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Overcoming the *Rippy* Effect: Why the North Carolina Business Corporations Act Should Allow Permissive Officer Exculpation*

INTRODUCTION

What if, in the popular board game Monopoly, "Get Out of Jail Free" cards could only be drawn by a predetermined segment of players?[1] Further, what if the opportunity to draw the liberating vouchers was based on an arbitrary distinction[2] that had no bearing on past or future performance? In all likelihood, players who could draw "Get Out of Jail Free" cards would engage in riskier and potentially more rewarding behavior than their opportunity-less counterparts because they might be able to "avoid jail" even after an unfortunate roll of the dice. Eventually, inducing opportunity-less gamers to play at all might prove problematic.

If corporate management can be considered the game—and directors and officers the players—then the Court of Appeals for the Fourth Circuit in *F.D.I.C. ex rel. Cooperative Bank v. Rippy*[3] recently interpreted North Carolina law to dictate that only directors have the chance to draw the little orange cards. In *Rippy*, the court held that while bank *directors* were not liable for ordinary negligence, sufficient evidence was presented to rebut the presumption that bank *officers* had acted on an informed basis.[4] The *Rippy* court interpreted the exculpatory provision as allowing exculpation for directors[5]—but not

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1. The Parker Brothers game allows players to buy, rent, and sell properties in an effort to bankrupt other players and become the wealthiest player. Parker Bros., *Monopoly Parker Brothers Real Estate Trading Game*, HASBRO.COM (2016), http://www.hasbro.com/common/instruct/monins.pdf [https://perma.cc/H2KV-XZKX]. "Get Out of Jail Free" cards allow players who would otherwise be forced to miss a turn waiting in "jail" to circumvent that obstacle and continue playing without interruption. *Id.* In a game predicated on generating money by "passing go" each turn, "Get Out of Jail Free" cards provide a significant advantage. *See id.*

2. For example, if there were a rule that permitted only players with last names beginning with letters A–H to be eligible for the bonus cards.

3. 799 F.3d 301 (4th Cir. 2015).

4. *Id*. at 313.

5. The *Rippy* court found that exculpation was not available to directors in cases of gross negligence. *Id.* This Recent Development concerns only breaches of care pursuant to ordinary negligence. *See infra* note 85.

officers.[6] Central to the *Rippy* court's finding of no liability for directors was their analysis of an exculpatory provision contained in the bank's bylaws and permitted by the North Carolina Business Corporations Act ("NCBCA").[7] Although the bank's directors and officers engaged in the same negligent behavior, only the officers were exposed to liability.[8]

This Recent Development argues that the NCBCA[9] should be amended to allow permissive officer exculpation in corporate charters. Analysis proceeds in four parts. Part I examines the *Rippy* facts and holding, and explains the genesis and evolution of exculpatory clauses. Part II argues that (1) North Carolina's management-insulating provisions leave a problematic "gap" in liability coverage for officers, (2) the marginal deterrent effect against officer misbehavior via liability pursuant to non-exculpation is likely outweighed by the costs of enforcing a non-officer exculpating scheme, and (3) the current lack of officer exculpation allows for inequitable and confusing outcomes as between directors and officers. Part III addresses counterarguments, and Part IV concludes by recommending that the NCBCA be revised to allow for officer exculpation.

I. BACKGROUND

A. *Facts and Procedural Posture of* Rippy

Cooperative Bank ("Cooperative") opened in 1898 and focused its operations on single-family housing loans for nearly a century.[10] Determined to increase bank assets, Cooperative's Board of Directors shifted its focus to commercial real estate loans in 2002.[11] Because the FDIC[12] backed Cooperative, the FDIC performed annual reviews[13] of Cooperative's underwriting and loaning

6. *Rippy*, 799 F.3d at 313.
7. *Id.* at 312; *see also* N.C. GEN. STAT. § 55-2-02 (2015).
8. § 55-2-02.
9. N.C. GEN. STAT. § 55-2-02 outlines permissive exculpation for directors in corporate charters and is a sensible place to position the proposed amendment. *See infra* notes 29–35 and accompanying text.
10. *Rippy*, 799 F.3d at 313.
11. *Id.*
12. The Federal Deposit Insurance Corporation ("FDIC") encourages borrowing and loaning activity because "insured deposits are backed by the full faith and credit of the United States Government." 12 U.S.C. § 1828(a)(1)(B) (2014).
13. The FDIC performed reviews in conjunction with the North Carolina Commission of Banks ("NCCB"). *Rippy*, 799 F.3d at 307.

practices.[14] While these initial reports[15] were relatively favorable, each report recommended changes and all of the feedback got progressively worse.[16] The final report,[17] condemning both Cooperative's cursory approval of nine large loans to land developers and their rampant use of equity-less "lot loans,"[18] gave Cooperative the worst possible score in all but one category.[19]

Cooperative did not address the issues highlighted in the reports.[20] During the Great Recession in 2009, Cooperative closed[21] and named the FDIC as receiver.[22] The FDIC subsequently sued

14. *Id.* at 308.

15. "Cooperative was scored in each of the following categories: Capital, Asset Quality, Management, Earnings, Liquidity, and Sensitivity to Market Risk. The examination categories collectively are commonly referred to by the acronym CAMELS, and are scored on scale [sic] from 1–5, with '1' being the best and '5' being the worst." *Id*. at 307–08.

16. Five reports are relevant. First, a 2006 FDIC report gave Cooperative a "2" rating in each of the CAMELS categories and recommended that Cooperative address issues in credit administration, underwriting, audit practices, risk management, and liquidity. *Id.* at 308. A 2007 NCCB investigation yielded a substantially similar report. *Id.* Third, an external review by Credit Risk Management (CRM), in addition to finding that Cooperative had been slow to address its previously identified issues, suggested that Cooperative review its credit files on a more regular basis. *Id*. In 2008, CRM issued a fourth report, again criticizing loan documentation and monitoring, and for the first time, assessing failing grades to certain loans. *Id.* Finally, the FDIC and NCCB issued a joint report in November 2008, giving the lowest possible rating to Cooperative in all but one of the CAMELS categories. *Id.*

17. *Id.* (FDIC and NCCB Joint Report).

18. A "[m]anufactured home lot loan means a loan for the purchase or refinancing of a portion of land acceptable to the Secretary as a manufactured home lot." 24 C.F.R. § 201.2 (2015). Cooperative encouraged customers to utilize lot loans by presenting investment seminars. After attending the investment seminar, optimistic customers became certain that he or she could buy a building lot without putting up any money for two years. The idea was to "flip" the lot to someone else as property values continued to climb. Floyd Norris, *Failed Bank's Broken Vows Mean Little*, N.Y. TIMES Sep. 19, 2014, http://www.nytimes.com/2014/09/19/business/in-ruling-that-favors-failed-bank-promises-meant-little.html [https://perma.cc/587U-5H92].

