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# INTEGRATING CORPORATE LAW PRINCIPLES WITH CERCLA LIABILITY FOR ENVIRONMENTAL HAZARDS

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## I. INTRODUCTION

Strict liability has rarely been imposed on the corporate officer or director. It is feared, however, that the federal courts may have imposed strict liability in the context of liability exposure for environmental hazards as critics voice concern over the extent and nature of corporate liability resulting under environmental hazard legislation.[1] Commentators have warned corporate officers that they could be held personally liable for the cleanup of corporate environmental hazards regardless of whether they were directly involved in the

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1. *See, e.g.*, Percy L. Angelo & Lynn L. Bergeson, *The Expanding Scope of Liability for Environmental Damage and Its Impact on Business Transactions*, 8 CORP. L. REV. 101 (1985); Tom McMahon & Katie Moertl, *The Erosion of Traditional Corporate Law Doctrines in Environmental Cases*, NAT'L RESOURCES & ENV'T, Fall 1988, at 29; Gregory P. O'Hara, *Minimizing Exposure to Environmental Liabilities for Corporate Officers, Directors, Shareholders and Successors*, 6 SANTA CLARA COMPUTER & HIGH TECH. L.J. 1 (1990); Barbara Billauer, *Directors and Officers Facing New Troubles in Liability Arena*, NAT'L L.J., May 1, 1989, at 22; Dixie L. Laswell, *Corporate Acquisitions and Mergers: Environmental Trap for the Unwary*, CBA REC., July/Aug. 1988, at 17.

wrongdoing.[2] With the average environmental waste cleanup costs in the United States approaching $50 million per site,[3] it is easy to understand corporate concern.

Yet, the outlook for corporate actors is not as grim as it might appear at first glance.[4] A review of the case law indicates that directors and officers have indeed been held personally accountable for corporate decisions to improperly dispose of hazardous wastes, however, further examination reveals that most individuals held liable were the persons who personally participated in the hazardous waste disposal activity.[5] Mere status as a corporate official has not actually given rise to strict liability for corporate violations.

Nevertheless, rather than relying on traditional corporate law principles for guidance in examining director and officer liability under the Comprehensive Environment Response, Compensation and Liability Act (CERCLA), the courts have developed at least three theories for holding individuals liable for corporate environmental torts.[6] It is noteworthy that the courts have not imposed liability upon individual corporate actors under any of these theories without evidence of a significant degree of involvement in the hazardous waste activities.[7] Unfortunately, the language of some of these opinions is rather broad. This language, if considered out of context, may lead future courts to adopt a standard based in liability without fault.

This article proposes an alternative framework for determining whether the corporate official should be held liable for corporate

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2. *See, e.g.*, Johnine Brown, *Corporate Officers May be Liable for Environmental Torts; Even the Passive Ones Stand at the Brink of a Slippery Slope*, ILL. LEGAL TIMES, Feb. 1991, at 18; Robert B. Koegel, *Revisiting Superfund's Personal Liability*, N.Y. L.J., Dec. 17, 1990, at 1; McMahon & Moertl, *supra* note 1, at 29; Margaret Murphy & Paul M. Samson, *Corporate Responsibility for Environmental Damages*, INSIGHTS, Apr. 1990, at 23.

3. Dale R. Jensen & Andrew W. Savitz, *How Owners, Operators Contest CERCLA Costs*, NAT'L L.J., May 18, 1992 at S6. *See also* National Priorities for Uncontrolled Waste Sites, 54 Fed. Reg. 33,846 (1989) (to be codified at 40 C.F.R. pt. 300) (proposed Aug. 16, 1989) (providing an earlier estimate of $20 million per site and stating that 1,226 sites targeted by the Environmental Protection Agency are to be added to the national priority list).

4. *See generally* Lynda J. Oswald & Cindy A. Schipani, *CERCLA and the "Erosion" of Traditional Corporate Law Doctrine*, 86 NW. U. L. REV. 259 (1992) (arguing that CERCLA litigation has resulted in decisions that are, for the most part, consistent with traditional corporate law principles).

5. *Id.* at 263.

6. *Id.* at 273.

7. *Id.*

violations of hazardous waste legislation. Instead of creating new doctrine, courts might employ corporate law doctrine as a useful tool in resolving these difficult issues of liability.

Part I of this article examines relevant federal legislation mandating payment for the cleanup of hazardous wastes. Part II reviews the judicial interpretation of this legislation, and Part III provides an overview of traditional corporate law doctrine. An alternative approach, advocating application of traditional corporate law duties in the context of hazardous waste legislation, is offered and applied in Parts IV and V. Concluding remarks are made in Part VI.

## II. THE ENVIRONMENTAL LEGISLATION

CERCLA has had the greatest impact in the corporate community.[8] Congress hastily enacted CERCLA in 1980 at the end of a lame-duck session[9] and did not provide much guidance regarding interpretation of the statute. Yet, the basic congressional objective in enacting the legislation is relatively clear. Congress sought to authorize the cleanup of hazardous substances released into the environment and to require the parties responsible for the contamination to pay for the costs of the cleanup.[10]

CERCLA describes the parties potentially responsible for the cost of cleanup in section 107(a).[11] These parties include:

> (1) the owner and operator of a vessel or a facility,
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> (2) any person who at the time of disposal of any hazardous substance owned or operated any facility at which such hazardous substances were disposed of,
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> (3) any person who by contract, agreement, or otherwise arranged for disposal or treatment, or arranged with a transporter for transport for disposal or treatment, of hazardous substances owned or possessed by such person . . ., and

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8. Pub. L. No. 96-510, 94 Stat. 2767 (1980) [hereinafter CERCLA], *as amended by* Superfund Amendments and Reauthorization Act of 1986, Pub. L. No. 99-499, 100 Stat. 1613 (1986) (codified as amended at 42 U.S.C. §§ 9601-9675 (1988)).

9. Frank P. Grad, *A Legislative History of the Comprehensive Environmental Response, Compensation and Liability (Superfund) Act of 1980*, 8 COLUM. J. ENVTL. L. 1 (1982).

10. H.R. REP. No. 253 (III), 99th Cong., 1st Sess. 15 (1986), *reprinted in* 1986 U.S.C.C.A.N. 3038, 3038.

11. 42 U.S.C. § 9607(a)(1)-(4) (1988).

> (4) any person who accepts or accepted any hazardous substances for transport to disposal or treatment facilities . . . .[12]

The term "person" is defined by CERCLA to include individuals, corporations, other business associations and governmental entities.[13] The liability exposure of these persons includes:

> (A) all costs of removal or remedial action incurred by the United States Government or a State or an Indian tribe not inconsistent with the national contingency plan;
> (B) any other necessary costs of response incurred by any other person consistent with the national contingency plan;
> (C) damages for injury to, destruction of, or loss of natural resources, including the reasonable costs of assessing such injury, destruction or loss resulting from such a release; and
> (D) the costs of any health assessment or health effects study carried out under section 9604(i) of this title.[14]

Moreover, CERCLA also contains provisions for criminal penalties which may be assessed under certain circumstances.[15]

Section 107(a), providing for liability of owners and operators of hazardous waste facilities,[16] is responsible for much of the concern of corporate actors. Although the statute states that the owner and operator is the potentially responsible party, the courts have uniformly held that either owner or operator status will suffice.[17] Consequently, even though it is relatively clear that corporate officers and directors do not own corporate facilities in their own right, whether these officials might be considered "operators" by virtue of their corporate

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12. *Id.*

13. *Id.* § 9601(21). The statute provides, in relevant part, that "[t]he term 'person' means an individual, firm, corporation, association, partnership, consortium, joint venture, commercial entity, United States Government, State, municipality, commission, political subdivision of a State, or any interstate body." *Id.*

14. *Id.* § 9607(a)(4)(A)-(D).

15. *Id.* § 9603(b).

16. *Id.* § 9607(a)(1).

17. *See, e.g.*, United States v. Fleet Factors Corp., 901 F.2d 1550, 1554 n.3 (11th Cir. 1990); Guidice v. BFG Electroplating & Mfg. Co., 732 F. Supp. 556, 561 (W.D. Pa. 1989); United States v. Moore, 698 F. Supp. 622, 624 n.1 (E.D.

decision-making authority is left unclear. Nevertheless, the courts have proceeded to find corporate officers and directors individually liable under CERCLA section 107(a) for the costs of cleanup of corporate environmental wastes.[18]

These decisions are particularly worrisome to the corporate community in light of the costs of environmental waste cleanup. Corporate officials may not find much solace in reassurances that although the courts speak in terms of strict liability, in practice only those corporate officials actively involved in the hazardous waste activity have been held liable for cleanup costs. There exists the possibility that a court in the future may adopt more expansive liability rules by seizing upon the broad language of prior decisions. This may eventually result in actual application of a strict liability standard for determining the corporate official's liability for corporate environmental violations.

## III. CORPORATE OFFICER AND DIRECTOR LIABILITY UNDER CERCLA AS DEFINED BY THE COURTS: THE THREE THEORIES

The courts have uniformly held that CERCLA contemplates strict liability.[19] Fortunately, for corporate officers and directors, the courts do not appear to have actually applied the strict liability standard against individual defendants. Instead, there are at least three theories the courts have used to hold corporate officials personally liable under CERCLA.[20] Under all three of these theories, liability of individuals is direct rather than derivative. Status in the corporate hierarchy does not appear to have been the basis for liability for corporate violations. Rather, direct involvement in the actual environmental violations appears to be a significant prerequisite to the imposition of individual liability.[21] In fact, activities as a corporate officer, as opposed to a director, appear to be the basis of liability. No director, who was not simultaneously acting as an officer, has been found personally liable for corporate CERCLA violations.[22]

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Va. 1988); Artesian Water Co. v. New Castle County, 659 F. Supp. 1269, 1280-81 (D. Del. 1987), *aff'd*, 851 F.2d 643 (3d Cir. 1988), *cert. denied*, 111 S. Ct. 752 (1991); United States v. Conservation Chem. Co., 619 F. Supp. 162, 190 (W.D. Mo. 1985); City of Philadelphia v. Stepan Chem. Co., 544 F. Supp. 1135, 1140 (E.D. Pa. 1982).

18. *See infra* notes 20-54 and accompanying text.

19. *See, e.g.*, United States v. Monsanto Co., 858 F.2d 160, 167 & n.11 (4th Cir. 1988), *cert. denied*, 490 U.S. 1106 (1989); J.V. Peters & Co. v. Administrator, E.P.A., 767 F.2d 263, 266 (6th Cir. 1985); Southland Corp. v. Ashland Oil, Inc., 696 F. Supp. 994, 1000 (D.N.J. 1988).

20. Oswald & Schipani, *supra* note 4, at 273.

21. *Id.* at 263.

22. *Id.* at 273-74.

The first theory is a personal participation theory,[23] which integrates traditional tort and agency doctrine. Cases decided under this theory include *United States v. Northeastern Pharmaceutical & Chemical Co. (NEPACCO II)*,[24] *United States v. Carolina Transformer Co.*,[25] *United States v. Bliss*,[26] *United States v. Conservation Chemical Co.*,[27] and *United States v. Ward*.[28] In these cases, the respective courts found the corporate officials, who personally participated in the illegal dumping of hazardous materials, accountable for their own actions.[29] Corporate agents who have participated in environmental torts in the name of a corporation have not been permitted to escape personal liability.[30] The results in these cases are consistent with the traditional notion that "[a] corporate officer may be held liable if he personally participates in the wrongful, injury-producing act."[31] It is a basic tenet of agency law that an agent is personally liable for his or her own torts, even if committed on behalf of a principal.[32]

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23. *Id.* at 273.

