PROFESSOR ANNE CONAWAY: All right, as everyone has been waiting, we now bring on our august Judicial Panel. It's not as if everyone doesn't know everyone, but just in case, to my far right we have our Chancellor, William Chandler, who has been providing us with wonderful decisions for what, 20 years? Over 20 years now.

I have enjoyed teaching the Chancellor's opinions for so many years that it's just a wonderful thing to have you here. Thank you so much for coming.

Just to my right, of course, we have our Third Circuit Judge, our local Tom Ambro. Once again, Tom, thank you so much for taking time out of your busy schedule to join us here today. And just to my—

JUSTICE THOMAS AMBRO: You notice she didn't call any of my opinions wonderful. Then again, no one else does either.

PROFESSOR CONAWAY: Oh, actually—you did have a couple of wonderful opinions that I should have referred to, but those are for the next symposium, of course.

JUDGE AMBRO: That's bankruptcy stuff.

PROFESSOR CONAWAY: Well, actually that's where we're heading next: bankruptcy.

To my left we have Justice Jacobs, whose opinions we have been enjoying for many, many years as well. I have been teaching your opinions as well. Justice Jacobs is on the Supreme Court, and of course actually authored the opinion of the Supreme Court in the Disney case. And then of course, to his left, we have the Chief Justice. And the Chief Justice now has been on how many Courts? Three?

CHIEF JUSTICE MYRON STEELE: Three.

PROFESSOR CONAWAY: Three Courts now. With that, Tom, I'm going to turn it over to you.

JUDGE AMBRO: Thank you. Obviously, the reason that I take this position is because I'm the lightweight here.
The best news about corporate law is that you have a State that people flock to for corporate and now alternative entity filings and ultimately decisions of its Courts. If you had corporate law in my area, the federal law, you would have about 13 different views from 13 different Circuits. So, it's good that we have one State that, in the world of ideas, has been listened to and followed throughout the 20th Century and now into the 21st Century.

The concept here today is whether you have a duty of good faith. I'll give you some general ideas from someone out in left field—myself—and then ask the panel some questions.

To me, this concept seems as if it's obviously not fully developed—that's not saying much. I don't find where Jack has said in the Disney opinion that there has to be a gap filler between duty of loyalty and duty of due care.

Good faith is something that's not even defined. We've heard a lot of people today, Frank [Balotti] among others, saying that perhaps it could be something like honesty of purpose. To me, it's almost the down-home question. Lou Holtz, the famous football coach, says: when you meet someone, you intuitively ask yourself three questions, the first of which is: "Can I trust you?" If the answer is no, you perceive that person as not having good faith towards you. So to me, good faith is nothing more than a label that we attach after we witness actions or facts occurring. So it's done in hindsight.

Essentially, good faith is just something that we know when we see it. And that doesn't quite work in the legal world, especially for a concept that it seems as if—based on everything that we've seen in the statutes and in the business judgment rule—it appears to be a safe-harbor mechanism that is available to you provided that you act in good faith. If you do not, or it's found that you do not act in good faith, you lose that safe harbor. That's it, as I see it so far.

So the first question I would ask the panel is: What gaps are people perceiving that need to be filled between loyalty and care? Bill?

CHANCELLOR WILLIAM CHANDLER: Well, I'm going to do what I always do when I get a question I'm not expecting. I'm going to describe what it feels like to be here today. It's akin to undergoing an autopsy while you're still alive. But I've actually enjoyed the experience of having Professor Balotti, and Professor Lowenstein, and others, members of the Bar and professors, dissect these decisions and talk about the concept of good faith.

First, I should explain another source of my trepidation about being on this panel. By my reckoning, I'm the only trial judge currently, sitting on this panel today. And so, it naturally reminds me of the remark by a well-known professor at
the University of Virginia who said that, "Appellate judges are wonderful people to be around. They are a lot like dogs; one-on-one they're very friendly. But in a pack, it's a different matter."

**CHIEF JUSTICE STEELE:** You notice I'm not disagreeing with you.

**CHANCELLOR CHANDLER:** Permit me to provide some background, and start from the beginning. Remember that this case, the Disney case, actually commenced in 1997, as I recall. The original case was fully briefed on a motion to dismiss, after an initial skirmish over whether it should be in Delaware or California. I granted the motion to dismiss, and that determination promptly was appealed to the Supreme Court. On appeal, Chief Justice Veasey wrote an opinion that affirmed in part and reversed in part. The Supreme Court's opinion read something like a brief on the gross inadequacies of the pleading, but carefully described how there might be a possible viable claim if the pleading was properly drafted. Interestingly, Chief Justice Veasey explicitly urged plaintiff's counsel to pursue an inspection of company records under section 220 before seeking leave to amend the deficient complaint. Well, unsurprisingly, plaintiff's counsel took the Chief's helpful advice and filed their books and records demand, with which the company complied.