19. *Rippy*, 799 F.3d at 307–08 (stating that Cooperative scored "fives" in the Capital, Asset Quality, Management, Earnings, and Liquidity categories, and a "four" in the Sensitivity to Market Risk category).

20. *Id.* at 313. The FDIC's expert witness stated that both directors and officers "approved loans over the telephone, without first examining the relevant documents." *Id.*

21. According to a review conducted by the FDIC Office of Inspector General, the FDIC suffered losses of over $200 million due to Cooperative's failure. *Id.* at 309.

22. The FDIC is statutorily authorized to function in two separate and distinct capacities. "[T]he [FDIC, as a corporation] shall insure the deposits of all insured banks," 12 U.S.C. § 1821(a)(1) (2012), and the FDIC shall "as receiver of a closed national bank . . . have the right to appoint an agent or agents to assist it in its duties as such receiver." § 1822(a). *See Rippy*, 799 F.3d at 307 n.1 (describing FDIC's receiver capacity).

Cooperative's directors[23] and officers[24] for negligence, gross negligence, and breach of fiduciary duties.[25] When the district court granted summary judgment in favor of the defendants,[26] the FDIC appealed to the Fourth Circuit.[27]

B. Holdings

The *Rippy* court[28] held that, while North Carolina law contemplates suits against bank directors and officers sounding in ordinary negligence,[29] Cooperative's directors were shielded from liability by an exculpatory provision contained in Cooperative's articles of incorporation.[30] Conversely, the *Rippy* court observed simply that "[Cooperative]'s exculpatory provision does not cover [Cooperative's] officers."[31] Because the officers were shielded from liability by the business judgment rule[32] but not by the articles of

23. The nine director-defendants were: Willetts (chief executive officer), Burton (director), King (director), Wright (director), Rippy (director), Fensel (director), Bridger (director), Hundley (director), and Burrell (director). *See* Complaint at 2–3, FDIC v. Willetts, 48 F. Supp. 3d 844 (E.D.N.C. 2014) (7:11-cv-00165-BO); Lance Duroni, *FDIC Loses $40M Suit Against NC Community Bank Execs*, LAW360 (Sept. 12, 2014, 7:48 PM), http://www.law360.com/articles/576912/fdic-loses-40m-suit-against-nc-community-bank-execs [https://perma.cc/QC6S-D9DE].

24. The officers were: Executive Vice-President of Mortgage Lending Bridger and Chief Operating Officer Burrell, who both attended almost all board meetings. Complaint, *supra* note 23, at 3.

25. *Rippy*, 799 F.3d at 308.

26. "The Court finds that defendants are entitled to the business judgment rule's protection as a matter of law and indisputable fact. Therefore the Court enters judgment against plaintiff's claims for negligence and breach of fiduciary duty." FDIC v. Willetts, 48 F. Supp. 3d 844, 851 (E.D.N.C. 2014) *aff'd in part, vacated in part, rev'd in part sub nom. Rippy*, 799 F.3d at 301.

27. *Rippy*, 799 F.3d at 309–10.

28. Throughout this Recent Development, "*Rippy* court" refers to the United States Court of Appeals for the Fourth Circuit and "*Willetts* court" refers to the Eastern District of North Carolina.

29. *Rippy*, 799 F.3d at 311.

30. "The exculpatory clause protects directors from monetary liability unless the directors 'knew or believed [that their acts or omissions] were *clearly* in conflict' with [Cooperative]'s best interests." *Id*. at 312–13 (quoting N.C. GEN. STAT. § 55-2-02(b)(3) (2012)).

31. *Rippy*, 799 F.3d at 313.

32. The business judgment rule is a common law presumption that "in making a business decision the directors . . . acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company." Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984); *see also* Constance Frisby Fain, *Corporate Director and Officer Liability*, 18 U. ARK. LITTLE ROCK L.J. 417, 439 (1996) (examining the business judgment rule's development in conjunction with the duty of care concept); Stephen P. Lamb & Joseph Christensen, *Duty Follows Function: Two Approaches to Curing the Mismatch Between the Fiduciary Duties and Potential Personal Liability of Corporate Officers*, 26 NOTRE DAME J.L. ETHICS & PUB. POL'Y 45, 51 (2012) ("The

incorporation, the *Rippy* court found that the FDIC had presented adequate evidence to rebut the initial presumption that the officer-defendants acted on an informed basis.[33] The officers, the *Rippy* court held, could be personally liable for simple negligence.[34]

Cooperative's exculpatory provision *did not* cover officers because it *could not* cover officers under current North Carolina law.[35] While the nine defendants were accused of essentially the same acts and omissions,[36] the statutory limitations on permissive exculpation in the NCBCA precluded Cooperative's officers from receiving the same level of protection as their director colleagues.[37] Hence, *Rippy* effectively highlights the "gap" in liability coverage between directors and officers that can arise in duty of care cases. To better understand why the liability gap should be closed, some background information regarding the origins of director exculpation is required.

C. Exculpation as a Response to Van Gorkom

The lack of officer exculpation in North Carolina[38] is best explained as an accident of history and should be conceptualized as a product of *Smith v. Van Gorkom*.[39] In *Van Gorkom*, the chairman of the board and CEO Van Gorkom was faced with a decision to sell the company.[40] After cursory negotiations with a single bidder, Van

business judgment rule sets the fundamental parameters within which control can be exercised. It forms a sort of compact between the stockholders and the management to whom they are entrusting their capital. The compact is that management will be permitted to use the stockholders' capital to operate the corporation in their best judgment without second-guessing by the stockholders (using the courts as the vehicle for such second-guessing) so long as management does so in pursuit of the corporation's best interests. In other words, the stockholder gives up his wealth to the corporation and irrevocably confers discretion on management to employ that wealth profitably.") (internal citations omitted); Lawrence A. Hamermesh & A. Gilchrist Sparks III, *Corporate Officers and the Business Judgment Rule: A Reply to Professor Johnson*, 60 BUS. LAW. 865, 870 (2005) (arguing that the business judgment rule should be applied to corporate officers).

33. *Rippy*, 799 F.3d at 313.

34. *Id.*

35. N.C. GEN. STAT. § 55-2-02(b)(3) (2015) (allowing for permissive exculpation of directors but not officers).

36. *Rippy*, 799 F.3d at 314. Of the nine negligently approved commercial real estate (CRE) loans, officers and directors approved eight of them together. Complaint, *supra* note 23, at 14.