24. 810 F.2d 726, 743-44 (8th Cir. 1986), *cert. denied*, 484 U.S. 848 (1987) (holding that CERCLA liability was not premised solely on the defendant's status as a corporate officer but also on his high level of participation in arranging for transportation and disposal of hazardous material).

25. 739 F. Supp. 1030, 1036-38 (E.D.N.C. 1989) (finding both the "owner" and "operator" of a company liable based on significant participation in daily business operations including the handling and disposal of hazardous materials).

26. [1990] 20 Envtl. L. Rep. (Envtl. L. Inst.) 20,879 (E.D. Mo. Sept. 27, 1988) (finding a corporate officer liable because he personally arranged for transportation and disposal of hazardous material).

27. 628 F. Supp. 391, 416-20 (W.D. Mo. 1986) (holding an officer, who had developed and implemented waste treatment processes, in violation of CERCLA).

28. 618 F. Supp. 884, 894-95 (E.D.N.C. 1985). *Accord* Riverside Mkt. Dev. Corp. v. International Bldg. Products, Inc., 931 F.2d 327, 330 (5th Cir., 1991); Commonwealth of Mass. v. Blackstone Valley Elec. Co., 777 F. Supp. 1036, 1039 (D. Mass. 1991); United States v. Production Plated Plastics, Inc., 742 F. Supp. 956, 963 (W.D. Mich. 1990). For a thorough discussion of the personal participation theory and the cases decided pursuant thereto, see Oswald & Schipani, *supra* note 4, at 275-82.

29. *See also* Oswald & Schipani, *supra* note 4, at 275 (discussing decisions holding officers individually liable for personal participation in the corporate CERCLA violation).

30. *Id.*

31. United States v. Wade, 577 F. Supp. 1326, 1341 (E.D. Pa. 1983) (citations omitted). *See also* Oswald & Schipani, *supra* note 4, at 275-82 (an individual who personally participated in the CERCLA violation may be held personally liable).

32. *See* Escude Cruz v. Ortho Pharmaceutical Corp., 619 F.2d 902, 907 (1st Cir. 1980) (quoting Lobato v. Payless Drug Stores, 261 F.2d 406, 408-09 (10th Cir. 1958)); Donsco Inc. v. Casper Corp., 587 F.2d 602, 606 (3d Cir. 1978); Snow v. Capitol Terrace, Inc., 602 A.2d 121, 127 (D.C. App. 1992) (quoting Vuitch v.

The second theory is a control-based theory[33] that appears to move closer toward holding corporate officials to a strict liability standard. Examples of cases decided under this theory include *New York v. Shore Realty Corp.*,[34] *United States v. Carolawn Corp.*,[35] and *United States v. Northernaire Plating Co.*[36] These courts held the corporate officers liable for environmental hazards based upon the degree of control they exercised in corporate affairs.[37]

Most of the courts that have articulated a control standard present little cause for concern.[38] Although application of the standard

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Furr, 482 A.2d 811, 821 (D.C. App. 1984)); RESTATEMENT (SECOND) OF AGENCY § 343 (1957); ALFRED F. CONRAD ET AL., ENTERPRISE ORGANIZATION 145 (4th ed. 1987); 3A WILLIAM M. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 1135 (perm. ed. rev. vol. 1986); Oswald & Schipani, *supra* note 4, at 262. *See also* Dudley v. USX Corp., 606 A.2d 916, 923 (Pa. Super. 1992) ("An officer of a corporation can only be held personally liable for the tort of the corporation if he participated in the tort." (citing Wicks v. Milzoco Builders, Inc., 470 A.2d 86 (Pa. 1983))).

33. Oswald & Schipani, *supra* note 4, at 282-91.

34. 759 F.2d 1032, 1042 (2d Cir. 1985). The defendant officer/shareholder in *Shore Realty* was held liable for the environmental hazards created by the corporation's waste disposal site under CERCLA § 107, as well as under state nuisance law. In discussing the defendant's state law liability, the *Shore Realty* court found it to be "beyond dispute" that the defendant personally participated in the activity giving rise to the nuisance. *Id.* at 1052. Nevertheless, when the court addressed the defendant's liability under CERCLA, it stated that "an owning stockholder who manages the corporation . . . is liable under CERCLA as an 'owner or operator.'" *Id.* Thus, the *Shore Realty* court apparently imposed liability upon the officer/shareholder pursuant to a control theory even though a personal participation theory would have sufficed.

35. [1984] 14 Envtl. L. Rep. (Envtl. L. Inst.) 20,699, 20,700 (D.S.C. June 15, 1984). The officers held liable in *Carolawn* were found to have been "personally involved in the operation of the site as a facility at which hazardous substances were stored and disposed of and from which hazardous substances were released." *Id.* at 20,699. Although the *Carolawn* court noted that "CERCLA contemplates personal liability of corporate officials . . . responsible for day-to-day operations of a hazardous waste disposal business," it nevertheless concluded that an individual may be held liable for the CERCLA violation "to the extent that an individual has control or authority over the activities of a facility from which hazardous substances are released or participates in the management of such a facility . . . ." *Id.* at 20,699-700.

36. 670 F. Supp. 742, 747-48 (W.D. Mich. 1987), *aff'd*, 889 F.2d 1497 (6th Cir. 1989), *cert. denied*, 494 U.S. 1057 (1990). In *Northernaire Plating Co.*, the court held the corporate president and sole shareholder personally liable for corporate CERCLA violations due to his control over environmental practices. The officer/shareholder was responsible for the day-to-day operations of the company as well as for arranging hazardous waste disposal.

37. Oswald & Schipani, *supra* note 4, at 282-88. For a thorough discussion of the control theory and the cases decided thereunder, see *id.* at 282-91.

38. *Id.* at 288.

might result in corporate officer liability for corporate activities due to their status in the corporate hierarchy and potential for control of corporate activity, in practice the term "control" has not been applied this broadly. Most corporate officers actually found personally liable under the control test not only occupied positions as corporate officers but were also personally involved in the environmental violations.[39] This application of the control standard does not differ greatly from holding corporate agents accountable for the torts they commit.[40]

At least three courts have, however, issued opinions for which this argument is suspect. In *Vermont v. Staco*,[41] *International Clinical Laboratories, Inc. v. Stevens*[42] and *United States v. Mexico Feed & Seed Co.*,[43] the federal district courts used broad control language and held the corporate officers personally liable for environmental hazards. These courts did not fully describe the officers' roles in the environmental harm.[44] Although it is possible that all of these officers were intimately involved with the hazardous waste disposal activities, it is also possible that the courts may have equated status as a corporate officer with the ability to control environmental affairs.[45]

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39. *Id.* at 282-88.

40. *Id.* at 288.

41. 684 F. Supp. 822, 831 (D. Vt. 1988), *vacated in part*, 31 Env't Rep. Cas. (BNA) 1814 (M.D. Pa. 1990) (dismissing plaintiff's claims under the Federal Water Pollution Control Act and the Resource Conservation and Recovery Act for lack of jurisdiction). Unfortunately, the *Staco* court held two officers of a parent corporation liable for the CERCLA violation of the wholly-owned subsidiary as "owning and managing stockholders" without describing the specific activities of these individuals that may have given rise to liability. The court merely noted that the executive officers had participated in the management and control of the subsidiary without describing the activities giving rise to management and control. *Id.*

42. [1990] 20 Envtl. L. Rep. (Envtl. L. Inst.) 20,560 (E.D.N.Y. Jan. 11, 1990). The *Stevens* court found the corporate president and principal shareholder personally liable for the corporation's environmental tort as an operator under CERCLA § 107(a) due to his "overall management responsibility" for the manufacturing corporation. *Id.* at 20,561. The court provided no discussion of any activities of the officer that may have led to the violation.

43. 764 F. Supp. 565, 571 (E.D. Mo. 1991). The *Mexico Feed & Seed* court held the president and majority shareholder of a waste oil storage company personally liable for the corporate CERCLA violation due to the president's "ultimate authority to control the disposal of hazardous substances" without any discussion of whether the officer was personally involved in any of the corporation's hazardous waste activities. *Id.*

44. *See id.*; *Stevens*, [1990] 20 Envtl. L. Rep. (Envtl. L. Inst.) at 20,561; *Staco*, 684 F. Supp. at 831.

45. *Mexico Feed & Seed*, 764 F. Supp. at 571.

As such, these courts may have imposed strict liability upon the corporate officers. If the earlier courts intended that personal participation in the environmental hazard be a prerequisite to liability, these later decisions may have overlooked this requirement.[46]

The third theory, articulated by the Western District of Michigan in *Kelley ex rel. Michigan Natural Resource Commission v. ARCO Industries Corporation.*[47] requires courts to consider an officer's authority to prevent the environmental harm before assessing personal liability.[48] The court explained that the standard was "different from the issue of personal knowledge, direct supervision or active participation found in most ordinary torts by corporate actors."[49] Factors to be considered under the *ARCO Industries* test are "authority to control . . . waste handling practices,"[50] along with "responsibility undertaken for waste disposal practices,"[51] and "responsibility neglected . . . ."[52] This test would not require that corporate officials be held strictly liable for corporate violations. Rather, corporate officers could be held liable "where strict traditional corporate principles"[53] would not otherwise apply. *ARCO Industries* appears to provide corporate officials with a safe harbor from CERCLA liabilities by encouraging efforts to prevent the harm from occurring.[54]

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46. *Compare* United States v. Northeastern Pharm. & Chem. Co., 810 F.2d 726, 744 (8th Cir. 1986), *cert. denied*, 484 U.S. 848 (1987) (NEPACCO II) (holding officer liable "because he personally arranged for the transportation and disposal of hazardous substances") *and Carolina Transformer*, 739 F. Supp. at 1038 (imposing liability because the officers "knew about the hazardous waste problem and willfully failed to correct it") *with Mexico Feed & Seed*, 764 F. Supp. at 571 (holding the officer liable "as owner and operator at time of disposal of the hazardous waste") *and Stevens*, [1990] 20 Envtl. L. Rep. (Envtl. L. Inst.) at 20,561 (holding the officers liable as "owner" and "operator" within the meaning of the statute) *and Staco*, 684 F. Supp. at 832 (finding the officers liable "in their respective executive capacities").

47. 723 F. Supp. 1214 (W.D. Mich. 1989).

48. *Id.* at 1220.

49. *Id.*

50. *Id.* at 1219.

51. *Id.*

52. *Id.*

53. *Id.*

54. Oswald & Schipani, *supra* note 4, at 294. *See also ARCO Indus.*, 723 F. Supp. at 1220 n.3, wherein the court stated that

> [t]his standard will encourage increased responsibility for two reasons: First, as power grows, the ability to control decisions about waste disposal increases; and second, as one's stake in the corporation increases, the potential for benefiting from less expensive (and less careful) waste disposal practices increases as well.

*Id.*

Although, for the most part, liability under any of the above theories is reserved for active participation in the harm, corporate officials are justifiably concerned over the failure of the courts and Congress to clearly articulate a standard of liability. If corporate officials could rely on future courts to apply the personal participation, control, and prevention theories only where corporate officials directly participate or purposefully turn a blind eye toward unlawful activities, perhaps their apprehension would not be justified. The fact of the matter is, they cannot. In nearly every case where courts discuss personal involvement of corporate officials they also gratuitously offer the insight that CERCLA imposes strict liability.[55] It might be successfully asserted in future cases that all officers and directors, because of the power with which they are vested in the corporate hierarchy, could have in some sense "controlled" or "prevented" the corporation's environmental practices. CERCLA liability exposure would not then be necessarily limited to corporate officers who actively participated in the hazardous waste disposal. The control and prevention theories, if carried to their logical extreme, could expose all corporate officers and directors to liability for corporate environmental violations without evidence of actual involvement in the activities leading to the violations.

