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Why Does the FDIC Sue Bank Officers? Exploring the Boundaries of the Business Judgment Rule in the Wake of the Great Recession

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Introduction

The business judgment rule is a venerable protection for corporate directors acting in good faith, ensconced in the common law and sometimes codified by statute. There has been a continuing debate, however, regarding the availability of the defense to corporate officers. In the wake of the Great Recession, the Federal Deposit Insurance Corporation ("FDIC") has brought numerous lawsuits in its role as receiver of failed banks against former bank directors and officers. The FDIC has mounted a sustained attack on the availability of the business judgment defense to bank officers in recent years, arguing—with mixed success—that the business judgment rule does not apply to them.

This article discusses the FDIC's approach to receivership litigation over the past five years, explores the background of the business judgment rule, evaluates whether the exclusion of officers from the scope of business judgment protection is consistent with the policies underlying the doctrine, and examines the current jurisprudence in three states—Georgia, California, and Florida—to illustrate the range of protections afforded to the judgments of bank officers. It concludes by examining some practical considerations to consider when asserting this affirmative defense.

I. The FDIC's Approach to Receivership Litigation after the Great Recession

The global economic crisis that roiled the subprime markets in 2007 and spread through all credit markets in 2008 proved to be the worst economic period in the United States since the Great Depression. Liquidity virtually disappeared, causing the failure of numerous financial institutions including Bear Stearns and IndyMac, and prompting the Federal Reserve to take unprecedented actions to infuse liquidity into financial markets. At the peak of the crisis in September 2008, financial markets were rocked by the bankruptcy of Lehman Brothers, the nationalization of Fannie Mae and Freddie Mac, the downgrade of AIG, and the failure of Washington Mutual, which had been the nation's largest savings-and-loan. Unemployment rates soared, rising from under 5% nationally in early 2008 to more than 10% by October 2009. The stock market lost over half of its value,[1] and housing values plunged, leaving millions of homeowners under water, delinquent on their mortgage payments, and facing foreclosure. Alan Greenspan, the former Chairman of the Federal Reserve, aptly described the financial crisis in 2008 as a "once in a century credit tsunami."[2]

Not surprisingly, the Great Recession devastated federally insured financial institutions. From 2001 through 2007, there were twenty-five bank failures in the United States—all but three of which occurred before 2005—with total losses estimated at just under $945 million.[3] From 2008 through the present, the number of bank failures skyrocketed to 507, more than eighteen times the rate seen in the preceding seven-year period.[4] Total losses were estimated to exceed $85 billion.[5] At the peak of the bank failures in 2010, regulators shuttered 157 banks across the nation—over fifty of them in Florida and Georgia alone.[6] In testimony given to the House Subcommittee on Financial Institutions and Consumer Credit on May 26, 2011, Sheila C. Bair, Chairperson of the FDIC, testified that the financial crisis that hit "in the fall of 2008" was "the worst financial crisis since the 1930s" and that "few at the time foresaw the extent of the emerging threat to our financial stability."[7] Or as Federal Reserve Chairman Ben Bernanke observed afterwards in

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1. The Dow Jones Industrial Average plunged from its peak of 14,165 on October 9, 2007 to its trough of 6,926 just 18 months later.
2. *The Financial Crisis and the Role of Regulators: Hearing Before the H. Comm. on Oversight and Government Reform*, 110th Cong. 11 (2008) (statement of Alan Greenspan, Chairman, Federal Reserve).
3. *FDIC Failures & Assistance Transactions*, FDIC (Dec. 23, 2014, 4:00 PM), https://www2.fdic.gov/hsob/SelectRpt.asp?EntryTyp=30.
4. *Id.*
5. *Id.*
6. *Id.*
7. *FDIC Oversight: Examining and Evaluating the Role of the Regulator during the Financial Crisis and Today*, *Before the H. Subcomm. on Financial Institutions and Consumer Credit*, 112th Cong. 48, 57 (2011) (statement of Sheila C. Bair, Chairman, FDIC).

discussions with the Financial Crisis Inquiry Commission, "a 'perfect storm' had occurred that regulators could not have anticipated."[8]

In the aftermath of this economic cataclysm, the FDIC has vigorously pursued officers and directors of failed financial institutions as it seeks to minimize losses to the Deposit Insurance Fund ("DIF"). Acting as a receiver for failed financial institutions, the FDIC succeeds to all rights and privileges of a failed bank, including claims against former directors and officers.[9] To date, the FDIC has authorized lawsuits in connection with nearly one-third of the Great Recession bank failures.[10] From January 1, 2009 through July 24, 2014, the FDIC authorized lawsuits in connection with 145 failed institutions against 1,171 individuals.[11] The FDIC has filed 97 lawsuits against 749 former directors and officers of failed financial institutions. Additional FDIC lawsuits against officers and directors can be anticipated over the next year or so, before the FDIC's three-year statute of limitations expires.[12]

The FDIC does not typically litigate the cause of a bank's failure, nor does the FDIC seek to recover all DIF losses stemming from a

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8. THE FINANCIAL CRISIS INQUIRY COMM'N, THE FINANCIAL CRISIS INQUIRY REPORT: FINAL REPORT OF THE NATIONAL COMMISSION ON THE CAUSES OF THE FINANCIAL AND ECONOMIC CRISIS IN THE UNITED STATES, at 3 (2011).

9. 12 U.S.C. § 1821(d)(2)(A)(i) (2012). Courts have recognized that the FDIC acts in a different capacity as a regulator than it does when it acts as a receiver. *See* FDIC v. Skow, 741 F.3d 1342 (11th Cir. 2013) (per curiam). The FDIC stands in the shoes of the failed bank and has statutory authority, in its role as receiver, to recover for creditors on their outstanding claims. Often, the largest creditor of the failed bank or thrift is the FDIC itself, because its deposit fund pays insured depositors the full amount of their claims.

10. By way of comparison, the FDIC brought claims against directors and officers in 24% of the bank failures between 1985 and 1992. *See* Professional Liability Lawsuits, FDIC (Oct. 6, 2014), *available at* https://www.fdic.gov/bank/individual/failed/pls/.

11. *Id.*

12. The FDIC has the longer of three years from accrual, or the appropriate limitations period under state law (whichever is longer), to bring tort claims and six years from accrual, or the applicable period under state law, to bring breach of contract claims. The date of accrual is the date the cause of action accrues under the applicable law or the date of the appointment of the FDIC as receiver, whichever is longer. 12 U.S.C. § 1821(d)(14)(B). In addition, claims alleging fraud, intentional misconduct resulting in unjust enrichment or resulting in substantial loss to a failed institution may be brought without regard to a limitations period under state law, if the limitations period for such actions did not expire more than five years before the appointment of the FDIC as the conservator or receiver. 12 U.S.C. § 1821(d)(14)(C).

bank's failure. The former is unnecessary, and the latter is pointless. Instead, the FDIC takes a practical, cost-benefit approach to its Director and Officer ("D&O") litigation aimed at ascertaining recoverable amounts (whether from insurance policies or potential defendants) and determining whether it can build a credible case for negligence, breach of fiduciary duty, or gross negligence to recover available amounts. Thus, even though a bank failure may cost the DIF hundreds of millions of dollars, it is not uncommon for the FDIC to file a D&O lawsuit premised on a handful of problematic loans where the recoverable damages are calibrated to the policy limits but amount to only a small fraction of the total loss to the DIF.

Although the FDIC acknowledges on its website that directors are entitled to business judgment protections—"[b]ank directors are allowed to exercise business judgment without incurring legal liability"[13]—it offers no such assurance to bank officers. In light of the economic catastrophe that our country experienced and the resulting losses to the DIF, there is tremendous pressure on the FDIC to scrutinize the decisions of bank directors and, especially, bank officers with the benefit of hindsight to search for possible bases for liability.