37. *See infra* Section II.A.

38. The North Carolina statute *is* the Model Business Corporations Act provision that follows the Delaware pattern.

39. 488 A.2d 858 (Del. 1985), *overruled by* Gantler v. Stephens, 965 A.2d 695 (Del. 2009).

40. *Id.* at 865.

Gorkom presented the board with a proposed merger at $55 per share.[41] Following a two-hour oral presentation, the board decided to sell the company.[42] The Delaware Supreme Court ultimately held that by failing to adequately deliberate about the proposed merger, the directors breached their duty of care.[43]

In response to this holding and in an attempt to protect directors, the Delaware legislature adopted Rule 102(b)(7),[44] which allows for director (but not officer)[45] exculpation if a court finds that the director-defendant did not breach the duty of loyalty. Commentators have suggested that 102(b)(7) effectively overruled the effect of *Van Gorkom*,[46] but such assertions give short shrift to the potential[47] liability of officers in some duty of care cases.[48] While *Van Gorkom* exposed both officers and directors, 102(b)(7) and its progeny, for reasons discussed below,[49] only protects directors. If *Van Gorkom*, by analogy, entirely removed "Get Out of Jail Free Cards" from the corporate governance game, then Rule 102(b)(7) reintroduced cards that only directors could use. Hence, assertions that director-exculpating provisions wholly erase the effect of *Van Gorkom* are premature because officers are still partially exposed.[50]

D. *The Lack of Officer Exculpation: An Accident of History?*

There are at least two reasons why Rule 102(b)(7), and parallel state laws (including North Carolina's) that have followed the rule[51] exclude officers from permissive exculpation: (1) the decision of the

41. *Id.* at 866–68.

42. *Id.* at 868–69.

43. *Id.* at 874.

44. For the purposes of this Recent Development, Rule 102(b)(7) claims are used to generally describe claims based on director exculpation.

45. "The view was that [102(b)(7)] did not . . . extend exculpation to officers, except insofar as an officer was 'exercis[ing] the authority of a director.' Moreover, the Delaware Supreme Court all but foreclosed that argument when it noted in *Gantler* that '[a]lthough legislatively possible, there currently is no statutory provision authorizing comparable exculpation of corporate officers.' " Lamb & Christensen, *supra* note 32, at 58.

46. *See, e.g.*, *id.* at 56–57.

47. While "[t]he exclusion of officers from exculpation has so far been a sleeping dog, . . . if and when it wakes, . . . it w[ill] be destructive to the rational incentive structures reclaimed and rebuilt after *Van Gorkom*." *Id.* at 47.

48. *See, e.g.*, FDIC v. Loudermilk, 984 F. Supp. 2d 1354, 1361–62 (N.D. Ga. 2013) (holding officers liable for breaching their duty of care by failing to maintain appropriate ratios of speculative and low-risk loans).

49. *See infra* Section I.D.

50. As one commentator has noted, "the chilly winds of *Smith v. Van Gorkom* still blow through the boardroom." Paul Graf, *A Realistic Approach to Officer Liability*, 66 BUS. LAW. 315, 336 (2011).

51. *See supra* note 38.

Van Gorkom court to limit its holding to director liability and (2) Delaware's (pre-2004) pro-officer jurisprudence of personal jurisdiction.[52]

Because *Van Gorkom* imposed liability on directors, it was directors—particularly outside directors[53]—who sought relief.[54] Because most corporate officers at the time were simultaneously serving as directors, "there seemed to be little need for extending protection to officers *qua* officers."[55] While the director/officer distinction may not have been crucial in the *Van Gorkom* analysis, *Rippy*[56] and other decisions[57] leave little doubt about contemporary courts' willingness to distinguish between officers and directors in duty of care cases.

A second reason for officer exclusion in Delaware's (and North Carolina's) exculpatory statute can be explained by examining the law of personal jurisdiction. Delaware passed a sequestration statute that allowed plaintiffs to sequester stock that directors owned in the subject corporation if directors did not appear in litigation proceedings.[58] Directors challenged this statute in *Shaffer v. Heitner*, where the Court struck it down as violative of the Fourteenth Amendment's Due Process Clause.[59] To rectify the defects in their sequestration statute, the Delaware legislature passed Section 3114, which provided that persons who accept service *as a director* are deemed to have consented to Delaware jurisdiction.[60] However, "[a]bsent traditional bases of personal jurisdiction, . . . Delaware courts [still] could not hale *officers* of Delaware corporations into their courts under Section 3114—officers would be able to cite *Shaffer* as precluding the exercise of such jurisdiction."[61] In 2004, an

52. Shaffer v. Heitner, 433 U.S. 186 (1977); *see* text accompanying *infra* notes 58–67.

53. An outside director is "[a]ny member of a company's board of directors who is not an employee or stakeholder in the company." *Outside Director Definition*, INVESTOPEDIA, http://www.investopedia.com/terms/o/outsidedirector.asp#ixzz3r90YJ1DO [https://perma.cc/VGF4-GWBK].

54. Dennis R. Honabach, Smith v. Van Gorkom*: Managerial Liability and Exculpatory Clauses—A Proposal to Fill the Gap of the Missing Officer Protection*, 45 WASHBURN L.J. 307, 307 (2006).

55. *Id.*

56. *See supra* notes 29–34 and accompanying text.

57. *See, e.g.*, McPadden v. Sidhu, 964 A.2d 1262, 1274–76 (Del. Ch. 2008) (holding non-director CEO liable for negligence while affirming efficacy of director-exculpating clause).

58. Act of July 7, 1977, ch. 119, 61 Del. Laws 328, 328 (codified at DEL. CODE ANN. tit. 10, § 3114(a) (2015)); Lamb & Christensen, *supra* note 32, at 60.

59. Shaffer v. Heitner, 433 U.S. 186, 216–17 (1977).

60. 61 Del. Laws at 328.

61. Lamb & Christensen, *supra* note 32, at 60.

amendment provided that persons who accept service *as an officer* of a Delaware corporation after January 1, 2004, are subject to Delaware jurisdiction in the same way as directors.[62]

The historical reasons for categorically excluding officers from exculpation, while never logically compelling, apply now with less force than ever. First, some modern corporate governance structures routinely require officers to perform directorial functions while remaining non-director officers.[63] Hence, while failing to distinguish between officers and directors for the purposes of exculpation eligibility may not have been terribly problematic at the time of *Van Gorkom*, the contemporary corporate governance structure represented in *Rippy* undoubtedly highlights the problems inherent in such a failure to so distinguish today. Further, the statutory restraints that limited the ability of plaintiffs to hale officer defendants into court no longer exist.[64] While plaintiffs' historical statutory inability to hale officers into court may have justified officers' original exclusion from exculpation, the removal of plaintiff limitations means that exculpation for officers is no longer a redundancy. Given these developments and the growing number of states that have amended their laws to allow officer exculpation,[65] the lack of permissive officer exculpation generally[66]—and in North Carolina specifically[67]—is best explained as a readily amendable accident of history.

