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The Modest Business Judgment Rule

*By Lyman Johnson**

INTRODUCTION

This Article argues that Delaware courts both wrongly formulate the business judgment rule and unsoundly make it the centerpiece of corporate fiduciary analysis. The faulty formulation stems from a 1984 Delaware Supreme Court decision, *Aronson v. Lewis*.[1] The flawed unifying of fiduciary review under the business judgment rule rubric first appears in key 1993 and 1995 decisions in the protracted *Cede* litigation.[2]

This Article advocates a vitally important, but modest, role for the business judgment rule in judicial assessment of corporate decision making. The business judgment rule, the argument runs, is better understood as a narrow-gauged policy of *non-review* than as an overarching framework for affirmatively shaping judicial review of fiduciary performance.

Delaware's doctrinal misstatement of, and conceptual misuse of, the business judgment rule are both understandable as adaptive responses to the same underlying historic void in Delaware law—the late emergence of, and still unformed contours of, the duty of due care. Lacking a judicially articulated duty of care until the 1960s,[3] Delaware's law on the business judgment rule developed before that time with no explicit connection to that vital duty. The business judgment rule, therefore, not the

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1. 473 A.2d 805, 812 (Del. 1984).

2. *See* Cede & Co. v. Technicolor, Inc., 634 A.2d 345 (Del. 1993), *modified*, 636 A.2d 956 (Del. 1994), *aff'd sub nom.* Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156 (Del. 1995). Where it is unnecessary in this Article to refer to a specific judicial opinion in the litigation, reference will be made to "*Cede*." For an informative statement of facts in the *Cede* litigation, see Jesse A. Finkelstein & Russell C. Silberglied, Technicolor IV: *Appraisal Valuation in a Two-Step Merger*, 52 BUS. LAW. 801 (1997).

3. *See* Graham v. Allis-Chalmers Mfg. Co., 188 A.2d 125, 130 (Del. 1963) (dictum) (stating "that directors of a corporation in managing the corporate affairs are bound to use that amount of care which ordinarily careful and prudent men would use in similar circumstances"). The *Allis-Chalmers* dictum appears to be the chief basis for believing that the Delaware Supreme Court, in the 1960s, began to recognize a director duty of care. *See* 1 R. FRANKLIN BALOTTI & JESSE A. FINKELSTEIN, THE DELAWARE LAW OF CORPORATIONS AND BUSINESS ORGANIZATIONS § 4.34, at 4-216 (3d ed. Supp. 1999).

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duty of care, became (and remains) the preeminent legal precept in Delaware corporate law. Regrettably, this development has led to an ambitious "burdening" of that rule with functions for which it was not designed and, indeed, is ill-suited. This inappropriate "burdening" is evident both in *Aronson's* overly broad formulation of the rule and in the comprehensive organizing function for fiduciary analysis it was given in *Cede.*

The Article first describes the prevailing *Aronson* formulation *of* the rule and *Cede's* unifying framework *for* the rule. The Article next advances an alternative model of the business judgment rule that, in both formulation and function, is considerably more "modest" than Delaware's rule. It then develops an argument as to why Delaware deploys the business judgment rule so sweepingly in its corporate jurisprudence. Finally, the Article offers several reasons why more explicit strengthening of the duty of care in Delaware would enrich that core duty and, consequently, redress the doctrinal imbalance between the duty of care and a more properly modest business judgment rule.

DELAWARE'S CURRENT FORMULATION AND USE OF THE BUSINESS JUDGMENT RULE

Beginning in 1984,[4] and continuing today,[5] the Delaware Supreme Court formulates the business judgment rule as "a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company."[6] In 1993 and 1995 decisions in the *Cede* litigation, the Delaware Supreme Court placed the *Aronson* formulation of the business judgment rule into a wider context, linking the rule to statutory and policy bases and, for the first time, analytically connecting the rule to a larger, seemingly streamlined judicial framework for reviewing director performance of fiduciary duties.[7] The court first noted that, by statute,[8] the business and affairs of a corporation are managed by or under the direction of its board of directors. The court next observed that, in exercising these statutory powers, directors are "charged with an unyielding fiduciary duty to protect the interests of the corporation and to act in the best interests of its shareholders."[9]

Describing the business judgment rule as "an extension of these basic principles,"[10] the court indicated that the rule "operates to preclude a

4. *See Aronson*, 473 A.2d at 812.

5. *See, e.g.*, Parnes v. Bally Entertainment Corp., 722 A.2d 1243, 1246 (Del. 1999) (quoting *Aronson*, 473 A.2d at 812).

6. *Parnes*, 722 A.2d at 1246; *Aronson*, 473 A.2d at 812.

7. *See Cinerama, Inc.*, 663 A.2d at 1162-63; *Cede*, 634 A.2d at 360-61.

8. DEL. CODE ANN. tit. 8, § 141(a) (1991), *cited in Cede*, 634 A.2d at 360.

9. *Cede*, 634 A.2d at 360.

10. *Id.*

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court from imposing itself unreasonably on the business and affairs of a corporation."[11] These unobjectionable and helpful assertions were followed by the court's description of the rule's "powerful presumption in favor of actions taken by the directors."[12] Finally, the court stressed what it regarded as the key analytical link-up between the business judgment rule and director fiduciary duties:

> To rebut the rule, a shareholder plaintiff assumes the burden of providing evidence that directors, in reaching their challenged decision, breached any one of the *triads* of their fiduciary duty—good faith, loyalty or due care. If a shareholder plaintiff fails to meet this evidentiary burden, the business judgment rule attaches to protect corporate officers and directors and the decisions they make, and our courts will not second-guess these business judgments. If the rule is rebutted, the burden shifts to the defendant directors, the proponents of the challenged transaction, to prove to the trier of fact the "entire fairness" of the transaction to the shareholder plaintiff.[13]

Under this analytical approach, the business judgment rule *always* applies for the procedural purpose of assigning to plaintiff the initial burden on the issue of whether a director breached one or more duties. This procedural burden-assigning function of the rule is fairly trivial, and creating a doctrine simply to assign plaintiff a burden it already had is widely acknowledged to be unwarranted.[14] If, however, plaintiff *does not meet* that evidentiary and proof burden, the weightier substantive dimension of the business judgment rule thereupon "attaches" to protect a director against further judicial inquiry, including inquiry into the merits or quality of the business decision itself. If, by way of contrast, the plaintiff *does meet* the burden assigned to him under the procedural aspect of the business judgment rule—as, for example, by proving a director's breach of duty, such as care—the substantive aspect of the rule, according to the *Cede* court, does not apply,[15] for doctrinal and policy reasons never stated by the court. The substantive shelter of the business judgment rule, in other words, hinges strictly on plaintiff failing to establish a breach of duty.

The non-application of the substantive aspect of the business judgment rule in the duty-breached context, however, is not, according to the *Cede* court, sufficient by itself to establish the substantive liability of the director.[16] Instead, although a plaintiff achieves non-application of the sub-

11. *Id.*

12. *Id.* at 361.

13. *Id.* (citations omitted).

14. *See* R. Franklin Balotti & James J. Hanks, Jr., *Rejudging the Business Judgment Rule*, 48 BUS. LAW. 1337, 1345 (1993).

15. *See* Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156, 1163 (Del. 1995); *Cede*, 634 A.2d at 361.

16. *See Cinerama, Inc.*, 663 A.2d at 1163.

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stantive business judgment rule by proving a breach of duty, the duty breach itself does not, *substantively*, go beyond that effect. Rather, at this stage the duty breach merely has the further *procedural* effect of shifting to the defendants the burden of proving the entire fairness of a challenged transaction.[17] Actual director liability and the damages outcome of the case turn on whether, subsequently, a defendant successfully carries that high burden. In short, under the *Cede* framework a proven duty of care breach results in loss of the procedural and substantive dimensions of the business judgment rule, but not necessarily in liability. Liability awaits application of the stringent entire fairness standard, the same standard traditionally reserved for determining whether a director violated the quite demanding duty of loyalty.[18]

Quite apart from the significant issue of whether *Cede's* attempted "roadmap" through fiduciary analysis is right or wrong on substantive policy grounds,[19] a recondite methodological question flows out of *Cede's* invitingly cogent exposition: Is it really the function of the *business judgment rule* to guide fiduciary analysis in such a crucial inquiry?

A MODEST BUSINESS JUDGMENT RULE

This Article does not dispute that the *Aronson* "presumption" formulation is a sound statement of legal principle. It does contend, however, that the statement of principle therein expressed is not—or should not be regarded as—the business judgment rule. Furthermore, this Article rejects the *Cede* court's statement of legal principle concerning the consequences of plaintiff proving a breach of director care and, moreover, disputes that the slender business judgment rule somehow encapsulates far-reaching substantive law principles.

Properly understood, business judgment rule should not be regarded as a generalized liability shield for directors and their decisions. The rule, likewise, is not designed to perform a host of other functions it frequently is assigned. It is not, for example, "essentially a presumption that directors did not breach their duty of care";[20] nor is it a watered-down duty of care (a sort of "Care Light").[21] Also, the business judgment rule is not usefully

17. *See id.*; *Cede*, 634 A.2d at 361.

18. *See Cinerama, Inc.*, 663 A.2d at 1163; *Cede*, 634 A.2d at 361; *infra* text accompanying note 30 (noting that judicial review standard is entire fairness where director loyalty is implicated).

19. For an extended critique of *Cede* on both doctrinal and policy grounds, see Lyman Johnson, *Rethinking Judicial Review of Director Care*, 24 DEL. J. CORP. L. (forthcoming 2000).