## IV. TRADITIONAL CORPORATE LAW DOCTRINE

As noted above, CERCLA explicitly provides that the persons financially responsible for the cleanup of hazardous waste include individuals as well as corporations.[56] All actions taken by the corporation, however, must, as a practical matter, have also been taken by an individual or another legal entity acting for the corporation. The question then becomes whether the individual or entity acting on behalf of the corporation may also be held personally responsible for these acts.

In the traditional model of the corporation, the shareholders might be thought of as occupying the base of a pyramid, the directors

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55. *See, e.g.*, *NEPACCO II*, 810 F.2d at 743; *Carolina Transformer*, 739 F. Supp. at 1035-36; *Bliss*, [1990] 20 Envtl. L. Rep. (Envtl. L. Inst.) at 20,881; *Ward*, 618 F. Supp. at 897.

56. The statute defines "person" as "an individual, firm, corporation, association, partnership, consortium, joint venture, commercial entity, United States Government, state, municipality, commission, political subdivision of a state, or an interstate body." 42 U.S.C. § 9601(21) (1988).

at the next level and executive officers at the top.[57] The officers are elected by the board of directors and execute the policies articulated by the board.[58] The board is elected by the shareholders and charged with managing the affairs of the corporation.[59] In practice, however, many boards only monitor the senior executives who manage the daily business operations.[60]

The directors and officers are said to be in a fiduciary relationship with the corporation and its shareholders.[61] The fiduciary duties include the duties of loyalty[62] and due care.[63] The duty of loyalty requires directors and officers to place corporate interests above personal interests and requires all actions to be taken in good faith

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57. *See, e.g.*, WILLIAM CARY & MELVIN A. EISENBERG, CASES AND MATERIALS ON CORPORATIONS 206-07 (6th ed. 1988); M. Eisenberg, *Legal Models of Management Structure of the Modern Corporation: Officers, Directors and Accountants*, 63 CALIF. L. REV. 375, 376 (1975); Douglas D. Haloftis, Note, *Revising the Texas Corporation's Power to Indemnify Directors: Evaluating, Incurring, and Distributing the Risk of Legal Liability*, 28 S. TEX. L.J. 619, 626 (1987).

58. REVISED MODEL BUSINESS CORP. ACT § 8.41 (1985); ALFRED F. CONARD, CORPORATIONS IN PERSPECTIVE 319 (1976); Haloftis, *supra* note 57, at 626.

59. Barnes v. Andrews, 298 F. 614, 615 (S.D.N.Y. 1924); Polk v. Good, 507 A.2d 531, 536 (Del. 1986); Aronson v. Lewis, 473 A.2d 805, 811 (Del. 1984); DEL. CODE ANN. tit. 8, § 141(a) (1991). *See also* Kaplan v. Peat, Marwick, Mitchell & Co., 540 A.2d 726, 729 (Del. 1988) ("It is a basic principle of the Delaware General Corporation Law that the business and affairs of a corporation shall be managed by the board of directors."); Ivanhoe Partners v. Newmont Mining Corp., 535 A.2d 1334, 1341 (Del. 1987) ("The board of directors has the ultimate responsibility for managing the business and affairs of a corporation."); REVISED MODEL BUSINESS CORP. ACT § 8.01(b) (1985) ("All 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 . . . ."); ERNEST L. FOLK ET AL., FOLK ON THE DELAWARE GENERAL CORPORATION LAW § 141.1, at 95-97 (2d ed. 1988) ("corporate affairs [shall] be managed by an elected board of directors").

60. *See, e.g.*, Lowell Hoit & Co. v. Detig, 50 N.E.2d 602, 603 (Ill. App. Ct. 1943); Burlington Indus., Inc. v. Foil, 202 S.E.2d 591, 603 (N.C. 1974); Haloftis, *supra* note 57, at 628-29; Marcia M. McMurray et al., Special Project Note, *The Corporate Governance Debate and the ALI Proposals: Reform or Restatement?* 40 VAND. L. REV. 693, 704-06 (1987).

61. PRINCIPLES OF CORPORATE GOVERNANCE AND STRUCTURE: ANALYSIS AND RECOMMENDATIONS § 4.01(a) (Tentative Draft No. 11, 1991) [hereinafter T.D. No. 11]; FOLK, *supra* note 59, at § 141.2. *See also* Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985); Field v. Allen, 457 A.2d 1089, 1099-100 (Del. Ch. 1983); Gottlieb v. McKee, 107 A.2d 240, 243 (Del. Ch. 1954); McMurray, *supra* note 60, at 709 (noting that few courts, prior to *Van Gorkom*, held directors liable for breach of the duty of care "absent self-dealing or truly egregious behavior") (citations omitted).

62. *See infra* notes 64-69.

63. One of the earliest cases to recognize the duty of due care was Percy v. Millaudon, 8 Mart. (n.s.) 68, 75-76 (La. 1829). *See also infra* notes 70-80.

and in the honest belief that they are in the corporation's best interests.[64] Examples of transactions which may violate this duty include those involving self-dealing,[65] usurpation of a corporate op-

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64. R. Franklin Balotti & Mark J. Gentile, Commentary from the Bar, *Elimination or Limitation of Director Liability for Delaware Corporations*, 12 DEL. J. CORP. L. 5, 14 (1987). *See also* Wardell v. Railroad Co., 103 U.S. 651, 658 (1880) (holding that directors "are not permitted to occupy a position which will conflict with the interest of the parties they represent"); Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1284 (Del. 1988) ("[C]orporate fiduciaries shall abjure every temptation for personal profit at the expense of those they serve."); Ivanhoe Partners v. Newmont Mining Corp., 535 A.2d 1334, 1345 (Del. 1987) ("The [duty of loyalty] embodies not only an affirmative duty to protect the interests of the corporation, but also an obligation to refrain from conduct which would injure the corporation and its shareholders or deprive them of profit or advantage."); Pogostin v. Rice, 480 A.2d 619, 625 (Del. 1984) ("The consideration . . . implicit in all stock option plans is 'the requirement that [all such plans] contain conditions or that surrounding circumstances are such, that the corporation may reasonably expect to receive the contemplated benefit from the grant of options.'" (quoting Beard v. Elster, 160 A.2d 731, 737 (Del. 1960))); Fliegler v. Lawrence, 361 A.2d 218, 221 (Del. 1976) (explaining that where defendant officers and directors "stood on both sides of a transaction in implementing and fixing the terms of an option agreement," by which one corporation acquired another, burden was on defendants to demonstrate the transaction's intrinsic fairness to the acquiring corporation and its shareholders); Guth v. Loft, 5 A.2d 503, 510 (Del. 1939) (holding that a director or officer has a duty to affirmatively protect the interests of corporation and to "refrain from doing anything that would work injury to the corporation, or to deprive it of profit or advantage which his skill and ability might properly bring to it, or to enable it to make in the reasonable and lawful exercise of its powers"); Grand Metro. Pub. Ltd. v. Pillsbury Co., 558 A.2d 1049, 1055 (Del. Ch. 1988) (holding that a board is obligated to make a determination whether a takeover bid is in the best interest of corporation; court will not reevaluate the board's decision if it is attributable to any rational business purpose) (citing Sinclair Oil Corp. v. Levien, 280 A.2d 717, 726 (Del. 1971))); AC Acquisitions Corp. v. Anderson Clayton & Co., 519 A.2d 103, 115 (Del. Ch. 1986) ("Where director action is not protected by the business judgment rule . . . the transaction can only be sustained if it is objectively or intrinsically fair . . . ."); MacAndrews & Forbes Holdings, Inc. v. Revlon, Inc., 501 A.2d 1239, 1250 (Del. Ch. 1985) (deciding that the business judgment rule does not protect a decision to grant a lock-up option restricting the alienability of shares in an active bidding situation in order to promote an agreement relieving directors of potentially damaging consequences of their own policies taken to defend against a takeover attempt), *aff'd*, 506 A.2d 173 (Del. 1986); ABA Comm. on Corporate Laws, *Corporate Directors Guidebook*, 33 BUS. LAW., 1591, 1599 (1978) [hereinafter *Guidebook*] (explaining that the interests of the corporation and its shareholders must prevail over any individual interest of the director).

65. *See, e.g.*, Andarko Petro. Corp. v. Panhandle E. Corp., 545 A.2d 1171, 1174 (Del. 1988) ("[D]irectors cannot stand on both sides of the transaction nor derive any personal benefit through self-dealing."); Dixmoor Golf Club v. Evans, 156 N.E. 785, 787 (Ill. 1927) (holding that directors are trustees of the corporation and "cannot, in their dealings with the business or property of the trust, use their

portunity,[66] transactions between corporations with interlocking directorates,[67] and loans from the corporation to the director.[68] A director, however, is not held strictly liable for violating this duty. The director may avoid liability by proving the entire "fairness" of the transaction to the corporation.[69]

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relation to it for their own personal gain"); H.B. Cartwright & Bros. v. United States Bank & Trust Co., 23 N.M. 82, 121, 167 P. 436, 453 (1917) (finding that there is no need to show fraud, because the director is required to act with utmost good faith). *See also* McMurray, *supra* note 60, at 626 (stating that self-dealing is perhaps the most obvious example of conflict of interest). *Cf. Sinclair Oil*, 280 A.2d at 720 (noting that parent-subsidiary dealings must be accompanied by self-dealing to evoke the intrinsic fairness standard); Simpson v. Spellman, 522 S.W.2d 615, 619-20 (Mo. Ct. App. 1975) (finding that a director may conduct personal transactions with the corporation if the profits are not unconscionable).

66. *See, e.g.*, Raines v. Toney, 313 S.W.2d 802, 808 (Ark. 1958) (stating that the corporate opportunity doctrine is merely "one phase of the rule of undivided duty and loyalty on the part of corporate fiduciaries"); Sequoia Vacuum Sys. v. Stransky, 40 Cal. Rptr. 203, 206 (Dist. Ct. App. 1964) (finding that a director or officer "may not seize for himself, to the detriment of his company, business opportunities in the company's line of activities"); *Guth*, 5 A.2d at 511 (explaining that if the interests of the corporation are betrayed, it "may elect to claim all of the benefits of the transaction for itself"); Miller v. Miller, 222 N.W.2d 71, 78 (Minn. 1974) ("At the outset we acknowledge the well-recognized, common-law principle that . . . an officer or director . . . may not exploit his position as an 'insider' by appropriating to himself a business opportunity belonging to the corporation."); Klinicki v. Lundgren, 695 P.2d 906, 910 (Or. 1985) ("corporate opportunity doctrine precludes corporate fiduciaries from diverting to themselves business opportunities in which the corporation has an expectancy, property interest or right"); McMurray, *supra* note 60, at 626; *Guidebook*, *supra* note 64, at 1600.

67. *See, e.g.*, Colorado Mgmt. Corp. v. American Founders Life Ins. Co., 359 P.2d 665, 668 (Colo. 1961) ("Once such a transaction is questioned it is thereafter subjected to the closest scrutiny by the courts . . . ."); McMurray, *supra* note 60, at 626. *Cf.* Shlensky v. South Parkway Bldg. Corp., 166 N.E.2d 793, 800 (Ill. 1960) ("transactions between corporations with common directors may be avoided only *if* unfair").

68. *See, e.g.*, MORTIMER FEUER, PERSONAL LIABILITIES OF CORPORATE OFFICERS AND DIRECTORS 59 (2d ed. 1974); McMurray, *supra* note 60, at 626-27.