That pressure is offset, to a degree, by the fact that federal law imposes a heightened liability requirement on the FDIC as Receiver unless applicable state law provides a lower accountability threshold. The Financial Institutions Reform Recovery and Enforcement Act of 1989 ("FIRREA") established gross negligence as a national minimum standard for officer and director liability:

> *A director or officer of an insured depository institution may be held personally liable* for monetary damages in any civil action by, on behalf of, or at the request or direction of [the FDIC] . . . acting as conservator or receiver . . . *for gross negligence*, including any similar conduct or conduct that demonstrates a greater disregard of a duty of care (than gross negligence) including intentional tortious conduct, as such terms are defined and determined under applicable State law. Nothing in this paragraph shall impair or affect any right of the Corporation under other applicable law.[14]

13. Professional Liability Lawsuits, *supra* note 10.
14. Pub. L. No. 101-73, § 212(k), 103 Stat. 183, 243 (codified as amended at 12 U.S.C. § 1821(k) (1989) (emphases added); *see also* Atherton v. FDIC, 519 U.S. 213, 216 (1997) ("The federal statute . . . sets a 'gross negligence' floor, which applies as a substitute for state standards that are more relaxed."); FDIC v. Stahl, 89 F.3d 1510, 1516 (11th Cir. 1996) ("[Section] 1821(k) permits claims against directors for gross

The statute, however, permits the FDIC to pursue claims against officers and directors under a stricter standard of liability (*e.g.*, ordinary negligence) if authorized by state law.[15] In most jurisdictions, a showing of gross negligence (as defined by relevant state law)[16] is the standard for successful actions against officers and directors. Unless state law permits officers and directors of a bank to be liable on a lesser showing of culpability, a court will typically dismiss the FDIC's ordinary negligence claims.[17]

In order to circumvent this heightened standard, the FDIC may elect to bring claims against officers in lieu of directors when the circumstances permit. When it does sue officers, the FDIC frequently relies upon state law negligence standards to argue that officers owe a duty to exercise the care an ordinary prudent person would exercise in similar circumstances, and that there is a lower standard to hold officers liable than gross negligence. The remainder of this article explores the interaction between this argument and the application of the business judgment rule.

II. THE ORIGINS OF THE BUSINESS JUDGMENT RULE

Directors of failed financial institutions alleged to have acted negligently or in breach of their fiduciary duty may avail themselves of the defense of the business judgment rule, which is a presumption that

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negligence regardless of whether state law would require greater culpability.") (emphasis and internal quotation marks omitted).

15. *See Stahl*, 89 F.3d at 1515-16 (holding that while FIRREA's gross negligence standard displaced any federal common law negligence claims, § 1821(k)'s savings clause allowed state law process due care claims to survive).

16. FDIC v. Aultman, No. 2:13-cv-58-FTM-384AM, 2013 WL 3357854, at *3 (M.D. Fla. July 3, 2013) ("FIRREA incorporates the definition of gross negligence provided by relevant state law.").

17. *See, e.g.*, FDIC v. Briscoe, No. 1:11-CV-02303-SCJ, 2012 WL 8302215, at *5 (N.D. Ga. Aug. 14, 2012) ("Defendants' motion to dismiss on the grounds of the applicability of the business judgment rule is hereby GRANTED as to the ordinary negligence and breach of fiduciary (based upon ordinary negligence) counts of the Complaint."); Fleet Nat'l Bank v. Boyle, No. Civ. A. 04CV1277DDD, 2005 WL 2455673 (E.D. Pa. Sept. 12, 2005); Lippe v. Bairnco Corp., 230 B.R. 906 (S.D.N.Y. 1999).

their decisions were made in good faith.[18] Generally speaking, the business judgment rule focuses on the reasonableness of the process used to reach a decision, and not on the ultimate outcome of that decision. "'Due care in the decision making context is *process* due care only.'"[19] The Delaware Supreme Court, for example, has held that decisions of directors will be upheld "unless [they] cannot be 'attributed to any rational business purpose.'"[20] The same court observed, in *Brehm v. Eisner*, that "[i]rrationality is the outer limit of the business judgment rule"[21] and, in *Brazen v. Bell Atlantic Corp.*, that "[a] board of directors enjoys a presumption of sound business judgment, and its decisions will not be disturbed if they can be attributed to any rational business purpose."[22] As one commentator has observed, "[t]he business judgment rule applicable to directors and officers goes much further that the honest-error-of-judgment rule of general tort law. . . . Under the business judgment rule, there is no liability even though a decision is unreasonable."[23]

The business judgment rule originated in the common law, and first appeared in the United States in *Percy v. Millaudon*, an 1829 decision of the Louisiana Supreme Court.[24] The case concerned the liability of bank directors for the wrongdoing of the bank's president and cashier. The court absolved the directors of liability, explaining that a bank director is not liable if he exercised ordinary care. In *Godbold v. Branch Bank*, the

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18. *See* Int'l Ins. Co. v. Johns, 874 F.2d 1447, 1461 (11th Cir. 1989) ("Under the business judgment rule, courts presume that directors have acted properly and in good faith.").

19. Stewart v. BF Bolthouse Holdco, LLC, No. 8119-VCP, 2013 WL 5210220 (Del. Ch. Aug. 30, 2013) (quoting McPadden v. Sidhu, 964 A.2d 1262, 1270 (Del. Ch. 2008)).

20. Brehm v. Eisner (*In re* Walt Disney Co. Deriv. Litig.), 906 A.2d 27, 74 (Del. 2006) (quoting Sinclair Oil Co. v. Levien, 280 A.2d 717, 720 (Del. 1971)).

21. 746 A.2d 244, 264 & n.66 (Del. 2000).

22. 695 A.2d 43, 49 n.19 (Del. 1997) (quoting Sinclair Oil Co. v. Levien, 280 A.2d 717, 720 (Del. 1971)).

23. Melvin A. Eisenberg, *The Duty of Care of Corporate Directors and Officers*, 51 U. PITT. L. REV. 945, 963 (1990); *see also* Sam Wong & Son, Inc. v. N.Y. Mercantile Exch., 735 F.2d 653, 678 n.32 (2d Cir. 1984) (Friendly, J.) (describing the rationality test as "a minimal requirement of some basis in reason"); *In re* Caremark Int'l Inc. Deriv. Litig., 698 A.2d 959, 967 (Del. Ch. 1996) (stating that no liability for a decision the fact finder believes to be "wrong," "stupid," or "egregious," "so long as the [decision-making process] was either rational or [was] employed in . . . good faith" (emphasis omitted)).

24. 8 Mart. (n.s.) 68, 1829 WL 1592 (La. 1829).

Alabama Supreme Court similarly absolved bank directors of wrongdoing, explaining that a rule holding a director liable for any error in decision-making would be "manifestly wrong" and that "[t]he inevitable tendency of such a rule, would be hostile to the end proposed by it, as no man of ordinary prudence would accept a trust surrounded by such perils."[25]

The justification for this widespread understanding of the business judgment rule goes back to several basic principles resting at the core of the traditional rule's limitation of liability. First, subjecting corporate decision-makers to liability for innocent mistakes deters them from assuming risks that are necessary for business operations.[26] As the Delaware Chancery Court explained, by eliminating the prospect of personal liability for ordinary errors in judgment, the rule "makes board service by qualified persons more likely."[27] Second, as a matter of institutional competence, judges and juries are poorly positioned to assess the propriety of complex business decisions, both because they lack the specialized skill, knowledge, and judgment of actual businessmen,[28] and because hindsight bias poses the risk that "a reasoned decision at the time made may seem a wild hunch viewed years later against a background of perfect knowledge."[29]

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25. 11 Ala. 191, 199, 1847 WL 159, at *6 (1847).

26. *See, e.g.*, Gagliardi v. TriFoods Int'l, Inc., 683 A.2d 1049, 1052 (Del. Ch. 1996).

27. *In re* Caremark Int'l. Inc. Derivative Litig., 698 A.2d at 971.

28. *See* W. Point-Pepperell, Inc. v. J.P. Stevens & Co. (*In re* J.P. Stevens & Co. S'holders Litig.), 542 A.2d 770, 780 (Del. Ch. 1988).

29. Joy v. North, 692 F.2d 880, 886 (2d Cir. 1982); *see also In re* Citigroup Inc. S'holder Deriv. Litig., 964 A.2d 106, 126 n.58 (Del. Ch. 2009) ("There is a substantial risk that suing shareholders and reviewing judges will be unable to distinguish between competent and negligent management because bad outcomes often will be regarded, ex-post, as having been foreseeable and, therefore, preventable ex-ante. If liability [arises] from bad outcomes, without regard to the ex-ante quality of the decision or the decision-making process, however, managers will be discouraged from taking risks." (first alternation in original) (internal quotation marks omitted)).

III. POLICY CONSIDERATIONS AFFECTING THE APPLICATION OF THE BUSINESS JUDGMENT RULE TO BANK OFFICERS

The wisdom of extending the rule to officers has been debated,[30] although many jurisdictions apply the business judgment rule to both officers and directors.[31] As one court has observed, "[a]lthough the business judgment rule is usually defined in terms of the role of corporate directors, it is equally applicable to corporate officers exercising their authority."[32] Both the American Law Institute and the ABA Committee on Corporate Laws endorse this expansive view of the rule.[33] Nonetheless, application of the business judgment rule to

30. *Compare* Lyman P.Q. Johnson, *Corporate Officers and the Business Judgment Rule*, 60 BUS. LAW. 439, 440 (2005) (asserting that business judgment rule should not extend to non-director officers), *with* Lawrence A. Hamermesh & A. Gilchrist Sparks III, *Corporate Officers and the Business Judgment Rule: A Reply to Professor Johnson*, 60 BUS. LAW. 865, 865 (2005) ("policy rationales underlying the development and application of the business judgment rule to corporate directors similarly justify application of the rule to non-director officers").

