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## Governance in the Public Corporation of the Future: The Battle for Control of Corporate Governance

Z. Jill Barclift\*

Eight years after passage of the Sarbanes-Oxley Act, Congress has again passed sweeping legislation in response to a corporate crisis.<sup>1</sup> In addition to changes in the regulatory environment for Wall Street financial firms and banks, the Dodd-Frank Act (D-F Act) also proposes reforms to corporate governance.<sup>2</sup> Before passage of the D-F Act, the Securities and Exchange Commission (SEC) began rulemaking on several governance matters addressed by Congress in the D-F Act; however, the SEC will begin rulemaking on many of the new corporate governance mandates over the next six to twelve months.<sup>3</sup> As federal securities laws and rulemakings continue to define corporate governance requirements, the new rules raise anew a discussion of what is (or perhaps what should be) the balance between state corporate law and federal securities laws in regulating corporate governance for public corporations.<sup>4</sup>

As Congress, the SEC, and national exchanges continue to develop rulemaking on director independence, compliance processes, disclosures, and leadership structure, any concerns over further intrusion of federal securities laws into state

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<sup>1</sup> Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (2002).

<sup>2</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

<sup>3</sup> *Testimony Before the Subcomm. on Sec., Ins., and Inv.*, 112th Cong. 6–8 (2011) (statement of Mary Schapiro, Chairman, U.S. Securities and Exchange Commission), available at [http://banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore\\_id=d1bd7e59-137a-4d00-93d0-8ede516f52a0](http://banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=d1bd7e59-137a-4d00-93d0-8ede516f52a0).

<sup>4</sup> Mark J. Roe, *Delaware's Competition*, 117 HARV. L. REV. 588, 592 (2003) (discussing the race to the bottom in corporate law, and how the “federal authorities set the broad boundaries—of an uncertain and changing demarcation—within which the states can move”); Richard A. Booth, *The Emerging Conflict Between Federal Securities Law and State Corporation Law*, 12 J. CORP. L. 73, 74 (1986) (discussing the “implication of the dependence of the federal law of disclosure upon the state law of fiduciary duty is that when state law changes, so will federal law”); Marcel Kahan & Edward Rock, *Symbiotic Federalism and the Structure of Corporate Law*, 58 VAND. L. REV. 1573, 1575 (2005) (discussing the relation between federal and state corporate lawmaking).

corporate governance are perhaps moot as the proverbial “camel’s nose” has already penetrated the tent.<sup>5</sup> Even federalists have begun to accept that not only does Congress have the right to regulate public corporations, but also that it will do so when investors lobby for federal rules to address fraud or other governance failures.<sup>6</sup> However, notwithstanding federal efforts to impose additional governance mandates, most corporate governance covering the relationship between shareholders and management remains firmly within the purview of state corporate law.<sup>7</sup> Perhaps, the more narrow issue then becomes not whether we are headed toward a federal system of governance for public companies, but whether the intrusion by federal securities laws into state governance matters are beneficial to shareholders.

In this Article, I examine the latest governance mandates under the D-F Act. In particular, this Article focuses on the disclosure requirements on the CEO and chairman positions, and argues that disclosures of whether the CEO is also the chairman benefit shareholders’ governance rights under state law. The new provisions under the D-F Act combined with recent SEC disclosure rulemaking on board leadership structure address a fundamental issue of board decision-making and the affects of structural bias and “group think” on director behavior. Bifurcation disclosures for public companies provide shareholders with beneficial information on board leadership structure, but more importantly, the disclosure requirements force directors to engage in discussion and analysis of how board decisions are made, and whether such decisions can be unduly influenced by a dominant CEO. State fiduciary duty requirements do not directly address social and structural decision-making biases. Shareholders benefit when federal disclosure rules address state governance shortcomings that are not otherwise conducive to private ordering.

Part I of this Article explains the complimentary relationship between federal and state law, and looks at how securities laws focus on disclosure and state laws focus on fiduciary duties to protect shareholders from management misconduct. This part looks at how Congress and the SEC use

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<sup>5</sup> Stephen M. Bainbridge, *The Short Life and Resurrection of SEC Rule 19C-4*, 69 WASH. U. L.Q. 565, 620 (1991); Z. Jill Barclift, *Codes of Ethics and State Fiduciary Duties: Where is the Line?*, 1 J. BUS. ENTREPRENEURSHIP & L. 237, 258 (2008).

<sup>6</sup> Leo E. Strine, Jr., *Breaking the Corporate Governance Logjam in Washington: Some Constructive Thoughts on a Responsible Path Forward*, 63 BUS. LAW. 1079, 1084 (2008).

<sup>7</sup> *Id.* at 1081.

federal disclosure mandates to affect behavioral changes in board and management conduct.

Part II examines recent efforts by the SEC to influence board and management governance prior to the passage of the D-F Act. This part looks at 2010 SEC rulemaking on risk, compensation, and governance; focusing specifically on the governance rulemaking on disclosure requirements for the CEO and chairman positions. This part discusses the rationale for the rulemaking to address leadership and structural biases in board decision-making, and why board structure influences board decision-making.

Part II also explores briefly the provisions of the D-F Act related to corporate governance and looks at which provisions use disclosure to effect corporate governance changes. While this part briefly identifies and explains other corporate governance provisions in the D-F Act, the focus is on the provisions of the D-F Act that provide Congressional support of the SEC's efforts to influence board leadership and structural bias by examining the legislative history of the bifurcation provisions in the Act.

Part III explores the meaning of structural bias and group-think. This part examines the social nature of boards, how such influences affect leadership structure, and why federal bifurcation rules may benefit shareholders.

Part IV explores Delaware's approach to structural bias and group-think in board decision-making. This part looks at the difficulty shareholders face in trying to demonstrate the governance harm when directors' decision-making is influenced by group-think and CEO dominance. This part argues that federal disclosures on bifurcation forces directors to assess its leadership structure for structural biases and that the D-F Act's and the SEC's disclosure mandates benefit shareholders.

