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Atherton v. FDIC: The Final Word on Bank Officer and Director Liability

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NOTES & COMMENTS

Atherton v. FDIC: The Final Word on Bank Officer and Director Liability?

I. INTRODUCTION

In the late 1980s, Congress reacted to the growing savings and loan crisis by passing the Financial Institution Reform, Recovery, and Enforcement Act of 1989 (FIRREA). Stories of mismanagement and outright fraud by officers and directors fueled sentiments that their conduct must be controlled to ensure the financial future of savings and loan associations (S&Ls). Buried within the 371 pages of legislation, 12 U.S.C. § 1821(k) announced the standard of care for bank officers and directors and 12 U.S.C. § 1821(d)(2)(A)(i) allowed the Resolution Trust Corporation (RTC) to pursue claims against them personally. Since FIRREA's passage, the ambiguous language of § 1821(k) has spawned extensive commentary and litigation and resulted in a split among the circuit courts.

3. See id. at 1706-07.
   A director or officer of an insured depository institution may be held personally liable for monetary damages in any civil action by [FDIC as 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.

Id.
5. See id. § 1821(d)(2)(A)(i).
Recently, in *Atherton v. FDIC*, the Supreme Court resolved some of the ambiguity. Specifically, the Court held that state law standards of care apply to officers and directors of state and federally chartered S&Ls. In reaching this conclusion, the Court determined that federal common law standards in this area no longer exist. Thus, the *Atherton* decision establishes that bank officers and directors are subject to the § 1821(k) "gross negligence" standard of care, as well as any applicable stricter state law standards of care.

Part II of this Note discusses the facts and holding of *Atherton*. Part III examines the background law and split among the lower courts over the applicable standard of care for bank officers and directors. Part IV analyzes the significance of *Atherton* for bank officers and directors. Finally, Part V concludes that *Atherton* raises as many questions as it answers.

II. STATEMENT OF THE CASE

In *Atherton*, the petitioners were a group of former officers and directors of a failed federal savings association known as City Federal Savings Bank (City Federal). Standing in place of the bank as receiver, the RTC brought this action in 1989 alleging that the officers' actions or omissions amounted to gross negligence, simple
negligence, and breach of fiduciary duty.\textsuperscript{17} Specifically, the RTC alleged that the officers and directors considered, approved, and oversaw the acquisition, development, and construction loans resulting in $100 million in damages to City Federal.\textsuperscript{18}

At trial, the defendant officers and directors argued that § 1821(k) of FIRREA established a gross negligence standard of care and, therefore, was intended to forbid actions amounting to only simple negligence.\textsuperscript{19} Agreeing with the officers and directors, the district court dismissed all but the gross negligence claims.\textsuperscript{20}

On interlocutory appeal to the Third Circuit,\textsuperscript{21} the court considered whether § 1821(k) preempts state law or supersedes federal common law.\textsuperscript{22} The Third Circuit found that the RTC could “seek recovery from officers and directors under all ‘other applicable laws,’ including the less forgiving negligence and fiduciary duty standard of care under state law and federal common law.”\textsuperscript{23} The court stated that the plain meaning of the statute’s savings clause indicated that any law could still apply after § 1821(k).\textsuperscript{24}

\textsuperscript{17} See id.
\textsuperscript{18} See RTC v. CityFed Fin. Corp., 57 F.3d 1231, 1237 (3d Cir. 1995), rev’d sub nom. Atherton v. FDIC, 117 S. Ct. 666 (1997). The RTC’s complaint alleged that the defendants failed to “discharge their duties and obligations properly as officers and directors.” Id. at 1236-37. Specifically, the defendants allegedly violated their duty of care by:

\begin{itemize}
\item (1) failing to obtain and verify necessary financial information from borrowers;
\item (2) maintaining inadequate appraisal procedures;
\item (3) consistently loaning funds based on excessively high loan-to-value ratios that violated mandatory limits placed on such ratios;
\item (4) making repeated imprudent long-range commitments to future lending or funding;
\item (5) failing to monitor loan disbursements and the ongoing status of projects and loans;
\item (6) improperly waiving risk limitations and other conditions contained in loan commitments to certain borrowers;
\item (7) failing to require and verify that necessary permits and approvals were obtained before funding the loans;
\item (8) improperly assessing the value of guarantees given as security for the loans; and
\item (9) not requiring adherence to the bank’s lending policies and procedures.
\end{itemize}

Id. at 1237.

\textsuperscript{19} See Atherton, 117 S. Ct. at 669.
\textsuperscript{20} See id.

\textsuperscript{21} See id. The consolidated appeal to the Third Circuit was brought by City Federal, a federal depository institution, and United Savings and Loan of Trenton, a New Jersey state chartered thrift. See CityFed, 57 F.3d at 1235. United Savings did not seek certiorari following the Third Circuit’s ruling that § 1821(k) does not supplant stricter state laws. See Lowy & Lowy, supra note 6.