II. WHY PERMISSIVE OFFICER EXCULPATION MAKES SENSE

Given the defects of 102(b)(7) and its progeny, this Recent Development argues that the NCBCA should be amended to allow permissive officer exculpation for at least three reasons. First, the lack of officer exculpation leaves a legally significant gap in liability coverage for officers. Second, while the gap between officers and directors is significant, the marginal effect on officer behavior that

62. Act of June 30, 2003, ch. 83, sec. 3, § 18-213(f), 74 Del. Laws 213, 213 (2003).

63. *See infra* Section II.C.

64. *See infra* Section II.C.

65. Several states have adopted permissive exculpation for officers: Maryland, Nevada, New Hampshire, New Jersey, Utah, and Virginia. *See* MD. CODE ANN., CORPS. & ASS'NS §§ 2-104(b)(8), 2-405.2 (LexisNexis 2015), MD. CODE ANN., CTS. & JUD. PROC. § 5-418 (West 2015); NEV. REV. STAT. § 78.138(7) (West 2015); N.H. REV. STAT. ANN. § 293-A:2.02(b)(4) (2016); N.J. STAT. ANN. § 14A:2-7(3) (West 2016); UTAH CODE ANN. § 16-10a-840(4) (West 2015); VA. CODE ANN. § 13.1-692.1 (2011), respectively.

66. *See generally* MARK A. SARGENT & DENNIS R. HONABACH, D&O LIABILITY HANDBOOK (West ed., Oct. 2015) (discussing various state provisions).

67. *See* N.C. GEN. STAT. § 55-2-02(b)(3) (2015) (exculpation allowed only for directors); § 55-8-51 (indemnification available to directors and officers).

potential liability for negligence via non-exculpation may have is likely outweighed by the costs of enforcing the current statutory scheme. Third, the current lack of officer exculpation allows for inequitable and confusing outcomes as between directors and officers.

A. *North Carolina's Business Corporations Act Leaves a Problematic "Gap" in Liability Coverage for Officers*

North Carolina's Business Corporations Act insulates directors from liability to a greater extent than it insulates officers. Directors may be exculpated[68] *and* indemnified,[69] while officers may only[70] be indemnified.[71] While both exculpation and indemnification are management-insulating devices, the differences between exculpation and indemnification are more than semantic. Exculpation is superior to indemnification as a protective shield because (1) exculpation is effective regardless of the defendant company's solvency,[72] (2) indemnification covers only "reasonable expenses" incurred in the case of a settlement,[73] and (3) exculpated defendants accused of ordinary negligence may be able to move for dismissal at the motion-to-dismiss stage of litigation.[74]

First, exculpation is superior to indemnification because, unlike indemnification agreements, the efficacy of exculpatory clauses is not dependent on company solvency.[75] As others have noted, the

68. N.C. GEN. STAT. § 55-2-02 (2015) ("The articles of incorporation may set forth any provision that under this Chapter is required or permitted to be set forth in the bylaws, and *may* also set forth: . . . *A provision limiting or eliminating the personal liability of any director* arising out of an action whether by or in the right of the corporation or otherwise for monetary damages for breach of any duty as a director. No such provision shall be effective with respect to (i) acts or omissions that the director at the time of such breach knew or believed were clearly in conflict with the best interests of the corporation.") (emphasis added).

69. § 55-8-51.

70. Insurance, while available to officers, does not cover suits brought against officers by the corporation. *See infra* note 155.

71. § 55-8-42(e).

72. *See infra* notes 75–78 and accompanying text.

73. *See infra* notes 79–80 and accompanying text.

74. *See infra* notes 81–84 and accompanying text.

75. J. Phil Carlton & M. Guy Brooks, *Corporate Director and Officer Indemnification: Alternative Methods for Funding*, 24 WAKE FOREST L. REV. 53, 58 (1989); *see also* Ronald E. Mallen & David W. Evans, *Surviving the Directors' and Officers' Liability Crisis: Insurance and the Alternatives*, 12 DEL. J. CORP. L. 439, 466 (1987) ("The failing of any indemnification agreement is that even if such an agreement is valid, its significance depends upon the financial stability of the corporation. For the established, financially solid corporation indemnification agreements afford meaningful and reliable protection for directors and officers. For the newly formed or thinly capitalized company, the protection of the indemnity agreement may be illusory. Many

deficiency of indemnification is that the "offer [to indemnify] is only as good as the ability and willingness of the corporation to pay."[76] When corporations become insolvent, as Cooperative did,[77] corporate officers seeking to enforce indemnity claims necessarily compete with other creditors.[78] No such problem exists for exculpated defendants.

Second, exculpation is superior to indemnification because in North Carolina, indemnified (but not exculpated) defendants must pay the "unreasonable" costs incurred in any litigation proceedings that do not end in a final adjudication.[79] Unlike only indemnified defendants, exculpated persons may avoid litigation of the messy "reasonableness" question and receive protection from *all* costs related to the litigation and settlement of the matter.[80]

Third, exculpatory clauses may provide defendants with tactical litigation advantages which indemnification does not. If exculpated, directors accused of duty of care breaches may successfully move for dismissal without expending the resources necessary for a trial.[81] While the paucity of non-Delaware case law regarding director exculpation makes North Carolina's future adjudication of 102(b)(7) claims less than certain,[82] Delaware's allowance of exculpated director-defendants to move for dismissal at the outset of cases suggests that North Carolina courts may follow suit.[83] Absent exculpation, officers are denied the tactical litigation advantages

lawsuits against directors and officers are brought because the financial failure of the corporation leaves them as the only potentially deep pockets.").

76. Carlton & Brooks, *supra* note 75, at 58.

77. *See supra* note 21.

78. Carlton & Brooks, *supra* note 75, at 58.

79. N.C. GEN. STAT. § 55-8-51(e) (2015) ("Indemnification permitted under this section in connection with a proceeding by or in the right of the corporation that is concluded without a final adjudication on the issue of liability is *limited to reasonable expenses incurred in connection with the proceeding*.") (emphasis added).

80. *See id*.