#### I. THE COMPLIMENTARY RELATIONSHIP: FEDERAL AND STATE CORPORATE LAW

The relationship between federal securities laws and state corporate law is best described as synergistic and complimentary.<sup>8</sup> Federal securities laws and regulations, with their emphasis on public disclosures and financial reporting, are complimentary to state law's focus on the relationships between shareholders and corporate managers, and the fiduciary obligations of the board.<sup>9</sup> Recognizing the complimentary order

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<sup>8</sup> *Id.* at 1080–81.

<sup>9</sup> *Id.*; Sean J. Griffith & Myron T. Steele, *On Corporate Law Federalism:*

of federal and state law, Congress has been careful not to intrude into areas reserved for state governance while carving out disclosure rules, which enables shareholders to make informed decisions.<sup>10</sup> The D-F Act provides an example of how Congress balances disclosure with state fiduciary obligations of directors. Language in the D-F Act on non-binding shareholders' vote on executive compensation specifically provides a rule of construction in which the non-binding shareholders' vote does not overrule a decision by the board, create or imply a change to fiduciary duties, or create additional fiduciary duties for directors.<sup>11</sup>

Notwithstanding the complimentary relationship of state and federal rules, the D-F Act and recent SEC rulemaking continue to demonstrate the effective use of disclosure rules to influence corporate governance.<sup>12</sup> Corporate governance requirements remain within states' regulatory purview and Delaware remains the dominant state for public company incorporation.<sup>13</sup> However, it is the truce between federal securities laws and Delaware corporate law, which continues to illustrate how governance, in particular fiduciary duties, develops in response to Congress' desire to act in the face of corporate crises.<sup>14</sup> History suggests that Congress acts in response to public pressures for reform.<sup>15</sup> Correspondingly, Delaware reacts by either amending its corporate laws or further defining fiduciary obligations of directors.<sup>16</sup> As Leo Strine writes, "why the American model of corporate governance has served investors so well is the synergies that arise from the combination of a strong regulatory structure governing public disclosures and

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*Threatening the Thaumatrope*, 61 BUS. LAW. 1, 3–4 (2005) (discussing the origins of corporate governance federalism).

<sup>10</sup> E. Norman Veasey, *State-Federal Tension in Corporate Governance and the Professional Responsibilities of Advisors*, 28 J. CORP. L. 441, 443–44 (2003) (discussing how federal law, such as the Sarbanes-Oxley Act, does not completely supplant state law); Griffith & Steele, *supra* note 9, at 4.

<sup>11</sup> *Executive Compensation and Corporate Governance*, COVINGTON & BURLING LLP, 2 (July 21, 2010), <http://www.cov.com/files/Publication/0fd9af21-04a7-4537-9d8e-bbc47050e295/Presentation/PublicationAttachment/e413a276-e87e-4af5-ac29-bfeb5f100ec/Dodd-Frank%20Act%20Executive%20Compensation%20and%20Corporate%20Governance.pdf>.

<sup>12</sup> Robert B. Thompson, *Corporate Federalism in the Administrative State: The SEC's Discretion to Move the Line Between the State and Federal Realms of Corporate Governance*, 82 NOTRE DAME L. REV. 1143, 1180–83 (2007).

<sup>13</sup> Mark J. Roe, *Is Delaware's Corporate Law Too Big to Fail?*, 74 BROOK. L. REV. 75, 76–77 (2008) (discussing Delaware's dominance in corporate law, including explanations for its dominance).

<sup>14</sup> *Id.* at 82 (discussing how Congress' response to corporate crises affects Delaware law rather than the law of other states due to its dominance in corporate law).

<sup>15</sup> *Id.* at 83.

<sup>16</sup> *Id.*

financial integrity, and a more nimble and enabling state law approach to the relations between corporate managers and stockholders.”<sup>17</sup>

Yet, as Congress and the SEC continue to respond to investor concerns over management misconduct and board failures, new regulations and rules requiring disclosures on governance processes directly impact governance matters traditionally covered by state law.<sup>18</sup> Recent SEC rules and the governance provisions in the D-F Act continue to use disclosure as the way to compel boards to implement changes to their governance processes.<sup>19</sup> Before describing the D-F Act’s governance provisions, it is necessary to examine rulemaking on governance by the SEC enacted prior to passage of the D-F Act and what effect the D-F Act may have on the SEC’s rulemaking.

## II. SEC RULES ON ENHANCED DISCLOSURE ABOUT RISK, COMPENSATION AND CORPORATE GOVERNANCE

Prior to passage of the D-F Act, effective in February 2010, the SEC implemented rulemaking covering board risk assessment, executive compensation, and corporate governance.<sup>20</sup> The new rules require disclosure of a company’s compensation policies and risk management; disclosure on the experience, qualifications, attributes or skills of the director; disclosures about each director’s experience at other public companies, including involvement in any legal proceedings; disclosure of how diversity is considered in the director nomination process; disclosure information about the role of the board’s oversight of risk and leadership structure, including whether the company has combined or separated the chairman and CEO position, and why the company believes this structure is appropriate; quicker shareholder voting results; revisions to disclosure on director compensation; and disclosure about compensation consultants including fees paid to the consultant.<sup>21</sup>

The SEC’s stated goal in adopting the new rules was to improve information in annual reports and proxy statements to give shareholders improved information to evaluate board leadership.<sup>22</sup> The D-F Act gave Congressional approval to many

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<sup>17</sup> Strine, *supra* note 6, at 1080.

<sup>18</sup> Thompson, *supra* note 12, at 1180.

<sup>19</sup> See generally Proxy Disclosure Enhancements, Exchange Act Release Nos. 33-9089; 34-62275 (Dec. 16, 2009), available at <http://www.sec.gov/rules/final/2009/33-9089.pdf>.

<sup>20</sup> *Id.* at 39–45.

<sup>21</sup> *Id.* at 29–45.