20. D. Gordon Smith, *The Shareholder Primacy Norm*, 23 J. CORP. L. 277, 280 n.6 (1998).

21. A striking instance of treating the business judgment rule as simply a toned-down version of the duty of care is *Norlin Corp. v. Rooney, Pace Inc.*, 744 F.2d 255 (2d Cir. 1984), where, in applying New York law, the court stated:

> The duty of care refers to the responsibility of a corporate fiduciary to exercise, in the performance of his tasks, the care that a reasonably prudent person in a similar position

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(*Footnote 21 continued*)

> would use under similar circumstances. In evaluating a manager's compliance with the duty of care, New York courts adhere to the business judgment rule, which "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."

Id. at 264 (citation omitted). In other words, the higher standard of care (that care of a "reasonably prudent person") is regarded as met if the lesser standards of "good faith" and "honest judgment" are present. *Norlin's* confused description of the inter-relationship between the duty of care and the New York business judgment rule led one commentator to describe the duty of care in that state as "largely aspirational." Joseph Hinsey IV, *Business Judgment and the American Law Institute's Corporate Governance Project: The Rule, the Doctrine, and the Reality*, 52 GEO. WASH. L. REV. 609, 615 (1984). This characterization, although accurate insofar as *Norlin* is concerned, fails to capture the way in which courts, including New York courts, pre-condition the protection of the business judgment rule on the exercise of care, a point the commentator himself notes. *See id.* at 611 (noting that directors must have "exercised a reasonable amount of diligence" before courts will apply the rule); *see infra* notes 43-45 and accompanying text.

The 1998 amendment of § 8.30 of the Model Business Corporation Act (MBCA or Model Act) and the simultaneous addition of a new section, § 8.31 captioned "Standards of Liability For Directors," carry forward the *Norlin* distinction between director "standards of conduct" (now found in § 8.30 and including the duty of care) and "standards of liability" (now found in § 8.31). MODEL BUS. CORP. ACT §§ 8.30, 8.31 (1998), *in* Committee on Corporate Laws, *Changes in the Model Business Corporation Act—Amendments Pertaining to Electronic Filings/Standards of Conduct and Standards of Liability for Directors*, 53 BUS. LAW. 157, 176 (1997) [hereinafter *1997 MBCA Changes*] (stating that "[s]ections 8.30 and 8.31 adopt the approach to director conduct and director liability taken in the *Norlin* decision"); *see also* Committee on Corporate Laws, *Changes in the Model Business Corporation Act Pertaining to the Standards of Conduct and Standards of Liability for Directors—Final Adoption*, 53 BUS. LAW. 813 (1998). To further complicate the relationship between standards of conduct and standards of liability, the Official Comment to § 8.31 indicates that section does not codify the business judgment rule "[b]ecause the elements of the business judgment rule and the circumstances of its application are continuing to be developed by the courts [and therefore] it would not be desirable to freeze the concept in a statute." MODEL BUS. CORP. ACT § 8.31 official comment, *in 1997 MBCA Changes*, *supra*, at 179. Having said that, however, the comment later states that the "principal elements" of the rule are "embedded" in § 8.31(a)(2). *Id.* at 180. If not all of the elements of the business judgment rule are "embedded" in that section, what was left out? We are never told. Under the revised Model Act, therefore, a director can fail to adhere to the standards of conduct set forth in § 8.30 (including the duty of care) and not be liable if he or she either adheres to the more relaxed standards of § 8.31 or, failing to adhere to § 8.31, nonetheless complies with the elements of the uncodified business judgment rule. Three standards, conceivably, rather than *Norlin's* two standards, might now apply to director conduct.

Prior to being amended in 1998, § 8.30(d) of the MBCA provided "[a] director is not liable for any action taken as a director, or any failure to take any action, if he performed the duties of his office in compliance with this Section." MODEL BUS. CORP. ACT § 8.30(d) (1997). As indicated in the Official Comment, § 8.30(d) followed former § 35 of the Model Act in providing that a director is exonerated from liability if he fulfilled the standard set forth in that section. *Id.* official comment. The Official Comment goes on to note, however, that if a director does *not* comply with the codified standard of conduct, then the application of the business judgment rule to the question of director liability must be considered. *Id.* The above comment must be read along with an earlier statement in the Official Comment that

> [t]he elements of the business judgment rule and the circumstances for its application are continuing to be developed by the courts. In view of that continuing judicial

regarded as either a substantive standard for affirmatively guiding judicial review of director conduct,[22] or a process-oriented standard for guiding judicial review;[23] and, finally, it is not at all designed for fulfilling the task

(*Footnote 21 continued*)

> development, section 8.30 does not try to codify the business judgment rule or to *delineate the differences, if any, between that rule and the standards of director conduct set forth* in this section.

Id. (emphasis added). *See e.g.*, Kreischer v. Kerrison Dry Goods Co., Nos. 97-1230, 97-1800, 1999 WL 30836, at **4 (4th Cir. Jan. 26, 1999) (applying the South Carolina business judgment rule rather than statutory standard of director conduct, based on language in Model Act comment). *See generally* Robert W. Hamilton, *Reflections of a Reporter*, 63 TEX. L. REV. 1455 (1985).

The *Norlin* and Model Act view of the business judgment rule as a more lenient standard than the duty of care also is the position of the American Law Institute (ALI). *See* ALI, PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS (1994) [hereinafter PRINCIPLES OF CORPORATE GOVERNANCE]. Section 4.01(c) of the Principles of Corporate Governance states, in pertinent part, that:

> A director . . . who makes a business judgment in good faith fulfills the duty under this Section if [he or she]:
> (1) is not interested . . . in the subject of the business judgment;
> (2) is informed with respect to the subject of the business judgment to the extent the director . . . reasonably believes to be appropriate under the circumstances; and
> (3) rationally believes that the business judgment is in the best interests of the corporation.

Id. § 4.01(c).

The "duty under this Section" referred to in § 4.01(c) is the duty of care set forth in § 4.01(a) of the Principles of Corporate Governance. Section 4.01(a) requires that a director act "in good faith, in a manner that he or she reasonably believes to be in the best interests of the corporation, and with the care that an ordinarily prudent person would reasonably be expected to exercise in a like position and under similar circumstances." *Id.* § 4.01(a). In other words, fulfilling the more relaxed business judgment standard set forth in § 4.01(c) is a way to fulfill the higher duty of care set forth in § 4.01(a). The Principles of Corporate Governance, in short, functionally regards its codified business judgment rule as a *broad-gauged* standard of review, albeit it also sets a substantively *lower* standard for director conduct than the duty of care, just as *Norlin* and the MBCA likewise regard the rule.

22. Samuel Arsht ends his well known analysis of the business judgment rule by very broadly suggesting it is a term meaning that a plaintiff must prove a decision maker's lack of good faith and care:

> [T]he term "business judgment rule" and the presumption that often identifies it mean simply that a stockholder who challenges a nonself-dealing transaction must persuade the court that the corporation's directors, officers, or controlling stockholders in authorizing the transaction did not act in *good faith*, did not act in a manner they reasonably believed to be in the corporation's best interest, or did not exercise the *care* an ordinarily prudent person in a like position would use under similar circumstances.

S. Samuel Arsht, *The Business Judgment Rule Revisited*, 8 HOFSTRA L. REV. 93, 134 (1979) (emphasis added).

23. Former Chancellor William Allen once stated that "the business judgment rule is process-oriented." *In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 967-68 (Del.

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assigned in *Cede*—organizing judicial fiduciary analysis into an overarching, seemingly coherent framework.

Properly understood, the business judgment rule is simply a policy of judicial *non-review*. Recall the *Cede* court's statement that "our courts will *not* second-guess these business judgments."[24] A more modest expression of the sound statutory and policy bases underlying this judicial deference to director decisions—as embodied in the business judgment rule—is, therefore, as follows:

"[W]here money damages or equitable relief is sought, the business judgment rule is a judicial policy of not reviewing the substantive merits of a board of directors' business decision for the purpose of determining whether directors breached or fulfilled their duty of care."[25]

Conversely, courts may review challenged board decisions: (i) for fraud, illegality, ultra vires, or waste;[26] (ii) under a reasonableness test, to ascertain (a) director compliance with the duty of due care,[27] (b) director compliance with the *Unocal* standard,[28] or (c) whether director action was taken in bad faith;[29] and (iii) under an entire fairness test, for the substantive merits of

Ch. 1996). The larger context of that statement indicates that Chancellor Allen was describing the directors' duty of care as process-oriented and that, to the extent directors fulfilled the process-oriented duty of care, the business judgment rule would operate to protect the decision itself. *See infra* note 32. That relationship between the duty of care and the business judgment rule, however, does not make the rule itself "process-oriented."

24. Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 361 (Del. 1993) (emphasis added), *modified*, 636 A.2d 956 (Del. 1994), *aff'd sub nom.* Cinerama, Inc. v. Technicolor, Inc. 663 A.2d 1156 (Del. 1995).

25. Throughout this Article the formulation in the text is referred to as the "modest business judgment rule." The rule is "modest" in that, functionally, the business judgment rule is strictly limited to forbidding judicial review of the substance of business decisions. The function of the rule thereby is sharply differentiated from the duty of care's broader inquiry into the reasonableness of the directors' decision-making process. This Article's formulation of the rule, concededly, might be described by some as quite "immodest" in that, as will be seen, this Article argues for full application of the business judgment rule even in the *breach* of care context.

26. *See* 3A WILLIAM MEADE FLETCHER ET AL., FLETCHER CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 1040 (perm. ed. rev. vol. 1994) [hereinafter FLETCHER CYCLOPEDIA].

27. For an extended discussion of a generally applicable "reasonableness" test in the duty of care area, both where director action involves a considered business judgment and where director action (or inaction) does not involve making a business decision, see Johnson, *supra* note 19.