Next came round two, where plaintiff filed an amended complaint based on the documents inspected during the books-and-records process. And that second complaint, which arrived on my doorstep, was a far different pleading than what had appeared in the first go-around. For example, the amended complaint contained numerous references to records of the company involving board and committee meetings, minutes concerning Ovitz's compensation package, the term sheet and actual contract with Mr. Ovitz, et cetera. The amended pleading provided a much richer context to the board's process—or lack thereof—than did the first pleading.

Well, to fast forward, given the richer and more detailed second pleading, it instantly seemed unlikely to me that the new complaint could be dismissed yet again, especially given the strong hint from the Supreme Court that there was a potentially viable claim if the plaintiff would follow the Supreme Court's guidance on how to do it right the second time. In a nutshell, that's how we got from a dismissed complaint in 1999 to a trial in 2004.

The trial court opinion, you will notice, is mostly factual, over 100 pages of facts. That is followed by a description of the legal standard to be applied by the court. A trial judge has to grapple with what he or she believes is the governing legal standard. I'm not in the position to make, or to redefine, the legal standard according to what I believe makes economic or legal sense. I follow the standard given to the trial court by the Supreme Court or by the Legislature.
Thus, I sought in this decision to explain, as best I could, the meaning of the concept of good faith as that concept had been articulated by the Delaware Supreme Court in a series of well-known decisions. Then, I had to apply it to the particular facts as I found them in Disney. Of course I was aware of views expressed by academics and by colleagues on my own court that no independent, free-standing fiduciary duty of good faith exists (or should exist) under our law; that the duty of loyalty was sufficiently capacious to cover bad-faith conduct. And I am not philosophically in disagreement with that view. The difficulty with writing a decision that way, however, is that it means, in my judgment, an explicit refusal to respect binding Supreme Court precedents that cannot be harmonized with that view without dissembling or overruling.

And so I tried to write a decision that was properly faithful to the Supreme Court's own words and that sought to describe what I perceived to be the Supreme Court's perhaps evolving view as to the meaning and application of good faith. It was not an accident, therefore, that the trial court opinion refers repeatedly to an obligation to "act in good faith"—a locution that I hoped would avoid the problems my colleagues and certain academics have alluded to about the free-standing fiduciary duty of good faith while remaining faithful to the Supreme Court's opinions on this subject.

Our law evolves by statutory changes and by judicial decisions. It was through the latter method that the good-faith concept crept into our lexicon. But I really think it reflects—and that's what my opinion tries to express—is an obligation to consider scienter, what is in the minds of the directors or the executives at the time they take (or fail to take) action. What is at stake is whether those actions or inactions are in conformity with their fundamental obligation to act honestly and conscientiously, to advance the best interests of the corporation and the ends of the stockholders who are the investors in that corporation, and not the interests of managers, themselves or other related parties. That's the essence of a fiduciary, in my judgment.

And as Judge Ambro said, if you fail to demonstrate that you have that state of mind, that you are acting in conformity with those guiding principles, those principles of devotion, faithfulness and fidelity, then you ought not expect the right to exculpation under 102(b)(7). Nor can you expect the immunity from relying on experts, or the right to indemnification. Yet it is not a free-standing independent duty, a fiduciary duty, that itself, standing alone, will trigger an independent liability claim against the director or executive.

Now, if any of this is a problem from the practitioners' point of view—or from the corporate counsel's or academic's point of view—then, with all due respect, go get it fixed by the Legislature. There are 62 earnest folks in the Legislature who can fix this in a heartbeat. Alternatively, there are five excellent jurists on the
Supreme Court who can fix it in a heartbeat as well. Trial judges don't have the time, unfortunately, to repair every rent in the jurisprudential fabric. That's what appellate courts are for. Thank you.

**Judge Ambro:** Let me ask then, without trying to predict the future. The latest word is the Supreme Court opinion that came out on June 8th—and the author is here, Justice Jacobs. Is there anything, Jack, in your opinion that talks about good faith filling gaps between loyalty and due care, or that you perceive was intended that way?