<sup>22</sup> *Id.* at 4.

of the rulemaking provisions put forth in the SEC's rulemaking on proxy disclosure enhancements.<sup>23</sup> It is therefore unclear what adjustments the SEC must make to its prior rulemaking in order to satisfy the requirements under the D-F Act or whether there will be additional disclosure requirements. Although the D-F Act addressed systemic risk issues for the financial system, the SEC, as part of its 2010 rulemaking, issued rules to address the board's role in monitoring systemic risk.<sup>24</sup>

#### A. SEC's Disclosure on Risk Management and New Compensation Committee Rules

The SEC mandated that companies disclose the board's role in risk oversight, and whether such policies "are reasonably likely to have a material adverse effect on the company."<sup>25</sup> The new rules require companies to disclose and evaluate their compensation policies and practices for all employees (including non-executive officers) and assess whether there are any risks associated with those compensation policies and practices.<sup>26</sup> The purpose of the disclosure is to assist investors in determining whether a company has compensation incentives, which may lead to aggressive risk-taking by employees.<sup>27</sup>

The types of examples provided by the SEC for disclosure include: design of compensation policies and practices for employees whose behavior is most affected by compensation incentives and how such policies may relate to risk taking by the employees; how the company considers risk assessment in designing compensation incentives; explanation of how the company's compensation policies and practices may lead to risk taking by employees in both the short term and long term; any policies or changes to such policies regarding changes to compensation practices to adjust to risk profiles; and procedures to monitor risk policies and practices to determine whether its risk objectives are being met.<sup>28</sup>

These disclosures will require boards to inform shareholders how they monitor the level of risk taken by not just corporate executives, but all employees.<sup>29</sup> Boards will be better able to identify and address risky decisions by the chief executive, which

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<sup>23</sup> *Alert SEC Disclosure and Corporate Governance*, WEIL, GOTSHAL & MANGES LLP, 4 (Apr. 4, 2011), [http://www.weil.com/files/upload/Weil\\_Alert\\_SEC\\_CG\\_April\\_4\\_2011.pdf](http://www.weil.com/files/upload/Weil_Alert_SEC_CG_April_4_2011.pdf).

<sup>24</sup> Proxy Disclosure Enhancements, *supra* note 19, at 1.

<sup>25</sup> *Id.* at 5.

<sup>26</sup> *Id.* at 8.

<sup>27</sup> *Id.* at 9.

<sup>28</sup> *Id.* at 15–16.

<sup>29</sup> *Id.* at 8–9.

may be driven by the CEO's compensation goals rather than the best interest of the corporation.<sup>30</sup> Improved risk management disclosures complement state fiduciary law by reinforcing good faith deliberations by the board.<sup>31</sup> Knowing that shareholders will be looking at its disclosures to see if the board's risk policies reward executives who take excessive risk with excessive compensation, directors will be careful to consider management decisions and engage in more open discord concerning management strategies.<sup>32</sup>

The combined new disclosures on compensation committee independence, executive compensation and risk management disclosures, and disclosures on the separation of CEO and chairman positions directly address issues of structural biases in board decision-making. The D-F Act provided Congressional approval of the SEC's rulemaking on board leadership structure.<sup>33</sup> The SEC's rationale for implementing bifurcation rules are explained below.

#### B. SEC Rulemaking on Board Leadership Structure

Under the SEC's rulemaking, companies are required to disclose why it has chosen to combine the positions of chairman and CEO and the reasons why the company believes this board leadership structure is appropriate for the company.<sup>34</sup> If the company combines the roles, but selects an independent lead director to chair meetings of independent directors, then the company must disclose why it has a lead director and the role the lead independent director plays in leadership of the company.<sup>35</sup> The disclosures are not intended to influence a company's leadership structure decisions; however, the purpose is to inform investors of the management's explanation for its board leadership structure, and to provide insight into the board's communication and the degree to which the board is able to exercise independent judgment about management.<sup>36</sup>

The SEC's rulemaking on governance remains within the traditional boundary of disclosure and financial integrity for federal rules. The disclosure function of the new bifurcation rule is consistent with recent federal efforts to influence director

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<sup>30</sup> *Id.* at 9.

<sup>31</sup> *Id.*

<sup>32</sup> *Id.* at 14.

<sup>33</sup> *Id.* at 39.

<sup>34</sup> *Id.*

<sup>35</sup> *Id.*

<sup>36</sup> *Id.* at 81 (discussing the benefits of the new disclosure about board leadership structure and the board's role in risk oversight).

behavior by mandating disclosures, notwithstanding the SEC's insistence that it did not intend to influence leadership structure decisions by the board.<sup>37</sup>

In response to investor concerns to perceived governance failures, the D-F Act includes several provisions to address governance lapses and enhance disclosure obligations of boards.<sup>38</sup> Congress' stated goals in passing legislation to further governance enhancements are to address the perceived failures of corporate governance in monitoring risk management and the governance failures.<sup>39</sup> The D-F Act provisions covering overall corporate governance is addressed below.

### C. Dodd-Frank Act: Governance Provisions

The pertinent section of the D-F Act concerning corporate governance is Title IX, Subtitles E and G.<sup>40</sup> The provisions give shareholders proxy access by requiring a shareholder's vote to approve executive compensation, disclosure on executive compensation and financial performance of the company and recovery of erroneously awarded compensation; disclosure on director and employee hedging; call for rules on independence of compensation committee members and their consultants; and disclosure on bifurcation of chairman and chief executive officer positions.<sup>41</sup> Below are synopses of each governance provision and its stated goal in improving governance for shareholders.

### D. Proxy Access: "Say on Pay"

Among the more talked about governance provisions are the so-called "say on pay" requirements.<sup>42</sup> The D-F Act authorizes the SEC to issue non-binding rules for shareholders' voting on executive compensation by giving shareholders greater

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<sup>37</sup> Josh Wright, *Stephen Bainbridge on Mandatory Disclosure: A Behavioral Analysis*, TRUTH ON THE MARKET (Dec. 7, 2010), <http://truthonthemarket.com/2010/12/07/stephen-bainbridge-on-mandatory-disclosure-a-behavioral-analysis/> (discussing how "mandatory disclosure is a—maybe *the*—defining characteristic of U.S. securities regulation"); Thompson, *supra* note 12, at 1181–82 (discussing that if shareholder access rules were implemented, the federalism issue would likely disappear); Z. Jill Barclift, *supra* note 5, at 250 (discussing how federal securities law regulates disclosure).