28. In *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985), the Delaware Supreme Court held that when a defensive measure is challenged, the board of directors must carry the initial burden of proving, first, that it has "reasonable grounds for believing that a danger to corporate policy and effectiveness existed"—a showing which can be made by demonstrating good faith and a reasonable investigation—and, second, the board must show that its defensive measure was "reasonable in relation to the threat posed." *Id.* at 955.

29. *See* Parnes v. Bally Entertainment Corp., 722 A.2d 1243, 1246 (Del. 1999) (noting that a business decision may be " 'so far beyond the bounds of reasonable judgment that it seems

business decisions, where director loyalty is implicated.[30]

Under a proper understanding of the business judgment rule as a policy of *non-review*, the "substantive" force of the business judgment rule *always* applies in a duty of care case, immunizing the *quality* of the business decision from judicial review whether or not care was exercised. The analytical approach of *Cede*, therefore, where a breach of due care leads only to application of a different review standard (i.e., entire fairness), is rejected. The modest business judgment rule emphasizes that, in the care setting, proper judicial inquiry into director conduct is process-oriented and centers on whether a neutral decision maker acted in the proper manner;[31] that inquiry, unlike a loyalty or bad-faith inquiry, never warrants judicial scrutiny *into* the substantive merits of a business decision, as opposed to the overall process *by* which the decision was made. The substantive "rationality" or "reasonableness" or "fairness" of the business decision itself is, in the pure care setting, categorically off limits to judicial review.[32] The institutional concern here, as recently observed by a British

essentially inexplicable on any ground other than bad faith' " (quoting *In re* J.P. Stevens & Co., 542 A.2d 770, 780-81 (Del. Ch. 1988)); *accord* West Point-Pepperell, Inc. v. J.P. Stevens & Co. (*In re* J.P. Stevens & Co.), 542 A.2d 770, 780-81 (Del. Ch. 1988). The *Aronson* "abuse of discretion" standard, *see infra* note 81, may best be understood as going to director bad faith. *See* E. Norman Veasey, *New Insights into Judicial Deference to Directors' Business Decisions: Should We Trust the Courts?*, 39 BUS. LAW. 1461, 1473 (1984) ("[I]rrational behavior or an abuse of discretion, perhaps tantamount to a lack of good faith, would be actionable.").

30. *See* Nixon v. Blackwell, 626 A.2d 1366, 1376 (Del. 1993); Weinberger v. UOP, Inc., 457 A.2d 701, 710-11 (Del. 1983).

31. The Delaware Supreme Court has made strong statements that the due care inquiry in the business judgment context should focus on a board's decision-making process: "[O]ur due care examination has focused on a board's decision-making process." Citron v. Fairchild Camera & Instrument Corp., 569 A.2d 53, 66 (Del. 1989); *see also* Brazen v. Bell Atl. Corp., 695 A.2d 43, 49 (Del. 1997) (dictum); Charles Hansen, *The ALI Corporate Governance Project: Of the Duty of Due Care and the Business Judgment Rule, a Commentary*, 41 BUS. LAW. 1237, 1240-42 (1986).

32. Former Chancellor William Allen made the best recent statement about this point:

> What should be understood, but may not widely be understood by courts or commentators who are not often required to face such questions, is that *compliance with a director's duty of care can never appropriately be judicially determined by reference to the content of the board decision* that leads to a corporate loss, apart from consideration of the good faith *or* rationality of the process employed. That is, whether a judge or jury considering the matter after the fact, believes a decision substantively wrong, or degrees of wrong extending through "stupid" to "egregious" or "irrational," provides no ground for director liability, so long as the court determines that the process employed was either rational or employed in *a good faith* effort to advance corporate interests.

In re Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 967 (Del. Ch. 1996) (emphasis added) (footnote omitted); *see* Davis v. Louisville Gas & Elec. Co., 142 A. 654, 660 (Del. Ch. 1928) (noting that a particular course of action "may argue stupidity," but is no ground for judicial intervention). Compare the views of another former Chancellor, retired Justice William T. Quillen: "[T]here can be no question that for years the courts have in fact reviewed directors' business decisions to some extent from a quality of judgment point of view. Busi-

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commentator, is that "[i]nstead of truly judging directors' *behaviour*, [judges] would take bad *results* as conclusive evidence of bad behaviour."[33] Concern about institutional encroachment arises not only when, as *Cede* recognized, plaintiff *fails* to prove lack of director care, but also, contrary to *Cede*, when plaintiff *succeeds* in proving a breach of due care. *Cede*, in short, nullifies half the scope of the business judgment rule—i.e., its application in duty-breached cases.

Cede's analytical framework creates confusion, first, by seeming to forget that the duty of care and the business judgment rule, although complementary, are two distinct legal concepts serving different roles. Second, by treating the rule as an all-purpose metric for gauging director liability, *Cede* devalues the duty of care. The duty of due care is a legal standard which specifies the manner in which directors must discharge their duties.[34] The business judgment rule is a policy of *judicial review*, or, as this Article suggests, a policy of judicial *non-review*. The duty of due care unremittingly requires that, at all times in all corporate settings,[35] corporate directors conduct themselves in a particular *manner*. As most frequently formulated, the standard of conduct is that a director act with the care of an ordinarily prudent person in a like position under similar circumstances.[36] Whether making a business judgment or not, the duty demands that a director act

nessmen do not like it, but courts do it and are likely to continue to do it because directors are fiduciaries." William T. Quillen, Trans Union, *Business Judgment, and Neutral Principles*, 10 DEL. J. CORP. L. 465, 492 (1985).

33. C.A. Riley, *The Company Director's Duty of Care and Skill: The Case for an Onerous but Subjective Standard*, 62 MODERN L. REV. 697, 710 (1999); *accord* Hansen, *supra* note 31, at 1239.

34. *See infra* notes 35, 36, and accompanying text. Messrs. Balotti and Hanks cogently differentiate the business judgment rule and the director standard of conduct under Delaware law, under the ALI's Principles of Corporate Governance, and under the Model Act. *See* Balotti & Hanks, *supra* note 14, at 1337-39. As to Delaware law, Messrs. Balotti and Hanks assert that the business judgment rule has "an uncertain nexus" to the director standard of conduct. *Id.* at 1338; *see* 3A FLETCHER CYCLOPEDIA, *supra* note 26, § 1036 (acknowledging "some tension" between the business judgment rule and the duty of care).

35. Recently, the Delaware Supreme Court expressed the constant and pervasive nature of director duty as follows: "[F]iduciary duty does not operate intermittently but is the constant compass by which all director actions for the corporation and interactions with its shareholders must be guided." Malone v. Brincat, 722 A.2d 5, 10 (Del. 1998).

36. *See* Graham v. Allis-Chalmers Mfg. Co., 188 A.2d 125, 130 (Del. 1963); NORMAN D. LATTIN, THE LAW OF CORPORATIONS 272 (2d ed. 1971) (explaining that "[t]he common expression of duty of care is that care which a reasonably prudent director of a similar corporation would have used under the circumstances of the particular case"); *see also* PRINCIPLES OF CORPORATE GOVERNANCE, *supra* note 21, § 4.01(a); DENNIS J. BLOCK ET AL., THE BUSINESS JUDGMENT RULE—FIDUCIARY DUTIES OF CORPORATE DIRECTORS 123 n.52 (5th ed. 1998) (collecting representative authority). *Compare* MODEL BUS. CORP. ACT

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with the specified degree of care. The standard of care is context-bound and cannot be reduced to a task-based notion because it demands all care "due" in a particular setting. Nonetheless, care by a director includes inquiring into and becoming reasonably informed about, deliberating over, and paying attention to and monitoring, all facets of directing the management of the corporation's business and affairs.

If plaintiff proves a director did *not* act with due care, whether from nonfeasance or misfeasance, that alone is a breach of fiduciary duty and, absent statutory exoneration,[37] he or she should be liable for all damages proximately caused thereby.[38] It is not the case, as *Cede* held, that a proven breach of care somehow "overrides" the policy of non-review embodied in the business judgment rule—a policy the *Cede* court must regard as highly contingent—and that the rule somehow "falls away" in a breach case, thereby freeing the judiciary to examine (and possibly uphold) the substantive quality of a carelessly rendered business decision.[39] The business judgment rule, as the name and policy underlying it reflect, is not a generalized, provisional policy of director non-liability, depending for its application on director compliance with care but summarily yielding when care is breached. It is, rather, both a narrow-gauged and quite potent policy preference designed to preclude judicial scrutiny of business deci-

§ 8.30(a)(2) (1997) (noting "the care an ordinarily prudent person in a like position would exercise under similar circumstances"), *with id.* § 8.30(b) (1998), *in 1997 MBCA Changes*, *supra* note 21, at 160 (noting "the care that a person in a like position would reasonably believe appropriate under similar circumstances"). For a critique of the customary standard, see Bayless Manning, *The Business Judgment Rule and the Director's Duty of Attention: Time for Reality*, 39 BUS. LAW. 1477 (1984). For a critique of the customary standard that the author of this Article regards as a significant overstatement, see Charles Hansen, *The Duty of Care, the Business Judgment Rule, and the American Law Institute Corporate Governance Project*, 48 BUS. LAW. 1355, 1374 (1993) ("It now is generally accepted that in a corporate context, the reasonably prudent person formulation is not only incorrect, but dangerously misleading."). Mr. Hansen's statement is descriptively inaccurate because a majority of states have statutes codifying that standard. The statement, as a normative position, takes a stance with which many thoughtful persons disagree, thereby signifying it is not now "generally accepted."

37. *See, e.g.*, 8 DEL. CODE ANN. tit. 8, § 102(b)(7) (Supp. 1998) (permitting reduction or elimination of director liability in certain instances).