69. REVISED MODEL BUSINESS CORP. ACT § 8.31(a)(3) (1985). *See, e.g.*, Edelman v. Fruehauf Corp., 798 F.2d 882, 886 (6th Cir. 1986) (ruling that a transaction is invalid unless fair and reasonable or ratified by disinterested directors or shareholders); Pappas v. Moss, 303 F. Supp. 1257, 1280 (D.N.J. 1969) (stating that because defendants "failed to sustain their burden of proving that the transactions were honest, fair and reasonable, they breached their fiduciary duty to the corporation"); International Bankers Life Ins. Co. v. Holloway, 368 S.W.2d 567, 576 (Tex. 1963) ("Contracts between a corporation and its officers and directors are not void but are voidable for unfairness and fraud with the burden upon the fiduciary of proving fairness."); McMurray, *supra* note 60, at 624. *See also* Geddes v. Anaconda Copper Mining Co., 254 U.S. 590, 599 (1921) (holding that the burden is upon those who would maintain the transaction to show its "entire fairness

Throughout the common law, there have been various formulations of the duty of care.[70] Many formulations are analogous to the reasonable person test utilized in tort law.[71] Directors are required to exercise the degree of care that ordinarily prudent persons would exercise under similar circumstances.[72] Some courts have articulated the standard as that of ordinarily prudent persons acting under similar circumstances in the conduct of their own affairs.[73] Today, many states have codified the common law duty of care. The American Law Institute in Tentative Draft No. 11 of its *Principles of Corporate*

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and where a sale is involved the full adequacy of the consideration"); Backus v. Finkelstein, 23 F.2d 531, 535 (D. Minn. 1924) (finding that the burden of proving fairness is on the party seeking to uphold the contract); Robert M. Bass Group, Inc. v. Evans, 552 A.2d 1227, 1239 (Del. Ch. 1988) ("because the fiduciaries charged with protecting the interests of the public shareholders have a conflicting self interest, those fiduciaries must establish the transaction's 'entire fairness' to the satisfaction of the reviewing court"); *AC Acquisitions*, 519 A.2d at 111 ("[W]here a self-interested corporate fiduciary has set the terms of a transaction and caused its effectuation, it will be required to establish the entire fairness of the transaction to a reviewing court's satisfaction."); Popperman v. Rest Haven Cemetery, Inc., 345 S.W.2d 715, 717-18 (Tex. 1961) (burden of proof is on the director).

70. *See infra* text accompanying notes 71-75.

71. *See generally* W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 32, at 173 (5th ed. 1984) (explaining that the reasonable person standard is used because of infinite variety of situations which may arise and with which law must deal; reasonable person is personification of community ideal of reasonable behavior, determined by the jury's social judgment); Krishnan Chittur, *The Corporate Director's Standard of Care: Past, Present and Future*, 10 DEL. J. CORP. L. 505, 507-08 (1985) (finding that business judgment rule is based upon tort law reasonable person standard; liability is imposed in cases of gross error or self-dealing).

72. *See, e.g.*, Briggs v. Spaulding, 141 U.S. 132, 152 (1891); Berkman v. Rust Craft Greeting Cards, 454 F. Supp. 787, 793 (S.D.N.Y. 1978); Graham v. Allis-Chalmers Mfg. Co., 188 A.2d 125, 130 (Del. 1963); McLeod v. Lewis-Clark Hotel Co., 164 P.2d 195, 197-98 (Idaho 1945); Burkhart v. Smith, 161 Md. 398, 403, 157 A. 299, 301 (1931); Neese v. Brown, 405 S.W.2d 577, 581 (Tenn. 1964); FMA Acceptance Co. v. Leatherby Ins. Co., 594 P.2d 1332, 1334 (Utah 1979); Williams v. Fidelity Loan & Sav. Co., 128 S.E. 615, 622-24 (Va. 1925). *See also* Marcia M. McMurray et al., Special Project Note, *An Historical Perspective on the Duty of Care, the Duty of Loyalty and the Business Judgment Rule*, 40 VAND. L. REV. 605, 608 (1987) (finding that modern trend is for courts to consider whether the directors and officers exercised degree of care that an ordinarily prudent person would exercise in a like position and under like circumstances).

In addition, there is some authority for applying a stricter standard of care in cases involving bank directors. This stricter standard has been said to be justified considering the quasi-public nature of banking institutions as well as the nature of the public trust in such institutions. *See, e.g.*, Litwin v. Allen, 25 N.Y.S.2d 667, 678 (Sup. Ct. 1940); Broderick v. Marcus, 272 N.Y.S. 455, 461 (Sup. Ct. 1934); *see also* Cindy A. Schipani, *Should Bank Directors Fear FIRREA: The FDIC's Enforcement of the Financial Institutions Reform, Recovery and Enforcement Act*, 17 J. CORP. L. ___ (1993).

73. *See, e.g.*, Hun v. Cary, 82 N.Y. 65, 71 (1880); Selheimer v. Manganese

*Governance*, requires directors and officers to exercise the care that an ordinarily prudent person would reasonably be expected to exercise under similar circumstances.[74]

Another formulation of the duty of care is that degree of care required to avoid gross negligence.[75] In *Francis v. United Jersey Bank*,[76] for example, the director was held personally accountable for the fraud committed by other corporate officers because of her inattentiveness to corporate affairs.[77] In *Francis*, the director had not read the financial statements, which on their face actually disclosed the fraud, nor had she any knowledge of the business of the corporation.[78] Absolute neglect constituted the basis of her liability.[79] The duty of care requires the board to act as more than a "rubber stamp" for management.[80]

Cases in which directors have been held liable for less than gross negligence are relatively few and far between. One scholar has commented that the search for cases in which directors have been held liable for mere negligence is like searching for a needle in a haystack.[81]

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Corp. of Am., 224 A.2d 634, 640 (Pa. 1966); Spering's Appeal, 71 Pa. 11, 24 (1872); Hodges v. New England Screw Co., 1 R.I. 312, 348 (1850).

74. T.D. No. 11, *supra* note 61.

75. *See* Godbold v. Branch Bank at Mobile, 11 Ala. 191, 200 (1847); *Percy*, 8 Mart. (n.s.) at 74-75, 78; Bart Arconti & Sons v. Ames-Ennis, 340 A.2d 225, 236 (Md. 1975); Nechis v. Gramatan Gardens, Inc., 231 N.Y.S.2d 383, 385 (Sup. Ct. 1962); *Spering's Appeal*, 71 Pa. at 24.

76. 432 A.2d 814 (N.J. 1981).

77. *Id.* at 829.

78. *Id.* at 819, 825-26.

79. *Id.* at 814, 829.

80. *See* DePinto v. Provident Sec. Life Ins. Co., 374 F.2d 37, 46 (9th Cir.), *cert. denied*, 389 U.S. 822 (1967). In *DePinto*, a physician became a corporate director at the request of a friend. The physician was unaware of corporate affairs, not even knowing that the company had operated at a loss for three years. *Id.* Minimal attention would have made him aware enough to investigate a proposal to transfer the company before giving his approval. *Id.* The transfer was to a valueless company. *Id.* at 41, 43-44. *See generally* Heit v. Bixby, 276 F. Supp. 217, 231 (E.D. Mo. 1967) (finding that a director's liability for an officer's breach of trust is not excused by reliance on the officer's apparent trustworthiness); Lutz v. Boas, 171 A.2d 381, 396 (Del. Ch. 1961) (holding directors liable for gross negligence in failing to discover illegal transactions between brokerage firm and its employee).

81. Joseph W. Bishop, Jr., *Sitting Ducks and Decoy Ducks: New Trends in the Indemnification of Corporate Directors and Officers*, 77 YALE L.J. 1078, 1099-100 (1968). Professor Bishop found only four cases in which directors of industrial corporations have been held liable for negligence: New York Credit Men's Adjustment Bureau, Inc. v. Weiss, 110 N.E.2d 397 (N.Y. 1953); Syracuse Television, Inc. v. Channel 9, Syracuse, Inc., 273 N.Y.S.2d 16 (Sup. Ct. 1966); Clayton v. Farish, 73 N.Y.S.2d 727 (Sup. Ct. 1947); Selheimer v. Manganese Corp. of Am., 224 A.2d 634 (Pa.

The lack of such cases may be due, at least in part, to the application of the business judgment rule.

The business judgment rule is the common law "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 was in the best interest of the company."[82] It is a

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1966). *See also* T.D. No. 11, *supra* note 61, § 4.01, at 204, 206 (discussing the scarcity of cases in which directors of industrial corporations were found potentially liable for negligence "uncomplicated by self dealing"). The American Law Institute also notes the following two cases: Meyers v. Moody, 693 F.2d 1196, 1215 (5th Cir. 1982), *cert. denied*, 464 U.S. 920 (1983); DePinto v. Provident Sec. Life Ins. Co., 374 F.2d 37 (9th Cir.), *cert. denied*, 389 U.S. 822 (1967). T.D. No. 11, *supra* note 61, § 4.01, at 204, 206. *See also* Kaplan v. Centex Corp., 284 A.2d 119, 124 (Del. Ch. 1971) (holding that in the absence of proof that directors acted in bad faith or grossly abused their discretion, courts will not interfere with their business judgment); Craig W. Hammond, Note, *Limiting Directors' Duty of Care Liability: An Analysis of Delaware's Charter Amendment Approach*, 20 U. MICH. J.L. REF. 543, 547 (1987) ("Before *Trans Union*, courts rarely found individual directors liable for breaching their duty of care in the absence of some form of self-dealing."). *Cf. Heit*, 276 F. Supp. at 230 ("As a general rule a director of a corporation is not liable for the misconduct of a codirector where he has not participated in the misconduct, unless the loss is the result of his own neglect of duty.") *But cf.* John C. Coffee, Jr., *Litigation and Corporate Governance: An Essay on Steering Between Scylla and Charybdis*, 52 GEO. WASH. L. REV. 789, 796 (1984) (noting that it is important to recognize that most cases, particularly those most favorable to the plaintiff, are resolved by settlement).

82. *Aronson*, 473 A.2d at 812. *See also* Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 954 (Del. 1985) (quoting *Aronson*) (discussing the applicability of the business judgment rule in the takeover context); *Pogostin*, 480 A.2d at 624-25 (finding that the test for determining demand futility as threshold requirement for bringing shareholder derivative action examines the challenged transaction "in relation to issues of independence, interest, and the exercise of business judgment by the directors"); *Sinclair Oil*, 280 A.2d at 720 ("court will not interfere with the judgment of a board of directors unless there is a showing of gross and palpable overreaching") (citation omitted); *Beard*, 160 A.2d at 737 (finding that because stockholder ratification of stock option plan for directors does not supply "the necessary element of good faith exercise of business judgment by Directors," there is the "necessity for the directors to prove that the bargain [was] at least as favorable to the corporation as they would have required if the deal had been made with strangers" (citation omitted)); Auerbach v. Bennett, 393 N.E.2d 994, 1000 (N.Y. 1976) (stating that the business judgment rule "bars judicial inquiry into actions of corporate directors taken in good faith and in the exercise of honest judgment in the lawful and legitimate furtherance of corporate purposes"); Balotti & Gentile, *supra* note 64, at 7-9 (criticizing the modern trend of courts to "scrutinize the decisions of a director . . . even where directors can demonstrate that they acted in good faith and not out of self interest").

The American Law Institute proposes the following formulation of the business judgment rule:

(c) A director or officer who makes a business judgment in good faith

judicial recognition of the directors' right to manage the company.[83] As a consequence, the courts generally will not substitute their judgment for that of the directors',[84] even if the directors are negligent.[85] Although the courts may articulate the standard of care in terms of negligence,[86] they generally have refrained from finding directors liable unless they are grossly negligent.[87]

There are, however, limitations to the application of the business judgment rule. To be entitled to the protection the rule offers, the director may not breach the fiduciary duties of loyalty[88] and due

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fulfills his duty under this Section if:

(1) he is not interested [§ 1.18] in the subject of his business judgment;

(2) he is informed with respect to the subject of his business judgment to the extent he reasonably believes to be appropriate under the circumstances; and

(3) he rationally believes that his business judgment is in the best interests of the corporation.