<sup>38</sup> Proxy Disclosure Enhancements, *supra* note 19, at 42.

<sup>39</sup> CCH ATTORNEY-EDITOR STAFF, DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT: LAW, EXPLANATION AND ANALYSIS 420–21 (Aspen Pub. 2010).

<sup>40</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, §§ 951-57, 971-79, 124 Stat. 1376, 1899-1907, 1915-26 (2010) (to be codified in scattered sections of 15 U.S.C.).

<sup>41</sup> *Id.*

<sup>42</sup> Lucian A. Bebchuk, & Scott Hirst, *Private Ordering and the Proxy Access Debate*, 65 BUS. LAW. 329 (Harv. L. & Econ. Discussion Paper No. 653, 2010), available at <http://ssrn.com/abstract=1513408> (discussing proxy access).

participation in executive compensation decisions.<sup>43</sup> Shareholders are given an advisory vote on executive compensation; however, shareholders are not permitted to micromanage executive compensation by setting limits and are limited to the right to express an opinion.<sup>44</sup> The purpose of the vote is to give shareholders information on compensation practices so that shareholders can evaluate whether such practices are in the shareholders' best interests.<sup>45</sup> Among the concerns expressed by Congress in passing these provisions was the desire to increase transparency and accountability, and to reinforce executive performance by rewarding short-term gain without penalizing for long-term consequences of decisions.<sup>46</sup>

The disclosures on pay versus performance require the SEC to develop proxy rules that provide an explanation of compensation and include information showing the connection between executive compensation paid and company performance.<sup>47</sup> Additionally, information on total median compensation of all employees, annual total compensation of the CEO, and a ratio comparing the CEOs total compensation to the median compensation of all employees must be disclosed.<sup>48</sup> The purpose of these disclosures is to improve the information provided to shareholders so that investors are informed about the relationship between executive pay and performance and can make comparisons with overall medians and assess what executives are being paid when the company's performance is failing.<sup>49</sup> The SEC addressed some of these enhanced compensation disclosure requirements in rulemaking effective February 2010 and will likely issue additional rulemaking to comply with the D-F Act requirements.<sup>50</sup>

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<sup>43</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 951-57; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 420-23.

<sup>44</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 951; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 421-23.

<sup>45</sup> CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 421-22 ("Shareholders have raised concerns about large bonus plans in situation which they, as the company's owners have experienced loss.").

<sup>46</sup> S. REP. NO. 111-176, at 133-34 (2010).

<sup>47</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 971; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 430-31.

<sup>48</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 953; S. REP. NO. 111-176, at 135.

<sup>49</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 953; S. REP. NO. 111-176, at 135.

<sup>50</sup> Proxy Disclosure Enhancements, *supra* note 19, at 1 (discussing that the amendments to these rules enhance the "information provided in connection with proxy solicitations and in other reports filed with the Commission"). The SEC issued a press release in January, 2011 adopting rules for Say-on-Pay and Golden Parachute Compensation in compliance with Dodd-Frank Act. Press Release, U.S. Sec. & Exch. Comm'n, SEC Adopts Rule on Say on Pay and Golden Parachute Compensation as

#### E. Executive Compensation: “Claw Backs”

The D-F Act imposes a requirement that public companies develop and disclose policies that, in the event the company is required to prepare an accounting restatement resulting from material noncompliance with financial reporting requirements, the company will recover from the executive officer any incentive compensation received.<sup>51</sup> Congress’ intent was to require companies to recover executive compensation received due to lack of compliance with applicable reporting requirements so that shareholders would not have to resort to costly litigation to recover erroneously paid compensation.<sup>52</sup>

#### F. Disclosures on Hedging

The disclosures on hedging by employees and directors require shareholders to receive information in any annual proxy solicitation on whether employees or directors are permitted to purchase hedging financial instruments.<sup>53</sup> The purpose of this disclosure is so that investors know whether employees or directors have hedged any compensation granted to them in the event the company fails to meet its financial targets.<sup>54</sup>

#### G. Independent Compensation Committee

Another noteworthy provision in the Act is the independence requirements for compensation committee members and consultants.<sup>55</sup> The legislative history of the D-F Act suggests that Congress was not only concerned with disclosure, but also equally concerned with corporate governance processes.<sup>56</sup> Mandating the independence of key committees is not a new approach by Congress to deal with board decision-making; Congress, the SEC, and Exchange Act rules require independent audit committees and set forth parameters defining the meaning

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Required under Dodd-Frank Act (Jan. 25, 2011), *available at* <http://www.sec.gov/news/press/2011/2011-25.htm>.

<sup>51</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 954; S. REP. NO. 111-176, at 135–36.

<sup>52</sup> S. REP. NO. 111-176, at 135–36. “It has become apparent that a significant concern of shareholders is the relationship between executive pay and the company’s financial performance for the benefit of shareholders.” *Id.* at 135.

<sup>53</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 955; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 427.

<sup>54</sup> CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 427.

<sup>55</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 952; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 423–25. “Independence” is not defined in the legislation, but rather that determination is left to the exchanges and associations. *Id.* at 423.

<sup>56</sup> S. REP. NO. 111-176, at 137.

of “independent.”<sup>57</sup> Similarly, the new requirements for independent directors on the compensation committee are consistent with prior federal governance rules on board committee structures.<sup>58</sup>

The D-F Act mandates that members of the compensation committee be independent board members.<sup>59</sup> The D-F Act leaves to the SEC the requirement of issuing rules for the national exchanges to prohibit listing companies that do not meet the compensation committee independence requirements.<sup>60</sup> The exchanges must consider certain factors when defining independence, including the source of the director’s compensation and the director’s affiliation with the company.<sup>61</sup> Additionally, compensation consultants to directors must also meet independence requirements.<sup>62</sup> The SEC must issue rules on the meaning of independence of compensation consultants, which must be considered by compensation committees before engaging the advisory services of consultants.<sup>63</sup> Factors in determining the independence of compensation committee consultants include whether the consultant provides other services to the company, the amount of fees paid to the consultant and the percentage of the consultant’s total revenue from these fees, any business or personal relationships of the consultant to the company, policies and procedures for hiring consultants, and stock of the company owned by the consultant.<sup>64</sup>

The D-F Act also directs that a company give its compensation committee sole discretion to retain or to obtain advice from the consultant.<sup>65</sup> The company must also disclose whether it retained a consultant and whether there are “any conflict[s] of interest[,] and, if so, the nature of the conflict of

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<sup>57</sup> 15 U.S.C. § 78f (2010); Proxy Disclosure Enhancements, *supra* note 19, at 34–35 (discussing standards relating to Listed Company Audit Committee).