38. *See In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 970 n.27 (Del. Ch. 1996); MODEL BUS. CORP. ACT § 8.31 (1998) (requiring causation); PRINCIPLES OF CORPORATE GOVERNANCE, *supra* note 21, § 4.01(d).

39. *See* Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 361 (Del. 1993), *modified*, 636 A.2d 956 (Del. 1994), *aff'd sub nom.* Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156, 1163 (Del. 1995). For a similar judicial misunderstanding, see *Stamp v. Batastini*, 636 N.E.2d 616, 621 (Ill. App. Ct. 1993) ("The plaintiff correctly points out that the shield of the business judgment rule is unavailable to directors who fail to exercise due care in their management of the corporation."). *See also* Veasey, *supra* note 29, at 1473.

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sions,[40] and this whether directors have or have not breached their distinctive duty of care.

The contrary *Cede* position, making the intensity of judicial review toward the merits of the directors' business judgment contingent on whether directors fulfilled or breached the due care duty, is unprecedented on doctrinal grounds,[41] faulty on a policy basis, and utterly counter to the deference embodied in a modest, but consistently-applied, business judgment rule. Damages, to be sure, for a breach of due care may be nonexistent or limited if, among other possibilities, the substantive quality of the challenged decision is sufficiently good, as it turns out, that little or no harm was legally caused by director carelessness. Remedial relief, however, is a distinct consideration from whether courts should substantively examine business decisions, in the first instance, to assign liability.

The rule, of course, has no application unless a "business judgment" has been made.[42] Thus, director conduct not involving the exercise of business judgment—such as an unconsidered failure to monitor corporate affairs—is reviewed for compliance with the always applicable duty of due care, but receives no protective shelter under the business judgment rule. The protection of the rule is grounded on various well known and widely agreed upon policy rationales.[43] In the garden-variety duty of care area, moreover, it applies pervasively, not contingently. This means, it bears underscoring, that *if* directors act in accordance with the applicable standard of care, then the substantive business decision that results from so acting will not be judicially reviewed as a basis for faulting directors, just as,

40. Although Messrs. Balotti and Hanks do not develop this point, they rightly emphasize the need to differentiate director *judgments* from other director *behavior*:

> A different rubric, however, should be employed to determine whether to impose liability for a *judgment* that later turns out to be erroneous than for an *act* that was not performed properly. Thus, the deference given to the judgments of the directors—i.e., the substantive aspect of the business judgment rule—prohibits courts from overturning *judgments* of the directors.

Balotti and Hanks, *supra* note 14, at 1344 (emphasis added). This Article contends that the duty of care is the "different rubric" that *always* should be applied to director conduct, whether that conduct involves the making of a judgment or not. Moreover, this Article's modest business judgment rule serves to differentiate from the always-applicable duty of care the separate policy preference, applicable only in the judgment context, that the business judgment of directors is to be accorded judicial deference *whether or not* directors have, independently, breached the duty of due care. For a judicial distinction between the standard of care and the "exercise of judgment" rule in the context of physicians' medical judgment, see *Aiello v. Muhlenberg Regional Medical Center*, 733 A.2d 433, 438-42 (N.J. 1999).

41. *See* Johnson, *supra* note 19.

42. *See* Aronson v. Lewis, 473 A.2d 805, 813 (Del. 1984) (explaining that "the business judgment rule operates only in the context of director action. Technically speaking, it has no role where directors have either abdicated their functions, or absent a conscious decision, failed to act.").

43. *See* 3A FLETCHER CYCLOPEDIA, *supra* note 26, § 1037; Johnson, *supra* note 19.

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conversely, if directors *breach* their duty of care a court is not to go on and assess the substantive fairness of a business decision as a basis for, as in *Cede*, absolving a careless director. Consequently, if directors comply with the applicable standard of care but, in spite of so acting, make an unreasonable, unwise, or even downright stupid business decision, the merits of that decision will not factor into judicial assessment of director compliance with legal duties.[44] Likewise, when directors breach the applicable standard of care, the merits of the resulting decision (except concerning damages) ought not enter into judicial assessment of director conduct.[45] This outcome reflects the sensible symmetry of deference that undergirds the modest business judgment rule's narrow-banded, but constant, policy of non-review.

The relationship between, on the one hand, the far-reaching, always-applicable director duty of due care and, on the other hand, the more finely drawn policy of non-review housed in the business judgment rule, is one of the most important, but least understood, relationships in corporate law. Why do *Aronson* and *Cede* both miscapture that relationship?

44. *See supra* note 32. This sound policy of not assessing a director's compliance with the due care duty by making reference to the merits of the business decision itself finds expression in the instructive language of *Casey v. Woodruff*, 49 N.Y.S.2d 625, 642-43 (Sup. Ct. 1944) (citations omitted):

> Mistakes in the exercise of honest business judgment do not subject the directors to liability for negligence in the discharge of their fiduciary duties. The standard [of care] is one of reasonable diligence, not the utmost amount of diligence. . . . The law recognizes that no director is infallible and that he will make mistakes, but if he is honest and uses reasonable diligence he will be absolved from liability although his opinion may turn out to have been mistaken and his judgment faulty.

This statement makes clear, first, that the standard of care for directors is reasonable diligence and, second, that the merits of a business decision are not examined as a basis for determining compliance or noncompliance with that standard for the reason that a mistake in judgment simply is not regarded, by itself, as a breach of the relevant care standard. *See also* Keyser v. Commonwealth Nat'l Fin. Corp., 675 F. Supp. 238, 258 (M.D. Pa. 1987) (finding that "application of the business judgment rule does not alter the statutory requirement . . . that directors or officers act with reasonable care so that they may be held liable for negligence").

45. The reason for this result is that, where directors breach the process-oriented duty of due care, that breach, by itself, creates liability for those resulting business decisions causing damage. The breach of care is not undone or atoned for by the merits of the business decision itself. As stated by a commentator sixty years ago:

> While honest managerial mistakes will not be penalized by the law, the courts are looking with disfavor upon blundering directors, whose errors grew out of their carelessness. Cases have therefore been frequent where corporate directors were held liable for mistakes of judgment which were *caused by their failure to exercise proper care and diligence.*

Rudolph E. Uhlman, *The Duty of Corporate Directors to Exercise Business Judgment*, 20 B.U. L. REV. 488, 491 (1940) (emphasis added).

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DELAWARE'S BUSINESS JUDGMENT RULE DEVELOPED SEPARATELY FROM DUE CARE

THE DISTINCTIVENESS OF, AND RELATIONSHIP BETWEEN, THE DUTY OF CARE AND THE BUSINESS JUDGMENT RULE

Courts and commentators frequently have addressed what they see as the relationship between the duty of care and the business judgment rule. For example, several decades ago Professor Ballantine stated: "[I]t is presupposed in this 'business judgment rule' that reasonable diligence and care have been exercised."[46] Samuel Arsht, writing twenty years ago, likewise stressed that decisional law required a director to exercise "reasonable diligence and care"[47] as a precondition to judicial deference to director judgment. Two representative judicial statements, one fairly recent and another 150 years old, also reflect this viewpoint: "[T]he business judgment rule protects directors from liability for good faith errors only after the directors have exercised reasonable care in fulfilling their corporate obligations."[48]

> [I]f the [directors'] mistake be such as with proper care might have been avoided, they ought to be liable. If, on the other hand, the mistake be such as the directors might well make, notwithstanding the exercise of proper care, and if they acted in good faith and for the benefit of the [corporation], they ought not to be liable.[49]

All of the authority above sharply differentiates the director duty of care from the business judgment rule, while at the same time acknowledging, however incompletely, their relationship. Professor Ballantine, Samuel Arsht, and the *Resolution Trust Corp. v. Hess*[50] opinion underscore, like the *Cede*[51] case, one way in which the substantive protection of the business judgment rule is obtained, that is, upon the plaintiff's failure to prove a director breach of care. Without such proof of breach, because directors themselves have no affirmative burden of persuasion that they *fulfilled* their duty of care, they will rightly be "presumed" to have acted with care.

46. HENRY W. BALLANTINE, LAW OF CORPORATIONS § 63a, at 161 (rev. ed. 1946).

47. Arsht, *supra* note 22, at 100.

48. Resolution Trust Corp. v. Hess, 820 F. Supp. 1359, 1367 (D. Utah 1993) (describing Utah law).

49. Hodges v. New England Screw Co., 1 R.I. 312, 346 (1850); *see* Hansen Trust PLC v. ML SCM Acquisition, Inc., 781 F.2d 264, 274-75 (2d Cir. 1986) (citing authority differentiating process-oriented due care inquiry from substantive judicial review of substance of business decision).

50. 820 F. Supp. at 1359; *see supra* notes 46-48.

51. Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 361 (Del. 1993), *modified*, 636 A.2d 956 (Del. 1994), *aff'd sub nom.* Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156, 1162 (Del. 1995).

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Accordingly, the policy of non-review found in the business judgment rule will foreclose judicial inquiry into the substantive merits of the decision as an independent basis for holding directors liable. The last sentence of the quote from the *Hodges v. New England Screw Co.*[52] decision, like authority cited earlier,[53] makes crystal clear the point that inquiry into the substance of business decisions will not becloud the duty of care inquiry.

The excerpt from the *Hodges* case, while supporting the point made above by the other authorities, makes a further point not clearly made by the others. That point, albeit made tersely, is often overlooked. It is that directors *should* be liable for damages caused by decisions not made with proper care.[54] Here the focus is pointedly the legal duty of director care, its breach being sufficient by itself to create liability, without regard to a further, judicial assessment of the business decision's substantive quality, except as is pertinent to damages.