T.D. No. 11, *supra* note 61, § 4.01(c) (footnotes omitted). This formulation of the rule has been criticized by the Business Roundtable, an organization composed of chief executive officers of approximately 200 large United States corporations, as representing an overly narrow formulation of the business judgment rule. Donald E. Pease, Aronson v. Lewis: *When Demand is Excused and Delaware's Business Judgment Rule*, 9 DEL. J. CORP. L. 39, 74-76, n.177 (1984). In particular, the Business Roundtable objected to the requirements of reasonable inquiry and rational basis, arguing that they were not uniformly accepted in the law and vitiated the protection of the rule. *Id.* (citing Memorandum prepared by Counsel for the Roundtable 7-8 (Jan. 13, 1984)) (criticizing PRINCIPLES OF CORPORATE GOVERNANCE AND STRUCTURE: ANALYSIS AND RECOMMENDATIONS § 4.01(a) (Tentative Draft No. 3, 1984)).

83. *See, e.g.*, *Aronson*, 473 A.2d at 812; Chittur, *supra* note 71, at 506-07.

84. *Selheimer*, 224 A.2d at 644 ("courts are reluctant to interfere in the internal management of a corporation, since that is a matter for the discretion and judgment of the directors and stockholders") (citations omitted); Daniel R. Fischel, *The Business Judgment Rule and the* Trans Union *Case*, 40 BUS. LAW. 1437, 1439 (1985) ("The rule limits the scope of judicial review of the merits of managerial decisions in a wide variety of situations.") (footnotes omitted).

85. *Auerbach*, 393 N.E.2d at 1000 ("[T]he exercise [of corporate directors' powers] for the common and general interests of the corporation may not be questioned, although the results show that what [the directors] did was unwise or inexpedient.") (citation omitted); Bishop, *supra* note 81, at 1095 ("[H]ard fact is that cases in which directors of business corporations are held liable, at the suit of stockholders, for mere negligence are few and far between."); Leo Herzel & Leo Katz, Smith v. Van Gorkom: *The Business of Judging Business Judgment*, 41 BUS. LAW. 1187, 1188 (1986) ("[T]he business judgment rule . . . says that a director is not liable for any mistaken business judgment as long as the director exercised reasonable care."). *See also Aronson*, 473 A.2d at 812 n.6 (noting that the standard is less exacting than simple negligence).

86. *See supra* notes 71-74 and accompanying text.

87. *See supra* notes 81 and 85 and accompanying text.

88. *See supra* notes 62-69 and accompanying text (discussing directors' fiduciary duty of loyalty).

care[89] owed to the corporation.[90] There may not be any evidence of any bad faith or self-dealing that would negate the presumption.[91] One case in which the corporate officials found no protection under the business judgment rule was *Smith v. Van Gorkom*.[92] In that case, the Delaware Supreme Court determined that the directors were grossly negligent in approving a merger agreement.[93] The basis of liability in *Van Gorkom* was the failure of the directors to ascertain the true intrinsic value of the company before agreeing to the proposed bid.[94] The price proposed to the buyer by the chief executive officer was based solely on the feasibility of a leveraged buyout.[95] No fairness opinion was obtained from an investment banker.[96] None of the directors had read the merger documents either before the discussion

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89. *See supra* notes 70-80 and accompanying text (discussing directors' fiduciary duty of care).

90. *See Aronson*, 473 A.2d at 812; Pease, *supra* note 82, at 65.

91. Miller v. AT&T, 507 F.2d 759, 762 (3d Cir. 1974) ("[S]ound business judgement [sic] rule . . . expresses the unanimous decision of the courts to eschew intervention in corporate decision-making if the judgement [sic] of the directors and officers is uninfluenced by personal considerations and is exercised in good faith.") (citations omitted). *See Unocal*, 493 A.2d at 954; *Aronson*, 473 A.2d at 812; *Sinclair Oil*, 280 A.2d at 720; *Auerbach*, 393 N.E.2d at 1000; Kamin v. American Express Co., 383 N.Y.S.2d 807, 810 (Sup. Ct.), *aff'd*, 387 N.Y.S.2d 993 (1976). *See also* Frank H. Easterbrook & Daniel R. Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161, 1195 (1981) ("Without some showing of either bad faith or self-dealing, courts almost uniformly refuse to subject the decisions of managers to review on the merits."); Fischel, *supra* note 84, at 1444 ("The business judgment rule has traditionally precluded judicial review of the merits of business decisions not involving conflicts of interest.").

92. 488 A.2d 858 (Del. 1985). The decision has been highly criticized. *See, e.g.*, Herzel & Katz, *supra* note 85, at 1188-90. *See also infra* notes 103-04 and accompanying text.

93. *Van Gorkom*, 488 A.2d at 881, 884. The agreement called for a cash-out merger in which the shareholders were to receive $55 per share of stock. *Id.* at 867, 868 n.7. Between 1975 and 1979, the stock had traded at a low of $24^1/_4$, and a high of $39^1/_2$. *Id.* at 866 n.5.

94. *Van Gorkom*, 488 A.2d at 876-78. Although directors have the right to rely on information provided by others, they must exercise due care in obtaining all relevant, credible information. *See, e.g.*, DEL. CODE ANN. tit. 8, § 141(e) (1991). This section provides:

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

95. *Van Gorkom*, 488 A.2d at 866.

96. *Id.* at 876.

or before the vote.[97] They voted in favor of the $660 million transaction after only two hours of deliberation following a twenty minute proposal made by the chairman and chief executive officer.[98] Although the court acknowledged that directors are fully protected in relying in good faith on reports made by officers,[99] it nevertheless found that the failure to seek out all reasonably available, relevant information regarding the intrinsic value of the corporation, before agreeing to the merger proposal, constituted gross negligence.[100]

The *Van Gorkom* decision shocked the corporate community.[101] Few courts had ever appeared to be so willing to "substitut[e their] own judgment regarding the proper procedure for the judgment of the board."[102] Many commentators viewed it as a change in Delaware law in degradation of the business judgment rule.[103] Fears were

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97. *Id.* at 868-69.

98. *Id.* The court found that the directors also relied on the supporting representations of the president, the legal advice of their attorney, and their knowledge of the market history of the company's stock. *Id.* at 869.

99. *Van Gorkom*, 488 A.2d at 874-75 n.15. *See supra* note 94.

100. *Van Gorkom*, 488 A.2d at 874, 881.

101. *See, e.g.*, Dierdre A. Burgman & Paul N. Cox, *Corporate Directors, Corporate Realities and Deliberative Process: An Analysis of the* Trans Union *Case*, 11 J. CORP. L. 311, 313 (1986); Chittur, *supra* note 71, at 521; William B. Glaberson & William J. Powell, *A Landmark Ruling that Puts Board Members in Peril*, BUS. WK., Mar. 18, 1985, at 56; Leo Herzel et al., *From the Boardroom Next-to-Last Word on Endangered Directors*, HARV. BUS. REV., Jan.-Feb. 1987, at 38, 39; Thomas C. Lee, *Limiting Corporate Directors' Liability: Delaware's Section 102(b)(7) and the Erosion of the Directors' Duty of Care*, 136 U. PA. L. REV. 239, 247 (1987); Bayless Manning, *Reflections and Practical Tips on Life in the Boardroom After* Van Gorkom, 41 BUS. LAW. 1 (1985); Kristen A. Linsley, Comment, *Statutory Limitations on Directors' Liability in Delaware: A New Look at Conflicts of Interest and the Business Judgment Rule*, 24 HARV. J. ON LEGIS. 527, 527 (1987). *See also Corporate Liability Crisis*, WALL ST. J., Aug. 21, 1986, at 22 (suggesting that the result in *Trans Union* was bizarre). *But see* James S. Altschul, *Corporate Directors' Liability in the U.S.*, INT'L FIN. L. REV., Oct. 1986, at 33, 33. "The [*Van Gorkom*] case does not represent a significant change either in the law itself or in its application, but it does constitute a novel interpretation of the facts." *Id.*

102. *See* Michael Bradley & Cindy A. Schipani, *The Relevance of the Duty of Care Standard in Corporate Governance*, 75 IOWA L. REV. 1, 41 (1989).

103. *See* Burgman & Cox, *supra* note 101, at 313 (citations omitted); Chittur, *supra* note 71, at 525, 542 (suggesting that the decision is a misreading of, or goes beyond, precedent); Glaberson & Powell, *supra* note 101, at 56; Herzel & Katz, *supra* note 85, at 1188-90; Lee, *supra* note 101, at 247, 249; Manning, *supra* note 101, at 1; Linsley, *supra* note 101, at 527. *See also* Herzel et al., *supra* note 101, at 39 (noting that the decision is "more than a little strange," but may actually reflect a growing trend). *But see* Altschul, *supra* note 101, at 33 (contending that the decision does not reflect significant change).

expressed that qualified persons would begin to refuse to serve as directors.[104]

The Delaware legislature's reaction was swift. A mere eighteen months[105] after the Delaware's Supreme Court's decision in *Smith v. Van Gorkom*,[106] the Delaware legislature added section 102(b)(7) to its Business Corporation Act to permit Delaware corporations to adopt or amend their articles of incorporation to limit or eliminate the directors' monetary liability for breach of the duty of care.[107]

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104. *See, e.g.*, Balotti & Gentile, *supra* note 64, at 8; Dennis J. Block et al., *Advising Directors on the D & O Insurance Crisis*, 14 SEC. REG. L.J. 130, 131-32 (1986); Karen L. Chapman, *Statutory Responses to Boardroom Fears*, 3 COLUM. BUS. L. REV. 749, 749-50 (1987); Herzel et al., *supra* note 101, at 38; E. Norman Veasey et al., *Delaware Supports Directors with a Three-Legged Stool of Limited Liability, Indemnification and Insurance*, 42 BUS. LAW. 399, 400-01 (1987); Laurie Baum & John A. Byrne, *The Job Nobody Wants*, BUS. WK., Sept. 8, 1986, at 56; Arthur M. Borden, *First Thoughts on Decision in Delaware on* Trans Union, N.Y. L.J., Feb. 25, 1985, at 1. *But see* William Prickett, *An Explanation of* Trans Union *to "Henny-Penny" and Her Friends*, 10 DEL. J. CORP. L. 451, 463 (1985) (comparing reaction of academics to *Trans Union* decision to that of Henny Penny who believed the sky was falling when a pea fell out of the sky and hit her head); William T. Quillen, Trans Union, *Business Judgment, and Neutral Principles*, 10 DEL. J. CORP. L. 465, 479-88 (1985) (*Trans Union* unlikely to produce devastation predicted by critics because it was decided upon very specific factual grounds so future cases can be distinguished; decision provides guidelines to help directors fulfill duty of care); *Corporate Directors Stay On*, MGMT. REV., July 1987, at 9.

> Despite worries about liability insurance and lawsuits, directors are not walking away from corporate boards in large numbers, as was predicted not too long ago. More than two-thirds of America's large public companies elected no new directors for 1986, and only 12 percent added more than one new member . . . .

*Id.*

105. *Van Gorkom* was decided on January 29, 1985. Section 102(b)(7) became effective on July 1, 1986. DEL. CODE ANN. tit. 8, § 102(b)(7) (Supp. 1990).

106. 488 A.2d 858 (Del. 1985).