**Justice Jack Jacobs:** Well, if somebody could tell me what filling gaps means, I might be able to answer that question. Before I do that, though, I have two disclaimers to make. One is that whatever you hear from me is only my individual point of view. I don't speak for my colleague to my left, or my colleagues that aren't here.

Secondly, at the outset, I feel compelled to express my abject apologies to Professor Balotti for not having vetted the draft of the *Disney* opinion with him before it went out, so that I would make sure that the right nomenclature was in there. I promise not to make that mistake again, Frank.

One comment that Chancellor Chandler made that I was struck by, when the task became ours to review his well-crafted opinion, is that whenever the words "good faith," or "duty of good faith" came up, he articulated them very carefully as "the duty to act in good faith." Indeed, I attempted to do precisely the same thing in the opinion that I wrote for the Supreme Court. There was a reason: the entire good faith area, as the opinion notes, is a bit of a work in progress.

The duty to act in good faith is a duty that corporate directors have had ever since the beginning. I don't think anybody would contest that. The real question is what is the consequence of a finding that that duty has been breached?

That really is the legal issue that we're facing at this point. That didn't become an issue until, beginning in 1993, the Delaware Supreme Court in the *Cede II* opinion first made reference to the triad—or triads—and described good faith as being a separate fiduciary duty, thereby suggesting that good faith was of the same dignity as the duty of loyalty.

Several opinions that followed made those same suggestions. None of those opinions, however, infused any content into the concept of good faith. That raised two questions, one of which we explicitly left open in the *Disney* opinion: Is a breach of the duty to act in good faith a liability-creating event?
If it is, that's one thing. If it isn't, then what good faith means—that is, what a finding that there has been a breach of the duty to act in good faith would mean—is that it negatives protections that would otherwise be available to directors. That is: an adjudicated breach of the duty to act in good faith negatives the protection of the business judgment standard of review. It also negatives the protection that is created by Section 102(b)(7), because acts not in good faith are carved out from the protection of that statute. And it negatives what otherwise would be an entitlement to indemnification under Section 145 of the Delaware General Corporation Law. And such a finding may have other collateral consequences as well.

So there is an open issue, even though some have argued that there is not. In Disney, that issue did not come up, because the only functional effect of a finding of bad faith would have been to negative the protection of the business-judgment rule. That is to say: there was no cause of action or claim for relief against the Disney directors for having acted in bad faith.

The other issue that has been alluded to—most strongly, I believe, by Vice Chancellor Strine—is whether there's any need to be talking about the duty to act in good faith as a separate fiduciary duty at all.

Vice Chancellor Strine's argument is that a breach of the duty to act in good faith is really an instance of a breach of the duty of loyalty. The reasoning is that any director who acts in bad faith cannot possibly be loyal—either in a verbal sense or in a legal sense—to the corporation. That's an issue that is obviously still being debated, not only in the academy, but also within the bar and among the bench as well.

So, to make a long, rambling story very short: Number one, I can't answer your question directly, Tom. And number two, there was a specific effort to limit the scope of the good-faith holding in the Disney case. The opinion was unanimous, obviously reflecting the views of all of the members of the Court.

JUDGE AMBRO: The one thing just to add before I ask the Chief for his comments is that Footnote 112 could not be clearer in saying: "We don't reach or otherwise address the issue of whether good faith is a duty that, like the duties of care and loyalty, can serve as an independent basis [for liability]." That's the last word. And what really awaits us is, as the Chief said this morning, the next group of people who bring the next case, with the next dispute that the Court has to decide. Chief?

CHIEF JUSTICE STEELE: Let me make four quick points, first because I take pains to memorize everything the Chancellor says. And when I can hear it live, I write it down. I believe he said he is "the only trial judge currently sitting here." I don't mean to feed your pack-of-dogs analogy, but I think what you meant to say
was that you're the only current trial judge sitting here, because there are three trial judges sitting here.

And as the leader of the toothless pack of dogs that you seem to have some concern about, I want to point out, first between the two Disney opinions, that people carefully noted what you just pointed out, Chancellor. And that is, you did use the phrase "obligation to act in good faith." And I think, and hope you note, that it was repeated by Justice Jacobs in the opinion. And had we not taken very careful note of your extraordinarily careful phraseology, there might not have been a five to nothing decision in Disney.

But we did note that. And I appreciate the fact that you repeated it so that I could make the point that the pack of dogs also noted it.