81. *See* Richard B. Kapnick & Courtney A. Rosen, *Using Exculpatory Clauses in Defending Against Breach-of-Fiduciary-Duty Claims*, 24:22 CORP. OFFICERS & DIRECTORS LIABILITY: ANDREWS LITIG. REPORTER 1, 3 (Apr. 27, 2009).

82. For example, state courts in Illinois and Texas, while dismissing suits against exculpated director-defendants, have not expressly relied on exculpatory clauses to do so. *See* Shaper v. Bryan, 864 N.E.2d 876, 879 (Ill. App. Ct. 2007) (basing dismissal on the plaintiffs' failure to allege facts sufficient to rebut presumption of business judgment rule); Elloway v. Pate, 238 S.W.3d 882, 896 (Tex. Ct. App. 2007) (holding that the plaintiff failed to produce evidence of defendants' gross negligence).

83. A New York court, applying Delaware law, emphasized that the "great deference given to the existence and legal effect of the exculpatory provision" seen in Delaware cases like *Malpiede v. Townson* greatly influenced the analysis dismissing the complaint. Kensington Int'l Ltd. v. Hiner, No. 602748/03, 2006 N.Y. Misc. LEXIS 9362, at *14 (N.Y. Sup. Ct. Aug. 29, 2006).

exculpatory clauses may provide and must further litigate duty of care claims.[84]

B. *Excluding Officers from Exculpation Is More Costly Than It Is Worth*

Because the costs of statutorily precluding officers from permissive exculpation likely outweigh the benefits that potential liability for negligence has on officer behavior, permissive officer exculpation should be allowed. Further, because the enforcement of an officer's duty of care[85] ultimately comes via litigation,[86] a system using litigation as a check on behavior is justified only if it accomplishes deterrence, compensation, or punishment.[87] While it is probable that exposure to potential liability deters some officers from negligent behavior, the important question, as Professor Honabach[88] notes, is whether the "marginal benefit of improved decision-making [is] greater than the sum of the cost of increased caution in decision-making and the cost of actual litigation necessary to make the threat of litigation credible."[89] This Recent Development asserts that those two costs—decision-making caution and actual litigation—make the preclusion of officers from permissive exculpation more expensive than it is worth.

Because many powerful deterrents of negligent officer behavior already exist,[90] measuring the exact impact that potential liability (via non-exculpation) for negligent acts has on officer behavior is difficult. Despite the continued prevalence of corporate officer negligence in the presence of non-litigation based deterrents, few doubt that such deterrents nevertheless exist and influence officer behavior.[91] When

84. *See generally* Kapnick & Rosen, *supra* note 81 (describing how exculpatory clauses can be used to defend against breach of duty claims).

85. The relevant officer behavior regards breaches of care, not loyalty. Exculpating officers for breaches of loyalty would violate public policy and create obviously perverse incentives for officers to self-deal or otherwise be disloyal. This Recent Development does not advocate for exculpation—permissive or otherwise—in such cases.

86. Honabach, *supra* note 54, at 332.

87. *Id.*

88. Professor Honabach is a leading scholar on director and author liability and a joint author of West's D&O Liability Handbook. *See supra* note 66.

89. Honabach, *supra* note 54, at 334.

90. *Id.* at 332. Such deterrents include: loss of reputation, loss of employment, desire to conform to cultural norms, and a desire to comport with ethical standards. In publicly traded companies, significant disclosures mandated by the SEC likely further deter negligent officer behavior. *See generally* Matthew R. King et. al., *Securities Fraud*, 46 AM. CRIM. L. REV. 1027, 1028–29 (2009) (discussing SEC disclosure requirements).

91. Honabach, *supra* note 54, at 332–33.

considering the existing and cost-free deterrents already in place,[92] the additional value of holding officers liable for ordinary negligence seems marginal at best.[93]

Even if holding officers liable by withholding exculpation adds significant deterrence-based value, its benefits are still likely outweighed by its costs because some risk-taking will be shifted to directors.[94] Statutory schemes where directors but not officers can be exculpated "simply encourage officers to place more decisions in the hands of the board, and to take fewer, and less risky, initiatives on their own, so as to avoid liability."[95] This makes delegation from the board to officers challenging and makes board service more time-intensive and costly to corporations.[96] It also may encourage officers, when they do make discretional decisions, to be overly cautious in their decision making to the detriment of the corporation.[97]

Rippy highlights the costly shift in risk-taking, from officers to directors, sometimes engendered by schemes exculpating only directors.[98] In *Rippy*, the two non-director officers were the vice president of mortgage lending and the chief operating officer[99]—positions requiring technical expertise and financial acumen. Conversely, six director-defendants, according to the complaint,[100] had no such expertise yet still participated in the loan approval process.[101] Would the decision-making process and structure have

92. *See supra* note 90.

93. This Recent Development is not examining the effect of non-exculpation on officer behavior in a vacuum. Hence, the relevant inquiry concerns the *marginal* effect that non-exculpation has on officer behavior *within the context of the current statutory scheme*. Crucially, the current officer protections (i.e. D&O insurance, indemnity, and the business judgment rule) reduce the value of non-exculpation as a deterrent because each of those protections overlap to some extent with the protections exculpation provides. In other words, adding permissive exculpation to the protections already available to officers will likely have little effect on their behavior. Paradoxically, the more officers are already protected, the more it makes sense (from a cost-benefit paradigm) to allow permissive exculpation. While the benefits of withholding exculpation (in the current statutory scheme) are small, the high costs of withholding exculpation (and seeking to impose liability) stay the same.

94. Hamermesh & Sparks, *supra* note 32, at 875. ("[A] default rule that would place officers at substantially greater risk of care-based liability than the risk faced by directors *would* impinge upon the board's managerial prerogative[.]").

95. *Id.*

96. *Id.*

97. Honabach, *supra* note 54, at 333. Of course, a lack of exculpation will not always encourage cautious behavior.

98. FDIC *ex rel.* Coop. Bank v. Rippy, 799 F.3d 301, 313 (4th Cir. 2015).

99. Complaint, *supra* note 23, at 3.

100. *Id.* at 2–3.

