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Foreword

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FOREWORD

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The economic recession of the past few years spurred a renewed discussion on the significance of directors' oversight, because of the increased risk corporations took prior to the recession such as heavy investment in derivatives. Substantial commentary suggests that had had directors not been "asleep at the switch" in their duty of oversight there would have been decreased corporate risk, which would have minimized the resulting damage. On October 22, 2012 the *University of St. Thomas Law Journal* hosted Professors Lisa M. Fairfax, Brett H. McDonnell, and Wulf A. Kaal to continue the discussion on the role of a director's duty of oversight. This issue of the *University of St. Thomas Law Journal* bears the fruit of Professor Fairfax's important annual Law Journal Lecture for 2012-2013. We are grateful for her remarks and participation and for the thoughtful responses by Professors Kaal and McDonnell.

In the lead article that follows, *Managing Expectations: Does the Directors' Duty to Monitor Promise More than it can Deliver?*, Lisa Fairfax "grapples with whether we are expecting too much from the duty of oversight."[1] Professor Fairfax begins by discussing the duty of oversight's evolution in the Delaware courts. She then provides three rationales for how the courts' interpretation may undermine directors' oversight compliance: recency, incoherency, and insufficiency. She states:

> As an initial matter, it is possible that the relatively recent emergence of the doctrine [of oversight] may make it difficult to use it as a guide until more time has passed. The relative incoherency of the doctrine also may pose challenges for its ability to provide meaningful guidance to directors seeking to determine how best to comply with the oversight duty. Finally, courts may have fashioned a liability standard that fails to appropriately encourage directors to comply with their oversight duties, potentially rendering fiduciary duty law irrelevant for the purposes of shoring up directors' oversight obligations. As this Part will discuss, these

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1. Lisa M. Fairfax, *Managing Expectations: Does the Directors' Duty to Monitor Promise More than it can Deliver?*, 10 U. ST. THOMAS L.J. 416, 416 (2012).

> defects in the development and articulation of the oversight doctrine do not bode well for efforts at enhancing board oversight.[2]

Professor Fairfax then provides a number of reasons why complying with the duty of oversight may prove difficult for directors, including: (1) the size and complexity of the modern corporation; (2) the unmanageable broad scope of the oversight duty; (3) the incapacity of a director to provide oversight due to increasingly greater responsibilities for a director; and (4) the emphasis on independent directors.[3] Professor Fairfax concludes by asserting that attempts to enhance directors' oversight risks offering "false hope" in the corporate arena by creating unrealistic expectations. In fact, an overemphasis on the "duty to monitor" might instead distract commentators and reformers from attending to other actors and advisors in the corporation and from assessing whether more targeted reforms or responsibilities might produce better results.[4]

Professors McDonnell and Kaal both agree with Professor Fairfax's assertion that the current duty of oversight is unworkable, but differ from Professor Fairfax's thoughts on improving the duty. In *Meeting Lowered Expectations*, Professor McDonnell focuses on the role of outside directors and suggests that outside corporate directors should play a more modest role in the modern corporation.[5] While Professor McDonnell acknowledges the valuable role that independent directors provide, he asserts "there are limits on how much detailed monitoring we can expect independent directors to do."[6] Professor McDonnell approves of the "relatively robust, helpful, and commonsensical common law process"[7] to the duty of oversight's development. He asserts that oversight "may still do some good, especially with a little tweaking."[8] Alternatively, in *A Comparative Perspective on the Limitations of the Duty of Oversight*, Professor Kaal compares the duty of oversight as construed by Delaware courts to the approach taken in Germany. Germany has established much stricter liability standards and is much more willing to second-guess directors' actions.[9] Professor Kaal suggests learning from the German approach, stating that "Delaware's signaling of expected conduct could be dramatically improved with a moderate standard for liability in cases involving breaches of the duty of oversight."[10] This would incentive less risky behavior by directors. But, Professor Kaal

2. *Id.* at 427.
3. *Id.* at 441.
4. *Id.* at 448.
5. Brett H. McDonnell, *Meeting Lowered Expectations*, 10 U. St. Thomas L.J. 449, 453 (2012).
6. *See id.* at 451.
7. *Id.* at 454.
8. *Id.* at 457.
9. Wulf A. Kaal, *A Comparative Perspective on the Limitations of the Duty of Oversight*, 10 U. St. Thomas L.J. 460, 462 (2012).
10. *Id.* at 464–65.

does agree with Professor Fairfax's conclusion that using improvements to oversight in order to enhance corporate governance would be misguided.[11] He suggests instead following a model of Dynamic Regulation – rather than static, inflexible rules – as a way to improve corporate governance.

The trio of articles that follow provide a valuable reminder about the limitations of a singular approach to regulation. Collectively, the articles agree that over-reliance on the directors' oversight duty (at least as currently constructed) is unworkable and will not lead to improved governance. Building on this descriptive analysis, the articles lay the groundwork for normative work to improving corporate governance in various ways.

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11. *Id.* at 465.