107. DEL. CODE ANN. tit. 8, § 102(b)(7) (1991). Corporations may include the following provision in their articles of incorporation:

> A provision eliminating or limiting the personal liability of a director to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, 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; (iii) under section 174 of this title; or (iv) for any transaction from which the director derived an improper personal benefit. No such provision shall eliminate or limit the liability of a director for any act or omission occurring prior to the date when such provision becomes effective. All references in this paragraph to a director shall also be deemed to refer to a member of the governing body of a corporation which is not

This provision does not provide relief from liability for "acts or omissions not in good faith or which involve intentional misconduct . . . ."[108]

A majority of jurisdictions have followed Delaware's lead and have adopted similar legislation.[109] A few of these jurisdictions permit

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authorized to issue capital stock.

*Id.*

Section 174 (referred to in § 102(b)(7)(iii)) concerns proscriptions against the unlawful payment of dividends and unlawful stock purchases and redemptions.

*Id.* § 174.

108. DEL. CODE ANN. tit. 8, § 102(b)(7) (1991).

109. The following statutes are similar to DEL. CODE ANN. tit. 8, § 102(b)(7) (1991): ALASKA STAT. § 10.06.210(1)(N) (1991) (prohibiting limitation of liability for negligent conduct involved in dividend payments or stock repurchases); ARIZ. REV. STAT. ANN. § 10-054(A)(9) (1990) (same); ARK. CODE ANN. § 4-27-202(B)(3) (Michie 1991); CAL. CORP. CODE § 204(a)(10) (Deering Supp. 1992) (prohibiting exculpation for actions showing a reckless disregard or unexcused pattern of inattention); CONN. GEN. STAT. ANN. § 33-290(c)(2) (West Supp. 1992) (capping limitation of liability to an amount not less than compensation the director received that year and providing that there may be no limitation of liability for an unexcused pattern of inattention); FLA. STAT. ch. 607.0831 (1991) (providing exculpation, but no need to include in articles of incorporation, and no exculpation for reckless conduct); GA. CODE ANN. § 14-2-202(b)(4) (Michie 1989); HAW. REV. STAT. § 415-48.5 (Supp. 1991) (prohibiting exculpation for willful or reckless disregard for fiduciary duties or negligent violation of laws regarding dividend payments or stock purchases; may include exculpation provisions in articles of incorporation or bylaws); IDAHO CODE § 30-1-54(2) (Supp. 1991); IND. CODE ANN. §§ 23-1-35-1(a), (c) (West 1989 & Supp. 1991) (providing no exculpation for willful misconduct or recklessness; statute provides exculpation, no need to include in articles of incorporation); IOWA CODE ANN. §§ 490.830, .832 (West 1991); KAN. STAT. ANN. § 17-6002(b)(8) (1988 & Supp. 1992); KY. REV. STAT. ANN. § 271B.2-020(2)(d) (Michie/Bobbs-Merrill 1989); LA. REV. STAT. ANN. § 12:24(C)(4) (West Supp. 1992); ME. REV. STAT. ANN. tit. 13A, § 716 (West 1981 & Supp. 1991) (providing that directors are not liable for breach of duty of due care unless they act dishonestly or without reasonable belief action was in or not opposed to corporate interest; statute provides exculpation, no need to include in articles of incorporation); MD. CORPS. & ASS'NS CODE ANN. §§ 2-405.2, 5-349 (Supp. 1991) (may also expand liabilities in the corporate charter); MASS. GEN. L. ch. 156B, § 13(b)(1½) (1988); MICH. COMP. LAWS § 450.1209(c) (1991); MINN. STAT. ANN. § 302A.111(4)(u) (West Supp. 1992); MISS. CODE ANN. § 79-4-2.02(b)(4) (Supp. 1991); MONT. CODE ANN. § 35-1-216(2)(d) (Supp. 1991); NEB. REV. STAT. § 21-2035(2) (Supp. 1990) (providing that the exculpation provision is applicable to outside directors only); NEV. REV. STAT. § 78.037(1) (Supp. 1991); N.H. REV. STAT. ANN. § 293-A:54 (I-a) (Supp. 1991); N.J. STAT. ANN. § 14A:2-7(3) (West Supp. 1992); N.M. STAT. ANN. §§ 53-11-35(B), -12-2(E) (Michie 1983 & Supp. 1992) (limiting liability but not if the breach of duty constitutes "negligence, willful misconduct or recklessness" on the part of a director); N.Y. BUS. CORP. LAW § 402(b) (Consol. Supp. 1992); N.C. GEN. STAT. § 55-2-02(b)(3) (1990); OHIO REV. CODE ANN. §§ 1701.59(C), (D) (Baldwin Supp. 1991) (providing no exculpation

corporations to limit both director and officer liability for breach of the duty of care,[110] while the Delaware provision only applies to directors.[111]

## V. TRADITIONAL CORPORATE LAW AND CERCLA

Most federal courts deciding issues of individual corporate actor liability seem to be relying intuitively on corporate law principles, regardless of the theory articulated. The basic rule of agency law that agents are liable for the torts they commit on behalf of their principal permeates much of the analysis. Yet this rule is not stated

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for actions taken with a deliberate intent to injure corporation or with reckless disregard of corporate interests; statute provides exculpation, no need to include in articles of incorporation); OKLA. STAT. tit. 18, § 1006(B)(7) (1991); OR. REV. STAT. § 60.047(2)(c) (1989); 15 PA. CONS. STAT. ANN. §§ 513, 1713 (Supp. 1992) (prohibiting exculpation for recklessness; exculpation provision must be in bylaws); R.I. GEN. LAWS § 7-1.1-48(a)(6) (Supp. 1991); S.C. CODE ANN. § 33-2-102 (c) (Law. Co-op. 1990) (prohibiting exculpation for gross negligence; exculpation available only to directors of corporations meeting certain minimum size requirements); S.D. CODIFIED LAWS ANN. § 47-2-58.8 (1991); TENN. CODE ANN. § 48-12-102(b)(3) (1988 & Supp. 1991); TEX. REV. CIV. STAT. ANN. art. 1302-7.06(B) (West Supp. 1991); UTAH CODE ANN. § 16-10-49.1(1) (1992) (providing that exculpation provision may be in articles of incorporation, bylaws or in a resolution); VA. CODE ANN. § 13.1-692.1 (Michie 1989) (stating that exculpation provision may be in articles of incorporation or bylaws; directors' liability is capped at lesser of amount in articles of incorporation or the greater of (a) $100,000 or (b) cash compensation received by the director or officer from the corporation during the 12 months prior to the act or omission for which the liability is imposed); WASH. REV. CODE § 23B.08.320 (1992); WIS. STAT. § 180.0828 (West 1992) (limiting liability unless corporation limits immunity in articles of incorporation); WYO. STAT. § 17-16-834 (1989). *See* Bradley & Schipani, *supra* note 102, at 72; Schipani, *supra* note 72; Paul Vizcarrando Jr. & Theodore N. Mervis, *Court OK's Director Exculpation*, NAT'L L.J., Dec. 16, 1991, at 23, 23.

110. LA. REV. STAT. ANN. § 12:24(c)(4) (West Supp. 1992); MD. CORPS. & ASS'NS CODE ANN. §§ 2-405.2, 5-349 (Supp. 1991); NEV. REV. STAT. § 78.037(1) (Supp. 1991); N.H. REV. STAT. ANN. § 293-A:54(I-a) (Supp. 1991); N.J. STAT. ANN. § 14A:2-7(3) (West Supp. 1992); VA. CODE ANN. § 13.1-692.1 (Michie 1989). *See also* Vizcarrando & Mervis, *supra* note 109, at 23 (discussing director exculpation statutes including the Delaware Chancery Court's approval of the Delaware statute in *In re Dataproducts Shareholder Litig.*).

It is not, however, clear that the Delaware response to the director liability concerns was the best one for all concerned. A recent study of the effects of the legislation draws the conclusion that the legislation may not be in the best interests of the stockholders. *See* Bradley & Schipani, *supra* note 102, at 65. An event study revealed that the relative value of Delaware firms, vis-à-vis firms incorporated elsewhere, fell significantly around the enactment of the legislation. *Id.* at 61-62. Moreover, Delaware firms amending their articles of incorporation to add a section 102(b)(7)-type provision have also suffered statistically significant negative abnormal returns in the wake of this amendment. *Id.* at 62-66.

111. DEL. CODE ANN. tit. 8, § 102(b)(7) (1991).

directly and the rules that have been articulated have potentially far-reaching consequences. No court appears to have considered the direct applicability of traditional corporate law doctrine in the CERCLA context.

As discussed above, corporate officers and directors are considered agents of the corporation and therefore occupy a fiduciary relationship with the corporation and its shareholders.[112] This position of trust requires the officials to exercise due care in all matters of corporate decision making.[113] The fiduciary duty of due care dates back to at least the early 1800's when articulated in *Percy v. Millaudon*.[114] It is a duty for which the courts and corporate officials are well-versed.

This article proposes a direct traditional corporate law analysis for considering the personal liability of individual corporate actors for corporate CERCLA violations. First, the basic rule that an agent is liable for his or her own actions[115] should be applied. It is no defense under general agency principles that an action was committed on behalf of a principal. Such actions expose both the agent and principal to liability. Thus, to the extent the corporate official has personally participated in the corporate environmental violation, he or she should be held personally accountable. The CERCLA cases already decided under a personal participation theory provide solid precedent for this approach.[116] The individuals who commit the environmental violation, as well as the corporation itself, should then be held directly liable under the terms of the statute to the government agencies or private parties engaging in the cleanup.

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112. *See supra* notes 62-74 and accompanying text.

113. *See supra* notes 70-74 and accompanying text.

114. 8 Mart. (n.s.) 68, 74-75, 78 (La. 1829).

115. *See supra* note 32 and accompanying text. *See also* David E. Pierce, *The Emerging Rule of "Liability-Forcing" in Environmental Protection*, 30 WASHBURN L.J. 381, 389 (1991) ("If the stockholder, officer, director, or employee is the actor that commits the tort, and they are pursuing corporate business at the time of their act, the corporation, and the person through which it acts are each liable for the tort.") (citation omitted).

116. *See supra* notes 24-30 and accompanying text. *See also* Donald B. Mitchell, Jr., Josylyn Mfg. Co. v. T.L. James & Co., Inc.: *Integrating CERCLA with the American Common Law Tradition*, 17 COLUM. J. ENVTL. L. 53, 87 (1992) (advocating a "common-law standard of personal participation in the corporation's wrongful conduct" in CERCLA cases); William Scott Biel, Comment, *Whistling Past the Waste Site: Directors' and Officers' Personal Liability for Environmental Decisions and the Role of Liability Insurance Coverage*, 20 U. PA. L. REV. 241, 247 (1991) (supporting business judgment rule protections for directors' and officers' environmental liability).

Second, if corporate officials have not personally participated in the CERCLA violation, but their decisions have exposed the corporation to CERCLA liabilities, they should also be held accountable for their decisions. The inquiry should then focus on whether they have exercised reasonable care rather than on whether they could have in some sense controlled or prevented the environmental harm.[117] Funds recovered for breach of the duty of care could be made available to cover cleanup costs.

The Canadian courts have considered whether directors and officers exercised due care before holding them liable for corporate environmental violations in the criminal arena. For example, in *Regina v. Sault Ste. Marie*,[118] the Supreme Court of Canada held that the directors may defend a charge of violation of the Ontario Water Resources Act[119] by proving that they took all reasonable care.[120] According to the court, "This involves consideration of what a reasonable man would have done under the circumstances."[121] In arriving at this standard, the court sought to strike a balance between a strict liability regime and other causes of action requiring the prosecution to prove a state of mind.[122] Noting that because violations of the Ontario Water Resources Act are considered public welfare offenses, the court held, "They are not subject to the presumption of full *mens rea*,"[123] as are criminal statutes, nor are they subject to absolute liability, which requires a clear directive from the legislature;[124] rather, "the accused may avoid liability by proving that he took reasonable care."[125]

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117. *See supra* notes 61-91 and accompanying text. The corporate officer's and director's duty of care has generally run in favor of the corporation. The proposed approach continues this obligation. Any funds recovered by the corporation for breach of the duty of care would also be made available to cover corporate cleanup costs. It is additionally contemplated, however, that the duty of care analysis could also be used to determine officer and director liability under CERCLA. Rather than consider whether officers and directors could have controlled or prevented the environmental harm, the courts could consider whether they exercised reasonable care.