This latter facet of a modest business judgment rule immunizes director business decisions from judicial scrutiny in the care context when directors *fail* to act with care as surely as when they *succeed* in acting with care. To be complete and consistent, the business judgment rule policy of non-review should apply in the duty-breached as well as in the duty-fulfilled settings; in neither setting should the directors' substantive business judgment enter into and muddy the separate duty of care analysis. The modest business judgment rule described earlier readily accomplishes this; the *Cede* holdings do not. That is, *Cede* punctures the protective shelter of the business judgment rule by invasively scrutinizing for fairness the substance of director decisions in a duty of care case involving the exercise of business judgment. Lacking a clear doctrinal and functional firebreak between the duty of care's rightful province and the business judgment rule's separate province, the court blurs the two concepts by treating a breach of the former as grounds for nullifying application of the latter. This would be unnecessary if Delaware had a robust, well developed duty of care the juridical domain of which was more strictly demarcated from the narrow ambit of the business judgment rule, and the breach of which, by itself, was thought to be serious enough to create liability for resulting damages.[55]

52. *See supra* note 49 and accompanying text.

53. *See supra* notes 32, 44, and accompanying text.

54. Both decisions cited by Professor Ballantine, *see supra* note 46 and accompanying text, support this point. *See* Casey v. Woodruff, 49 N.Y.S.2d 625, 642-43, 647 (Sup. Ct. 1944); *supra* note 44. The other decision is *Otis & Co. v. Pennsylvania R. Co.*, 61 F. Supp. 905 (E.D. Pa. 1945), *aff'd*, 155 F. 2d 522 (3d Cir. 1946), where the court stated that " 'the failure to observe this standard of care [of reasonable, ordinary care and diligence] imposes liability on a defaulting director.' " *Id.* at 911 (quoting Fell v. Pitts, 106 A. 574, 576 (Pa. 1919) (holding directors liable)); *see also supra* note 45 and accompanying text.

55. *Cede*, in other words, treats a duty of care breach as non-liability creating, not, as is the case with *Norlin*, the ALI, and the Model Act, *see supra* note 21, *because* of the business judgment rule, but *in spite of* it.

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DELAWARE'S LONGSTANDING SEPARATION, AND EVENTUAL JOINING, OF CARE AND THE BUSINESS JUDGMENT RULE

Unlike the authority cited above, Delaware courts appear to have initially developed the concept of the business judgment rule without directly linking it, functionally or doctrinally, to the director duty of due care. This is not surprising given that the Delaware Supreme Court did not even explicitly acknowledge such a duty until 1963.[56] Even today, Delaware refuses to expound a robust, all-encompassing duty of due care, an odd failing that continues to distinguish Delaware law. Instead, with a few exceptions that deserve more attention,[57] Delaware courts tend, more or less, to equate that key duty with a duty to be informed, a critical but less full-bodied duty than due care.[58]

Lacking an express and vigorous duty of care, Delaware developed its "business judgment" jurisprudence earlier than, and independent of, the doctrinal emergence of that fiduciary duty. Although the phrase "business judgment rule" apparently was not used by the Delaware Chancery Court until 1959,[59] the phrase "business judgment"—and the concept of the rule itself—had been in use for several decades.[60]

What is striking about the Delaware judiciary's early verbal expression of the business judgment concept is its similarity, save for one element, to the 1984 *Aronson* formulation. For example, in 1928, the Delaware Chancery Court stated as follows:

> The judgment of the directors of corporations enjoys the benefit of a *presumption* that it was formed in *good faith* and was designed to promote *the best interests of the corporation* they serve . . . . "If . . . there is nothing to show that the directors did not exercise their discretion

56. *See supra* note 3.

57. *See, e.g.*, Paramount Communications, Inc. v. QVC Network, Inc., 637 A.2d 34, 48 (Del. 1994) (describing the corporate director as having a two-fold duty "to obtain, and act with due care on, all material information reasonably available"); Smith v. Van Gorkom, 488 A.2d 858, 872-73 (Del. 1985) (describing the director's duty to exercise an informed judgment as "in the nature of *a* duty of care," not *the* duty of care (emphasis added)). Elsewhere, Chief Justice Veasey rightly refrains from equating care and informedness by describing care as including (but not being limited to) informedness: "The duty of care includes the requirement that directors inform themselves of all material information reasonably available to them before making a business decision." E. Norman Veasey, *The Defining Tension in Corporate Governance in America*, 52 BUS. LAW. 393, 397-98 (1997).

58. *See e.g.*, Citron v. Fairchild Camera & Instrument Corp., 569 A.2d 53, 64 (Del. 1989) (noting the business judgment rule "creates a 'presumption that in making a business decision, the directors of a corporation acted on an informed basis [i.e., with due care]' " (quoting Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984))).

59. *See* Nadler v. Bethlehem Steel Corp., 154 A.2d 146, 149 (Del. Ch. 1959).

60. *See, e.g.*, Gottlieb v. Heyden Chem. Corp., 90 A.2d 660, 663 (Del. 1952); Davis v. Louisville Gas & Elec. Co., 142 A. 654, 660 (Del. Ch. 1928) (stating that "I can see no justification in this court's interfering. It is a matter of business judgment . . . .").

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> for what they *believed* to be the *best interest of the corporation*, certainly an *honest* mistake of business judgment should not be reviewable by the court."[61]

Compare the above with the more compact *Aronson* expression of similar elements, i.e., that there is a "*presumption* that in making a business decision the directors of a corporation acted on an informed basis, in *good faith* and in the *honest belief* that the action taken was in *the best interests of the company*."[62] Two of the three *Aronson* elements—good faith and honest belief that the decision was in the best interests of the corporation—existed as part of the business judgment concept as early as 1928.

In *Aronson*, the Delaware Supreme Court cites as authority for its formulation of what it calls the business judgment rule not its own decisions, but two Chancery Court opinions, one decided in 1971 and another from 1924. The 1971 decision referred to in *Aronson*—*Kaplan v. Centex Corporation*[63]—cited as authority for its business judgment rule formulation a 1966 Delaware Supreme Court decision which, after stating that the "acts of directors are presumptively acts taken in *good faith* and inspired for *the best interests of the corporation*,"[64] cited yet another Chancery Court decision rendered in 1943.[65] The 1943 decision, in turn, referenced a 1931 Chancery Court decision,[66] which cited both the 1928 Chancery Court decision quoted above[67] and the 1924 Chancery Court decision[68] relied on directly by *Aronson*.[69]

In all of these decisions undergirding *Aronson*—running from *Kaplan* through each case cited above, back to the wellspring decisions of *Davis v. Louisville Gas & Electric Co.*,[70] *Bodell v. General Gas & Electric Corp.*,[71] and *Robinson v. Pittsburgh Oil Refining Corp.*[72]—the two elements of good faith and honest belief as to the corporation's best interests are present. What is conspicuously missing from all these formulations, however, is the first *Aronson* element, that of being "informed." The 1971 *Kaplan* case states that the business judgment rule "of necessity depends upon a showing that informed directors did, in fact, make a business judgment."[73] Although

61. *Davis*, 142 A. at 659 (emphasis added) (quoting Bodell v. General Gas & Elec. Corp., 140 A. 264, 267 (Del. 1927)).
62. *Aronson*, 473 A.2d at 812 (emphasis added).
63. 284 A.2d 119 (Del. Ch. 1971).
64. Warshaw v. Calhoun, 221 A.2d 487, 493 (Del. 1966) (emphasis added).
65. *See* Porges v. Vadsco Sales Corp., 32 A.2d 148, 151-52 (Del. Ch. 1943).
66. *See* Cole v. National Cash Credit Ass'n, 156 A. 183, 188 (Del. Ch. 1931).
67. *See supra* notes 60-61 and accompanying text.
68. *See* Robinson v. Pittsburgh Oil Ref. Corp., 126 A. 46 (Del. Ch. 1924).
69. *See* Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984).
70. 142 A. 654 (Del. Ch. 1928).
71. 140 A. 264 (Del. 1927).
72. 126 A. at 46.
73. Kaplan v. Centex Corp., 284 A.2d 119, 124 (Del. Ch. 1971).

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the emphasis in that phrase seems less on the word "informed" and more on the necessity of a *judgment* being made in order for the protection of the rule to operate, three years later, citing *Kaplan*, the Chancery Court nevertheless described the "presumption of having made an informed judgment in good faith."[74]

The eventual incorporation of the "informed" element into Delaware's business judgment rule, coupled with the notable lack of direct historical linkage between that rule and the duty of care, raises two obvious questions. Is the "informed" element simply one aspect of, or is it the same as, the concept of due care? Is injection of the "informed" element into the *Aronson* formulation meant to add in Delaware what Professor Ballantine, Samuel Arsht, and much decisional law had described, essentially, as a precondition to the substantive protection of the business judgment rule, i.e., the exercise of due care?

There is no assertion in the *Aronson*, *Muschel*, *Kaplan*, or *Beard* decisions themselves that the "informed" element originally was conceived of as being coextensive with due care. That certainly would be a strained reading of the 1960 *Beard* decision which predates by three years the Delaware Supreme Court's first express acknowledgment of director care by means of a commonplace formulation phrased quite differently than a mere duty to be "informed."[75] *Aronson* itself, moreover, appears to differentiate between a director becoming informed and a director acting with care, stating that "[h]aving become so *informed*, they [directors] must then act with requisite *care* in the discharge of their duties."[76] *Aronson* also, however, follows Professor Ballantine, Samuel Arsht, and certain decisional law in wrongly predicating the substantive shelter of the business judgment rule on director informedness, stating that "to invoke the rule's protection directors have a duty to inform themselves, prior to making a business decision, of all material information reasonably available to them."[77] Thus, *Aronson*, on the one hand, rightly distinguishes informedness and care; on the other hand, the court wrongly pre-conditions application of the business judgment rule on informedness, thereby suggesting many years before

74. Muschel v. Western Union Corp., 310 A.2d 904, 906, 909 (Del. Ch. 1973). Although not cited by *Aronson* or *Kaplan*, an even earlier emphasis on the importance of directors being informed can be found in *Beard v. Elster*, 160 A.2d 731, 737 (Del. 1960) (stating that where directors who were "fully informed, could well differ in opinion, then the sound business judgment rule required the court to approve the plan").