<sup>58</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 952; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 423–25.

<sup>59</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 952; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 423.

<sup>60</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 952; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 425.

<sup>61</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 952; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 423.

<sup>62</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 952; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 424.

<sup>63</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 952; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 424.

<sup>64</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 952; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 424.

<sup>65</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 952; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 424.

interest.”<sup>66</sup> The mandates for independent compensation committee members and rules on hiring and disclosure of compensation consultants are to provide investors with adequate information to assess the reliability of compensation committee reports.<sup>67</sup> Some of the legislative concerns over consultants have been addressed in earlier SEC rulemaking on compensation committee members’ independence, and the SEC may modify or tweak its previously issued rules on compensation committee director independence to meet the requirements under the D-F Act.<sup>68</sup>

#### H. Disclosures on Bifurcation of CEO and Chairman Positions

The D-F Act requires the SEC to develop rules that require disclosure in annual proxy statements, which state the reasons why a company has chosen the same person to serve as chairman of the board of directors and CEO or why it has chosen different individuals in these positions.<sup>69</sup> The legislative history suggests that Congress understood there were valid reasons for having the same person serve as Chairman and CEO, yet recognized the importance of independent board leadership.<sup>70</sup> The SEC issued rulemaking on board leadership structure calling for disclosures on CEO and chairman roles, therefore additional SEC rulemaking may not be required to comply with D-F Act.<sup>71</sup>

All of the D-F Act’s governance requirements cover governance areas traditionally left to federal securities laws—proxy rules, independent board members, and disclosure requirements.<sup>72</sup> What makes the federal rules on disclosing bifurcations in board leadership new is that, unlike rules for independent audit or compensation committee members, board leadership structure rules address the social and psychological reasons behind board decision-making.<sup>73</sup> It seems almost impossible not to disclose information on board leadership structure without the board first engaging in a discussion about

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<sup>66</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 952; CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 424.

<sup>67</sup> CCH ATTORNEY-EDITOR STAFF, *supra* note 39, at 424.

<sup>68</sup> Proxy Disclosure Enhancements, *supra* note 19, at 47.

<sup>69</sup> Dodd-Frank Wall Street Reform and Consumer Protection Act § 972; S. REP. NO. 111-176, at 147.

<sup>70</sup> S. REP. NO. 111-176, at 147.

<sup>71</sup> Proxy Disclosure Enhancements, *supra* note 19, at 39–45 (discussing proposed amendments and final rules on new disclosure about board leadership and the board’s role in risk and oversight).

<sup>72</sup> Holly J. Gregory, *Corporate Governance—United States*, WEIL.COM (last visited Mar. 23, 2011), <http://www.weil.com/news/pubdetail.aspx?pub=4049>.

<sup>73</sup> Proxy Disclosure Enhancements, *supra* note 19, at 39 (requiring companies to disclose the reasons behind their choice of structure).

what is the most appropriate structure to encourage frank and open dialogue among directors. The SEC has designed rules, which give investors information on the inherent or the structural design of board membership, so that shareholders will know whether a dominant CEO or leader has exerted undue influence on board decision-making.<sup>74</sup> The influences Congress and the SEC seek to address are known as structural biases in decision-making by directors and the inability of boards to minimize the negative consequences of group-think. Part III examines the meaning of structural bias and group think.

### III. STRUCTURAL BIAS AND THE SOCIAL NATURE OF BOARDS

Social science research documents that cohesive groups, such as boards, tend to engage in “group think” behavior and strongly identify with the group leader.<sup>75</sup> A dominant leader can often manipulate the group to comply with his wishes.<sup>76</sup> Directors thus often conform to the social norms of “group think” and limit frank discussion or dissent.<sup>77</sup> Governance processes to counter the effects of “group think” include not only independent directors, but removing the CEO as chairman or selecting an independent director to lead discussions with other independent directors without the influence of the CEO.<sup>78</sup> Boards engage in group think when there is limited discussion of ideas and few directors are willing to engage in critical analysis of ideas put forth by management.<sup>79</sup>

Rakesh Khurana, a noted leadership development scholar, and Katharina Pick, a Ph.D. candidate, in their article, *The Social Nature of Boards*, outline the challenges faced by boards as groups subject to influence by charismatic leaders.<sup>80</sup> Professor Khurana and Pick note the difficulty individual members of a group face in trying to stand up to leaders and why social norms of conformity often lead the board to acquiesce to the wishes of

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<sup>74</sup> *Id.* at 42–44.

<sup>75</sup> See generally Marleen A. O'Connor, *The Enron Board: The Perils of Groupthink*, 71 U. CIN. L. REV. 1233 (2003).

<sup>76</sup> Donald C. Langevoort, *Resetting the Corporate Thermostat: Lessons from the Recent Financial Scandals About Self-Deception, Deceiving Others and the Design of Internal Controls*, 93 GEO. L.J. 285, 297–300 (2004) (discussing the duration of CEO power and how it is obtained).

<sup>77</sup> *Id.* at 295.

<sup>78</sup> *Id.* at 313–14.

<sup>79</sup> Troy A. Paredes, *Too Much Pay, Too Much Deference: Behavioral Corporate Finance, CEOs, and Corporate Governance*, 32 FLA. ST. U. L. REV. 673, 724–25 (2005); O'Connor, *supra* note 75, at 1238.