118. (1978), 85 D.L.R. No. II (3d) 161.

119. Ontario Water Resources Act, R.S.O. ch. 332, § 32(1) (1970) (formerly Ontario Water Resources Commission Act, renamed by ch.1, 1972 S.O. § 70(1)).

120. *Sault Ste. Marie*, 85 D.L.R. No. II (3d) at 181.

121. *Id.*

122. *Id.* at 181-82.

123. *Id.* at 182.

124. *Id.*

125. *Id.* at 183.

More recently, the Provincial Division of the Ontario Court of Justice in *The Queen v. Bata Industries Ltd.*[126] attempted to clarify directors' and officers' responsibilities under criminal environmental laws. In *Bata Industries*, two corporate directors were convicted for criminal violations of the Ontario Water Resources Act.[127] The court considered whether the likelihood of an unlawful discharge was reasonably foreseeable and whether the directors took reasonable precautions in accordance with the standards of their industry.[128] According to *Bata Industries*, the "minimum profile against which directors' liability could be measured" involved examination of the following factors:

- Did the Board Directors establish a pollution prevention "system" . . . . was there supervision or inspection? Were there improvements in business methods? Did he exhort those he controlled or influenced?
- Did each director ensure that the corporate officers have been instructed to set up a system sufficient within [the] terms and practices of its industry of ensuring compliance with environmental laws, to ensure that the officers report back periodically to the Board on the operation of the system[,] and to ensure that the officers are instructed to report any substantial non-compliance to the Board in a timely manner?
- [The] directors are responsible for reviewing the environmental compliance reports provided by the officers of the corporation [but] are justified in placing *reasonable* reliance on reports provided to them by corporate officers, consultants, counsel or other informed parties.
- The directors should substantiate that the officers are promptly addressing environmental concerns brought to their attention by government agencies or other concerned parties including shareholders.

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126. (Ont. Ct. J., Prov. Div., Belleville, Hastings Co., Feb. 7, 1992). *See also* Michael I. Jeffrey, *Environmental Liability for Directors and Officers in the Aftermath of the* Bata Industries *Decision*, ENVIROFLASH (Frazer & Beatty, Barristers and Solicitors, Toronto, Ont.), Mar. 1992, at 1 (discussing the liability ramifications of *Bata Industries* to officers and directors).

127. *Bata Indus.*, slip op. at 42-45.

128. Jeffrey, *supra* note 126.

- The directors should be aware of the standards of [their] industry and [other] industries which deal with similar environmental pollutants or risks.
- The directors should immediately and personally react when they have notice the system has failed.
- Within this general profile and dependent upon the nature and structure of the corporate activity, one would hope to find remedial and contingency plans for spills, a system of ongoing environmental audit, training programs, sufficient authority to act and other indices of a pro-active environmental policy.[129]

The *Bata Industries* court proceeded to find that the minimum profile existed and held two of the three defendant directors criminally liable for the offenses.[130]

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129. *Id.* at 3-4 (quoting *Bata Indus.*, slip op. at 39-40). It is interesting to note that, before articulating its "minimum profile," the Canadian court quoted a passage from Kelley *ex rel.* Michigan Natural Resource Comm'n v. ARCO Indus. Corp., 723 F. Supp. 1214 (W.D. Mich. 1989), in which the American court focused on the individual authority to control, and evidence of responsibility undertaken in developing, a legal standard by which corporate officers and directors may be held liable. *Bata Indus.*, slip op. at 37-38.

130. *Bata Indus.*, slip op. at 40-45. There were three director-defendants in *Bata Indus.*, Messrs. Thomas G. Bata, Douglas Marchant, and Keith Weston. Mr. Bata was found not guilty of the environmental offenses. The court stated that he was the "[d]irector with the least [ ] contact with the plant . . . ." *Id.*, slip op. at 41. The court further noted that Mr. Bata visited the site of the offending plant only once or twice per year and that when a problem with chemical storage was brought to his attention, he immediately reacted to minimize the effect of the problem on the environment. The court saw no evidence that Mr. Bata was aware of the environmental problems at issue. Matters brought to his attention were responded to "promptly and appropriately." *Id.*, slip op. at 42.

The court did, however, convict Messrs. Marchant and Weston of the environmental offenses. *Id.*, slip op. at 42-45. There was evidence that the environmental problem was brought to Marchant's personal attention. *Id.*, slip op. at 42. In the six months that he knew of the problem, Marchant took no action. The court found that "[h]e had a responsibility not only to give instruction but also to see to it that those instructions were carried out." *Id.*, slip op. at 43. His delay showed lack of due diligence.

Mr. Weston was also convicted. Weston's defense stressed the fact that Bata Industries committed $250,000 (CDN) for a water treatment system for the village during Weston's tenure. *Id.*, slip op. at 43-44. This evidence did not, however, convince the court of Weston's due diligence. Instead, the court found that the evidence merely showed that the Bata family cared for the village. It was the Bata family who donated the needed land and established the financial amounts for assistance. *Id.*, slip op. at 44.

Moreover, Weston was said to be an "on-site" director. "He demanded the

The Ontario criminal law approach appears to impose liability upon corporate officials for acts of negligence and is somewhat analogous to the approach advocated in this article. Instead of simply focusing on the amount of control or power required to prevent the harm that the individual possesses in the abstract, courts should also consider whether the individual exercised reasonable care. The question becomes whether the individual exercised the care of a reasonably prudent person acting under similar circumstances. State law could be invoked to determine whether simple or gross negligence standards should be applied. If the corporate official has not exercised reasonable care, then liability would ensue.

The Canadian approach is of course not directly analogous to the CERCLA issues at hand. The reasonable care standard in Canada is a defense to a violation of a criminal statute. Pursuant to *Sault Ste. Marie* and *Bata Industries*, once the government has proven that an environmental violation has taken place, the burden of proof shifts to the individual defendants to show that their actions were reasonable under the circumstances. The focus of this article, however, is potential civil liability of individual corporate actors. The proposal advocated in this article does not contemplate burden-shifting; rather, the burden of proof would remain on the plaintiff to prove breach of the duty of care by a preponderance of the evidence as it would in any other civil case involving a breach of duty. The *Bata Industries* factors, however, could be considered in determining whether a corporate officer or director exercised reasonable care.

## VI. APPLICATION OF THE ALTERNATIVE CORPORATE LAW APPROACH

To illustrate the application of an alternative corporate law approach, consider the facts in *NEPACCO II*,[131] where the Eighth

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authority to control his work environment before he took the job. He had experience in the production side and was aware toxic chemicals were used in the process. He was reminded of his environmental responsibilities . . . ." *Id.*, slip op. at 44. The court further noted that a red flag should have been raised regarding the environmental problems. *Id.* Weston obtained a price quote for $58,000 (CDN) for removal of a chemical waste drum. *Id.* The court said that he should have made inquiries regarding why the quote was so high rather than merely accepting a second quote of $28,000 (CDN). *Id.* The business judgment rule did not protect him because of the failure to make an informed decision. *Id.*

In a later hearing, Marchant and Weston were each fined $12,000 (CDN). The Queen v. Bata Indus. Ltd., (Ont. Ct. J., Prov. Div., Belleville, Hastings Co., Apr. 6, 1992).

131. 810 F.2d 726 (8th Cir. 1986), *cert. denied*, 484 U.S. 848 (1987).

Circuit focused on the vice-president's personal participation in the environmental harm before finding him personally liable as a generator of hazardous waste.[132] In *NEPACCO II*, a decision was made to dispose of dioxins by transporting them to a farm, digging a trench, and burying them in the trench.[133] The vice-president "assisted in the selection"[134] of the site, "had direct knowledge and supervision"[135] of the contract with the transporter, and was "directly responsible for arranging for the transportation and disposal of the . . . hazardous substances."[136]

This personal participation would find no safe haven under the proposed analysis. Corporate agents who directly participated in such activities could be held directly liable under the terms of the statute for their actions. Such actions were engaged in purposefully, with reckless if not intentional disregard for the environmental laws. It, therefore, follows that the officers might also be found in breach of their duty of care. The business judgment rule does not protect reckless or intentional misconduct.

Nor would the officers that were held accountable in *United States v. Carolina Transformer Co.*,[137] *United States v. Bliss*,[138] *United States v. Conservation Chemical Co.*,[139] or *United States v. Ward*[140] find that a traditional corporate law approach would have protected them from liability for their environmental misdeeds. These officers were also directly involved in the decisions and activities resulting in environmental law violations.[141] All of them could be held directly liable under the terms of the statute, and traditional agency theory, for their personal participation in the environmental wrongs. They might also be found in violation of their duty of care by either recklessly or intentionally exposing the corporation to CERCLA liability.

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132. *Id.* at 742-46.

133. *Id.* at 730.

134. United States v. Northeastern Pharm. & Chem. Co., 579 F. Supp. 823, 847, *modified*, 810 F.2d 726 (8th Cir. 1986), *cert. denied*, 484 U.S. 848 (1987).

135. *Id.*

136. 810 F.2d at 743.

137. 739 F. Supp. 1030 (E.D.N.C. 1989).

138. [1990] 20 Envtl. L. Rep. (Envtl. L. Inst.) 20,879 (E.D. Mo. Sept. 27, 1988).

139. 628 F. Supp. 391 (W.D. Mo. 1986).

140. 618 F. Supp. 884 (E.D.N.C. 1985).

141. *See Carolina Transformer*, 739 F. Supp. at 1038 (stating that directors were aware of polychlorinated biphenyl (PCB) problems yet decided to release PCBs into the environment and ignore an engineer's plan to avoid the damage); *Bliss*, [1990] 20 Envtl. L. Rep. (Envtl. L. Inst.) at 20,879 (finding that officers of a corporation

The proposed corporate law approach would require courts utilizing the control and prevention theories to also consider whether the individual corporate actor directly participated in the environmental harm and the degree of care exercised in making the corporate decisions. Cases such as *New York v. Shore Realty Corp.*,[142] *United States v. Carolawn*,[143] and *United States v. Northernaire Plating Co.*,[144] in which the courts found liability under a control test, may still result in individual liability. Rather than simply stating that liability is based upon being the person "in charge"[145] of a facility, the premise for direct liability under CERCLA in *Shore Realty*[146] would have to include the officer's personal participation in the environmental harm. The officer in *Shore Realty* knew that hazardous wastes were stored at the property he purchased for the corporation,[147] and did nothing to prevent approximately 90,000 gallons of additional chemicals to be dumped on the site.[148] Similarly, rather than base officer liability in *Carolawn* solely upon "the extent that an individual has control or authority over the activities of a facility from which hazardous substances are released or participates in the management of such a facility,"[149] liability would be premised upon personal involvement in the operation of the site.[150] Likewise, the president making the decisions regarding the chemical waste disposal in *Northernaire Plating*[151] would be held liable for his direct participation in the decisions resulting in the corporation's contamination of a particular site.

Analysis based in traditional corporate law should prevent the limited analysis employed by the courts in *Vermont v. Staco*,[152] *International Clinic Laboratories, Inc. v. Stevens*[153] and *United States v. Mexico*

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that owned a site where hazardous waste was disposed, gave permission and assisted in the unloading); *Conservation Chem.*, 628 F. Supp. at 420 (finding that the founder, chief executive officer, and majority stockholder conceived of, and implemented, several waste processes that led to the disposal of hazardous waste into lagoons); *Ward*, 618 F. Supp. at 890-91 (stating that corporation's president and principal shareholder knowingly allowed a transporter to continue disposing PCB-contaminated oil on a military reservation and along various North Carolina roadways).