101. *Rippy*, 799 F.3d at 313.

looked differently if the non-director officers were exculpated? While the answer to this question is difficult to ascertain, it seems likely that a reason[102] for the non-director officers' unwillingness to lead the loan-approval process may have been their lack of liability protection relative to the directors.[103]

Another cost of withholding officer exculpation is the literal cost of enforcement. Because corporate litigation is so expensive,[104] there is good reason to believe that, at least in some cases, shareholders would want to prevent liability litigation directed at corporate officers.[105] Notably, even when officers are found liable for ordinary negligence and are compelled to render monetary damages, merely shifting money from negligent officers to angry shareholders does not add value to the company.[106] Because officers must at times be sued to make the lack of officer exculpation even a marginally effective deterrent and because such litigation is painfully expensive, the "benefit" of precluding officers from exculpation likely is outweighed by its pecuniary cost.[107]

Rippy illustrates the marginal value of holding officers liable for ordinary negligence in duty of care cases. In *Rippy*, the non-director officers[108] committed potentially negligent acts even though they were not exculpated.[109] The exculpated directors committed the same acts.[110] The fact that the non-exculpated officers acted in the same manner as their exculpated director colleagues suggests that potential officer liability *via non-exculpation*[111] played a relatively small role in shaping officer behavior regarding individual loan decisions.[112] The

102. It is also likely that the relatively small size of the company played a role in blurring the roles of Cooperative's management.

103. *See supra* notes 35–37 and accompanying text.

104. No one knows exactly how much is spent each year on corporate litigation. However, a 2010 survey of Fortune 200 companies revealed that respondents spent an average of nearly $115 million per year on litigation in 2008—up 73% from $66 million per year in 2000. U.S. CHAMBER INSTITUTE FOR LEGAL REFORM, LITIGATION COST SURVEY OF MAJOR COMPANIES 2 (2010) (reporting at the 2010 Conference on Civil Litigation at Duke Law School).

105. Honabach, *supra* note 54, at 332.

106. Indeed, Honabach correctly points out that litigation costs incurred to bring about the shift in monies are a deadweight loss. *Id.* at 334.

107. *See supra* notes 104–106 and accompanying text.

108. *See supra* note 24.

109. FDIC *ex rel.* Coop. Bank v. Rippy, 799 F.3d 301, 313 (4th Cir. 2015).

110. *See id.* at 313.

111. *See supra* note 94 and accompanying text.

112. It is important to distinguish between the lack of officer exculpation's effect on the *structure* of the decision-making process and the lack of officer exculpation's effect on *individual decisions*. As has been noted, non-officer exculpating schemes often engender atypical corporate decision-making structures by encouraging officers to share the risks of

tenuous connection between the deterrent effect of potential liability pursuant to non-exculpation and actual officer behavior makes the exclusion of officers from permissive exculpation hard to justify from a cost-benefit standpoint. While the benefits of officer non-exculpation are probably marginal and often unclear, the cost of attempting to impose liability on officers in non-exculpation schemes has not been ambiguous.[113]

C. The Current Lack of Officer Exculpation Allows for Inequitable and Confusing Outcomes as between Directors and Officers

Because officers and directors have the same duties of care and fiduciary duties, allowing permissive officer exculpation will engender fairer outcomes and less confusing jurisprudence. Directors have a duty to act in good faith and with ordinary care.[114] As the *Rippy* court noted,[115] officers[116] are held to an identical standard.[117] Directors and officers also have the same fiduciary duties.[118] Further, in some cases,

decision-making with directors. *See supra* note 93 and accompanying text. However, once the decision-making structure is in place and decision-making duties are shared, the lack of exculpation for officers but not directors likely plays a negligible role in determining the outcome of individual decisions. The reasons for this are not entirely clear, but it is possible that officers believe that sharing their decision-making burden with directors affords them the same protections as directors, at least in regards to jointly-made decisions. In states without permissive officer exculpation, of course—and as Cooperative's officers painfully learned—this is simply not the case.

113. While the exact amount of the legal fees is unknown, the *Rippy* litigation has spanned four years and involved dozens of attorneys from at least five law firms. *See Rippy*, 799 F.3d at 306, 309.

114. *See* N.C. GEN. STAT. § 55-8-30(a) (2015) ("A director shall discharge his duties as a director, including his duties as a member of a committee: (1) In good faith; (2) With the care an ordinarily prudent person in a like position would exercise under similar circumstances; and (3) In a manner he reasonably believes to be in the best interests of the corporation.").

115. *Rippy*, 799 F.3d at 311.

116. The statute applies to officers "with discretionary authority." N.C. GEN. STAT. § 55-8-42(a) (2015). While there is some debate as to which officers should be deemed to have discretionary authority under the statute, there is no doubt that the officers in *Rippy* had such authority. Complaint, *supra* note 23, at 14–15 (discussing officer approval of loans).

117. N.C. GEN. STAT. § 55-8-42 (2015) (providing the identical standard of care for officers as is given for directors in § 55-8-30). Of course, the application of the duty of care standard for officers and directors can vary greatly depending on, among other things, the level of knowledge officers have relative to directors. *See infra* Section III.A.

118. *See* Gantler v. Stephens, 965 A.2d 695, 708–09 (Del. 2009) (holding that officers have identical fiduciary duties as directors); *see also* State v. Custard, No. 06 CVS 4622, 2010 WL 1035809, at *28 (N.C. Super. Ct. Mar. 19, 2010).

officers and directors are responsible for the same tasks.[119] Because the duty of care and fiduciary duties imposed on directors and officers are the same,[120] it follows that *permissible* statutory protections for each group should likewise be congruous.

The *Rippy* facts are especially illustrative of the inequities inherent in holding officers and directors to the same standards but affording them different levels of protection. In *Rippy*, there were nine defendants—one director/officer, six directors, and two officers.[121] Both the district and appellate courts generally examined the defendants' actions in the aggregate without distinguishing between officer and director behavior.[122]

In *FDIC v. Willetts*,[123] the Eastern District of North Carolina repeatedly referred to and analyzed the defendants as a group; specifically, the court referred to "the *decisions of defendants*" when discussing the business judgment rule.[124] The court further considered "whether *defendants* employed" a rational process in making loans[125] and later examined whether the challenged "actions *of the defendants*" could be attributed to a rational business purpose.[126] In eventually ruling in favor of the defendants, the *Willetts* court did not discuss any differences between director and officer behavior.[127]

The Court of Appeals for the Fourth Circuit similarly failed to distinguish between directors and officers when examining conduct.[128] The *Rippy* court observed that "Bank *management* promised to address the issues" highlighted in the CAMELS reports.[129] The *Rippy* court also noted that the joint report alleged that "Cooperative's

119. Ironically, while the jurisprudential impact of *Van Gorkom* concerned directors, much of the actual criticized behavior was arguably behavior normally attributed to officers. Lamb & Christensen, *supra* note 32, at 56 n.51.

120. *See supra* notes 114–118.

121. *See supra* notes 23–24.

122. *See infra* notes 123–130 and accompanying text.