<sup>80</sup> Rakesh Khurana & Katharina Pick, *The Social Nature of Boards*, 70 BROOK. L. REV. 1259, 1260 (2005).

the CEO, even when the CEO makes flawed decisions.<sup>81</sup> CEOs are often blinded in their decision-making by being unable to see the shortcomings of plans and by being surrounded by individuals unwilling or unable to challenge the prevailing views of the CEO.<sup>82</sup> Shareholders benefit from separating the CEO and chairman positions or designating a lead independent director because bifurcation affects structural biases and group think of board decision-making. State fiduciary duty laws limit the ability of shareholders to address issues of structural organizational bias, thus, the D-F Act governance provisions, combined with recent SEC rulemaking disclosure, enhance shareholders' rights under state corporate law, and arguably move federal securities laws even closer to regulating state corporate governance matters.<sup>83</sup> It is noteworthy to look at how Delaware, the state of choice for most public corporations, addresses the issue of structural bias in board decision-making in order to gain a better understanding of the limitations and benefits of federal bifurcation disclosures.

#### IV. THE DELAWARE APPROACH

Two Delaware cases, *Beam v. Stewart* and *In re Oracle Corp Derivative Litigation*, illustrate the issues faced by shareholders when trying to argue that a board or individual directors lack independence based on arguments of social or structural bias.<sup>84</sup>

In *Beam*, the shareholder brought derivative claims against Martha Stewart and other officers and directors for a variety of actions taken by the board after allegations of insider trading were brought against Martha Stewart, who was chairman and CEO, and the largest shareholder of Martha Stewart Living Omnimedia, Inc. (MSO).<sup>85</sup> It was agreed that Stewart and another officer were not independent or disinterested for

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<sup>81</sup> *Id.* at 1271. See also James D. Cox & Harry L. Munsinger, *Bias in the Boardroom: Psychological Foundations and Legal Implications of Corporate Cohesion*, 48 LAW & CONTEMP. PROBS. 83, 85–108 (1985).

<sup>82</sup> Cox & Munsinger, *supra* note 81, at 85; Khurana & Pick, *supra* note 80, at 1273–74.

<sup>83</sup> Kenneth B. Davis, Jr., *Structural Bias, Special Litigation Committee, and the Vagaries of Director Independence*, 90 IOWA L. REV. 1305, 1308 (discussing the meaning of structural bias for special litigation committees).

<sup>84</sup> *Beam v. Stewart*, 845 A.2d 1040, 1040 (Del. Super. Ct. 2004) (“Shareholder brought derivative action against corporation’s founder, officers and directors, and against corporation as a nominal defendant, seeking relief in relation to accusations of insider trading by founder, private sales of sizable shares of stock by some of the directors following insider trading scandal, and board of director’s decision to provide founder with ‘split-dollar’ life insurance.”); *In re Oracle Corp Derivative Litigation*, 824 A.2d 917, 917 (Del. Ch. 2003) (“Shareholders brought derivative action alleging insider trading by chief executive officer (CEO), chief financial officer (CFO), and two directors.”).

<sup>85</sup> *Beam v. Stewart*, 845 A.2d at 1044.

purposes of demand.<sup>86</sup> The shareholders argued that other members of the board were not independent because of either their longstanding personal relationships with Martha Stewart, or their indebtedness to Stewart in some personal or professional manner.<sup>87</sup> In affirming the Chancery Court's conclusion that the shareholder had failed to show facts raising a reasonable doubt as to the independence of the named directors, the Delaware Supreme Court stated that the court must make a fact-specific determination "by answering the inquiries: independent from whom and independent for what purpose? To excuse pre-suit demand in this case, the plaintiff has the burden to plead particularized facts that create a reasonable doubt sufficient to rebut the presumption that [the directors were] independent of defendant Stewart."<sup>88</sup> The court went on to state that the jurisprudence balance was to deter baseless shareholder lawsuits while permitting shareholders to demonstrate with particularized facts a lack of independence by directors.<sup>89</sup>

The court was unwilling to find that personal friendships or business relationships alone result in bias enough to render a director incapable of exercising independent judgment.<sup>90</sup> The court characterized the shareholders' arguments as "structural bias" and directly stated that while it was aware of the biases common to boards as part of the socialization process, it was unwilling to take notice of such arguments unless established in appropriately plead complaints.<sup>91</sup> The court acknowledged that the assessment of director independence varies depending on the state of litigation and that at the demand stage, a shareholder's limited discovery on independence may be "outcome-determinative" on the issue of independence.<sup>92</sup>

In *Oracle*, a case distinguished in *Beam*, the court concluded that close personal relationships were a factor in deciding that a special litigation committee was not independent.<sup>93</sup> The Oracle board established a Special Litigation Committee (SLC) in response to the derivative action filed by shareholders against the officers and directors.<sup>94</sup> The SLC recommended termination of the litigation.<sup>95</sup> The SLC had the burden of proof to establish

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<sup>86</sup> *Id.* at 1045.

<sup>87</sup> *Id.* at 1046.

<sup>88</sup> *Id.* at 1049–50.

<sup>89</sup> *Id.* at 1050.

<sup>90</sup> *Id.*

<sup>91</sup> *Id.* at 1050–51.

<sup>92</sup> *Id.* at 1055.

<sup>93</sup> *In re Oracle Corp Derivative Litig.* 824 A.2d 917, 938 (Del. Ch. 2003).

<sup>94</sup> *Id.* at 923.

