maintain ultimate control and majority ownership of the largest enterprises. *Id.* at 275 (citing Wu Naitao, *Guarantee for Modern Enterprise System*, BEIJING REV., Apr. 4-5, 1994, at 14).

183. A process of "corporatization" rather than "privatization," China's Corporation Law restructures state enterprises, adopts the corporate form, and institutes stock ownership and trade, but does not give up the state's enterprises and does not forgo the state's ultimate control of production means. *Id.* at 275.

184. Art & Gu, *supra* note 182, at 295 (citing Corporation Law art. 115).

185. *Id.* (citing Corporation Law art. 45).

186. Members of the supervisory committee attend board meetings in a nonvoting capacity, inspect the company's financial affairs, and have the responsibility to prevent the board of directors and company managers from violating regulations and company bylaws. *See id.* at 296 (citing Corporation Law arts. 54, 126).

187. *Id.* (citing Corporation Law art. 128).

188. *Id.* (citing Corporation Law arts. 63, 128).

189. *Id.* (citing Corporation Law art. 128).

190. However, shareholders, directors, or supervisors may call special meetings. *Id.* (citing Corporation Law art. 42).

liquidations.[191] Chinese shareholders have the right to sue for an injunction and damages if a decision of the board "violates laws and administrative rules, and invades the legal interests of the shareholders."[192] In addition, shareholders "consider[] and approv[e] the plan of distribution of profits and recovery for losses."[193] In contrast, American corporate law places those decisions exclusively within the scope of the directors' authority.[194]

Thus, while the Corporation Law does not specifically address a director's duty of care, it still offers shareholders extensive protection through a wide accord of power.[195] In doing so, China's Corporation Law primarily is not oriented to entrepreneurial, capitalist business but rather is designed to restructure state-owned enterprises and private business interests of lesser importance.[196]

F. Canada

Canadian corporation statutes, traceable to the new Ontario Business Corporations Act that was adopted in 1970, draw heavily on U.S. statutory patterns.[197] Canada has, in addition to provincial competition statutes,[198] a federal corporations statute, the Canada Business Corporations Act (CBCA).[199]

Canada is known for highly concentrated share ownership and for the predominant position of a small number of family-based groups as share owners.[200] Consequently, a substantially larger number of Canadian companies with public equity

191. *Id.* While Chinese board procedures and powers are somewhat analogous to those in American corporate practice, the Corporation Law specifies the number of directors, limits director terms to three years, and allows directors not attending a meeting to vote by proxy. *Id.* (citing Corporation Law arts. 112, 115, 118). American corporation laws, on the other hand, generally set no standards on the number of directors, limit terms to one year in most cases, and do not allow directors to vote by proxy. REV. MODEL BUS. CORP. ACT §§ 8.03, 8.05, 8.20 (1991).

192. Art & Gu, *supra* note 182, at 295 (citing Corporation Law art. 111).

193. *Id.* (citing Corporation Law art. 38) (alterations in original).

194. REV. MODEL BUS. CORP. ACT § 8.01(b) (1994) states the general rule that "[a]ll corporate powers shall be exercised by or under the authority of, and the business and affairs of the corporation managed under the direction of, its board of directors. . . ."

195. The Corporation Law defines the powers of shareholders broadly so the government may exercise its ultimate powers over enterprises through stock ownership. The law protects workers and investors through safeguards such as administrative sanctions for managers' breaches of duty as a substitute for the derivative actions used in corporate law outside China. Art & Gu, *supra* note 182, at 297.

196. *Id.*

197. *See* JACOB S. ZIEGEL ET AL., CASES AND MATERIALS ON PARTNERSHIPS AND CANADIAN BUSINESS CORPORATIONS 99 (2d ed. 1989).

198. In addition, securities regulation is a provincial matter in Canada. Deborah A. DeMott, *Oppressed But Not Betrayed: A Comparative Assessment of Canadian Remedies for Minority Shareholders and Other Corporate Constituents*, 56-WTR LAW & CONTEMP. PROB. 181 n.2 (1993).