123. 48 F. Supp. 3d 844 (E.D.N.C. 2014).

124. *Willetts*, 48 F. Supp. 3d at 850 (emphasis added).

125. *Id.* (emphasis added).

126. *Id.* at 851 (emphasis added).

127. *Id.* A reason for the *Willetts* court's lack of differentiation between director and officer behavior likely stemmed from their interpretation of the business judgment rule—an interpretation the *Rippy* court explicitly rejected. *Id.*

128. As previously noted, the *Rippy* court distinguished between officers and directors for the purposes of exculpation eligibility. FDIC *ex rel.* Coop. Bank v. Rippy, 799 F.3d 301, 313 (4th Cir. 2015) ("[Cooperative]'s exculpatory provision does not cover Bank officers."). *See supra* note 31 and accompanying text.

129. *Rippy*, 799 F.3d at 308 (emphasis added). *See supra* note 15 (explaining CAMELS).

management" had ignored previously raised concerns.[130] The *Rippy* court's analysis deserves a nuanced examination.

First, the *Rippy* court found that directors and officers could be sued for ordinary negligence.[131] Next, they applied the exculpatory provision, which pertained only to the directors.[132] Because the exculpatory provision did not apply to officers, the *Rippy* court then examined officer behavior in the context of the business judgment rule.[133] The court did not readily distinguish between officer and director behavior in their discussion of the business judgment rule—the director behavior was simply considered irrelevant pursuant to the exculpatory provision.[134] However, the expert FDIC witness, used by the plaintiff to rebut the initial presumption that the defendants acted with due care, testified that "the review process was inconsistent with practices at other banking institutions, and did not comport with his understanding of officer *and director* duties."[135] Hence, the behavior that removed the officer-defendants from the protection of the business judgment rule would likely have had the same inculpatory effect on the directors in the absence of an exculpatory clause. Cooperative's directors were not protected because they acted differently or knew less than the officers; they were protected via statute.

A closer examination of the defendants' behavior in *Rippy* further highlights the confusion that can arise when directors, but not officers, are exculpated. In *Rippy*, defendant Frederick Willetts was both president and chairman of the Board.[136] That is, he was both an officer and a director.[137] Such role duality can be problematic when assessing the applicability of exculpatory clauses. As one commentator has noted, "[an exculpatory] statute that applies only to directors creates the possibility that directors who are also officers may face personal liability for their actions as officers, but not as

130. *Id*. (emphasis added).
131. *Id.* at 311.
132. *See supra* note 30.
133. *Rippy*, 799 F.3d at 313.
134. This Recent Development does not argue that the *Rippy* court's interpretation of § 55-2-02 of the North Carolina General Statutes was per se faulty and should have been otherwise conducted; the *Rippy* court did not meaningfully distinguish between officer and director behavior because the current statutory scheme does not require such an analysis. Allowing permissive exculpation for directors *and* officers would require courts to look *separately* at both groups' behavior to determine whether either or both groups could legitimately receive exculpation.
135. *Rippy*, 799 F.3d at 313 (emphasis added).
136. Complaint, *supra* note 23, at 2.
137. *Id.*

directors. This would mean that only outside directors, as a practical matter, would benefit from the statutory limitation on liability."[138] By allowing exculpation for directors but not officers, state legislatures—in cases dealing with director and officer liability—leave questions[139] regarding exculpation eligibility unanswered. Such messy, and potentially litigious,[140] questions could be avoided in a statutory scheme allowing officer exculpation.

III. COUNTERARGUMENTS

A. *"Officers and Directors Are Not the Same and Should Be Treated Differently"*

In the Monopoly game analogy, the distinction made between players was arbitrary.[141] Some commentators have suggested that, for the purposes of imposing liability, directors and officers *are* different in salient ways and should therefore receive different levels of protection.[142] They essentially contend that officers' proximity to decision-making (relative to directors) justifies placing on them a different (non-arbitrary) standard for exculpation eligibility.[143] Further, the argument goes, viewing officer-director liability in the principal-agent paradigm (with officers as agents) provides a meaningful differentiation between the two groups and a coherent structure with which to evaluate conduct.[144]

138. Mark A. Sargent, *Symposium: Two Cheers for the Maryland Director and Officer Liability Statute*, 18 UNIV. BALT. L. REV. 278, 304 (1989).

139. Several questions remain unanswered: Was Willetts acting as a director or an officer when he approved eight out of the nine commercial real estate loans in question? Should he be exculpated for some acts but not others? How should courts decide? Is directorship dispositive and therefore wholly exculpatory? *See* Complaint, *supra* note 23, at 2.

140. *See In re* Capital One Derivative S'holder Litig., 979 F. Supp. 2d 682, 691 (E.D. Va. 2013) ("[Defendant-officer/CEO] cannot be liable for breaches of the duty of care when he acts as a director. It follows that to state a claim against [defendant officer–CEO] for breach of the duty of care where, as here, there are no allegations of bad faith, intentional misconduct, or knowing violation of the law, plaintiffs must plead facts plausibly alleging that he acted *solely* in his capacity as an officer, thereby removing his actions from protection under the exculpatory clause.").

141. *See supra* note 2 and accompanying text.

142. *See* Lyman P. Q. Johnson & David Millon, *Recalling Why Corporate Officers Are Fiduciaries*, 46 WM. & MARY L. REV. 1597, 1603 (2005).

143. *Id.* ("Recalling the agency law status of corporate officers . . . clarifies immensely why courts can and should scrutinize officer conduct more closely than they now review director performance—i.e., the fiduciary duties of agents are more demanding than those of directors, and officers rightly face a greater risk of personal liability for misconduct.").

144. *See id.* at 1602.

It is true that, in some cases, officer and director functions are sufficiently different to justify imposing disparate standards for liability.[145] This is especially true in corporations with boards containing a significant proportion of outside directors.[146] In such cases,[147] information asymmetry or effective CEO control[148] over the board may justify allowing permissive exculpation for directors but not officers.[149] However, that officer and director roles are sufficiently different in *some* corporations[150] to impose different standards for liability does not imply that such differences *universally* exist. As Cooperative's management structure illustrates,[151] some corporations intermingle classic director duties with quintessential officer responsibilities and vice versa. When this occurs, corporations should have the opportunity to impose the same liability standard on officers as they do on directors via permissive exculpation.[152] That single

145. Such cases include companies where outside directors comprise a significant portion of the board. Because "[b]eing an outside director is a part-time job[,]" outside directors have less time to review the information they have. 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). Outside directors also have limited access personnel who might help them vet important issues and must otherwise depend on the CEO and other high-ranking officers to supply crucial information. *Id.* at 725.