31. *See* Am. Soc'y for Testing & Materials v. Corrpro Cos., 478 F.3d 557, 572 (3d Cir. 2007); FDIC v. Briscoe, No. 1:11-cv-02303-SCJ, 2012 WL 8302215, at *4–5 (N.D. Ga. Aug. 14, 2012); Stanziale v. Nachtomi, 330 B.R. 56, 62–63 (D. Del. 2004), *aff'd in part, rev'd in part*, 416 F.3d 229 (3d Cir. 2005); Grassmueck v. Barnett, No. C03-122P, 2003 WL 22128263, at *3 (W.D. Wash. July 7, 2003); Estate of Detwiler v. Offenbecher, 728 F. Supp. 103, 147–48 (S.D.N.Y. 1989) (applying Michigan law); Massaro v. Vernitron Corp., 559 F. Supp. 1068, 1080 (D. Mass. 1983) (applying Delaware law); Rosenfield v. Metals Selling Corp., 643 A.2d 1253, 1261 n.16 (Conn. 1994); Selcke v. Bove, 629 N.E.2d 747, 750 (Ill. App. Ct. 1994); Potter v. Pohlad, 560 N.W.2d 389, 391–92 & n.1 (Minn. Ct. App. 1997); Omnibank of Mantee v. United S. Bank, 607 So. 2d 76, 85 (Miss. 1992); McKnight v. Midwest Eye Inst. of Kansas City, Inc., 799 S.W.2d 909, 913 (Mo. Ct. App. 1990); Para-Med. Leasing, Inc. v. Hangen, 739 P.2d 717, 720-21 (Wash. Ct. App. 1987).

32. Rosenfield v. Metals Selling Corp., 643 A.2d 1253, 1261 n.16 (Conn. 1994).

33. *See* ABA Comm. on Corporate Laws, *Changes in the Model Business Corporation Act Pertaining to the Standards of Conduct for Officer; Inspection Rights and Notices—Final Adoption*, 54 BUS. LAW. 1229, 1231 (1999) ("[T]he business judgment rule will normally apply to decisions within an officer's discretionary authority."); American Law Institute, *Principles of Corporate Governance: Analysis and Recommendations* § 4.01 cmt. a (1994) ("Sound public policy points in the direction of holding officers to the same duty of care and business judgment standards as directors . . . ."); *see also* 3A William M. Fletcher, *Cyclopedia of the Law of Private Corporations* § 1039, at 45 (perm rev. ed. 1986), § 1039, at 4 (Supp. 1992) ("It is too well settled to admit of controversy that ordinarily neither the directors nor the other officers of a corporation are liable for mere mistakes or errors of judgment . . . . This rule is commonly referred to as the 'business judgment rule,' and applies to decisions of executive officers as well as those of directors.") (citations omitted).

corporate officers is not well settled in every jurisdiction,[34] and has come under attack by the FDIC in numerous receivership cases. The FDIC's choice of defendants sometimes appears to be driven by a tactical desire to deprive defendants of business judgment protection. For example, it is not uncommon for the FDIC to sue former bank officers (and officer-directors, but only in their capacity as officers of the bank) for wrongdoing and then argue that the defendants are not entitled to the protection of the business judgment rule.[35] The resolution of this issue has important ramifications for the FDIC's ability to establish liability in typical receivership cases.

None of the traditional justifications for the rule—encouraging corporate service, incentivizing appropriate decision-making, or preventing hindsight-based criticisms—suggests that officers and directors should be treated differently; indeed, stripping officers of their protection under the business judgment statute would be particularly problematic in the banking industry, where officers and directors sometimes sit on the same committees and sometimes are called upon to make the exact same business decisions—when it comes to approving loans, for example, there is little difference between an officers loan committee and a directors loan committee other than the amount of loans at issue.

A. ENCOURAGING CORPORATE SERVICE

A typical justification for applying business judgment protection to directors stems from the fear that qualified individuals will refrain from advising companies due to liability exposure. As one federal court explained:

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34. *See, e.g.*, STEPHEN A. RADIN, THE BUSINESS JUDGMENT RULE 398–99 (6th ed. 2009) ("Numerous courts, construing the law of Delaware and the law of other states, have referred to the business judgment rule as a doctrine protecting directors and officers without distinguishing between the rule's applicability to directors and officers. There is, however, only sparse case law that specifically addresses this question." (citations omitted)).

35. *See* Motion for Partial Summary Judgment of Plaintiff at 5, FDIC v. Smith, Civ. Action No. 2:13-cv-14151 (S.D. Fla. Feb. 12, 2014) ("Plaintiff is entitled to summary judgment on the statutory business judgment rule defense . . . because all defendants are sued in their capacity as officers (or members of management), not as directors.").

> Compelling reasons exist for limiting the circumstances under which directors may be held personally liable. Directors, particularly bank directors, regularly make complex decisions involving risk, and many such decisions may appear in hindsight to have been made improvidently. Competent persons would not serve as directors if such decisions could lead to liability under ordinary tort standards.[36]

The operative question here is whether business judgment protections are needed to encourage competent individuals to assume management roles within a bank. Unlike directors, officers receive salaries and bonuses and derive a substantial portion of their income from their employment. Director compensation tends to be less significant. But the compensation afforded to bank officers does not vitiate this particular rationale for extending business judgment protection to them. After all, a banker's salary pales in comparison to the millions of dollars of potential liability the FDIC has demanded from hundreds of defendant officers in the aftermath of the Great Recession.[37] And while exculpatory clauses enshrined in statutes provide defenses to certain types of claims,[38] including breach of the duty of care and breach of fiduciary duties, these statutes generally apply to directors, but not to officers. For example, Section 102(b)(7) of the Delaware General Corporation Law limits directors' personal liability for monetary damages for breaches of the duty of care.[39] Many other states have

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36. RTC v. Blasdell, 930 F. Supp. 417, 423 (D. Ariz. 1994).

37. *See* Hamermesh & Sparks, *supra* note 30, at 871 ("[T]he scope of potential negligence-based liability for officers is enormous in comparison to any but the most generous incentive compensation packages: even at the median $3 million level, CEO compensation (let alone presumably lesser compensation for more junior officers) is trivially small in relation to corporate harm potentially arising from officer neglect.").

38. Delaware courts recognize that the exculpatory clause serves a salutary purpose, i.e., "to encourage directors to undertake risky, but potentially value-maximizing business strategies, so long as they do so in good faith." Prod. Res. Grp. LLC v. NCT Grp., Inc., 863 A.2d 772, 777 (Del. Ch. 2004).

39. DEL. CODE ANN. tit. 8, § 102(b)(7) (2014) (allowing a corporate charter to include "[a] provision eliminating or limiting the personal liability of a director to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, provided that such provision shall not eliminate or limit the liability of a director: (i) For any breach of the director's duty of loyalty to the corporation or its stockholders; (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law; (iii) under § 174 of this title; or (iv) for any transaction from which the director derived an improper personal benefit. No such provision shall eliminate or limit the liability of a director for any act or omission occurring prior to the date when such provision becomes effective. All references in this paragraph to a director shall also be deemed to refer to such other person or

statutes that grant similar protections to directors,[40] but only a handful have extended the same protections to officers.[41] In most states, officers lack these protections, making officers more financially vulnerable than directors, and making business judgment rule protections even more essential.

Officers usually devote far more time to the institution than directors. Unlike a director whose interaction with the bank is likely to be episodic at best, a corporate officer presumably will devote his or her complete attention to the bank's business on a daily basis. But an officer's full-time position does not mean that his or her judgments should receive less protection. After all, a full-time position does not guarantee that a corporate officer, any more than a director, will be able to control the outcome of the underlying business decisions. If the aftermath of the Great Recession has taught us anything, it is that business strategies can go awry for many reasons and that no individual person, whether officer or director, has the ability to guarantee a good outcome no matter how much time they devote to the task.

B. INCENTIVIZING APPROPRIATE DECISION-MAKING

Another rationale underlying the business judgment rule is to incentivize appropriate decision-making. An officer whose judgments may be second-guessed is more likely to make decisions that minimize risk. The issue, in other words, "is not whether people will serve as corporate officers; the issue is whether, once serving, officers will be unduly cautious in their business conduct if faced with liability for lack of ordinary care."[42] To borrow a basketball analogy, without the protections afforded by the business judgment rule, bank officers might

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persons, if any, who, pursuant to a provision of the certificate of incorporation in accordance with § 141(a) of this title, exercise or perform any of the powers or duties otherwise conferred or imposed upon the board of directors by this title.").

40. *See, e.g.*, N.Y. BUS. CORP. LAW § 402(b)(1) (McKinney 2014); MD. CODE ANN., CTS. & JUD. PROC. § 5-418(a)(1)–(2) (West 2014).