\textsuperscript{22} See CityFed, 57 F.3d at 1235.
\textsuperscript{23} Id. at 1237.
\textsuperscript{24} See id. at 1238; see also infra note 58 (quoting the language of the savings clause).
Furthermore, the court noted that the legislative history indicates that Congress, reacting to the growing trend in the states to protect officers and directors from liability, intended to pass legislation that would ensure that the RTC had a cause of action against negligent individuals.\textsuperscript{25} Thus, according to the Third Circuit, the City Federal defendants could be subject to federal common law that was stricter than gross negligence.\textsuperscript{26} Consequently, the Third Circuit reversed the district court’s ruling and concluded that the RTC could pursue any claim available under federal common law.\textsuperscript{27} By finding that federal common law still existed to govern the standard of liability for bank officers and directors,\textsuperscript{28} the Third Circuit departed from the holdings of other circuits.\textsuperscript{29}

The Supreme Court granted certiorari to settle the dispute between the circuits regarding the standard of care applicable to bank officers and directors under § 1821(k).\textsuperscript{30} Justice Breyer, writing for a nearly unanimous court,\textsuperscript{31} began the analysis by determining whether federal common law, in the absence of § 1821(k), would articulate the standard of corporate governance for federally chartered banks.\textsuperscript{32} Although the Court established a federal common law standard in \textit{Briggs v. Spaulding},\textsuperscript{33} this holding and most federal common law did

\begin{itemize}
\item \textsuperscript{25}See \textit{CityFed}, 57 F.3d at 1238-39.
\item \textsuperscript{26}See \textit{id.} at 1249. The Third Circuit also held that the United Savings defendants could be subject to state laws applying a stricter standard than gross negligence. See \textit{id.} These defendants were no longer a party at the time of the \textit{Atherton} decision. See \textit{ supra} note 21.
\item \textsuperscript{27}See \textit{CityFed}, 57 F.3d at 1249.
\item \textsuperscript{28}See \textit{id.} Part of the court’s reasoning for retaining federal common law was to avoid an anomalous situation where bank officers and directors who are sued before receivership are subject to a simple negligence standard, but bank officers and directors who are sued after receivership are held to a gross negligence standard, if § 1821(k) supersedes federal common law. See \textit{id.} at 1246. The court found that \textit{Briggs v. Spaulding}, 141 U.S. 132 (1891), announced the federal common law standard of care for bank officers and directors. See \textit{CityFed}, 57 F.3d at 1247 n.16.
\item \textsuperscript{29}See \textit{infra} notes 107-32 and accompanying text.
\item \textsuperscript{30}See \textit{infra} notes 107-32 and accompanying text (discussing the interpretation of § 1821(k) by the circuit courts).
\item \textsuperscript{31}See \textit{Atherton}, 117 S. Ct. at 677. Justices O’Connor, Scalia, and Thomas concurred in part and in the judgment, except for the majority’s reliance on legislative history. See \textit{id.} at 676-77 (O’Connor, J., concurring in part and concurring in the judgment). They felt no need to rely on contradictory legislative history when a plain reading of the statute clearly points out the meaning of the savings clause in § 1821(k). See \textit{id.}
\item \textsuperscript{32}See \textit{id.} at 669-70.
\item \textsuperscript{33}141 U.S. 132 (1891). 
\end{itemize}
not survive *Erie Railroad Co. v. Tompkins*. The Court defined federal common law as "a rule of decision that amounts, not simply to an interpretation of a federal statute or a properly promulgated administrative rule, but, rather to the judicial ‘creation’ of a special federal rule of decision." The Court maintained that the creation of a special rule is only justified when a "‘significant conflict between some federal policy or interest and the use of state law’" exists. To determine whether the *Briggs* standard survived *Erie*, the Court examined each argument made by the Federal Deposit Insurance Corporation (FDIC) for the existence of a significant conflict that would justify the use of federal common law.

First, the FDIC argued that federal common law would provide uniformity among federally chartered financial institutions. The Court rejected this argument on two grounds. First, uniformity would only be furthered by this federal rule for half of all banks, since only half are federally chartered. Second, the federal banking system has always functioned with disparities in the corporate governance standard. Therefore, the Court concluded that no overriding federal interest would be served by a federal common law rule.

Next, the FDIC argued that only federal common law could properly govern federally chartered banks. The Court traced the history of banks in the United States and noted that since 1870 federally chartered banks have been subject to state law. The

34. 304 U.S. 64, 78 (1938) (holding that “[t]here is no federal general common law”).
36. *Id.* (quoting O’Melveny & Myers v. FDIC, 512 U.S. 79, 80 (1994)).
37. *See id.* at 671.
38. *See id.* ("[A] federal standard that increases uniformity among [federally chartered banks] would increase disparity with [state chartered banks]."). The Court cited a 1995 FDIC study that found approximately 1600 federally chartered and 1500 state chartered institutions. *See id.*
39. *See id.* The Court said that state chartered banks are subject to the various laws of each state. *See id.* Likewise, federally chartered banks are subject to the various lower court interpretations of the *Briggs* standard. *See id.* Furthermore, the Court noted that the Comptroller of the Currency “permits considerable disparity in the standard of care applicable to federally chartered banks other than savings banks (which are under the jurisdiction of the OTS).” *Id.*
40. *See id.* at 670-71.
41. *See id.* at 671.
42. *See id.* at 672. The Court cited *National Bank v. Commonwealth* as the first case holding that federal banks “are subject to the laws of the [s]tate, and are governed in their
historical use of state laws to govern the activities of federal banks indicated to the Court that no significant conflict with federal policy exists that justifies the use of federal common law.\footnote{43}