142. 759 F.2d 1032 (2d Cir. 1985).

143. [1984] 14 Envtl. L. Rep. (Envtl. L. Inst.) 20,699 (D.S.C. June 15, 1984).

144. 670 F. Supp. 742 (W.D. Mich. 1987), *aff'd*, 889 F.2d 1497 (6th Cir. 1989), *cert. denied*, 494 U.S. 1057 (1990).

145. *Shore Realty*, 759 F.2d at 1052.

146. 759 F.2d 1032 (2d Cir. 1985).

147. *Id.* at 1038.

148. *Id.* at 1039.

149. *Carolawn*, [1984] 14 Envtl. L. Rep. at 20,699-700.

150. *Id.* at 20,699.

151. 670 F. Supp. 742 (W.D. Mich. 1987), *aff'd*, 889 F.2d 1497 (6th Cir. 1989), *cert. denied*, 494 U.S. 1057 (1990).

152. 684 F. Supp. 822 (D. Vt. 1988).

153. [1990] 20 Envtl. L. Rep. (Envtl. L. Inst.) 20,560 (E.D.N.Y. Jan. 11, 1990).

*Feed & Seed Co.*[154] In *Staco*, the court only described the level of personal involvement of the defendants as "owning and managing stockholders"[155] and based liability on "their respective executive capacities in the corporate structure."[156] In *Stevens*, the corporate president was held liable due to "overall management responsibility."[157] Similarly, the president in *Mexico Feed & Seed*[158] was found "in charge of and directly responsible for all of the . . . operations . . . ."[159]

These cases, if decided pursuant to the proposed corporate law approach, could not be decided on such limited facts. A traditional corporate law approach would mandate examination of the actual activities of the officers prior to determining liability. Such evidence is necessary in order to determine first, whether the officers personally participated in the CERCLA violation and are thus directly liable to outside parties under the provisions of CERCLA and second, whether the officers might be held liable for breach of their duty of care.

Finally, consider the *ARCO Industries* court and its prevention standard.[160] The *ARCO Industries* court articulated a standard it found necessary to prevent officers from failing to become involved in environmental decisions.[161] Although this standard incorporated a safe haven from liability to those officers who made efforts to prevent the harm,[162] it could, like the control test, reasonably evolve into a strict liability standard. If failure to exercise authority to prevent the harm is indeed considered sufficient to justify the imposition of personal liability, every corporate official might be said to possess such authority. Unfortunately, the court in *ARCO Industries* did not have occasion to actually apply its standard to particular facts.

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154. 764 F. Supp. 565 (E.D. Mo. 1991).
155. *Staco*, 684 F. Supp. at 832.
156. *Id.*
157. *Stevens*, [1990] 20 Envtl. L. Rep. at 20,561.
158. 764 F. Supp. 565 (E.D. Mo. 1991).
159. *Id.* at 571.
160. Kelley *ex rel.* Michigan Nat. Resources Comm'n v. ARCO Indus. Corp., 723 F. Supp. 1214 (W.D. Mich. 1989).
161. *Id.* at 1219.
162. *Id. See also* Oswald & Schipani, *supra* note 4, at 294 (citing *ARCO Industries* where the test for liability provides "a safe harbor for those individuals who attempt, albeit unsuccessfully, to prevent or alleviate the harm, thereby providing a direct incentive for individuals to undertake preventative measures").

The proposed traditional corporate law analysis should serve to promote the goals of the prevention standard while discouraging a conclusion of liability based solely on status. The *ARCO Industries* court expressed concern that a test which bases liability upon personal participation may encourage corporate officials to turn a blind eye toward corporate environmental concerns.[163] Imposing personal liability on the officials for breach of their duty of care should go a long way toward achieving the goals of the *ARCO Industries* court. First, corporate officers who fail to inform themselves of corporate affairs have been held liable for breach of their duty of care.[164] Second, the duty of care does not permit a corporate official to turn a blind eye toward corporate affairs.[165] Thus, the proposed corporate law analysis should encourage corporate officials to take an active role in environmental affairs without fear that their involvement will result in strict liability.

As discussed above, most jurisdictions permit corporations to limit the monetary liability exposure of corporate directors to the corporation for breach of the duty of care.[166] A few states also make this provision available to officers.[167] To the extent a corporation has adopted a provision in its articles of incorporation to eliminate or limit directors' or officers' liability for breach of the duty of care, these parties would not be held monetarily liable to the corporation for CERCLA violations, even if the breach of duty involved acts of gross negligence. The corporate actors would, however, still be held accountable for intentional misconduct and actions taken in bad faith.[168] It is important to note that this result would not be unique to consideration of CERCLA liabilities. The result in the CERCLA context would be consistent with the results in any other context where breach of the duty of care has been alleged.

If current trends are accurate predictors of the future, these exculpatory provisions would most likely have little effect on the

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163. *ARCO Indus.*, 723 F. Supp. at 1220.

164. *See supra* notes 76-80, 92-100 and accompanying text.

165. *Id.*

166. *See supra* note 109 and accompanying text.

167. *See supra* note 110 and accompanying text.

168. *See, e.g.*, DEL. CODE ANN. tit. 8, § 102(b)(7) (1991). The Delaware statute was recently applied by the Delaware Chancery Court in *In re* Dataproducts Corp. Shareholders Litig., [1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) § 96,227 (Del. Ch. Aug. 22, 1991), *reprinted in* 17 DEL. J. CORP. L. 1159 (1992). The court stated that § 102(b)(7) "exculpate[s] the directors from liability for monetary damages for acts amounting to gross negligence." *Id.* at 91,183, *reprinted in* 17 DEL. J. CORP. L. at 1169. *See also* Vizcarrando & Mervis, *supra* note 109, at 23 (discussing limitations on the Delaware director exculpation).

proposed corporate law approach. As discussed above, in no case reported to date has a director, who was not also an officer, been held liable for CERCLA violations.[169] In fact, it was these individuals' actions as officers, not as directors, that led to liability.[170] Most states that permit liability limitations permit such relief for directors only. Officers are still generally held accountable to the corporation for breach of the duty of care.

CERCLA mandates that responsible parties be held liable for environmental harms.[171] CERCLA does not direct the courts to defy traditional corporate law dictates in the process. The corporation itself is still held strictly liable for its CERCLA violations. Neither the terms of the statute, nor its legislative history direct the courts to ignore corporate law doctrine when defining potentially responsible parties.[172] If Congress desires to hold individual officers and directors liable without fault for corporate violations of the statute, the statute should be appropriately amended to clearly reflect this drastic change in corporate law.

## VII. CONCLUSION

The purpose of the environmental legislation is to hold all parties responsible for hazardous waste pollution financially accountable for its cleanup.[173] Difficulty arises in the determination of the responsible parties, particularly when the violation involves corporate liability.

Although it is clear that CERCLA was meant to impose liability on both corporations and individuals,[174] it is not clear that the intent was to hold corporate officers and directors strictly liable for corporate violations. Under general principles of corporate law, corporate officers and directors are held directly liable to third parties for the

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169. *See supra* text accompanying note 22.

170. *Id.* It should also be noted that it would not be necessary for a court deciding whether to impose CERCLA liability on a corporate director to consider state exculpatory legislation. State exculpatory legislation merely permits director exoneration from monetary liability to the corporation or its shareholders. A court applying the alternative approach advocated in this article could find that the director is liable for the CERCLA violation due to his or her failure to exercise reasonable care. This would not necessarily involve only monetary liability to the corporation but may also include monetary liability to the CERCLA plaintiff.

171. *See supra* text accompanying note 10.

172. *See supra* notes 8-14 and accompanying text.

173. *Id.*

174. *See supra* note 13 and accompanying text.

torts they commit[175] and held accountable to the corporation for their decisions but enjoy the protection of the business judgment rule. Under the business judgment rule, informed decisions made in good faith with the honest belief that they are in the best interest of the corporation generally do not subject the officer to personal liability.[176] Business judgment rule protection is available provided that the officers have not violated their fiduciary duties of loyalty and due care.[177] The directors and officers are obligated to ascertain all relevant and reasonably available information before making a decision.[178] The business judgment rule affords protection only in the cases where a decision is made. It does not protect a corporate official who fails to act.

In the context of environmental statute violations, the courts have been accused of disregarding these general principles of corporate law.[179] Although not directly employing corporate law principles, the results the courts have reached to date appear largely consistent with traditional corporate law analysis.[180] The consistency may be the result of the relatively easy situations that have been presented to the courts thus far. In most of these cases, the officer held liable for corporate CERCLA violations personally participated in the corporation's egregious hazardous waste disposal method and would have been held liable under traditional corporate law analysis anyway. Yet, the courts have not articulated corporate law analysis in their opinions and have instead created new theories. These theories, if taken to their logical conclusions, might be used in a future, less-compelling case to drastically erode familiar corporate law notions.[181]

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175. *See supra* notes 31-32 and accompanying text.

176. *See supra* note 82-85 and accompanying text.

177. *See supra* notes 88-91 and accompanying text.

178. *See supra* notes 94, 100 and accompanying text.

179. *See supra* notes 1-2 and accompanying text.

180. *See* Oswald & Schipani, *supra* note 4, at 329.

181. For example, the court in Conductron v. Williams, 785 F. Supp. 271 (D.N.H. 1991), appears to have come dangerously close to adopting a rule that would hold managing shareholders personally liable for corporate CERCLA violations because of their status in management, rather than requiring personal participation in the environmental wrong. In *Conductron*, defendant Pappas was the sole stockholder of O.K. Tool, a corporation alleged to be a "potentially responsible party" for the contamination of the Savage Well Superfund site. *Id.* at 273. Pappas contended that the alleged contamination occurred before his ownership of O.K. Tool. *Id.* at 275. Pappas also argued that "corporate officers and shareholders who do not participate in the corporation's tort" should not be held personally liable

It would, however, be consistent with both corporate law notions and the intent of the environmental statutes to hold corporations strictly liable for corporate acts and to analyze the individual corporate actor's liability in accordance with traditional corporate law doctrine. Thus, the relevant analysis before imposition of personal liability for response costs on corporate officers and directors might be (1) whether the officials are directly liable under CERCLA for their personal participation in the environmental harm in accordance with traditional agency analysis, and (2) whether they are personally liable for failure to exercise due care. This analysis should discourage officials from ignoring corporate environmental affairs in order to avoid liability based upon personal participation. Turning a blind eye toward corporate affairs should still result in personal liability for failing to act with due care while mere status as a corporate official should not result in strict liability for corporate environmental wrongs.

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for that tort. *Id.* The *Conductron* court disagreed, citing New York v. Shore Realty, 759 F.2d 1032 (2d Cir. 1985), for the control test and held that the defendant shareholder "could well be found to be an 'owner and operator . . . .'" *Conductron*, 785 F. Supp. at 276.

> Pappas [was] the sole owner of the company which ultimately owns the contaminating facility. Like LeoGrande [the *Shore Realty* individual defendant], Pappas purchased this facility with full knowledge of its environmental problems. And like LeoGrande, Pappas has exerted and apparently maintains the power to exert a high degree of control over both the facility and the corporate entities . . . which own it.

*Id.* The court thus denied Pappas' motion for summary judgment.

The *Conductron* court failed to note that the individual defendant, LeoGrande, held liable for corporate CERCLA violations by the *Shore Realty* court, was "in charge of the operation of the facility in question." *Shore Realty*, 759 F.2d at 1052. The *Conductron* court did not address specific involvement in the environmental violations or the offending facility.