<sup>95</sup> *Id.* at 928.

that it satisfied the independence requirements set forth in *Zapata v. Maldonado*.<sup>96</sup> Focusing on whether the SLC was capable of being impartial and objective in reaching its decision, the court analyzed the ties of two SLC directors, professors at Stanford University, who were asked to investigate the conduct of a fellow director, who also had connections to Stanford.<sup>97</sup> The chairman and CEO was Lawrence Ellison, who was also a large contributor to Stanford.<sup>98</sup>

The court examined the close personal relationships among the directors with the Stanford connections and concluded that there was reasonable doubt as to the independence of the SLC.<sup>99</sup> While acknowledging that the SLC had engaged in extensive work and investigation, the court concluded that the Stanford ties and the relationship with Ellison made the SLC directors beholden to Ellison even though there were no financial ties.<sup>100</sup> Focusing less on whether the directors were in fact dominated or controlled by Ellison, but rather on knowledge of human motivations, the court stated:

Delaware law should not be based on a reductionist view of human nature that simplifies human motivations on the lines of the least sophisticated notions of the law and economics movement. . . . We may be thankful that an array of other motivations exist that influence human behavior; not all are any better than greed or avarice, think of envy, to name just one. But also think of motives like love, friendship, and collegiality, think of those among us who direct their behavior as best they can on a guiding creed or set of moral values.<sup>101</sup>

The court took further notice of the social behavior and structural biases of boards by stating,

corporate directors are generally the sort of people deeply enmeshed in social institutions. Such institutions have norms, expectations that, explicitly and implicitly, influence and channel the behavior of those who participate in their operation. Some things are “just not done,” or only at a cost, which might not be so severe as a loss of position, but may involve a loss of standing in the institution. In being appropriately sensitive to this factor, our law also cannot assume—absent some proof of the point—that corporate directors are, as a general matter, persons of unusual social bravery, who operate

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<sup>96</sup> *Id.*

<sup>97</sup> *Id.* at 929–36.

<sup>98</sup> *Id.* at 932.

<sup>99</sup> *Id.* at 942.

<sup>100</sup> *Id.* at 925.

<sup>101</sup> *Id.* at 938.

heedless to the inhibitions that social norms generate for ordinary folk.<sup>102</sup>

*Beam* and *Oracle* demonstrate the different approaches taken by the Delaware courts in dealing with structural biases. In explaining the different approaches, noting the uniqueness of the SLC, the court in *Beam* writes “[u]nlike the demand-excusal context, where the board is presumed to be independent, the SLC has the burden of establishing its own independence by a yardstick that must be ‘like Caesar’s wife’—‘above reproach.’”<sup>103</sup> The court went on to state “unlike the pre-suit demand context, the SLC analysis contemplates not only a shift in the burden of persuasion but also the availability of discovery into various issues, including independence.”<sup>104</sup>

When shareholders have the burden of demonstrating independence, they must demonstrate with particularized facts more than structural biases.<sup>105</sup> When directors have the burden of demonstrating independence, they must demonstrate impartiality and courts are willing to consider structural biases in assessing independence.<sup>106</sup> Delaware’s approach leaves shareholders at a disadvantage when structural biases limit the ability of shareholders to move a derivative case forward prior to the formation of a special litigation committee established to evaluate the merits of a derivative claim.<sup>107</sup>

#### A. Federal Bifurcation Rules and Common Law Fiduciary Duty

The D-F Act requirements and SEC disclosure mandates will require boards to evaluate and disclose its rationale for a board structure in which the CEO also serves as chairman of the board.<sup>108</sup> In circumstances where the CEO is also the chairman, under SEC rules, a company is permitted to appoint a lead independent director.<sup>109</sup> In such instances, company disclosures must define the responsibilities of the lead director.<sup>110</sup> Requiring companies to disclose and explain its governance policies as it relates to the CEO and chairman provides shareholders with

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<sup>102</sup> *Id.*

<sup>103</sup> *Beam v. Stewart*, 845 A.2d 1040, 1055 (Del. Super. Ct. 2004).

<sup>104</sup> *Id.*

<sup>105</sup> *Id.* at 1048–49.

<sup>106</sup> *Id.* at 1049–51.

<sup>107</sup> *Id.* at 1054.

<sup>108</sup> For an example of recent company disclosures on board leadership see MCDONALD’S CORP., NOTICE OF 2010 ANNUAL SHAREHOLDERS’ MEETING AND PROXY STATEMENT 2 (2010), available at [http://www.aboutmcdonalds.com/etc/medialib/aboutMcDonalds/investor\\_relations0.Par.34096.File.dat/2010%20mcd%20proxy.pdf](http://www.aboutmcdonalds.com/etc/medialib/aboutMcDonalds/investor_relations0.Par.34096.File.dat/2010%20mcd%20proxy.pdf).

<sup>109</sup> Proxy Disclosure Enhancements, *supra* note 19, at 43.

<sup>110</sup> *Id.*

important information on the potential for the CEO to exercise dominance over board decision-making.

Delaware currently has no legislative requirements on the make-up of the board. Delaware common law examines director independence under a duty of loyalty and a demand futility analysis.<sup>111</sup> The analysis focuses on whether a director is interested or independent.<sup>112</sup> In a demand futility analysis, the court assesses whether a director is personally interested in the outcome of the litigation, or whether the director benefits or suffers directly from the outcome of the shareholder litigation.<sup>113</sup> Director independence in a duty of loyalty analysis also includes an assessment by the court of whether the director is dominated by an interested director.<sup>114</sup> In determining whether a director might be beholden to an interested director, Delaware courts have focused on whether there were financial ties between the directors.<sup>115</sup> Although the burden of proof depends on whether the allegations of lack of director independence are at the demand futility or the fiduciary analysis stage of the litigation, Delaware relies on its business judgment rule presumption and enhanced judicial scrutiny of board decisions in circumstances when there is a conflict of interest or breach of the duty of loyalty.<sup>116</sup> Provided an independent board or a committee has performed its duties in good faith, Delaware courts are reluctant to substitute its judgment for that of the board.<sup>117</sup>

While Delaware law permits shareholders to raise issues of domination in the context of assessing director independence, Delaware's fiduciary duty does not permit shareholders to shift the burden to directors to demonstrate that a board leadership structure in which the CEO is also chairman is not a conflict of interest or otherwise a breach of the duty of loyalty.<sup>118</sup> Provided the directors otherwise demonstrate independence and good faith, the board will be entitled to the business judgment rule presumption.<sup>119</sup> Delaware fiduciary law has done little to address directly CEO biases and domination when the CEO holds

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<sup>111</sup> See *In re Tyson Foods, Inc. Consol. S'holder Litig.*, 919 A.2d 563, 582–83 (Del. Ch. 2007) (discussing the *Aronson* test for demand futility and the test for determining whether a duty of loyalty claim survives a motion to dismiss); *In re Oracle Derivative Litig.*, 824 A.2d 917, 939 (Del. Ch. 2003) (discussing the standards set forth in *Aronson v. Lewis* and *Rales v. Blasband*).