The FDIC also argued that applying the "internal affairs doctrine" in the banking context would result in the use of federal common law.\footnote{44} This doctrine, normally used to settle conflict of law issues for corporations, suggests that the controlling law is that of the state of incorporation.\footnote{45} By analogy, the FDIC would apply federal common law to federally chartered banks.\footnote{46} The Court, however, found that this argument did not meet the legal requirement for the creation of federal common law.\footnote{47} In fact, the Court noted that this analogy could even support a counter argument for the application of state law.\footnote{48}

Finally, the FDIC noted that the Office of Thrift Supervision (OTS)\footnote{49} has applied the federal common law standard of \textit{Briggs} to savings and loan officers and directors.\footnote{50} However, the Court was not persuaded by this observation because the OTS was not employing this standard based on any significant conflict between daily course of business far more by the laws of the [s]tate than of the nation." See \textit{id.} (citing \textit{National Bank v. Commonwealth}, 76 U.S. (9 Wall.) 353, 362 (1869)). After \textit{National Bank}, several cases have applied state laws to federally chartered institutions. See, \textit{e.g.}, \textit{California Fed. Sav. & Loan Ass'n v. Guerra}, 479 U.S. 272, 280 (1987) (holding that state employment discrimination law applies to a federally chartered savings and loan association); \textit{Anderson Nat'l Bank v. Luckett}, 321 U.S. 233, 252-53 (1944) (holding that a Kentucky escheat statute applies to deposit accounts in a national bank); \textit{Wichita Royalty Co. v. City Nat'l Bank}, 306 U.S. 103, 107 (1939) (holding that state tort law applies for a claim against directors of a national bank).

\footnote{43. See \textit{Atherton}, 117 S. Ct. at 672. The Court's history lesson on the application of state laws to federally chartered institutions does not distinguish between banks and savings associations. See \textit{id.}}

\footnote{44. See \textit{id.} at 673.}

\footnote{45. See \textit{id.}}

\footnote{46. See \textit{id.}. This analogy had been drawn by several of the lower courts. See \textit{infra} notes 124-32 and accompanying text (discussing \textit{RTC v. Chapman}, 29 F.3d 1120, 1123-24 (7th Cir. 1994)).}

\footnote{47. See \textit{Atherton}, 117 S. Ct. at 673 ("To find a justification for federal common law in this argument, however, is to substitute analogy or formal symmetry for the controlling legal requirement, namely, the existence of a need to create federal common law arising out of a significant conflict or threat to a federal interest.").}

\footnote{48. See \textit{id.}. An analogy can be drawn between the state of incorporation of an ordinary business and the state of the principal place of business or main office for federal banking institutions. See \textit{id.}}

\footnote{49. The OTS has the authority to fine or remove from office the officers and directors of a savings and loan for breach of fiduciary duty. See \textit{id.}}

\footnote{50. See \textit{id.}}
federal and state laws or pursuant to authority delegated by Congress.\textsuperscript{51}

Having considered and rejected the FDIC's arguments for federal common law, the Court went even further to point out that the FDIC is not representing the federal government, but "acting only as a receiver of a failed institution."\textsuperscript{52} Furthermore, the Court found the interest at stake in this case to be far weaker than the instances when the Court has invoked federal common law.\textsuperscript{53}

After concluding that a federal common law standard does not exist,\textsuperscript{54} the Court next questioned whether the federal statutory law could supplant state law standards of care.\textsuperscript{55} In answer, the Court stated that the federal ""gross negligence' standard provides only a floor—a guarantee that officers and directors must meet at least a gross negligence standard. It does not stand in the way of a stricter standard that the laws of some [s]tates provide."\textsuperscript{56} The Court based this decision on the plain language of the statute and the legislative history of FIRREA.\textsuperscript{57}

The Court stated that a literal reading of the savings clause in § 1821(k)\textsuperscript{58} supports the interpretation that stricter state law statutes can determine the standard of care.\textsuperscript{59} At issue was the meaning of statutory language protecting the FDIC's ability to pursue "any right ... under other applicable law."\textsuperscript{60} The FDIC argued that Congress

\begin{enumerate}
\item See id. The OTS, rather than promulgating a federal regulation, interpreted the "pre-existing judge-made federal common law standard." Id.; see also infra notes 149-51 and accompanying text.
\item Atherton, 117 S. Ct. at 673. In support of this proposition, the Court noted its recent decision in O'Melveny & Myers v. FDIC, 512 U.S. 79 (1994). In O'Melveny & Myers, the Court decided that state law, rather than federal common law, governed the tort liability standard as applied to attorneys for a federally insured S&L. See id. at 84-85.
\item See Atherton, 117 S. Ct. at 673-74. The Court cited several cases creating federal common law that it judged to involve much more compelling circumstances. See id. For instance, the Court mentioned cases involving conflicts between states, with federal officials or officers, and relationships with foreign countries. See id.
\item More accurately, the Briggs standard did not survive Erie. See id. at 674.
\item See id.
\item Id.
\item See id. at 674-76.
\item The last sentence of the statute is popularly referred to as the savings clause. It reads: "Nothing in this paragraph shall impair or affect any right of the Corporation [meaning the FDIC/RTC] under other applicable law." 12 U.S.C. § 1821(k) (1994).
\item See Atherton, 117 S. Ct. at 675.
\item 12 U.S.C. § 1821(k).
\end{enumerate}
only meant to preserve any other rights in the FIRREA statute.\textsuperscript{61} However, the Court rejected this limited interpretation and broadly read the phrase to protect any other action available in any statute, state or federal.\textsuperscript{62} In support of its broad interpretation, the Court noted the historical context surrounding the passage of the FIRREA legislation.\textsuperscript{63} After the failure of many federally insured savings associations and large payments by the federal government to insured bank depositors, the federal government had an interest in trying to recover these funds from negligent officers and directors.\textsuperscript{64} At the same time, states concerned with attracting competent individuals for corporate positions passed legislation "designed to limit preexisting officer and director negligence liability." Therefore, explained the Court, history supports the view that Congress responded to this state legislation by creating a minimum standard of care that would preserve the federal government's ability to recover funds from negligent officers and directors.\textsuperscript{65}