41. *See, e.g.*, MD. CODE ANN., CTS. & JUD. PROC. § 5-418(a); LA. REV. STAT. ANN. § 12:24(C)(4) (2014); NEV. REV. STAT. § 78.037(2) (2014); N.J. STAT. ANN. § 14A:2-7(3) (2014); VA. CODE ANN. § 13.1-692.1(A)(1) (2014). Notably, Nevada provides exculpation for both directors and officers "unless it is proven that . . . [his] breach of those duties involved intentional misconduct, fraud or a knowing violation of law." NEV. REV. STAT. § 78.138(7) (2014).

42. Hamermesh & Sparks, *supra* note 30, at 873.

go into the equivalent of a "four corners" offense, simply passing the ball near half-court without making any serious attempt to score. Just like playing a "prevent" defense in football when you are ahead seems to do nothing but prevent your team from winning, adopting an overly conservative business approach can harm a bank's capital cushion and, in extreme cases, doom it to failure. In short, being too conservative can be as damaging as being too aggressive. A bank can miss out on strategic opportunities and ultimately find itself in a weaker, more vulnerable position than had it taken calculated business risks. In addition to directors, officers too should be encouraged to aim for that regulatory sweet spot of reasoned decision-making that supports reasonable risks. The business judgment rule encourages reasonable risk-taking by ensuring that officers, like directors, are not guarantors of the business outcome that flows from their strategy.

C. Discouraging Second-Guessing

Courts also recognize that business judgment protection functions as an insurance policy against hindsight-based second-guessing of board decisions. This rationale applies with equal force to decisions made by bank officers. Bank officers make decisions every day that reflect reasoned risk/benefit calculations but where the ultimate outcome is beyond their control. For example, bank officers must weigh numerous factors in deciding whether and under what circumstances the bank should lend its money. Does a self-employed borrower have a sufficiently stable source of income? What is the appropriate interest rate to charge or term to offer? Is the value of the collateral sufficient to offset the risk of the loan to the bank? Should the bank make more of certain types of loans, such as residential real estate loans, or should its focus be elsewhere, such as commercial and industrial loans? These and a host of other issues routinely present themselves in a typical officer-level loan committee. And in those institutions that have a director-level loan committee, the same issues arise albeit with greater financial consequences (reflecting the fact that most director-level loan committees do not review and approve individual loans unless they exceed a certain monetary threshold). There is no principled basis for protecting directors from second-guessing but leaving bank officers exposed to hindsight-based criticisms.[43]

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43. As Hamermesh and Sparks have noted, "at least where an officer is simply attempting to implement board policy and exercise delegated corporate authority,

IV. CASE STUDIES ILLUSTRATING THE RANGE OF BUSINESS JUDGMENT PROTECTIONS AFFORDED TO BANK OFFICERS

Over the past few years, federal courts in Georgia, California, and Florida have addressed questions regarding the applicability of the business judgment rule to bank officers. Although they do not all reach the same outcome, these three states illustrate the way that courts have evaluated the common law in their state, reconciled statutory enactments, and drawn conclusions in this area.

A. THE BUSINESS JUDGMENT RULE IN GEORGIA

Georgia courts have a long history of affording both corporate officers and directors the protection of the business judgment rule. Until recently, though, there was some uncertainty about whether bank officers were entitled to this protection.

In *Brock Built, LLC v. Blake*, the Court of Appeals of Georgia held that "[i]n determining whether a corporate officer has fulfilled his or her statutory duty, Georgia courts apply the business judgment rule."[44] The court observed that "[t]he business judgment rule affords an officer the presumption that he or she acted in good faith, and absolves the officer of personal liability unless it is established that he or she engaged in fraud, bad faith or an abuse of discretion."[45] The court also concluded that Georgia's business judgment rule foreclosed liability against both officers and directors for ordinary negligence.[46] As the *Brock* court explained, Georgia courts will not interfere with the decisions of directors or officers absent "fraud, bad faith, or an abuse of discretion."[47]

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imposing a more demanding standard of liability upon officers than upon directors seems unfair in that it would shift to officers the burden of legal liability for risk-taking activity that the directors themselves encouraged." Hamermesh & Sparks, *supra* note 30, at 872.

44. 300 Ga. App. 816, 821 (Ga. Ct. App. 2009).

45. *Id.* at 821–22.

46. *See also* Regenstein v. J. Regenstein Co., 213 Ga. 157, 162 (Ga. 1957) (stating that "unless sufficient facts are alleged which show that such a course is pursued for reasons which are fraudulent, ultra vires, or illegal, a court of equity will not interfere to control the management of a corporation."); Flexible Prods. Co. v. Ervast, 284 Ga. App. 178, 182 (Ga. Ct. App. 2007) (stating that Georgia's business judgment rule "forecloses liability in officers and directors for ordinary negligence.").

47. *Brock*, 300 Ga. App. at 822 (internal quotation marks omitted).

Notwithstanding this solid body of law, the FDIC argued—with limited initial success—that bank officers in Georgia were not entitled to the protections of the business judgment rule.[48] Two federal courts certified this question to the Supreme Court of Georgia,[49] with one observing that "no Georgia state court has explicitly extended the business judgment rule to protect . . . [bank] officers and directors" on its way to rejecting the reasoning of federal court rulings that had applied the rule in the banking context.[50] The court observed:

> There is every reason to treat bank officers and directors differently from general corporate officers and directors. In general, when a business corporation succeeds or fails, its stockbrokers bear the gains and losses. . . . But when a bank, instead of a business corporation fails, the FDIC and ultimately the taxpayer bear the pecuniary loss. The lack of care of the officers and directors of banks can lead to bank closures which echo throughout the local and national economy.[51]

Because the case "is not simply a private case between individuals but rather a case that involves a federal agency appointed as receiver of a failed bank in the midst of a national banking crisis," the court was "not convinced that Georgia law affords the Defendants the protection of the business judgment rule in a lawsuit by the FDIC."[52] In reaching this conclusion, the court found that decisions affording bank officers and directors the business judgment rule defense were in tension with Official Code of Georgia Annotated Section 7-1-490, which imposes on bank officers and directors the duty of care that "ordinarily prudent men would exercise under similar circumstances in like positions."[53] Because the court was "not convinced that Georgia law affords the Defendants

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48. *Compare* FDIC v. Miller, No. 2:12-cv- 00042 (N.D. Ga. Dec. 26, 2012); FDIC v. Whitley, No. 2:12-cv-170 (N.D. Ga. Dec. 10, 2012); FDIC v. Briscoe, No. 1:11-CV-02303-SCJ, 2012 WL 8302215 (N.D. Ga. Aug. 14, 2012); FDIC v. Blackwell, No. 1:11-CV-03423-RWS, 2012 WL 3230490 (N.D. Ga. Aug. 3, 2012) (applying business judgment rule to bank officers); *with* FDIC v. Adams, No. 1:12-cv-00726-JOF (N.D. Ga. Mar. 21, 2013) (refusing to apply business judgment rule to bank officers); FDIC v. Loudermilk, 984 F. Supp. 2d 1354 (N.D. Ga. 2013).

49. *See Loudermilk*, 984 F. Supp. 2d at 1354; FDIC v. Skow, 741 F.3d 1342 (11th Cir. 2013).

50. *Loudermilk*, 984 F. Supp. 2d at 1358.

51. *Id.* at 1359 (citation omitted).

52. *Id.* (internal quotation marks omitted).

53. *Id.* (internal quotation marks omitted).

the protection of the business judgment rule in a lawsuit by the FDIC,"[54] it certified the following "unsettled question of law" to the Georgia Supreme Court: "Does the business judgment rule in Georgia preclude as a matter of law a claim for ordinary negligence against the officers and directors of a bank in a lawsuit brought by the FDIC as receiver for the bank?"[55]

In *FDIC v. Skow*, the district court granted defendants' motion to dismiss the ordinary negligence claims, holding that under Georgia law the negligence claims that the FDIC brought against former bank officers and directors failed to state a claim as a matter of law.[56] On appeal, however, the Eleventh Circuit was concerned that applying the business judgment rule to bank officers and directors "might contradict the plain language" of the Georgia statute holding bank directors and officers to an ordinary negligence standard of care.[57] "In the light of the plausible conflict between the plain language of O.C.G.A. § 7-1-490 and the state intermediate appellate courts' discussions of Georgia's business judgment rule,"[58] the court certified the following two questions to the Supreme Court of Georgia:

> (1) Does a bank director or officer violate the standard of care established by O.C.G.A. § 7-1-490 when he acts in good faith but fails to act with "ordinary diligence," as that term is defined in O.C.G.A. § 51-1-2?
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> (2) In a case like this one, applying Georgia's business judgment rule, can the bank officer or director defendants be held individually liable if they, in fact as alleged, are shown to have been ordinarily negligent or to have breached a fiduciary duty, based on ordinary negligence in performing professional duties?[59]

In the recent *Loudermilk* and *Skow* decisions, the Georgia Supreme Court definitively answered the questions raised by these two federal courts. In the *Loudermilk* decision, the Georgia Supreme Court held that corporate officers, including bank officers, are entitled to business judgment protection. The Court began its analysis by examining whether

54. *Id.*
55. FDIC v. Loudermilk, 761 S.E.2d 332, 334 (Ga. 2014).
56. 955 F. Supp. 2d 1357 (N.D. Ga. 2012).
57. FDIC v. Skow, 741 F.3d 1342, 1346 (11th Cir. 2013).
58. *Id.* at 1346.
59. *Id.* at 1347.