146. *Id.*

147. *See, e.g.*, McPadden v. Sidhu, 964 A.2d 1262, 1273–76 (Del. Ch. 2008) (holding that directors who placed non-director CEO in charge of the acquisition process were not liable for negligence, while CEO with conflict of interest was liable for breach of care and loyalty).

148. SEC Commissioner Cynthia Glassman stated that the "closed nomination process dominated by powerful CEOs, and the entrenchment of directors, . . . [leads] to an unhealthy coziness in some instances between ostensibly independent directors and the executives whose performance they [are] supposed to oversee." Cynthia A. Glassman, Comm'r, Sec. & Exch. Comm'n, Issues Surrounding the SEC's Shareholder Access Proposal (Mar. 8, 2004). *See* Johnson & Millon, *supra* note 142, at 1613–14 (arguing that the "overly 'cozy' relationship between boards of directors and senior officers . . . may result in a corporate culture in which directors do not regard officers as persons owing high fiduciary duties to the corporation").

149. *See* Paredes, *supra* note 145, at 725.

150. This Recent Development concedes that officer exculpation may not be appropriate in corporations where director and officer roles and responsibilities are sufficiently distinguishable and separate. *See supra* note 117.

151. *See supra* notes 99–101 and accompanying text.

152. Whether courts should be able to intervene in cases where the articles of incorporation are insufficiently tailored to a corporation's management structure is beyond the scope of this Recent Development. However, given the deference traditionally afforded corporations regarding business decisions, it seems likely that courts should generally allow even poorly tailored articles to remain in effect. *See generally* Susanna M. Kim, *The Provisional Director Remedy for Corporate Deadlock: A Proposed Model Statute*, 60 WASH. & LEE L. REV. 111, 138–40 (2003) (discussing judicial intervention and rewriting of corporations' articles of incorporation in deadlock situations). Because

persons working in relatively smaller companies continue to share director and officer titles further underscores the importance of allowing corporations the kind of bylaw flexibility permissive officer exculpation provides.

B. *"Officers Already Have Adequate Protection from Liability"*

Another argument against officer exculpation is that the protections already afforded them adequately insulate them from liability. While indemnity, director and officer ("D&O") insurance,[153] and the business judgment rule undoubtedly protect officers, such protections may be inadequate when officer and director behavior are indistinguishable from each other. As has been shown, indemnification is inferior to exculpation as a liability shield.[154] D&O insurance can mitigate officer exposure, but is inferior to exculpation in many of the same ways that indemnification is.[155] Finally, the business judgment rule provides some common law protection for decisions made in good faith.[156] However, as *Rippy* illustrates, just because officer conduct is evaluated in light of the business judgment rule does not preclude liability in cases of ordinary negligence.[157] Because the current available officer protections—though not inconsequential—are inferior to the protections available via exculpation,[158] shareholders should have the option of providing the

judicial intervention regarding poorly tailored articles would require an evaluation of shareholders' decision to exculpate officers, it seems likely that courts would be hesitant to do so.

153. D&O insurance can in some cases cover liability where indemnification cannot. *See* Lamb & Christensen, *supra* note 32, at 70.

154. *See supra* Section II.A.

155. Namely, D&O insurance does not provide the tactical litigation advantages which exculpation does and requires insured defendants to seek, and in some cases negotiate with, insurers to settle the claims made against them. D&O insurance is also not available in cases where the corporation brings suit against management. Hamermesh & Sparks, *supra* note 32, at 871 & n.42 ("[D]irector and officer liability insurance policies uniformly include an 'insured v. insured' exclusion, denying coverage where the corporation itself initiates the claim against the officer.").

156. *See supra* note 32.

157. FDIC *ex rel.* Coop. Bank v. Rippy, 799 F.3d 301, 313–14 (4th Cir. 2015).

158. While there are significant differences in protection between exculpation and existing officer liability shields, it may not be reasonable to assume that officers' familiarity (or lack thereof) with these differences will effectuate a meaningful difference in their behavior. Hence, while exculpation is clearly legally superior to existing officer protections, it is likely that allowing officer exculpation would not significantly *further* deter negligent officer behavior. *See supra* note 93. Hence, that the high degree of overlap between exculpation and other available protections makes non-exculpation a marginally less valuable deterrent of negligent behavior does not necessarily beg the conclusion that the differences between exculpation and other protections are legally insignificant. *Id.*

highest protection to officers when the management structure of their corporation renders director and officer functions indistinguishable.

CONCLUSION

When officers and directors have the same information, functions, standard of care, and fiduciary duties, they should be afforded the same protections. Nominal nonconformity alone does not justify imposing disparate standards for liability. Unfortunately, the NCBCA, as it is currently codified and understood, allows for disparate exculpation eligibility treatment based on just such titular technicalities.[159]

While the actual differences between officers and directors in some cases are largely technical, the differences between the protections afforded them are material and significant.[160] *Rippy* represents these problematic differences in liability protection.[161] Further, while the gap between officers and directors is significant, the marginal effect on officer behavior that potential liability for negligence via non-exculpation may have is likely outweighed by the costs of enforcing the current statutory scheme.[162] In addition to being costly, the current lack of officer exculpation allows for inequitable and confusing outcomes as between directors and officers.[163]

While this Recent Development argues for the expansion of officer protections, it does so only in a narrow set of circumstances. Exculpation—for officers and directors—should only be available for non-grossly negligent breaches of care.[164] Self-dealing, fraudulent, embezzling, or reckless officers would receive no respite under the proposed change.[165] Further, the proposed amendment calls for allowance of *permissive* officer exculpation. Shareholders—those most sensitive to any potential negative effects of exculpation—would be the arbiters of this important corporate governance question. While it is difficult to predict in what circumstances shareholders would opt for officer exculpation, this Recent Development suggests

159. *Rippy*, 799 F.3d at 313.
160. *See supra* Section II.A.
161. *See supra* notes 35–37 and accompanying text.
162. *See supra* Section II.B.
163. *See supra* Section II.C.
164. *See supra* note 85.
165. *See supra* note 85.

that such exculpation is appropriate when officer and director duties and functions are significantly intermingled.[166]

The economic, theoretical, and policy justifications for allowing director exculpation apply, at least in some cases, to officers. For those reasons, North Carolina should follow the example of states[167] that have recognized this by amending the NCBCA to allow permissive officer exculpation.

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166. *See* FDIC *ex rel.* Coop. Bank v. Rippy, 799 F.3d 301, 313 (4th Cir. 2015); Complaint, *supra* note 23, at 2–3.

167. *See supra* note 65.

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