The Court cited statements by congressional members that supported this reading of the statute,\textsuperscript{66} but also identified contradictory statements, which they dismissed as inconsistent with the overall legislative history.\textsuperscript{67} The Court primarily relied on a Senate report that specifically addressed the interpretation of §1821(k).\textsuperscript{68} The report reads: "This subsection does not prevent the FDIC from pursuing claims under [state] law or under other applicable [federal law, if such law permits the officers or directors

\begin{itemize}
\item \textsuperscript{61} See \textit{Atherton}, 117 S. Ct. at 675.
\item \textsuperscript{62} See \textit{id}.
\item \textsuperscript{63} See \textit{id}.
\item \textsuperscript{64} See \textit{id}.
\item \textsuperscript{65} \textit{Id}. These statutes are referred to as "insulation" statutes. \textit{See infra} notes 100-01 and accompanying text.
\item \textsuperscript{66} See \textit{Atherton}, 117 S. Ct. at 675.
\item \textsuperscript{67} See \textit{id}. For instance, Senator Riegle said: "[T]he establishment of a Federal standard of care is based on the overriding [federal interest in protecting the soundness of the FDIC fund and is very limited in scope. It is not a wholesale preemption of longstanding principles of corporate governance." See \textit{id}. (quoting 135 CONG. REC. S7,150-51 (daily ed. June 19, 1989)).
\item \textsuperscript{68} See \textit{id}. Senator Sanford stated that he supported "provisions relating to [state laws affecting the liability of officers and directors of financial institutions" because "these changes are essential if we are to attract qualified officers and directors to serve in our financial institutions." See \textit{id}. (quoting 135 CONG. REC. S7,150 (daily ed. June 19, 1989)).
\item \textsuperscript{69} See \textit{id}.
\end{itemize}
of a financial institution to be sued for violating a lower standard of care, such as simple negligence." Although this language explicitly supports the Court's interpretation, the Court acknowledged that the report was published after enactment of the law. In prior cases, the Court stated that such legislative history does not carry "substantial weight" in interpreting statutes, but differentiated this report on the grounds that it had been circulated in Congress several weeks before the vote.

Finally, the Court dismissed a "complicated argument" made by the petitioner to displace federal common law with an absolute standard set by § 1821(k). Starting with the "universally conceded fact" that the § 1821(k) "gross negligence" standard applies to both state and federal banks, City Federal assumed that without a state statute the federal common law would control. Because the federal common law standard is closer to simple negligence, City Federal argued that the statute would actually be less strict and, therefore, should be interpreted to set an absolute standard instead of a minimum standard. The Court responded to this argument by pointing out that it had already rejected City Federal's assumption that federal common law would control in the absence of a federal statute. In addition, the Court noted that § 1821(k) does not consider federal and state banks separately. Therefore, the Court concluded that the congressional "silence" on the difference

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70. Id. (quoting S. REP. No. 101-19, at 318 (1989)).
71. See id. at 675.
72. See id. (citing Clarke v. Securities Indus. Ass'n, 479 U.S. 388, 407 (1987)). In Clarke, the Court interpreted a provision of the McFadden Act, but refused to place "substantial weight" on comments inserted by Representative McFadden into the Congressional Record ten days after Congress passed the Act. See Clarke, 479 U.S. at 406-07.
73. See Atherton, 117 S. Ct. at 675.
74. See id. at 676. The officers and directors argued that federally chartered banks should not be subject to state law and that § 1821(k) establishes an absolute standard of gross negligence rather than a floor. See id.
75. Id. Apparently City Federal is referring to the lower court decisions that applied § 1821(k) to both state and federally chartered institutions. See infra notes 107-32 and accompanying text.
76. See Atherton, 117 S. Ct. at 676.
77. See id.
78. See id.
79. See id.
indicated that the statutory language brings both kinds of banks within its scope.  

In summary, the Court decided that § 1821(k) of FIRREA establishes a minimum standard of care of gross negligence for the officers and directors of savings associations. The Court held that the statute, rather than supplanting state law, establishes a minimum standard that state law can raise. Furthermore, the federal statutory minimum standard of care applies to state and federally chartered associations alike.

III. BACKGROUND LAW

Over one hundred years ago, the Supreme Court first considered the standard of care that should be applied to the officers and directors of a national bank. In Briggs v. Spaulding, a receiver for a national bank sought to hold several officers and directors liable for losses incurred by the bank on risky loans and general mismanagement of the institution. The Court held that “directors must exercise ordinary care and prudence in the administration of the affairs of a bank, and that this includes something more than officiating as figure-heads.” Furthermore, the Court stated that the standard of care for bank directors was “that which ordinarily prudent and diligent men would exercise under similar circumstances.”