Georgia common law recognizes the business judgment rule. After examining three common law cases that the Court deemed "especially instructive," the Georgia Supreme Court held:

> From our precedents, we conclude that the business judgment rule is a settled part of our common law in Georgia, and it generally precludes claims against officers and directors for their business decisions that sound in ordinary negligence, except to the extent that those decisions are shown to have been made without deliberation, without the requisite diligence to ascertain and assess the facts and circumstances upon which the decisions are based, or in bad faith. Put another way, the business judgment rule at common law forecloses claims against officers and directors that sound in ordinary negligence when the alleged negligence concerns only the wisdom of their judgment, but it does not absolutely foreclose such claims to the extent that a business decision did not involve "judgment" because it was made in a way that did not comport with the duty to exercise good faith and ordinary care. We note as well that the business judgment rule applies equally at common law to corporate officers and directors generally and to bank officers and directors.[60]

The Court then analyzed whether the legislature had abrogated the common law business judgment protection when it enacted Official Code of Georgia Annotated Section 7-1-490(a), which provides that "[d]irectors and officers of a bank . . . shall discharge the duties of their respective positions in good faith and with that diligence, care, and skill which ordinarily prudent men would exercise under similar circumstances in like positions,"[61] and goes on to enumerate sources of information that officers and directors are entitled to rely upon in good faith. The Court disagreed with the position advanced by the FDIC that this statute supersedes the common law business judgment rule. The Court reconciled the rule with the statute by pointing out that the statute is "largely addressed to the process by which an officer or director is to become informed about the matters as to which he is to exercise judgment."[62] As the Court later explained, the "statutory reference to ordinary 'diligence, care, and skill' is most reasonably understood to refer to the care required with respect to the process by which a decision is made, most notably the diligence due to ascertain the relevant facts."[63]

60. *Loudermilk*, 761 S.E.2d at 338.
61. *Id.* at 339 (internal quotation marks omitted).
62. *Id.* at 340.
63. *Id.* at 341–42.

In the companion *Skow* case, the Georgia Supreme Court reaffirmed its emphasis on the underlying process that bank officers utilize to make their decisions. The Court held that good faith, by itself, was not sufficient to preclude liability if the officer, "with respect to the process by which he makes decisions, fails to exercise the diligence, care, and skill of ordinarily prudent men [acting] under similar circumstances in like positions."[64]

The Georgia Supreme Court's efforts to reconcile common law business judgment protections with a statutory ordinary negligence provision echoes the positions taken by other states that have addressed this issue. Like Georgia, a host of other states provide the identical standard of care for officers and directors, and yet apply the business judgment rule to bar ordinary negligence claims. For example, Maine requires bank and non-bank directors and officers to discharge their duties with ordinary care,[65] but insulates them from liability unless they were grossly negligent.[66] New Jersey also imposes an ordinary negligence standard on bank and non-bank directors,[67] but shields them from liability absent gross negligence.[68] Alabama also requires bank and non-bank directors to conform with the ordinary negligence standard of care,[69] but shields them from liability so long as they acted "in good faith and without gross negligence supporting an imputation of fraud."[70]

B. THE BUSINESS JUDGMENT RULE IN CALIFORNIA

California courts have reached a different, and only slightly less definitive answer, when it comes to the scope of the business judgment rule in that state. In *Berg & Berg Enters., LLC v. Boyle*, the court explained that California's business judgment rule "has two components – immunization from liability that is codified at Corporations Code Section 309 and a judicial policy of deference to the exercise of good faith business judgment in management decisions."[71] Notwithstanding

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64. FDIC v. Skow, 763 S.E.2d 879, 881 (Ga. 2014).
65. ME. REV. STAT. tit. 13-C, §§ 831(2), 843(1)(B) (2014).
66. *See id.* § 832(1)(B) (directors), § 843(3) (officers).
67. N.J. STAT. ANN. § 14A:6-14(1) (West 2014).
68. *See, e.g.*, Fink v. Codey (*In re* PSE & G S'holder Litig.), 801 A.2d 295, 306 (N.J. 2002).
69. ALA. CODE § 10A-2-8.30(a)(2) (2011).
70. Deal v. Johnson, 362 So. 2d 214, 218 (Ala. 1978).
71. 178 Cal. App. 4th 1020, 1048 (Cal. Ct. App. 2009).

this dual-faceted scheme, courts have found that neither the statute nor the common law protects an officer's business judgments in California.

Section 309 of California General Corporation Law, titled "Performance of [D]uties *by [D]irector*; liability," provides in relevant part as follows:

> (a) A director shall perform the duties of a director, including duties as a member of any committee of the board upon which the director may serve, in good faith, in a manner such director believes to be in the best interests of the corporation and its shareholders and with such care, including reasonable inquiry, as an ordinarily prudent person in a like position would use under similar circumstances. . . .
>
> (c) A person who performs the duties of a director in accordance with subdivisions (a) and (b) shall have no liability based upon any alleged failure to discharge the person's obligations as a director. . . .[72]

While some California courts, such as the court in *Berg & Berg*, have characterized the statute as codifying the "immunization from liability" component of the business judgment rule, the California Law Revision Commission in 1996 observed that "Section 309 does not codify the business judgment rule; it codifies the duty of care of directors, upon which the business judgment rule acts as a limitation."[73] This protection is limited, by its terms, only to directors. No court in California has found that this statutory protection extends to officers.

The common law provides no recourse for officers in California. Although courts agree that the "judicial policy of deference to the exercise of good-faith business judgment in management decisions" remains a protection afforded not by statute, but by California's common law business judgment rule,[74] a number of federal district courts in California over the past three years have held that neither Section 309 nor the common law rule extends the business judgment defense to corporate officers.[75] In *FDIC v. Perry*,[76] for example, the

72. CAL. CORP. CODE § 309 (1975) (emphasis added).

73. *See* CALIFORNIA LAW REVISION COMMISSION, MEMORANDUM 96-12, at 4 (Jan. 30, 1996), *available at* www.clrc.ca.gov/pub/1996/M96-12.pdf.

74. FDIC v. Van Dellen, No. CV 10-4915 DSF, 2012 WL 4815159 (C.D. Cal. Oct. 5, 2012); *Berg & Berg*, 178 Cal. App. 4th at 1048; Lee v. Interinsurance Exch., 50 Cal. App. 4th 694, 714 (Cal. Ct. App. 1996).

75. *See* FDIC v. Hawker, No. CV F 12-0127, 2012 WL 2068773 (E.D. Cal. June 7, 2012); *Van Dellen*, 2012 WL 4815159; FDIC v. Faigin, No. CV 12-03448 DDP, 2013

court determined that the plain language of Section 309 of the statute, which is framed solely in terms of directors and its legislative history,[77] supports the conclusion that the protections of the statute do not extend to corporate officers. The court also held that it was unable to find any California judicial decisions applying the common law business judgment rule to corporate officers, and therefore refused to do so in that case.[78] These decisions have focused (1) on the language and legislative history of Section 309, and (2) on the ruling of the California Court of Appeals in *Gaillard v. Natomas Co.*,[79] which held that the business judgment rule did not apply to directors' approval of golden parachute agreements because the directors were not performing the duties of directors but acting as officers.[80]

Although the argument for extending business judgment protection to corporate officers is not technically foreclosed (given that the

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WL 3389490, at *11 (C.D. Cal. July 8, 2013); Nat'l Credit Union Admin. v. Siravo, No. CV 10-1597-GW, 2011 WL 8332969 (C.D. Cal. July 7, 2011).

76. No. CV 11-5561-DDW, 2012 WL 589569 (C.D. Cal. Feb. 21, 2012).

77. The legislative committee that drafted Section 309 stated, as relevant: "[I]t is the intent of the draftsmen of this provision, by combining the requirement of good faith within the standard of care, to incorporate the familiar concept that, these criteria being satisfied, a director should not be liable for an honest mistake of business judgment." *See* Cal. Corp. Code § 309 (Legislative Committee Comment) (1975) (noting that "[t]he standard of care does not include officers," reasoning that, "[a]lthough a non-director officer may have a duty of care similar to that of a director . . . his ability to rely on factual information, reports or statements may, depending upon the circumstances of the particular case, be more limited than in the case of a director in view of the greater obligation he may have to be familiar with the affairs of the corporation.").