75. *See* Graham v. Allis-Chalmers Mfg. Co., 188 A.2d 125, 130 (Del. 1963) (noting that "it appears that directors of a corporation in managing the corporate affairs are bound to use that amount of care which ordinarily careful and prudent men would use in similar circumstances"); *supra* note 36 and accompanying text.

76. Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) (emphasis added). This distinction is occasionally, but not always, maintained, *see supra* notes 57-58, and accompanying text.

77. *Aronson*, 473 A.2d at 812; *see also* Veasey, *supra* note 29, at 1464 ("Simply stated, the director forfeits the benefit of the business judgment rule as a defense if he or she has violated the proper duty of loyalty and the proper duty of care.").

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Cede that the judiciary may examine the substance of director judgments not made on an informed basis. Furthermore, although *Aronson* regards the duty to be informed as a pre-condition to invocation of the business judgment rule, a breach of the duty to be informed apparently was not thought in 1984 to be sufficiently important, by itself, to create liability for the breaching director. At least the *Aronson* court failed to develop the liability implications of such a breach. Lack of informedness alone, for the *Aronson* court, like breach of due care for the *Cede* court years later, may not have created liability, but inexplicably, it apparently did free courts to substantively examine business decisions under some standard as yet unspecified in 1984.[78] Viewed this way, the seeds of *Cede's* analytical linking of a director due care breach to entire fairness review actually were sown in *Aronson.*

Whatever the initial intent or origins, fifteen years of decisional law since *Aronson* make clear that the "informed" element too frequently is equated with care.[79] That "shrinking" of due care to being informed is problematic enough on substantive policy grounds, and leads to a bifurcated rather than singular notion of care, one for the business judgment context and another for the non-judgment context.[80] The chief point here, however, is how, historically and doctrinally, the Delaware business judgment rule both preceded articulation of the due care duty and later enveloped care

78. The Delaware Supreme Court may have thought the only alternative to "business judgment" review in Delaware was "entire fairness" because in 1984 Delaware had not fully developed an intermediate "reasonableness" test as among its repertoire of standards. The 1995 Delaware Supreme Court *Cede* opinion interpreted the 1985 decision in *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985), as holding that entire fairness is the proper standard where directors are not informed prior to making a business judgment. *See* Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156, 1166 (Del. 1995). At least that is the case, according to *Cinerama*, where the director failure to be informed is accompanied by a breach of the duty of disclosure. *See id.* This 1995 interpretation of the 1985 *Van Gorkom* decision partially supplies an answer to a question invited by the *Aronson* dictum that directors must be informed to invoke the business judgment rule, namely, what standard of review applies where directors are *not* so informed?

79. *See supra* note 58. *See generally* Johnson, *supra* note 19.

80. Both the PRINCIPLES OF CORPORATE GOVERNANCE, *supra* note 21, § 4.01 and the Model Act make clear that director care in the decision-making context is to be differentiated from care in the oversight context. For example, the Model Act's revised § 8.30(b) formulates director care in the decision-making context as applying only "when" a director is "becoming informed" and formulates care in the oversight context as applying only "when" directors are "devoting attention." MODEL BUS. CORP. ACT § 8.30(b) (1998), *in 1997 MBCA Changes*, *supra* note 21, at 160. In other words, apparently directors are not generally required to act with care, but are required to do so only "when" "becoming informed" and "when" "devoting attention." *See supra* note 21. To more broadly express the duty of care, the second clause of revised § 8.30(b) *should* state: "in connection with their decision-making and oversight functions." Given the distinction between "standards of conduct" and "standards of liability" in the revised Model Act, *see supra* note 21, the downgrading and weakening of care in new § 8.30 is quite puzzling, inasmuch as breach of that section, unlike § 8.31, lacks liability "bite" anyway.

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(in the sense of being "informed") within the *Aronson* formulation of the rule,[81] thereby "triumphing," if you will, over the duty of care as the more preeminent and central corporate law precept in Delaware.[82] The duty of care, a doctrinal latecomer in Delaware, rather quickly was methodologically and analytically subsumed within the edifice of the business judgment rule, the rule itself remaining the intellectual centerpiece. This sweeping role for the business judgment rule may be precisely what both Samuel Arsht, in his important reprise on the rule,[83] and Justice Horsey,[84] author of the 1993 *Cede* opinion, envisioned for the rule.

Perhaps the late emergence, and thinness, of the due care concept in Delaware made this fusion of care and a robust business judgment rule less obvious or bothersome than might otherwise have been the case. No one, to be sure, can fault the requirement that directors be informed before exercising judgment. It is unfortunate, however, to stunt the growth of a vigorous, all-encompassing duty of due care by delimiting that core duty to a duty to "be informed."[85] It is even more unfortunate, once a duty of

81. *Aronson's* functional conflating of the duty of due care and the business judgment rule is captured in the following sentence where the court abruptly shifts from care to the business judgment rule: "While the Delaware cases use a variety of terms to describe the applicable *standard of care*, our analysis satisfies us that *under the business judgment rule director liability* is predicated upon concepts of gross negligence." *Aronson*, 473 A.2d at 812 (emphasis added). Further confusion results when the court switches from having used the term "standard" in conjunction with care in the above-quoted text of the opinion to using the same term, in a companion footnote, in conjunction with business judgment: "While the Delaware cases have not been precise in articulating *the standard by which the exercise of business judgment is governed*, a long line of Delaware cases holds that director liability is predicated on a standard which is less exacting than simple negligence." *Id.* at 812 n.6 (emphasis added). The court then cites cases articulating "fraud," "gross overreaching," and "abuse of discretion" standards, all of which go more to the *substantive* extremeness of the directors' decisions themselves than to the *care* of the decision-making process. *See supra* notes 29, 31.

82. The Chancellor, in *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1134, 1141 (Del. Ch. 1994), stated that "the law of fiduciary duties of corporate directors is older and more basic than the modernly popular 'business judgment rule.' " The Chancellor's assertion is not inconsistent with the point made in the text of this Article. The point in the text is not that Delaware directors have not long been under fiduciary duties, but rather that explicit articulation of the care duty emerged fairly recently and that, the Chancellor's statement notwithstanding, the concept of the business judgment rule in Delaware both *preceded* articulation of that duty and *subsequently* has enveloped care within its formulation. One of the aims of this Article is to dislodge care from the rubric of the business judgment rule and return it to the more basic role contemplated for it by the Chancellor.

83. *See* Arsht, *supra* note 22, at 111-12, 114, 118-21 (discussing the substance of the business judgment rule and its broad role in Delaware law).

84. *See* Henry Ridgely Horsey, *The Duty of Care Component of the Delaware Business Judgment Rule*, 19 DEL. J. CORP. L. 971 (1994). Justice Horsey's article was published several months after the 1993 *Cede* opinion and the year before the 1995 *Cede* opinion.

85. No doubt the heated reaction to *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985), and the resulting enactment of DEL. CODE ANN. tit. 8, § 102(b)(7) (Supp. 1998) were instrumental in this. Quite apart from the soundness or unsoundness of *Van Gorkom's* ruling on the facts, viewed historically, the Delaware Supreme Court, having finally formulated the "informed"

care began haltingly to emerge in Delaware, that the notion was not allowed to develop independently—and its violation treated meaningfully by creating liability—rather than being encased as a "component" of the business judgment rule.[86] The eventual upshot of this odd conjoining of the *duty* of due care and the business judgment rule *review standard* is *Cede's* holding that although breach of the former *duty* leads, methodologically, only to loss of the latter's *review standard*, the exacting "fairness" standard is thereupon illogically applied to assess director conduct that at most should be measured for compliance with a "reasonable" or "prudent" standard. This analytical move diminishes the independent, functional significance of due care for fiduciary conduct, while, at the same time, it inappropriately applies a too-demanding fairness standard upon its breach. This functional downgrading of due care, coupled with judicial encroachment into substance, reflects the functional immodesty of Delaware's business judgment rule as an analytical construct. It is also exactly the reverse of healthy corporate law.

It is quite clear, therefore, that, in Delaware at least, the business judgment rule is by no means "modest" in its analytical sweep. Far from being simply a judicial policy of non-review, it augmented in the 1980s and 1990s the prominence it had in the decades before the express emergence of care and actually became the unifying prism through which baseline director duties are examined. Viewed this way, *Cede* was the inexorable culmination of the post-*Aronson* effort to unify fiduciary analysis under the auspices of the business judgment rule, a herculean task for which the rule was never designed. One striking irony of this "immodest" business judgment rule, however, is that it actually fails to protect from judicial review that category of business decisions where directors were not informed—i.e., in the duty-breached setting. Under this Article's more "modest" business judgment rule, which simultaneously treats breaches of due care (or, minimally, failures of informedness) as independent wrongs creating liability, no such judicial incursion into business judgment is called for or allowed. In this sense, the "modest" business judgment rule more faithfully honors the policy core of the rule than does Delaware's more "immodest" version.[87]

element in *Aronson* many decades after other courts had verbally linked due care and the business judgment rule, at some point was going to apply that overdue element in a meaningful fashion. What is striking about *Van Gorkom*, again viewed historically, is both that the importance of care was so *late* in being vigorously expressed and that reaction to the decision was so *swift* as to result, two years later, in statutory authorization to exculpate directors from liability for all care breaches.