Briggs became the basis of the federal common law regarding bank officers and directors, but the lower courts interpreted the

80. See id.
81. See supra notes 30-80 and accompanying text.
82. See supra notes 54-80 and accompanying text.
83. See supra notes 79-80 and accompanying text.
84. 141 U.S. 132 (1891).
85. See id. The receiver alleged that the directors failed to keep accurate books, have regular meetings, and oversee the actions of the bank’s president. See id. at 137. They were accused of “passive negligence,” the failure to act when a duty existed, but not of “positive misfeasance.” See id. at 151.
86. Id. at 165.
87. Id. at 152. Although announcing this standard, the Court found that the directors in question had not breached their duty because, in large part, they had been directors for a short period of time before the insolvency and did not have adequate time to examine and supervise the operations of the bank officers. See id. at 166.
Court's broad language in various ways. Some courts treated the standard of liability as one of ordinary negligence because of the sensitive nature of the business of banking. Others have treated the standard as one of gross negligence and have found liability only in situations involving director omission or inaction. Regardless of the interpretation, the standard announced in Briggs appeared to be the starting point for the statutory language in many states.

Under any formulation of the standard of care, historically few directors were found liable, absent fraud or self-dealing, due to the business judgment rule. Under this rule, a presumption exists that corporate officers and directors will not be held liable for business decisions resulting from an exercise of business judgment. Typically, to have the benefit of the business judgment rule presumption, a director or officer must: (1) make the decision in good faith; (2) honestly believe the decision is in the best interests of the corporation; and (3) make an informed decision using due care in the decision-making process. The purpose of the rule is to allow officers and directors to take the risks inherent in business without fear of liability for well-informed, but ultimately unwise decisions.

88. See Fischer, supra note 2, at 1719. After this decision, directors were expected to balance their supervisory duties against their right to rely on subordinates. See id. The Briggs formulation of the standard of care was so flexible that “similar fact patterns may result in liability or absolution, depending not only on the objective circumstances and facts but also on the judge . . . and other inscrutable factors.” Id. at 1719.


90. See Stevens & Nielson, supra note 6, at 186 (citing examples where the Briggs standard is articulated as an ordinary negligence standard, but applied as a gross negligence standard).

91. See Fischer, supra note 2, at 1716 n.51 (citing twelve states that have adopted “ordinary prudent” and “under similar circumstances” phrases for the standard of liability, like the language in Briggs).


94. See id.

95. See id.
Although commonly applied by courts as a state common law doctrine in the general business context, the rule has been unevenly applied to the business of banking.  

Following a controversial 1985 Delaware Supreme Court decision, states feared that the business judgment rule would no longer provide adequate protection to officers and directors. The court, in *Smith v. Van Gorkom*, applying a “gross negligence” standard, held that the directors of Trans Union Corporation breached their duty of care. After *Van Gorkom*, states became concerned about attracting competent officers and directors if the standard of care was too strict. Consequently, state legislatures either revised existing corporate laws or passed new laws limiting director liability. These “insulating statutes” generally limited director liability to “reckless, willful, and wanton boardroom misconduct.”

96. See Schooner, supra note 89, at 181. Although no Supreme Court case has directly confronted this issue, some federal courts have applied the business judgement rule to bank directors. See, e.g., FDIC v. Harrington, 844 F. Supp. 300, 306-07 (N.D. Tex. 1994); RTC v. Vanderweele, 833 F. Supp. 1383, 1387 n.4 (N.D. Ind. 1993). These cases were decided prior to *Atherton*, which never mentions the business judgement rule in interpreting § 1821(k).

97. 488 A.2d 858 (Del. 1985).

98. See id. The court held that the decision of the board of directors of Trans Union Corporation to approve a cash-out merger proposal was “not the product of an informed business decision.” Id. at 864. The directors, all men of considerable business experience, spent less than two hours discussing the approval of a takeover bid. See id. at 869. Commentators have not agreed on the basis of the court’s rationale, but the decision prompted much discussion on the application of the business judgement rule and the interpretation of the “gross negligence” standard of care adopted by the *Van Gorkom* court. See, e.g., Daniel R. Fischel, *The Business Judgement Rule and the Trans Union Case*, 40 BUS. LAW. 1437 (1985) (arguing that the directors’ actions should have been protected by the business judgment rule); Jonathan R. Macey & Geoffrey P. Miller, *Trans Union Reconsidered*, 98 YALE L.J. 127 (1988) (arguing that *Van Gorkom* should not be analyzed under the business judgment rule but under takeover law).


100. See id. Delaware has significant influence over the corporate law of other jurisdictions. See, e.g., Mullen v. Academy Life Ins. Co., 705 F.2d 971, 973 n.3 (8th Cir. 1983) (“Courts of other states commonly look to Delaware law . . . for aid in fashioning rules of corporate law.”). As a result, many commentators feared that following *Van Gorkom* would damage the business judgment rule. See Lam, supra note 99, at 1043-44 & n.55.