78. *Perry*, 2012 WL 589569, at *3 ("Defendant's proposition, however, seems unprecedented as the Court's research reveals no judicial decision in California applying common law BJR to corporate officers.").

79. 208 Cal. App. 3d 1250 (Cal. Ct. App. 1989).

80. The California Law Revision Commission initially criticized that decision in a preliminary report recommending that the business judgment rule be codified to include officers, arguing that the court reached the right outcome for the wrong reason—namely, that the *Gaillard* officers did not deserve protection because they were interested in the transaction. *See* CALIFORNIA LAW REVISION COMMISSION, *supra* note 73, at 4. But the Commission softened its stance in its final report, recommending that the proposed "codification of the business judgment rule should be limited to directors, and that its possible application to officers be made the subject of a separate study. Codification of the business judgment rule for directors should not affect the common law and existing statutory protection of officers and employees." CALIFORNIA LAW REVISION COMMISSION, RECOMMENDATION, at 17-18 (1998).

California Supreme Court has not addressed this issue), the decisions to date paint a bleak picture about its prospects. There are a handful of cases that can be read to support the argument,[81] but a three-year unbroken string of federal court decisions interpreting state law to the contrary presents a formidable obstacle.

C. THE BUSINESS JUDGMENT RULE IN FLORIDA.

Unlike Georgia and California, where the scope of business judgment protections are clearly demarcated, the availability of a business judgment defense to corporate officers in Florida is unsettled. In recent cases brought against bank officers, the FDIC has taken the position that Florida's limitation-of-liability statute does not apply to officers and abrogates the common law business judgment protections that existed prior to its enactment. The FDIC's arguments have met with mixed success.

1. The Florida Limitation-of-Liability Statute

The Florida limitation-of-liability statute, which took effect in 1987, speaks only in terms of directors. It provides that a director must discharge his or her duties "(a) [i]n good faith; (b) [w]ith the care an ordinary prudent person in a like position would exercise under similar circumstances; and (c) [i]n a manner he or she reasonably believes to be in the best interests of the corporation."[82] The statute then narrows the actions that can impose liability on directors of Florida banks, limiting liability to situations where there has been a criminal violation, an improper personal benefit, or conduct that was "in bad faith or with malicious purpose or in a manner exhibiting wanton and willful disregard of human rights, safety, or property."[83]

By virtue of this statute, "imposition of liability on a director requires not only a violation of the duty of ordinary care set forth in Fla.

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81. *See, e.g.*, Frances T. v. Vil. Green Owners Ass'n, 42 Cal. 3d 490, 497 n.14 (Cal. 1986) (en banc) (suggesting application of the rule to corporate officers); Biren v. Equality Emergency Med. Grp., 102 Cal. App. 4th 125, 131 (Cal. Ct. App. 2002) (concluding officer director was protected by the business judgment rule); PMC, Inc. v. Kadisha, 78 Cal. App. 4th 1368, 1386–87 (Cal. Ct. App. 2000) ("Generally, an officer or director who commits a tort because he or she reasonably relied on expert advice or other information cannot be held personally liable for the resulting harm.").

82. FLA. STAT. § 607.0830(1) (2014).

83. FLA. STAT. § 607.0831.

Stat. § 607.0830, but a violation that falls into one of the five categories set forth in Fla. Stat. § 607.0831(1)(b)."[84] When the FDIC brings suit, its claims generally fall within § 607.0831(1)(b)(4), which applies when the allegations allege "conscious disregard for the best interest of the corporation, or willful misconduct."[85] Claims against directors for ordinary negligence are not cognizable under the statute,[86] which accords with the general rule that directors cannot be sued for garden variety negligence claims.

Initially, some federal courts did not draw a distinction between directors and officers when applying the limitation-of-liability statute. In 1988, less than one year after the statute went into effect, a court in the Southern District of Florida observed that "the Florida legislature has recently passed [an] Act . . . which created greater protections from liability for official acts in their capacity of corporate *officers and directors*."[87] Five years later, in *Gonzalez-Gorrondona*, another court in that district was presented with a case in which the FDIC brought a claim for ordinary negligence based on director and officer conduct that occurred between March 1983 and December 1988—a range that spanned July 1, 1987, the date on which the Florida limitation-of-liability statute took effect.[88] As to conduct post-dating the effective date of the statute, the court held that "the Florida statute insulates corporate *directors and officers* from conduct amounting to gross negligence, and permits liability only for greater derelictions of the duty of care."[89] Evaluating the conduct by the defendant directors and officers, the Court

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84. FDIC v. Price, No. 2:12-cv-148-FTM-99DNF, 2012 WL 3242316, at *6 (M.D. Fla. Aug. 8, 2012).

85. FLA. STAT. § 607.0831(1)(b)(4). Florida law defines "[g]ross negligence" as conduct "so reckless or wanting in care that it constituted a conscious disregard or indifference to the life, safety, or rights of persons exposed to such conduct." Fla. Stat. § 768.72(2)(b). Florida courts have found willful misconduct to be the same standard as gross negligence. *See, e.g.*, FDIC v. Aultman, No. 2:13-cv-58-FTM-384AM, 2013 WL 3357854, at *3 (M.D. Fla. July 3, 2013); FDIC v. Florescue, No. 8:12-cv-2547-T-30TBM, 2013 WL 2477246, at *6 (M.D. Fla. June 10, 2013); Wood v. Musa, 168 So. 2d 701, 702 (Fla. Dist. Ct. App. 1964) ("Gross negligence and willful or wanton misconduct mean the same thing." (internal quotation marks omitted)).

86. *See Florescue*, 2013 WL 2477246, at *3; FDIC v. Gonzalez-Gorrondona, 833 F. Supp. 1554, 1556 (S.D. Fla. 1993).

87. Int'l Ins. Co. v. Johns, 685 F. Supp. 1230, 1238 n.4 (S.D. Fla. 1988) (emphasis added), *aff'd*, 874 F.2d 1447 (11th Cir. 1989).

88. *Gonzalez-Gorrondona*, 833 F. Supp. at 1556.

89. *Id.* (emphasis added).

ruled that the "challenged corporate decisions . . . made prior to July 1, 1987 will be subject to an ordinary standard of care" but "any misconduct alleged to have taken place after July 1, 1987 must be scrutinized according to the 'gross negligence' standard of § 1821(k) of FIRREA."[90] In other words, the Court dismissed the ordinary negligence claims with respect to all conduct that occurred after the effective date of the statute. Because the defendants in *Gonzalez-Gorrondona* were directors *and* officers,[91] the import of that decision was that the statutory protection of Section 607.0831 extended to officers as well.

This interpretation of Section 607.0831 was subsequently endorsed by the Eleventh Circuit, which recognized in 1996 that "[t]he Florida legislature passed [Section 607.0831] to afford corporate *officers and directors* greater protection from liability."[92] In *Stahl*, the FDIC brought negligence claims against former officers and directors of a savings and loan association, alleging that the defendants had negligently approved deficient loans, and the defendants claimed the protection of the business judgment rule. Because the conduct at issue in *Stahl* occurred prior to the effective date of Section 607.0831, the Eleventh Circuit held that the standard of care under Florida law was ordinary negligence.[93] But as a corollary to this holding, the court specifically identified that Section 607.0831 created "greater protection from liability" for "causes of action accruing on or after July 1, 1987," and that this protection was afforded to "corporate officers and directors."[94] Thus, for the first quarter-century that Florida's limitation-of-liability statute was in effect,

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90. *Id.* at 1559; *see also id.* at 1556 ("In sum, prior to July 1, 1987, the law of Florida imposed liability on corporate directors and officers for simple negligence, and after that date, Florida imposed liability only for acts constituting more than gross negligence.").

91. *Gonzalez-Gorrondona*, 833 F. Supp. at 1548.

92. FDIC v. Stahl, 89 F.3d 1510, 1516 n.12 (11th Cir. 1996) (emphasis added); *see also id.* at 1517–18 (citing with approval the analysis in *Gonzalez-Gorrondona*).

93. *Id.* at 1516.

94. *Id.* at 1516 n.12; *see also* Official Comm. of Unsecured Creditors of Toy King Distribs., Inc. v. Liberty Sav. Bank (*In re* Toy King Distribs., Inc.), 256 B.R. 1, 168 (Bankr. M.D. Fla. 2000) ("[T]o overcome the presumption of the business judgment rule under [Section 607.0831], the plaintiff must establish . . . that the *officer or director* has been more than grossly negligent." (emphasis added)); FDIC v. Mintz, 816 F. Supp. 1541, 1545–46 (S.D. Fla. 1993) ("Florida has passed an 'insulating' statute which was intended to afford greater protection against suit for directors and officers."); Brandt v. Bassett (*In re* Se. Banking Corp.), 827 F. Supp. 742, 755 n.6 (S.D. Fla. 1993) ("Florida also arguably applies the Business Judgment Rule to officers."), *rev'd on other grounds*, 69 F.3d 1539 (11th Cir. 1995).

courts, as clear holding or dictum, interpreted its protections as extending to both officers and directors.

