

Corporate directors face new liabilities

Serving in the corporate board room may be hazardous to a director's financial health, according to a corporate law specialist.

"Corporate America has been hit by a double whammy," said Robert Profusek, a Dallas-based partner specializing in takeovers and corporate governance matters. He is in the international law firm of Jones, Day, Reavis & Pogue.

The twin blows: • A series of court decisions that have significantly eroded the legal protections afforded people who serve on boards of directors, potentially jeopardizing their personal fortunes and reputations. Some have felt forced to resign or refuse to take jobs as directors.

• Companies increasingly are unable to obtain adequate liability insurance for their directors. New legislation will be required to restore the necessary protection, he said.

"THE VERY quality of corporate governance in America could be at stake," Profusek said.

"While the board of directors is ultimately responsible for overseeing the company's profit-making function for its stockholders, a company

and its directors also have other constituencies — including employees, customers and suppliers, and the communities in which the company is located."

Federal and stock exchange rules require that large, publicly owned companies have a majority of directors who are not employed by the company. "Outside" directors, as they are called, bring an unbiased or independent perspective to the company's affairs.

"ONE POSSIBLE outcome of all the uncertainties caused by recent adverse legal developments is that we may end up with professional directors, which is similar to what exists in some other countries," Profusek said.

"However, we would lose much of the benefits of having a board of directors made up of a cross-section of the business community, such as a bank president, the CEO of another public company, or a distinguished business professor. They bring new ideas and enthusiasm to the boardroom."

"Until the current wave of hostile takeovers, the law was such that directors were assured they didn't have any personal liability at stake

In 1985, the Delaware Supreme Court dealt a blow to the financial shield of directors. It imposed personal liability against outside directors for doing something in which they had no personal stake.

when they were acting in their capacity as directors, unless they did something clearly improper or illegal.

"The 'Business Judgment Rule' basically protected directors when they were challenged by stockholders over making decisions that turned out to be wrong after the fact. The idea was that courts really aren't very well equipped to decide in retrospect whether decisions by directors, which frequently must be made with less than perfect information, were right."

OVER THE LAST two years, however, some courts have halted a number of takeover defenses because of directors' alleged breaches of fiduciary duty, he said.

Other courts have ruled that the business judgment rule doesn't really apply in takeover cases because the interests of the directors are necessarily, to some degree, inconsistent with or pitted against the inter-

ests of the stockholders.

"It has been the position of some courts, as well as of the Securities and Exchange Commission, that takeovers are good for everyone, including stockholders. The marketplace is and should be the determinant of affairs. These courts and the SEC, as a result, view almost any defensive action authorized by a target company's board as inherently suspect," Profusek said.

In 1985, the Delaware Supreme Court dealt a blow to the financial shield of directors.

"Trans Union was the first case in which personal liability was imposed against outside directors for doing something in which they really didn't

have any personal stake."

THE DELAWARE Court said the Trans Union directors should be personally liable because they had decided to sell the company in a two-hour meeting without receiving an opinion from an investment banker.

While the case was eventually settled, the court intimated the directors should pay the difference between the offer they approved and the price the company might have commanded on the open market.

"After the Trans Union case was decided, the bottom fell out of the director and officer insurance market," Profusek said.

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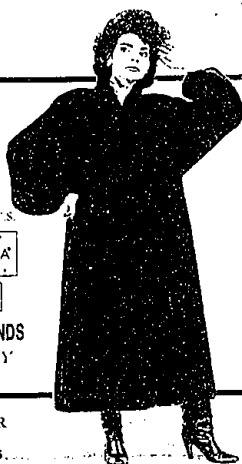
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