Then in the late 1980s, public and congressional concern over the savings and loan crisis led to the quick passage of FIRREA.\(^{102}\) Federally insured financial institutions were failing at an alarming rate, and Congress saw the need to try to recover some of the federal funds used for bailouts and to fix blame on the responsible parties.\(^{103}\) Section 1821(k), as added by FIRREA, was specifically debated only on the Senate floor.\(^{104}\) Perhaps due to the legislation's hasty passage, the courts and commentators have debated the seemingly clear language of § 1821(k).\(^{105}\) The main dispute arose over the preemptive effect of this statute on state law and federal common law.\(^{106}\)

The Tenth Circuit became the first federal court of appeals to address the preemptive effect of § 1821(k) in *FDIC v. Canfield*.\(^{107}\) In that case, the FDIC sued the officers and directors of a state chartered and federally insured bank under Utah state law which established a simple negligence standard of care.\(^{108}\) The district court found that § 1821(k) preempts state law and dismissed the claims.\(^{109}\) The Tenth Circuit reversed, and agreeing with the FDIC, held that § 1821(k) preempts only state laws that require a higher degree of culpability than gross negligence.\(^{110}\) Relying on the "evident meaning" of the statutory language to reach this conclusion, the court refused to consider policy issues.\(^{111}\)

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102. See Fischer, *supra* note 2, at 1746-48. Under pressure from President Bush and voters, Congress hurried the passage of legislation in response to the savings and loan crisis. See *id.* at 1746. In fact, the haste with which the bill was debated in the Senate was itself the object of Senate debate. See *id.* The House of Representatives took only two months to pass its version of the FIRREA legislation. See *id.* at 1751. The section by section analysis of the bill was not available until both chambers passed the legislation. See *id.* at 1752; see also *supra* notes 68-73 and accompanying text.


104. See Fischer, *supra* note 2, at 1751. The Senate bill version of § 1821(k) was revised at the urging of a number of Senators concerned that the strictness of the original language would make attracting the best officers and directors difficult. See *id.* The House of Representatives spent more time debating the FIRREA legislation but did not discuss officer and director liability. See *id.* at 1751-52.

105. See *supra* note 6 and accompanying text; *infra* notes 107-32 and accompanying text.


107. 967 F.2d 443 (10th Cir. 1992).

108. See *id.* at 444.

109. See *id.*

110. See *id.* at 446.

111. See *id.* The court stated: "Unlike a state legislature making such a policy choice,
The Ninth Circuit also considered the issue of the preemptive effect of § 1821(k) in the case of state chartered banks. Following the reasoning of the Tenth Circuit, the court in FDIC v. McSweeney held that the statute was not intended to establish a uniform national standard of gross negligence for federally insured, state chartered banks. Once again, a circuit court allowed the FDIC to pursue a claim against the officers and directors of a failed savings and loan based on the state standard of simple negligence.

After these two cases, the trend seemed clear for state chartered banks: officers and directors could be held liable for acts amounting only to simple negligence. Then the Seventh Circuit was called upon to decide if § 1821(k) preempts federal common law for federally chartered banks. In RTC v. Gallagher, the RTC sued the officers and directors of a federally chartered bank in Illinois. The defendants made a familiar argument—§ 1821(k) establishes a national standard of gross negligence for the officers and directors of federally chartered banks. The RTC countered that § 1821(k) does not preempt federal common law or state law that establishes a higher standard of care than gross negligence. The district court dismissed the claims, holding that state law did not establish a standard that applied to federally chartered banks. The RTC sought interlocutory appeal to determine if § 1821(k) preempts federal common law.

The Seventh Circuit was the first court of appeals to entertain this precise issue. The court acknowledged that federal common law applies only in a "few and restricted" situations, and if Congress has spoken directly on a question, no federal common law can

we are in no position to weigh these factors." Id. at 448.
112. 976 F.2d 532 (9th Cir. 1992).
113. See id. at 536-37.
114. See id. at 538.
115. See RTC v. Gallagher, 10 F.3d 416, 418 (7th Cir. 1993).
116. 10 F.3d 416 (7th Cir. 1993).
117. See id. at 418.
118. See id.
119. See id.
120. See id.
121. See id. at 418-19 (noting that no other circuit court had directly addressed this issue, but that a majority of district courts agreed that § 1821(k) preempts federal common law).
exist.\textsuperscript{122} Relying on the plain language of the statute, the legislative history, and Supreme Court rulings concerning the creation of federal common law, the Seventh Circuit held that Congress intended to preempt federal common law standards of negligence.\textsuperscript{123}

Having lost the federal common law approach to pursue claims stricter than gross negligence, the RTC next argued for the application of stricter state laws to federally chartered banks. In \textit{RTC v. Chapman},\textsuperscript{124} the Seventh Circuit considered whether state laws could apply to federally chartered banks in the context of § 1821(k).\textsuperscript{125} Because the court agreed that § 1821(k) does not preempt state laws,\textsuperscript{126} the court faced a choice of laws issue.\textsuperscript{127} The court answered this question by analogy to a common principle in corporate law known as the "internal affairs doctrine."\textsuperscript{128} Under this principle, the law of the state of incorporation is applied to a corporation in recognition of the "benefits of using one rule of law."\textsuperscript{129} Consequently, the court decided that federal law should apply to a federally chartered bank.\textsuperscript{120} Under \textit{Gallagher} that federal law was § 1821(k).\textsuperscript{131} The consequence of this holding was that the RTC had to prove gross negligence for federally chartered banks in order to establish director or officer liability.\textsuperscript{132}