More recently, though, several Florida federal courts have concluded that the limitation-of-liability statute is more circumscribed, protecting directors but not officers from FDIC claims of ordinary negligence and breach of fiduciary duty. In *FDIC v. Brudnicki*, the court denied a motion to dismiss filed by a director-officer.[95] The court concluded that "legislators intentionally differentiated between directors, officers, employees, and agents . . . . Officers, employees, and agents may be liable for something less than conscious disregard for the best interests of the corporation or willful misconduct."[96] In *FDIC v. Florescue*, another court followed the reasoning in *Brudnicki*, but observed that "[w]hether § 607.0831 extends to an officer-director is an unsettled issue under Florida law."[97] Both decisions acknowledge that *Gonzalez-Gorrondona* established a contrary view.[98] To date, this issue remains unresolved, although the more recent cases refusing to apply the limitation-of-liability statute suggest that courts look more skeptically at this argument now than they did before.[99]

2. Florida's Common Law Business Judgment Rule

But even if the limitation-of-liability statute provides no refuge, bank officers in Florida may still avail themselves of common law business judgment protections to defend themselves against FDIC liability claims. A number of Florida decisions that both pre-date and post-date the enactment of Florida's limitation of liability statute recognize a common law business judgment protection for officers.[100] In

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95. No. 5:12-cv-398-RS-GRJ, 2013 WL 2145720, at *2 (N.D. Fla. May 15, 2013).

96. *Id.*

97. FDIC v. Florescue, No. 8:12-cv-2547-T-30TBM, 2013 WL 2477246, at *4 (M.D. Fla. June 10, 2013).

98. *See id.* (citing *Gonzalez-Gorrondona* as dictum); *Brudnicki*, 2013 WL 2145720, at *2 ("Interpreting the statute during its infancy, one federal district court found 'that the Florida statute insulates corporate directors and officers . . . .'" (ellipsis in original) (citation omitted) (quoting FDIC v. Gonzalez-Gorrondona, 833 F. Supp. 1554, 1556 (S.D. Fla. 1993)).

99. *See* Order Denying Motion for Partial Dismissal at 4-5, FDIC v. Dodson, et al., No. 4:13-cv-416-MW-CAS (N.D. Fla. Feb. 27, 2014) (holding that "officers are not shielded from personal liability" by Section 607.0831).

100. *See, e.g.*, Schein v. Caesar's World, Inc., 491 F.2d 17, 18–20 (5th Cir. 1974) (per curiam) (affirming grant of summary judgment to defendant "officers and

a recent FDIC case litigated and eventually settled in the Southern District of Florida, the officer defendants moved to dismiss the FDIC's claims for negligence and breach of fiduciary duty on the ground that their judgments were protected by either the limitation-of-liability statute or the common law business judgment rule. Without expressly addressing their statutory argument, the court found "application of the business judgment rule [to be] a question of fact and therefore inappropriate for consideration on a motion to dismiss."[101] The court did not accept the argument advanced by the FDIC that there was no common law business judgment rule.

Under the common law rule Florida courts will presume that officers and directors acted in good faith, in the absence of a showing of "abuse of discretion, fraud, bad faith, or illegality."[102] In *AmeriFirst Bank v. Bomar*, the court made this point emphatically:

> Under the business judgment rule, officers and directors of a corporation are presumed to have acted properly and in good faith. Although required to discharge their duties with the diligence and skill of an ordinary prudent person in a like position under similar circumstances, officers and directors "incur no liability to the corporation for issues of business expediency which they resolve through the mere exercise of their business judgment." Thus, unless there is a showing of an abuse of discretion, fraud, bad faith or illegality, a court will not substitute its own judgment for that of corporate management.[103]

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directors" because the undisputed facts established that defendants' actions were "indisputably a sound exercise of their business judgment"); Pujals *ex rel.* El Rey de los Habanos, Inc. v. Garcia, 777 F. Supp. 2d 1322, 1327, 1331 (S.D. Fla. 2011) (refusing to strike business judgment rule defense for defendant "officers and directors," and stating that "[t]he business judgment rule is a judicial presumption that corporate officers and directors acted in good faith"); AmeriFirst Bank v. Bomar, 757 F. Supp. 1365, 1376 (S.D. Fla. 1991) ("Under the business judgment rule, officers and directors of a corporation are presumed to have acted properly and in good faith."); Univ. Clinical Assocs., Inc. v. Intracoastal Health Sys., Inc., No. CL 99-7605 AG, 2000 WL 1466097, at *6 (Fla. Cir. Ct. Sept. 25, 2000) (describing the business judgment rule as a defense available to officers and directors).

101. Order Denying Defendants' Motion to Dismiss at 8, FDIC v. Smith, et al., 2:13-cv-14151-DLG, (S.D. Fla. Nov. 13, 2013).

102. Kloha v. Duda, 246 F. Supp. 2d 1237, 1244 (M.D. Fla. 2003).

103. 757 F. Supp. at 1376 (citations omitted); *see also* Sheridan Healthcorp, Inc. v. O'Rourke, No. 00-020282 (09), 2007 WL 7035809 (Fla. Cir. Ct. July 12, 2007) ("[O]fficers and directors of a valid corporation are afforded protection under the Business Judgment Rule, no matter how poor their business judgment, unless it is

There is no textual support for the assertion that the limitation-of-liability statute displaced the common law business judgment rule. Section 11 of the Florida limitation-of-liability statute also states that "[n]othing in this act shall be construed as increasing or decreasing the liability of any person not herein specifically delineated."[104] To the extent that officers are deemed not to be encompassed by the statutory protection, then nothing in the statute affects their common law protections. As one Florida court observed in a different context, "The presumption is that no change in the common law is intended unless the statute is explicit and clear in that regard."[105]

Not surprisingly, Florida courts generally have rejected arguments that the limitation-of-liability statute abrogated the common law business judgment rule.[106] For example, in *Brandt v. Bassett (In re Southeast Banking Corp.)*, the court ruled that "[t]here is nothing in the statute that expressly indicates that it has affected the Business Judgment Rule. The legislative history . . . does not indicate that the legislature intended to affect the Business Judgment Rule. . . . [T]here is no case law to support the contention that the business judgment rule has been subsumed by the Florida statute."[107] Likewise, in *Banco Latino International v. Gomez Lopez*, the court observed that "[t]hrough *both statute and case law*, Florida has developed rather strict standards for imposing personal liability upon corporate *officers and directors* for actions taken in their official capacities."[108] In support of this point, the Court cited both Section 607.0831 and *In re Southeast Banking Corp.*, which the Court described as "discussing the case law developing

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alleged and there is proof they acted fraudulently, illegally, oppressively and in bad faith.").

104. 1987 Fla. Sess. Law Serv. 87-245, § 11 (West).

105. Thornber v. City of Fort Walton Beach, 568 So. 2d 914, 918 (Fla.1990).

106. *See Kloha*, 246 F. Supp. 2d at 1244 n.20 (recognizing that the rule survives the statute, but observing that the case law "remains unclear as regards the complete relationship between the business judgment rule and Florida Statute § 607.0830"). Several other courts have applied Florida's common law business judgment rule even after the enactment of the 1987 statute. *See In re* Bal Harbour Club, Inc., 316 F.3d 1192, 1194-95 (11th Cir. 2003); Pujals *ex rel.* El Rey De Los Habanos, Inc. v. Garcia, 777 F. Supp. 2d 1322, 1327, 1331 (S.D. Fla. 2011); *Bomar*, 757 F. Supp. at 1376.

107. 827 F. Supp. 742, 755 (S.D. Fla. 1993), *rev'd on other grounds*, 69 F.3d 1539 (11th Cir. 1995).

108. 95 F. Supp. 2d 1327, 1335 (S.D. Fla. 2000) (emphases added).

Florida's standard for imposing officer and director liability and the business judgment rule affirmative defense."[109]

Common law rules remain in force unless they are *inconsistent* with acts of the Florida legislature.[110] There is obviously nothing "inconsistent" about providing business judgment protections through both the statute and the common law; indeed, if the FDIC is correct that Section 607.0831 covers only directors, then a separate and continuing common law protection for officers is not merely consistent but essential to the overall slate of business judgment protections under Florida law. Accordingly, the Southern District of Florida's conclusion in *In re Southeast Banking Corp.* remains true: nothing in the statute, its legislative history or the relevant case law indicates that the statute has affected the business judgment rule.[111] Although sound arguments can be made that bank officers are entitled to assert the business judgment defense, whether under the limitation-of-liability statute or the common law, it remains to be seen how courts will interpret and apply these protections.