199. *Id.*

200. Family dynasties significantly impact the destinies of Canadian corporations. *See, e.g.*, Deborah A. DeMott, *Comparative Dimensions of Takeover Regulation*, 65 WASH. U. L.Q. 69, 74 (1987) ("In 1985, . . . nine families were reported to control forty-six percent of the top 300 companies traded on the Toronto Stock Exchange."). Further, over 60% of the 300 large, publicly traded companies included in the Toronto Stock Exchange index have a shareholder or coalition of associated

investors also have controlling shareholders. As a result, more occasions for inter-shareholder conflict arise.

Canadian law differs from U.S. law in a number of significant respects. Specifically, under Canadian law a majority shareholder is not a fiduciary toward the minority, and Canadian statutes expressly protect the interest of a large cast of nonshareholder constituents, who may enforce their rights through private litigation.[201] In *Brant Investments,* the Ontario Court of Appeals held that other components of Canadian law made it unnecessary and even "inappropriate" to impose a fiduciary obligation in favor of minority shareholders on majority shareholders or, for that matter, on directors.[202] The court relied upon the breadth and generality of the remedy for oppression created by the CBCA.[203]

The origins of Canadian oppression remedies are readily traceable to provisions in the English companies acts.[204] Canadian statutory language, however, clearly expands the grievances beyond the "oppressive" acts and omissions covered by the initial English provisions. The CBCA encompasses the corporation's acts and omissions, the conduct of its business, and the exercise of its directors' powers. A complainant may seek relief based on corporate acts and omissions that are " 'unfairly prejudicial to or that unfairly disregard[] the interests of any security holder, creditor, director or officer. . . .' "[205]

Therefore, the choice of framework under which corporate behavior is evaluated and defined by either U.S. fiduciary concepts or Canadian oppression statutes matters greatly.[206] Canadian oppression statutes reflect different assumptions regarding the primacy of shareholders' interests and about the significance of prior contractual definitions for other constituents' expectations and interests.[207] Oppression jurisprudence generally leads to fewer and duller lines of demarcation than does analysis using contractual or fiduciary norms.[208]

The relative conservatism of Canadian judges and the lingering influence of English law explain why Canadian courts have not followed the lead of their

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shareholders with legal control, while only 14% of the index's companies are widely held. *See* Ronald J. Daniels & Jeffrey G. MacIntosh, *Toward a Distinctive Canadian Corporate Law Regime,* 29 OSGOODE HALL L.J. 863, 884 (1992).

201. Brant Investments Ltd. v. KeepRite Inc., 80 D.L.R.4th 161 (Ont. App. 1991).

202. *Id.* at 171, 172.

203. *Id.* Statutory oppression remedies and fiduciary doctrines operate fairly generally. Brian Cheffins, *The Oppression Remedy in Corporate Law: The Canadian Experience,* 10 U. PA. J. INT'L BUS. L. 305, 321-22 (1988). Moreover, as the operative concepts of oppression and fiduciary duty are not precise, these doctrines do not operate with a high level of predictability. Further, because of the oppression statutes' generality, it is difficult to discern, in analytic form, the constituent elements of conduct that violate the statute. *Id.*

204. *Id.*

205. *See* Jeffrey G. MacIntosh, *Bad Faith and the Oppression Remedy: Uneasy Marriage, or Amicable Divorce?* 69 CAN. BUS. REV. 276, 279 (1990).

206. DeMott, *supra* note 198, at 187.

207. *Id.*

208. *Id.*

counterparts in the United States in imposing a fiduciary obligation on majority shareholders. The characteristics of judges, however, do not explain the distinctive legislative contribution to corporate law made by the Canadian oppression statutes. The Canadian system has been said to reflect a dominant value of egalitarianism.[209] For example, the regulation of corporate takeovers in Ontario and Quebec mandates equal treatment of target shareholders to a far larger degree than the same regulation in the United States.[210] Further, the Canadian resolution seems to disfavor clearly drawn demarcations that differentiate among interests created by the varied relationships that creditors, shareholders, and other parties have to a corporation.[211]

