

# Corporate officers may be exculpated from personal liability under new amendment to Delaware law

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SEPTEMBER 1, 2022

## Key takeaways

- Newly amended DGCL Section 102(b)(7) allows Delaware corporations to provide officers with exculpatory protections for personal monetary damages resulting from a breach of fiduciary duty in certain actions.
- While the protections are subject to limitations and not as broad as those provided for directors, the amendment addresses the historic disparate treatment of officers and directors in class action litigations.
- A Delaware corporation seeking to expand exculpatory protections to officers must affirmatively build those protections into its certificate of incorporation.

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A Delaware corporation may now provide its officers with exculpatory protections for personal monetary damages similar, but not identical, to those from which directors have long benefited.

Historically, as a tool to protect directors only, Delaware law eliminated or limited personal liability for monetary damages resulting from a breach of fiduciary duty, subject to certain limitations and as provided for in the corporation's certificate of incorporation. The exclusion of corporate officers from this protection resulted in increased litigation against them when claims against directors were not viable.

In recognition of this disparity, the law has now been changed. Following a recent amendment to Section 102(b)(7) of the Delaware General Corporation Law (DGCL), effective as of Aug. 1, 2022, the scope of available exculpatory protections now extends to corporate officers. Consequently, a Delaware corporation may act to protect its corporate officers by affirmatively including an appropriate exculpatory provision in its certificate of incorporation.

The Delaware legislature enacted Section 102(b)(7) of the DGCL in 1986 after the Delaware Supreme Court's ruling in *Smith v. Van Gorkom* rendered it extremely difficult for a corporation to obtain liability insurance for its directors at reasonable premiums. In *Van Gorkom*, the Delaware Supreme Court reversed a Chancery Court ruling in favor of defendant directors providing that they had satisfied their duty of care in approving a transaction without considering all material information.

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Section 102(b)(7) was historically limited only to a corporation's directors and did not extend to officers, due in large part to the legislative focus on director liability in the wake of *Van Gorkom* and the prevailing view at the time that Delaware's long-arm statute did not provide jurisdiction over corporate officers.

In 2009, the Delaware Supreme Court in *Gantler v. Stephens* reaffirmed that officers of Delaware corporations owe the same fiduciary duties as directors. In recent years, Delaware courts have seen an increase in litigation, particularly class actions, alleging officers and directors violated their duty of care.

While directors have seen such claims dismissed based on Section 102(b)(7), officers have not. In effect, by exploiting the disparate treatment of officers and directors when challenging the decision of a majority independent board, the plaintiffs' bar successfully created a "back door" by singling out officers as defendants. In turn, this prompted a real need for the amendment.

Under the amendment, a Delaware corporation can now take action to adopt a charter provision that effectively eliminates its covered officers' personal liability for breach of the duty of care for direct claims by stockholders (including class actions). These types of claims commonly arise in the context of an M&A transaction.

This is not to say, however, that corporate officers and directors are now on equal footing. Notably, the newly amended Section 102(b)(7) does not eliminate liability of officers for breach of fiduciary duty arising out of claims brought by the corporation itself or for derivative claims brought by the corporation's stockholders

in the name of the corporation. This is a significant difference from how the DGCL treats exculpation of directors.

The amendment also precludes elimination or limitation of liability for the types of claims with respect to which exculpation of directors is not permissible, such as (i) a breach of the duty of loyalty, (ii) acts or omissions not in good faith or that involve intentional misconduct or a knowing violation of law, and (iii) any transaction from which the officer derived an improper personal benefit.

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*After obtaining the requisite approvals, a certificate of amendment must be filed with the Delaware secretary of state in order to effect the amendment.*

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Additionally, the amended Section 102(b)(7) only applies to certain officers, namely a person who (during the course of conduct alleged to be wrongful) (i) is or was president, chief executive officer, chief operating officer, chief financial officer, chief legal officer, controller, treasurer or chief accounting officer; (ii) is or was identified in the corporation's public filings with the U.S. Securities and Exchange

Commission because such person is or was one of the most highly compensated executive officers of the corporation; or (iii) has, by written agreement with the corporation, consented to be identified as an officer for purposes of accepting service of process.

A Delaware corporation seeking to expand the benefits of the newly amended Section 102(b)(7) to its corporate officers must take action to do so, as the protections will not spring to life until and unless the corporation's certificate of incorporation provides for it, and then only to the extent provided for. When a new Delaware corporation is in the formation stage, organizers should therefore consider including a provision expressly providing exculpatory protections for both directors and officers.

An existing Delaware corporation, on the other hand, should consider amending its certificate of incorporation to include a provision expressly covering officers that, depending on the corporation's organizational documents, may require both board and stockholder approval. After obtaining the requisite approvals, a certificate of amendment must be filed with the Delaware secretary of state in order to effect the amendment.

Should you have any questions regarding the above, please contact Asim Grabowski-Shaikh of the Capital Markets and Corporate Governance team or Matthew Gases of the Mergers and Acquisitions and Corporate Governance team.

### About the authors



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This article was published on Westlaw Today on September 1, 2022.

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