V. PRACTICAL CONSIDERATIONS WHEN ASSERTING THE BUSINESS JUDGMENT DEFENSE

Although the business judgment rule can be a formidable defense, its deterrent effect is lessened if defendants cannot use it to knock out claims for simple negligence or breach of fiduciary duty prior to trial. In addition to arguing that business judgment protection is not available as a matter of law, the FDIC typically also contends that it is inappropriate for the court to consider it at the motion to dismiss stage. Several courts have endorsed this argument, holding that the business judgment rule is too fact-intensive to be disposed of on a motion to dismiss. For example, in *FDIC v. Baldini*, a district court recently observed that "there is overwhelming authority to support the FDIC's position that the business judgment rule is highly fact dependent and, therefore, inappropriate for consideration on a motion to dismiss."[112] But the court principally relied on the Third Circuit's decision in *Stanziale v. Nachtomi (In re Tower*

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109. *Id.*
110. Maronda Homes, Inc. v. Lakeview Reserve Homeowners Ass'n,127 So. 3d 1258, 1268 (Fla. 2013).
111. 827 F. Supp. at 755.
112. 983 F. Supp. 2d 772, 783 (S.D. W. Va. 2013).

Air, Inc.),[113] to support its conclusion that the business judgment rule is a fact-based defense.

Tower Air and other similar court decisions predate the Supreme Court's rulings in *Bell Atlantic Corp. v. Twombly*[114] and *Ashcroft v. Iqbal*,[115] which "retired" the venerable "no set of facts" pleading standard of *Conley v. Gibson*.[116] The Supreme Court established a new standard: plaintiffs could no longer ignore the substantive law that governed their claim; to survive a motion to dismiss the plaintiff must plead facts that plausibly suggest they are entitled to relief. The Court stated that,

> To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.' A claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged.[117]

The Court rejected the argument that groundless claims could be "weeded out" early in discovery,[118] and found that summary judgment was not a viable alternative to the new pleading standards. *Iqbal* confirmed the wide applicability of the *Twombly* pleading standard, and clarified that (1) a court must only accept well-pled factual allegations; and (2) must determine whether the claim for relief is plausible in light of the court's experience and common sense. *Iqbal* is particularly instructive to advancing the business judgment rule at the motion to dismiss stage because it concerned qualified immunity; the Court made it clear that qualified immunity's status as a "defense" did not alter the Court's reasoning.

Faced with the twin Supreme Court rulings in *Twombly* and *Iqbal*, some courts have recognized that decisions such as the Third Circuit's ruling in *Tower Air* are now no longer good law and that the outcome of

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113. 416 F.3d 229, 238 (3d Cir. 2005).
114. 550 U.S. 544 (2007).
115. 556 U.S. 662 (2009).
116. 355 U.S. 41, 45-46 (1957).
117. *Iqbal*, 556 U.S. at 678 (quoting Bell Atlantic Corp. v. Twombly, 550 U.S. 544, 570 (2007)).
118. *Id.* at 685 (quoting Bell Atlantic Corp. v. Twombly, 550 U.S. 544, 559 (2007)).

such motions depends on the underlying allegations.[119] But other courts have concluded that this defense cannot be resolved at the motion to dismiss stage. Bank officer defendants should bear this in mind when framing their motions to dismiss so that courts do not reflexively deny their motions without testing them against these heightened pleading standards.[120] Any allegations that demonstrate that bank officers followed a process when weighing the challenged decisions, availed themselves of information, or made any inquiries are tailor-made to establishing the exercise of business judgment. "Allegations amounting to mere negligence, carelessness, or lackadaisical performance are insufficient as a matter of law [to rebut the . . . rule]."[121]

But even if a court is unwilling to engage at the motion to dismiss, officer defendants should not despair. Although they may have to navigate a path through discovery, officer defendants are likely to have an even more compelling argument at the summary judgment stage. Assuming that defendants followed a reasonable process when making decisions and did not put their own personal interests over those of the institution, then the business judgment rule should end the case. Undoubtedly, the FDIC and its experts will have a long litany of mistakes and shortcomings in connection with the loan—typically referred to as variances in lending parlance. But if the officer defendants can demonstrate that they considered those variances when approving

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119. *See, e.g.*, Kaye v. Lone Star Fund V (U.S.), L.P., 453 B.R. 645, 679 (N.D. Tex. 2011) (finding business judgment rule protections are substantive and independent of the notice purpose of procedural rules of pleading); Data Key Partners v. Permira Advisers LLC, 849 N.W.2d 693, 703 (Wis. 2014) (concluding, in light of *Twombly*, that *Tower Air* suffers from "fatal flaws" and that plaintiffs must "plead facts sufficient to avoid the business judgment rule, even when it is not raised on the face of the complaint").

120. Other defenses are beyond the scope of this article. These defenses include, but are not limited to, statute of limitations, comparative or contributory negligence, failure to mitigate, waiver, laches and estoppel. When directors and officers are sued by the FDIC, or other federal agencies, the agencies often claim unique rules appropriate to preserve the public interest. The Supreme Court in *O'Melveny & Myers v. FDIC*, rejected the argument that national interests justified the creation of special common law rules governing director and officer liability. 512 U.S. 79 (1994); *see also* FDIC v. Skow, 741 F.3d 1342 (11th Cir. 2013) (finding no federal common law rule that exempts the FDIC from defenses under state law). For a full discussion of these additional matters, *see* John K. Villa, BANK DIRECTORS', OFFICERS', AND LAWYERS' CIVIL LIABILITIES, (CCH Supp. 2014).

121. FDIC v. Blackwell, No. 1:11-CV-03423-RWS, 2012 WL 3230490, at *4 (N.D. Ga. Aug. 3, 2012) (brackets and internal quotation marks omitted).

the loan as part of the approval process, then that should suffice to establish that the decision making process was rational and employed in good faith.[122]

It was for that very reason that a district court in North Carolina recently granted summary judgment to both directors and officers of a failed bank.[123] Rejecting the FDIC's argument that the defendants had deviated from prudent lending practices, the court noted that,

> Under the business judgment rule, there can be no liability for officers and directors even when 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,' so long as the court determines that the process employed was either rational or employed in a *good faith* effort to advance the corporate interests.[124]

As the court explained,

> Although the decisions of defendants to engage in various forms of lending and to make the particular loans . . . raise interesting discussion points in hindsight, the business judgment rule precludes this Court from delving into whether or not the decisions were 'good' and limits the Court's involvement to a determination of whether the decisions were made in 'good faith' or were founded on a 'rational business purpose.[125]

Nor does the fact that the lending decisions entailed risks constitute irrationality.[126] This opinion is a textbook illustration of the power of the business judgment protection at the summary judgment stage. If business judgment is to mean anything, it should protect directors and officers who adhered to an established process from having to go to trial to vindicate their process or decisions.

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122. Sam Wong & Son Inc. v. N.Y. Mercantile Exch., 735 F.2d 653, 678 n.32 (2d Cir. 1984) (Friendly, J.) (describing the rationality test as "a minimal requirement of some basis in reason"); *In re* Caremark Int'l Inc. Deriv. Litig., 698 A.2d 959, 967 (Del. Ch. 1996) (finding no liability for a decision the fact finder believes to be "wrong," "stupid," or "egregious," "so long as the [decision-making process] was either rational or [was] employed in . . . good faith" (emphasis omitted)).

123. FDIC v. Willetts, No. 7:11-CV-165-BO, 2014 WL 4828330, at *6 (E.D.N.C. Sept. 11, 2014). The FDIC has since filed an appealed with the Fourth Circuit.

124. *Id.* (internal quotation marks and citations omitted).

125. *Id.*

126. *Id.* at *5.

CONCLUSION

FIRREA's heightened liability standard poses the most significant obstacle to the FDIC's efforts to recover losses to the Deposit Insurance Fund. After all, proving reckless or intentional conduct by former directors and officers of failed banks is far more difficult than proving ordinary negligence. That explains why the FDIC as receiver asserts ordinary negligence claims whenever possible; it recognizes that those claims pose a far greater risk to defendants than a case premised only on gross negligence, and that defendants are far more vulnerable to those claims if they cannot avail themselves of business judgment protections. As we have seen, the law in many states (including Georgia, Louisiana, Nevada, New Jersey, and Virginia) affords defendant officers complete protection from ordinary negligence claims. In other states, such as Florida, decisions are at odds and, therefore, give defense counsel room to argue that the business judgment rule protects the good faith decisions of their clients, even when the statutory codification of the rule speaks only in terms of directors. In a handful of states, including California, the prospect of insulating business judgments made by bank officers from second-guessing is improbable. Officer defendants confronting these claims in states that recognize the existence of business judgment protections should focus their efforts on demonstrating the existence of a standard, reasonable process underlying their decisions.