\textsuperscript{122} See \textit{id.} at 419 (quoting Wheeldin v. Wheeler, 373 U.S. 647 (1963)).
\textsuperscript{123} See \textit{id.} at 424. However, the court specifically refrained from deciding if § 1821(k) preempts state law. See \textit{id.}
\textsuperscript{124} 29 F.3d 1120 (7th Cir. 1994).
\textsuperscript{125} See \textit{id.} at 1121. The court said "Here we go again." \textit{Id.}
\textsuperscript{126} See \textit{id.} at 1122. The court noted that two other decisions, \textit{McSweeney} and \textit{Canfield}, held that § 1821(k) does not preempt state law, but made no attempt to distinguish these cases on the ground that they concern state chartered banks. See \textit{id.; see also supra} notes 107-14 and accompanying text (discussing \textit{Canfield} and \textit{McSweeney}).
\textsuperscript{127} See \textit{Chapman}, 29 F.3d at 1122.
\textsuperscript{128} See \textit{id.} The court indicated that the internal affairs doctrine is accepted by all the states and by the Supreme Court. See \textit{id.}
\textsuperscript{129} \textit{Id.}
\textsuperscript{130} See \textit{id.} at 1123.
\textsuperscript{131} See \textit{id.} \textit{Gallagher} was also decided in the Seventh Circuit, so that precedent bound the court. See \textit{supra} notes 115-23 and accompanying text.
\textsuperscript{132} See \textit{Chapman}, 29 F.3d at 1123.
IV. SIGNIFICANCE OF THE CASE

The Atherton decision appeared to settle a long running controversy in the circuit courts regarding the proper interpretation of § 1821(k) for federally chartered banks. The decision that state law controls both state and federally chartered institutions, as long as the state standard meets a floor level of gross negligence, appeared simple at first glance. However, a second look at the consequences of the holding indicates that the controversy surrounding § 1821(k) is far from settled.

Prior to the Atherton decision, a number of commentators argued that federal common law, as established in the Briggs line of cases, should control the standard for bank officer and director liability. The arguments supporting the application of federal common law had the attractive features of logic and simplicity on their side: state law governs state chartered savings and loans, and federal common law governs federally chartered savings and loans. However, interpretations of the Briggs standard have varied due to the ambiguous language used in the case. Regardless of these arguments, the Supreme Court clearly stated that federal common law is no longer viable in this area. By abolishing this source of law, the Supreme Court added some certainty to determining the standard of care for bank officers and directors.

While disagreeing on the exact standard, practitioners and commentators both recognize the need for certainty in attracting the most skilled people to fill director positions. The Court clarified

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133. See, e.g., Ramirez, supra note 89, at 648 & nn.116-18 (arguing that the Briggs case established a federal common law standard of ordinary care and should be applied to directors of federally insured banks). But see Lowy, supra note 92 (suggesting that the Briggs case established a standard of care, but that the regulatory agencies should promulgate regulations in order to make the state of the law clear).

134. See supra notes 41-43 and accompanying text.


136. See supra notes 32-54 and accompanying text.

137. See, e.g., Martin Lowy & Peter Lowy, D&O Duty of Care After Atherton Case: The Story Isn’t Over, BANKING POL’Y REP., Mar. 17, 1997, available in LEXIS, BANKNG Library, BKNPOL File; see also Dennis & Feinberg, supra note 6, at 768 (suggesting that corporate directors will shy away from board positions in corporations chartered in states
that applicable state law standards should be applied to federally chartered savings and loans. The key question that remains unclear is which state law standard is applicable. In the few states that have codified laws that specifically address the standard for bank officers and directors, the Atherton decision will be perfectly clear. However, many more states have only general corporate law standards for officers and directors. Some of these statutes allow the articles of incorporation to be drafted to eliminate director liability for certain specified conduct. Presumably, these provisions can only limit liability to gross negligence, the floor established after Atherton. Other states specifically codify the standard for all corporations. Commentators would apply general corporate statutes, without hesitation, to bank officers and directors. Arguably, however, the business of banking requires special consideration. State legislatures may prefer to debate the opposing views on officer and director liability and formulate a specific statute. States without any codification of corporate or banking laws rely on the case law announced in their courts, although this law is frequently very old and less than clear. For

with strict or unclear standards of care).

138. See supra notes 55-80 and accompanying text.
139. See, e.g., N.Y. BANKING LAW § 7015 (McKinney 1997); GA. CODE ANN. § 7-1-490 (1997).
140. When the statutory requirement is phrased as "good faith" or "prudent person," state common law may clarify whether this is a gross or simple negligence standard. See, e.g., N.C. GEN. STAT. § 55-8-30 (Supp. 1997); Myers & Chapman, Inc. v. Thomas G. Evans, Inc., 374 S.E.2d 385, 394 (N.C. 1988) ("As the Court of Appeals correctly determined, this portion of the instruction was erroneous because it suggested ... that directors and managing officers are chargeable with an omniscient knowledge of the company's affairs and are liable for damages to third parties resulting from simple negligence. This is not the law of North Carolina.").
143. See, e.g., Fischer, supra note 2, at 1740-41; Gormon, supra note 135, at 661.
144. See Stevens & Nielson, supra note 6, at 193-231 (surveying all state standard of care laws, codified and common law, and interpreting which level of care the state applies, simple or gross negligence).
officers and directors in those states, the standard will be even more
difficult to ascertain. Even if each state announces clear laws, the
standard will vary from state to state. This ruling may provide
states, hoping to attract the banking industry, an opportunity to pass
clear laws that are no stricter than gross negligence.