86. *See supra* note 85 and accompanying text.

87. *See* Manning, *supra* note 36, at 1491 ("The heart of the business judgment rule has always been a recognition by the courts that business decisions should not be evaluated retrospectively."); *see supra* note 25 and accompanying text.

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DRAWBACKS OF AN IMMODEST BUSINESS JUDGMENT RULE

Cede's analytical framework is novel. It also is probably the inevitable outcome of Delaware's double response to the late emergence of the due care duty. The two responses—*substantively* short-circuiting fuller growth of care by too quickly equating it with informedness and *methodologically* subsuming care within the business judgment rule framework—each mutually and negatively reinforce each other. That is, the subsuming of care allows continuation of an overly broad business judgment rule as the centerpiece of fiduciary analysis, while the continuing immodesty of the business judgment rule inhibits healthy independent growth of the due care duty. The *Cede* framework both reflects and perpetuates this problematic relationship between the duty of care and the business judgment rule. This, no doubt, contributes to the chronic lack of resolution to what two expert commentators on Delaware corporate law have politely described as the "uncertain nexus" between the business judgment rule and director duties.[88]

Having added the third "informedness" element to its business rule in *Aronson*, the court in *Cede* equated that element with care and treated its breach identically to breaches of good faith and loyalty. This accounts for the following key statement in *Cede*:

> [A] shareholder plaintiff assumes the burden of providing evidence that directors, in reaching their challenged decisions, breached *any one* of the *triads* of their fiduciary duty—good faith, loyalty or due care. If the rule is rebutted, the burden shifts to the defendant directors . . . to prove . . . the "entire fairness " of the transaction . . . .[89]

Treating breaches of care, good faith, and loyalty similarly may create a superficial uniformity of analysis, but it generates many problems as well. First, the analysis of care and loyalty claims is not really similar. With respect to loyalty, the plaintiff must properly raise a loyalty concern, but having done so need not prove a breach of that duty.[90] Rather, upon director loyalty properly being brought into issue, the burden of proof shifts to the self-interested director(s) for the purpose of convincing a court

88. Balotti and Hanks, *supra* note 14, at 1338.

89. Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 361 (Del. 1993) (citations omitted) (first emphasis added).

90. As stated by the Delaware Supreme Court: "When a board of directors' loyalty is questioned, Delaware courts determine whether a conflict has deprived the stockholders of a 'neutral decision-making body.' " Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156, 1170 (Del. 1995). Where a majority of directors is interested in a matter, the board is not a "neutral decision-making body." *See, e.g.*, Paramount Communications, Inc. v. QVC Network, Inc., 637 A.2d 34, 42 n.9 (Del. 1994) (noting that "where actual self-interest is present and affects a majority of the directors approving a transaction, a court will apply [the entire fairness test]").

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that, because the transaction was entirely fair,[91] the duty of loyalty was fulfilled, not breached. The burden shift precedes, rather than follows, an ultimate finding on breach or fulfillment of that duty.

The same is not true with care. Here plaintiff must do more than call care into question; plaintiff must *prove* a duty of care breach, whereupon, under *Cede*, the burden shifts to the director(s) to prove the entire fairness of the transaction.[92] Unlike the case with loyalty, the burden shift *follows*, rather than precedes, the finding of breach of that particular duty. Thus, the consequences of a *breach* of the duty of care are different than the consequences of a *breach* of the duty of loyalty. The former is not outcome determinative while the latter is.[93] *Cede's* uniformity of analysis, therefore, is more apparent than real.

Second, this asymmetric treatment of duty breaches stems from failure to apply, fully, the business judgment rule in a duty-breached context. Courts, including *Cede*, rightly apply half the business judgment rule in holding that, where directors *fulfill* their care duty, a court should not review the substantive merits of the business decision as a separate basis either for upsetting that decision or holding directors personally liable for a "bad" decision. Courts, including *Cede*, however, too infrequently apply the other half of the modest business judgment rule in failing to hold that, where directors *breach* their care duty, a court likewise should (and need) not review the substantive merits of the business decision as a separate basis for upholding the decision or absolving directors of liability for a "good" (or "fair") decision. The same policy rationales for judicial nonintervention into review of business decisions in the one care setting remain fully in force in the other setting as well. The real issue in the duty-breached context where there is an admitted failure to fulfill care—an already established independent wrong—is whether that breach will be taken seriously by holding that such a breach in and of itself creates liability. That issue should be faced openly by disentangling care from the

91. *See Cinerama*, 663 A.2d at 1172.

92. *See id.* at 1163.

93. In the 1995 *Cede* opinion, the Delaware Supreme Court makes clear that although the 1993 *Cede* opinion had held that directors had breached their duty of care—thereby denying defendants the procedural and substantive protection of the business judgment rule—the court in 1993 had not decided whether the directors had violated the duty of loyalty. *See id.* at 1165-66. This point, coupled with longstanding law in Delaware that entire fairness review is applied when director loyalty is sufficiently *challenged* not when the duty of loyalty actually has been found to have been *breached*, reveals the error of *Cede*'s assertion that to rebut the business judgment rule plaintiff must provide evidence that directors *breached* their duty of loyalty. It is not necessary that a court make a finding that directors actually breached the duty of loyalty prior to applying the entire fairness standard of review. In *Cede* itself, however, plaintiff's proof of an actual breach of due care by directors was necessary to alter the standard of review to an entire fairness standard. The court, therefore, wrongly equates the showings that must be made in the care and loyalty areas in order to apply the entire fairness standard.

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business judgment construct. If liability is held to result, ensuing remedial relief then turns on plaintiff proving damages as a proximate cause of the breach or establishing the conditions for equitable relief.[94]

Third, failure to apply fully the modest business judgment rule—recalling that rule as a pervasive policy of non-review—in a duty-breached context serves to denigrate breaches of care and thereby further weaken that already frail duty. Understanding the duty of care as a vital and independent duty of directors, not merely a "component" of the *Aronson/Cede* business judgment rule,[95] will lead to breaches of that duty being treated as wrongs in and of themselves, not simply as triggers for effecting a burden shift and a concomitant dropping of judicial inhibitions against examining the merits of business decisions. The *Aronson/Cede* formulation-framework, in short, simultaneously serves to downgrade care breaches in Delaware while also subjecting director decisions to close substantive review in a way that nullifies full application of a properly modest business judgment rule.[96]

Fourth, this belittling of care detracts from efforts to emphasize both the significance and reach of the duty of care. Unlike the business judgment rule, which by its terms has no application where directors exercise no business judgment,[97] the duty of care is a pervasive duty governing directors at all times, even when they are *not* exercising business judgments.[98] For this reason, due care should not rhetorically or analytically be conceived of as a "component" of (or mere precondition to) the business judgment rule because the latter operates in a far narrower province than care. For example, a breach of the duty of care resulting from faulty director monitoring of corporate affairs, where no identifiable business judgment was made, simply does not fit into a formulation that analytically subsumes the richer duty of care under the more confined business judgment context. Ironically, this serves to splinter, not unify, efforts to reinvigorate care as a robust and foundational duty coherently applying in both judgment and non-judgment contexts.[99]

94. *See supra* note 38 and accompanying text.

95. *See supra* note 82 and accompanying text.

96. *See* Melvin A. Eisenberg, *The Divergence of Standards of Conduct and Standards of Review in Corporate Law*, 62 FORDHAM L. REV. 437, 464 (1993) (stating that "a director who makes a disinterested decision will be subject to a due-care rather than a rationality standard of review if the requirements of the business-judgment rule are not satisfied"). After *Cede*, such a director will not be subjected to the "reasonable" and "prudent" standard of due care, but to an "entire fairness" standard formerly reserved for loyalty claims.

97. *See supra* note 42 and accompanying text.

98. *See supra* note 35 and accompanying text; *see also In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 967-970 (Del. Ch. 1996).

99. Some commentators believe the modern duty of care has been drained of meaningful ability to constrain fiduciary conduct. *See, e.g.* ARTHUR R. PINTO & DOUGLAS M. BRANSON, UNDERSTANDING CORPORATE LAW § 8.05 (1999) (discussing "The Demise of the Duty of Care"); Sanjai Bhagat et al., *Director Ownership, Corporate Performance, and Management Turnover*,

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Fifth, *Cede's* burden shift and entire fairness approach to a care breach simply led to a judicial assessment of factors which should have been done as part of a more thorough threshold duty of care analysis.[100] Recognizing the care-like nature of the factors it was evaluating in its entire fairness review,[101] the court could only rationalize its two-stage care analysis by stating that the "degree of procedural due care a board of directors exercises has been recognized as a continuing component of an entire fairness analysis."[102] What later comprised the court's "fair dealing" portion of its entire fairness analysis should have been done as part of the initial due care inquiry. This more thorough care assessment at the outset would have splendidly highlighted that due care encompasses more than the *Aronson* element of informedness. It also would have more efficiently resulted in what should have been an earlier finding of no duty of care breach in that case, or at least none causing damages. As it is, the court eventually found director compliance with a strict entire fairness test after first finding a director care breach under a more deferential standard.[103] This revisiting of care under the rubric of entire fairness obscures rather than clarifies the distinctive contours of the due care duty. Care is only diminished as a result.