<sup>112</sup> *In re Tyson Foods, Inc. Consol. S'holder Litig.*, 919 A.2d at 582.

<sup>113</sup> *Id.*

<sup>114</sup> *Id.*

<sup>115</sup> *In re Oracle Derivative Litig.*, 824 A.2d at 936.

<sup>116</sup> *In re Tyson Foods, Inc. Consol. S'holder Litig.*, 919 A.2d at 582.

<sup>117</sup> *Id.*

<sup>118</sup> *Id.*

<sup>119</sup> *Id.* at 584.

both positions.<sup>120</sup> With improved federal disclosures on why a CEO holds dual positions or appointment of independent lead director, investors can evaluate structural biases in board decision-making.<sup>121</sup> More importantly, it is the opportunity for directors to more fully account for the effects of group think on board decision-making by understanding what social science data reveals about how decisions are made in groups.<sup>122</sup>

#### B. Bifurcation: The Benefit to Shareholders

Prior to passage of the D-F Act and SEC rules on bifurcation, shareholders had limited information on board leadership and structural bias.<sup>123</sup> Federal rules requiring disclosures of board leadership structure benefit shareholders by not only providing better information on board structure, but also by requiring directors to assess its board structure for structural biases and independence.<sup>124</sup> Engaging in a review of its board leadership structure improves directors' fiduciary obligations by ensuring independent directors are able to engage in frank discord without undue management influences.<sup>125</sup> Although companies are not required to separate the CEO and chairman's job, by forcing disclosures, the board must at least engage in an analysis of how its board structure works.<sup>126</sup> Separating the role of the CEO and chairman improves corporate governance by recognizing the social dynamic of board interaction in ways state fiduciary analysis does not.<sup>127</sup> Having the board justify its leadership structure also benefits shareholders in situations where shareholder derivative claims for breach of fiduciary limit the ability of shareholders to use discovery to uncover structural biases.<sup>128</sup> Shareholders may be better able to demonstrate demand futility when the board has disclosed its rationale for a leadership structure that does not separate the roles of chairman and CEO.

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<sup>120</sup> Langevoort, *supra* note 76, at 289–91 (discussing capture and the balance of power between the board and CEO); Paredes, *supra* note 79, at 724–25 (discussing how Delaware corporate law provides that the “[t]he business and affairs of every corporation . . . shall be managed by or under the direction of [the] board of directors,” and thus the CEO has control because the board delegates it to him).

<sup>121</sup> Joseph McCafferty, *Splitting the CEO and the Chair*, BLOOMBERG BUSINESSWEEK (June 12, 2009, 2:08 PM), [http://www.businessweek.com/managing/content/jun2009/ca20090612\\_359612.htm](http://www.businessweek.com/managing/content/jun2009/ca20090612_359612.htm).

<sup>122</sup> See *supra* note 85, and accompanying text.

<sup>123</sup> Proxy Disclosure Enhancements, *supra* note 19, at 4.

<sup>124</sup> *Id.* at 4–5.

<sup>125</sup> *Id.* at 43–44.

<sup>126</sup> *Id.* at 44.

<sup>127</sup> McCafferty, *supra* note 121.

<sup>128</sup> Proxy Disclosure Enhancements, *supra* note 19, at 44.

Bifurcation disclosure requirements are a positive benefit for state corporate governance. Until state corporate law, in particular Delaware, begins to reexamine its rules on board structure, federal securities laws are likely to continue to legislate disclosure requirements to address issues of board group think in decision-making. Bifurcation of the CEO and Chairman moves a bit closer to blurring the complementary balance between federal and state law on governance.

#### CONCLUSION

In 2003, Professor Roe<sup>129</sup> wrote an article in which he argued that the real competition in corporate governance was not between Delaware and other states, but between Delaware and federal securities laws.<sup>130</sup> I agree with Professor Roe's observation. Federal rules continue to use disclosure mandates to affect behavior of corporate managers in their relationship with shareholders. The politics of responding to corporate crises is unlikely to see Congress or the SEC limit its role in effecting corporate governance changes for the public corporation. Congress sought to address specific corporate failures in the D-F Act—governance failures such as highly paid executive compensation in the wake of corporate failures, compensation committees rewarding executives for taking excessive risk, and directors seemingly unwilling to engage in critical analysis of the CEO or management's decisions.<sup>131</sup>

Do the new federal disclosure requirements on corporate governance benefit shareholders under state law? I believe the short answer to this question is yes; however, I am not convinced that the disclosure requirements can achieve improvements in board leadership without a corresponding shift in state corporate governance. The new rules will force the boards of public companies to engage in greater oversight of risk and disclose such risk. More importantly, the disclosures on board leadership structure will likely increase the overall independence of the board, allowing for improvements in frank discussion among board members. Where state fiduciary duty does not address or, as in Delaware, varies depending on the stage of shareholder litigation, shareholders are likely to face litigation disadvantages in a demand futility analysis for independence. State fiduciary

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<sup>129</sup> Professor Mark Roe is a noted scholar, who writes in the areas of corporate law and governance. He is the author of *Strong Managers Weak Owners: The Political Roots of American Corporate Finance*. Professor Roe is currently a professor at Harvard Law School.

<sup>130</sup> Roe, *supra* note 4, at 592.

<sup>131</sup> McCafferty, *supra* note 121.

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duty analysis will continue to be supplemented by federal rules of disclosures. As Congress responds to specific corporate failures, state corporate law can respond to investor concerns with a more methodological, nuanced analysis of corporate conduct. Courts will respect good faith efforts by independent boards, and shareholders can be informed of how compensation committees and their consultants make their decisions. Boards who have an independent source of information with new rules on compensation consultants will continue to have the protection of business judgment rule. So in the end, notwithstanding federal laws' increasing push on state corporate law, the complimentary balance of federal and state law remains.