However, even if state legislatures were to clarify their
banking laws, the courts will still have to determine which state’s law
to apply. Due to interstate branching, a federally chartered bank
could have branches in many states with laws that could conceivably
differ. The site of the main office, the main branch, the CEO’s
office, or the corporate office could serve as indicators of the state
law that appropriately governs a federally chartered bank’s officers
and directors. Because Atherton only summarily addresses the
choice of law issue between the states, litigation is likely to continue
on this point.

The Atherton Court brushed aside the suggestion that federal
agency regulations could determine the standard of care for officers
and directors. Prior to Atherton, at least one commentator

145. See id. The Court specifically addressed this issue and determined that century old
case law announced that federally chartered banks could be subject to state law. See
Atherton, 117 S. Ct. at 672. The implicit suggestion is that this case law should make state
law standards of care for officers and directors applicable to federal banking institutions
100 years later. As a matter of law this appears true, but as a matter of practicality the
premise is not as sound.

146. See Lowy & Lowy, supra note 137.

147. See id. The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994,
Pub. L. No. 103-328, 108 Stat. 2338 (codified at scattered sections of 12 U.S.C), provides
that the “home state” of a federally chartered institution is “[t]he state in which the main
not specifically reference laws regarding officers and directors, it may nonetheless provide
guidance in which state law to apply. Applied pursuant to the internal affairs doctrine, the
law of the state in which a bank’s main office is located would most likely control in
determining officer and director liability. See Atherton, 117 S. Ct. at 673 (“[C]ourts
applying the internal affairs doctrine could find (we do not say that they will find) that the
state closest analogically to the state of incorporation of an ordinary business is the state in
which the federally chartered bank has its main office . . . .”).

148. See Lowy & Lowy, supra note 137; see also Stanley I. Langbein, U.S. Supreme
Court rejects FDIC’s assertion that federal common law trumps state law in determining
standard of liability for officers and directors of banks, Nat’l L.J., Mar. 10, 1997, at B6,
B6 (“The [Atherton] decision did not resolve all issues confronting institution officers and
directors, and it raises far-reaching questions . . . .”).

149. In dicta, the Atherton Court indicated that regulations promulgated by the OTS
would not be binding without congressional authority. See Atherton, 117 S. Ct. at 673. In
the past, the Office of the Comptroller of the Currency published guidelines on bank officer
and director liability. See OCC Interpretive Letter 483, Personal Liability for Monetary
suggested regulations as a viable solution, in light of the Office of the Comptroller of the Currency’s power to regulate other banking activities. Congress could give this suggestion life by clearly assigning the regulatory power to the OTS or another federal agency. In a broader sense, the Atherton decision may signal an end to pro-FDIC treatment following the savings and loan crisis.

V. CONCLUSION

Depository institutions, both state and federally chartered, and the bank regulatory agencies have struggled with the meaning of § 1821(k) since its enactment. The Supreme Court clarified some long-standing debates in Atherton, which held that federal common law does not apply in questions of officer and director liability, but state law standards stricter than gross negligence do apply. Officers and directors now face a choice of law question as to which state standard applies. In the past, the debate over § 1821(k) focused on the level of care required of the officers and directors. However, as a practical matter, the more important issue for banks seeking to attract competent directors, and the counsel advising those directors, is to be sure of the exact expectations of the law, no matter how strict. Arguably, the Atherton decision has not clarified the law in that respect. Even with the Atherton decision, officers and

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150. See Lowy & Lowy, supra note 137.
151. By alluding to the possibility in its opinion, the Court may even be inviting Congress to specifically delegate regulatory authority. See Atherton, 117 S. Ct. at 673 (“The FDIC does not claim, however, that these OTS statements, interpreting a pre-existing judge-made federal common-law standard (i.e., that of Briggs) themselves amount to an agency effort to promulgate a binding regulation pursuant to delegated authority.”). Previously, the Court held that if a statute is ambiguous with regard to a specific issue, then the agency’s interpretation will be given considerable deference, as long as the interpretation is based on a permissible construction. See Chevron, U.S.A. v. Natural Resources Defense Council, 467 U.S. 837 (1984). The Atherton court did not cite this case, but one commentator raised the issue of its applicability. See Langbein, supra note 148, at B6.
152. See Langbein, supra note 148, at B6. The O’Melveny & Myers case represents another recent defeat for the FDIC. See id.; see also supra note 52 and accompanying text.
153. See supra notes 107-32 and accompanying text.
154. See supra notes 30-83 and accompanying text.
155. See supra notes 137-48 and accompanying text.
156. See supra notes 30-83, 107-32 and accompanying text.
directors seeking clarity can only look to lawmakers, state or federal, to supply sure answers through new legislation.157

STACEY TAYLOR KERN

157. The Chairperson of the House Banking Subcommittee on Financial Institutions and Consumer Credit, Representative Roukema, announced in her tentative agenda plans to hold hearings regarding the Atherton decision. See Roukema Subcommittee has Aggressive Banking Agenda for 1997-98, BANKING POL'Y REP., Feb. 17, 1997, available in LEXIS, BANKNG Library, BNKPOL File. Representative McCollum introduced House Bill 220 on January 7, 1997, which would specifically allow a business judgment rule defense for officers and directors of depository institutions. See id. For the complete text of the current proposed bill, see Legislation in the House of Representatives (visited Feb. 24, 1998) <http://thomas.loc.gov>. As of February 1998, the bill was still in subcommittee and no hearings had been convened. See id.