Finally, the *Cede* framework ignores the underpinnings for judicial deference in the care area, in contrast to the loyalty area. A key rationale for judicial deference in the care area is the perceived institutional impropriety of public officials evaluating the substantive quality of private sector business decisions. The absence of *Aronson's* informedness element alone, or even an affirmative showing by plaintiff of unreasonableness in the overall decision-making process, does not warrant a court in supplanting a board of directors and passing its own judgment—usually long after the fact—on the substantive merits of a business decision. Two matters are troublesome in this regard. First, the legislatively enacted corporations statute places the business and affairs of a corporation under the "direction" of a board of directors, not a court.[104] Failure of a board to act with requisite

54 BUS. LAW. 885, 918 (1999) ("[T]he traditional [procedurally] based legal duty of care . . . [has] led not to more effective management oversight but, instead, to a classic triumph of form over function—where, although prescribed procedure has been followed, decision-making appears to be little more than staged play-acting, absent critical engaged oversight."). *Compare* Riley, *supra* note 33, *with* Eisenberg, *supra* note 96, *and* Johnson, *supra* note 19 (each seeking to reclaim for corporate law the value of the due care duty).

100. *See* Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156, 1172-80 (Del. 1995).

101. The court approved the Court of Chancery's consideration of the directors' "now undisputed lack of care" along with its consideration of how the directors "had carefully" acted in other ways. Thus, the directors had demonstrated both a "lack of care" and had acted "carefully." *See id.* at 1175.

102. *Id.*

103. *See id.* at 1179-80.

104. *See* DEL. CODE ANN. tit. 8, § 141(a) (1991); *see also* Quickturn Design Sys. v. Shapiro, 721 A.2d 1281, 1291 (Del. 1998); Beard v. Elster, 160 A.2d 731, 738 (Del. 1960) ("We think, therefore, we are precluded from substituting our uninformed opinion for that of experienced business managers of a corporation who have no personal interest in the outcome.").

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care in discharging this statutory responsibility neither transfers this responsibility to the judiciary nor is the failure negated by a judicial conclusion that the ultimate outcome was, after all, "fair." Second, although the duty of care mandates only that directors act with reasonable prudence (whether understood as informedness or as a richer "due care" notion), a director found to have breached that duty is saddled, after *Cede*, with the further, unexpected duty of proving that what was done was "entirely fair." The *ex post* judicial review standard of fairness, therefore, is more demanding than the *ex ante* duty to act with care. A director acting in good faith and having no disqualifying self-interest in a matter may rightly believe his or her only remaining duty is to act carefully. Yet, *Cede* tells a director that, upon a judicial finding of breach of care, having acted fairly will atone for the care breach,[105] possibly leading some directors to believe, out of caution, that the *ex ante* duty of care is best regarded as including a fallback duty to act fairly. The *judicial review* standard, therefore, indirectly may raise the *director* standard of conduct.[106] The result may be overly cautious *business* behavior aimed at avoiding transactions that directors cannot confidently conclude are substantively "fair," and overly cautious *decision-making* behavior so as to comply with the "fair dealing" aspect of entire fairness.

Care cases, unlike loyalty cases, do not deprive corporations of a "neutral decision-making body."[107] The prevailing loyalty rationale for judicial assessment of the substantive fairness of business decisions, therefore, does not obtain in care cases, even where care is breached. Consequently, a care breach, contrary to what *Cede* holds, should not result in judicial review of *substance*. At the same time, a care breach should have more than *Cede*'s burden-shifting *procedural* effect; it should have substantive force. It is in this sense that the substantive force of the modest business judgment rule always applies in a care case, immunizing the quality of the decision from judicial review whether or not care was exercised. In the care setting involving the exercise of business judgment, the proper inquiry is, instead, whether an undoubtedly neutral decision maker acted in a reasonably prudent *manner*; that investigation does not ever necessitate or warrant judicial inquiry into the substantive merits of a decision, only (but no less than) a probing inquiry into the process by which it was made.[108] Whether the decision-making process is found to be sound or unsound, the court is not to pass on the substantive merits of the actual business decision.

105. *See Cinerama, Inc.*, 663 A.2d at 1175.

106. In Professor Eisenberg's terminology, this is a peculiar instance of "divergence," *see* Eisenberg, *supra* note 96, at 438, between a standard of conduct and a standard of review where the latter, being higher, may effectively raise the former.

107. Oberly v. Kirby, 592 A.2d 445, 467 (Del. 1991), *quoted in Cinerama, Inc.*, 663 A.2d at 1170.

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

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If the directors' decision-making process was sound, the court looks at the business decision itself only to verify a linkage between process and outcome. Importantly, the inquiry is not an examination of substance—even for minimal rationality[109]—but only of whether the decision actually made was a "rational outcome of" the decision-making process actually undertaken. Put another way, the court asks whether there is a "rational connection between" the sound process actually undertaken and the decision actually reached.[110] This mild requirement avoids a complete disjunction between process and outcome. If, on the other hand, the process is defective, directors will be liable without regard to decisional quality—on the rationale that judicial views of decisional quality are irrelevant in the care area—for all damages proximately caused by their carelessness, excepting only rescissory damages.[111] To reduce liability exposure, directors can seek *ex ante* shareholder exculpation from damages,[112] or, notwithstanding the breach of care, they can defend against an award of damages or equitable relief by extolling the "fair" economic merits of their decision as negating the existence of any harm from their breach.

Cede adopted its uniform analysis of fiduciary duty breaches with no attention to these fundamental differences between judicial review of care and loyalty. A modest business judgment rule would highlight, rather than obscure, these importance differences.

CONCLUSION

The duty of due care and the business judgment rule oftentimes seem hopelessly entangled. Why try to untangle them? After all, corporate law and the corporate institution seem to be flourishing at the beginning of a new century.

The history of legal thought teaches us that sometimes analytical constructs enhance our understanding of social phenomena and sometimes they impede it. Whether the duty of due care and the business judgment rule need sorting out depends, ultimately, on how important a strong, distinctive duty of due care is thought to be for contemporary corporate law. A rhetorical mainstay of corporate law for decades outside Delaware, due care in Delaware emerged rather recently. Once it was analytically

109. Thus, the "any rational business purpose" requirement of *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720 (Del. 1971), and of PRINCIPLES OF CORPORATE GOVERNANCE, *supra* note 21, § 4.01(c) is inappropriate and unnecessary under a modest business judgment rule which, simultaneously, takes due care seriously. *See supra* note 32.

110. The "rational connection" expression is an administrative law notion, requiring that an agency offer a linkage ("rational connection") between its findings and its decision. *See* Burlington Truck Lines, Inc. v. United States, 371 U.S. 156, 168 (1962).

111. Chancellor Allen forcefully argued against awarding rescissory damages in a duty of care case. *See* Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1134, 1144-50 (Del. Ch. 1994), *aff'd*, 663 A.2d 1156 (Del. 1995).

112. *See supra* notes 37-38 and accompanying text.

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expressed in *Aronson* and applied with force in *Van Gorkom*, a statutory opt-out of liability for its breach was quickly provided. Meanwhile, in the statutory law of other business associations—such as partnerships and limited liability companies—the duty of care wholly lost its affirmative thrust and was reduced to a "duty to refrain" from grossly negligent (or worse) behavior,[113] a duty that neither inspires nor packs much legal punch.

One response to this decades-long development is to assert that modern corporate law (along with partnership and LLC law) now treats the concept of due care in a way that more closely reflects good policy. This amounts, frankly, to a view that care's role in corporate law has been overstated all along. Another response—Professor Eisenberg's[114]—is to maintain care's importance by conceiving of it as a "standard of conduct" though not a "standard of review" carrying liability "bite." Among other problems with that account, as a standard of conduct due care remains a pre-condition to the business judgment standard of review, meaning director care is *reviewed* for compliance with a standard of *conduct*. This looks like more "convergence" than "divergence." Moreover, notwithstanding the revised Model Act's supposed reliance on Professor Eisenberg's "divergence" account,[115] the Act proceeds to weaken the traditional care formulation (section 8.30) and adopt a lower standard of liability/review (section 8.31) that may still be higher than the uncodified business judgment rule, thereby suggesting that the divergence account does not fully capture positive law developments. The same can be said for developments in partnership and LLC formulations of the duty of care, with their dictate that decision makers must act only in a way that avoids violation of the legal liability standard.

Against that backdrop, the purpose of this Article is simple. It contends that the place of due care in corporate law—whether central or marginal—is best addressed head-on. To facilitate this, the duty of due care, in formulation and function, should be differentiated from the single-focus policy expressed in the business judgment rule. To the extent the two corporate law concepts can be distinguished, the choice between a weak or strong duty of due care can then be made in reference to policy considerations distinct from those underlying the business judgment rule.

Toward that end, this Article advocates that, as between the two concepts, the business judgment rule should be the more modest construct; that it, not due care, is the better choice to "freeze," leaving due care with its concise, but fluid, "reasonable" and "prudent" elements as the superior candidate for remaining what it should be—a highly adaptive precept in

113. *See, e.g.*, Revised Uniform Partnership Act § 404(c) (1994 & Supp. 1997); Uniform Limited Liability Company Act § 409(c) (1995).

114. *See generally* Eisenberg, *supra* note 96.

115. *See* MODEL BUS. CORP. ACT § 8.31 official comment (1998), *in 1997 MBCA Changes*, *supra* note 21, at 176.

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the hands of common law and equity judges. Delaware, *not* having codified due care, is well positioned to pursue this approach. States with codified standards of director conduct reflecting a traditional due care formulation should refrain from following the revised Model Act's complex approach without thoughtful study and a stronger case being made for why and how those changes improve corporate law.

Whatever the fate of due care in corporate law in the new century, at this stage the role of different legal rules is to carry different policy preferences. With policy choices made clearer, through strictly limiting the function of the business judgment rule doctrine, due care in corporate law may indeed be cast off as a concept whose importance has been historically overstated. Alternatively, more meticulous use of legal vocabulary may promote a rethinking of whether and why due care remains important in modern business law. The policy stakes in that choice are more easily seen with the help of a modest business judgment rule.

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