III. Conclusion

While the world's securities markets increasingly are internationalized and as countries look to the United States in formulating corporation laws, Delaware's duty of care remains largely impotent. A showing of "gross negligence" that is required to overcome the business judgment rule's presumption is very difficult to meet, as evidenced by the few duty of care decisions in Delaware. Furthermore, a director can show the entire fairness of a transaction even where the court found the director guilty of an "undisputed lack of care" in fulfilling some duties.[212] Consequently, the Delaware duty of care has been said to have very little effect on corporate governance.[213]

As Delaware's duty of care sluggishly evolves, other countries' fiduciary laws are at various stages of development. Western Europe's well-developed standard of care ranges from the United Kingdom's subjective "reasonably diligent person" standard,[214] and Germany's more rigorous orderly prudent business manager standard under which directors bear the burden to show that they did not breach their duties of care,[215] to France's *bons pères de famille* standard under which directors must expressly disapprove of board actions to escape joint liability.[216] Japan offers far less shareholder protection through its court system, administra-

209. *Id.*

210. Indeed, the Ontario Securities Act, subject to a few exceptions, defines any transaction in which a person acquires 20% or more of a class of shares as a takeover bid, which must be made at the same price to all holders in the same class. *Id.* Further, the Ontario Securities Act defines corporate control to be an asset of the corporation. *Id.* The protectable interests of shareholders are similarly equated with those of nonshareholder constituents. *Id.* Canadian oppression statutes minimize the special status of equity investment. This framework makes it difficult for courts to attach explicit fiduciary constraints to any particular relationship created by the corporate form of organization. *Id.*

211. *Id.* at 20.

212. *Cede III*, 663 A.2d 1156, 1175 (Del. 1995).

213. *Id.*; *see* Horsey, *supra* note 12, at 977-80; Chittur, *supra* note 69, at 505; Cohn, *supra* note 69, at 593.

214. *See supra* part II.A.

215. *See supra* part II.B.2.

216. *See supra* part II.B.3.

tive agencies, and Commercial Code.[217] Recently enacted Eastern Europe codes remain largely obscure in searching for a more developed standard of care.[218] Chinese corporate laws, continuously evolving with the country's economy, currently impose a strict duty on directors to fulfill their duties "sincerely and diligently."[219] Finally, Canada, drawing upon oppression remedies, offers less clear lines of demarcation than even U.S. fiduciary laws.[220]

While the world's fiduciary laws are transforming, U.S. investors (and Delaware citizens) are investing in corporations worldwide. U.S. (and Delaware) corporations increasingly are bound by foreign countries' standards of care. The result is that Delaware citizens frequently encounter the greater risks of director misconduct, such as corporate corruption, that arise in developing countries.[221] While Delaware's physical boundaries cease in the United States, its citizens' interests are tied into corporations internationally. Furthermore, countries developing their commercial codes are encouraged to look to the United States in refining their standards of care.[222]

Thus, compelling reasons exist for Delaware to reassess its standard of care in light of corporate internationalization. Not only should Delaware lead the developing world by establishing a more meaningful standard of care, it should protect its citizens doing business abroad. Consequently, Delaware should require directors, prior to invoking the business judgment rule, to make a showing of subjective good faith and due care.[223] Alternatively, Delaware should require a showing of ordinary negligence, as opposed to gross negligence, to overcome the business judgment rule's presumptions.[224] In the final analysis, regardless of how Delaware ultimately formulates its standard of care, its need to look beyond the United States in so doing is fundamental.

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217. *See supra* part II.B.4.

218. *See supra* part II.C.

219. *See supra* part II.D.

220. *See supra* part II.E.

221. The opportunity for corporate corruption may be greater in developing than in developed countries. *See, e.g.*, Horsey, *supra* note 12, at 1961 ("[t]he risk of looting is far higher in emerging than in developed markets."); John Hogarth, *Bribery of Official in Pursuit of Corporate Aims*, 6 CRIM. L. FORUM 557 (1995) (noting corruption in developing countries such as Russia).

222. *See* Breskovski, *supra* note 4, at 80.

223. For a similar analysis, see Dent, *supra* note 70, at 644–45.

224. Directors will still have the business judgment rule's presumptions. But a plaintiff will be able to rebut the rule's presumption of good faith and due care more effectively.