I think it's also important for people to understand the point that the Chancellor made, as two of us are also former trial judges. That is: you have to deal with the opinions that are out there whether you agree with them or not, or whether they give you the kind of guidance you'd like to have, or because in some ways they don't give you the guidance you'd like to have. The lawyers can't give you the kind of guidance they'd like to give you. No one can fault a trial judge who is working in that kind of atmosphere, and trying the case that's as complex factually as the one that the Chancellor had to deal with.

Now the actual question you asked us to address—I will try to answer. What is a gap-filler? Well, a gap-filler is when you, like my alma mater, play a 3-5-3 defense. The gaps you're filling are the holes left because you've only put three people on the front line to stop the tailbacks, who have routes to run right between the three linemen. So the linebackers are supposed to jump in and fill the gaps. Sports analogies normally work for me anyway.

The gap-filler advocates are offering another opportunity to correct the wrongs that they believe were driven by the corporate crisis of the last few years. If they can create another basis for liability, they believe, that will lead to a case-by-case correction of conduct. It will ripple throughout the corporate world and better people will serve on boards, and those who serve on boards will perform better service. Shareholders will have more accountability or have a way to redress their grievances, because there is yet another mechanism filling the gap they perceive to exist by providing an additional methodology for liability.

And I think deep down what they're looking for—forget exculpation for gross negligence. They'd like to be able to create fact situations that don't fit neatly into loyalty by definition. Now they're exculpated from negligence liability, but if they can create this gap filler, in their minds, a new standard of conduct that they think
is definable, one that actually tells people what their conduct should be, there'll be another opportunity to find those people liable and create greater accountability.

And it is, I think, the functional equivalent of slipping negligence back into the equation as a basis for liability. Years ago, I was a tort lawyer. And I am frankly mystified by phrases like "intentional gross negligence." I don't get what that is. I know what negligence is. I can make a decent argument for what gross negligence can be. I can turn to a statute that mentions criminal negligence and try to explain the difference between gross negligence and criminal negligence—maybe. But there's no way you'll ever see me able to explain what intentional gross negligence means.

I think the gap that's trying to be filled is to create greater accountability on the part of the boards of directors, and ultimately management, by creating a clandestine slip back to negligence as a basis for liability.

Maybe that's a perverse view. But it's a quarter to five—and I tend to get perverse at about a quarter to five. So maybe that explains at least a rationale for the gap-filler logic. I don't know that it works, but it's the best I can come up with at 4:45 PM.

**JUDGE AMBRO:** Why don't we have questions from the audience, if anyone has any questions. There are going to be a lot of things that you've thought about during the course of the day because there have been so many speakers that have had different points of view. Anyone?

** SPEAKER:** Tom, Would any of the judges and justices care to react on public policy versus freedom of contract?

**CHANCELLOR CHANDLER:** In instances where you're dealing with alternative entities, it's always been the law in Delaware that the parties can craft the agreement as explicitly as they want. I wrote a decision—that got reversed implicitly—that said that informed parties could even craft an agreement that eliminated fiduciary duties. And it got reversed, and I think probably that was part of the impetus for this statutory amendment. I don't know, but there is a point, or at least it seems so to me, when every agreement that parties enter into, no matter how explicit they make it, a trial judge and a court of equity is always going to want to have some kind of fundamental—it's a Schnell versus Chris-Craft kind of thought process that a chancellor is going to go through.

Yes, you've eliminated all of these duties and you've said that there can be conflicts, but if it's really just an artifice, a deceit or fraud, then no court of equity is going to stand by and say, "Okay, that's what you bargained for, and that's what
you get.” Because people don't bargain that way. They don't knowingly give their money away to someone who's a thief.

And so if there's evidence of deceit, or artifice, or overreaching, then those are the kinds of things that a court of equity will scrutinize and measure against fundamental obligations of good faith and fair dealing.

**Judge Ambro:** Anyone else want to comment?

**Justice Jacobs:** I think Bill Chandler said it all, but perhaps I can say it in just slightly different words. You know, for those of us who have been equity judges, it's part of our culture, and part of our tradition, that that sense of doing equity dies hard. And so if the legislature, as it has, permits fiduciary duties to be written out by contract, and we are persuaded that on a particular set of facts fiduciary duties have been written out, and the parties agree to this scenario—however unfair it may be—I think in those circumstances the fact that it was agreed to and is clear would make it enforceable.

But, as you know, courts must be very sure that a result that appears to be unfair has really been agreed to by the parties. And that is why the cases tend to basically resolve all doubts against the unfair results. That is, all doubts are resolved against the elimination of fiduciary duties. But, if worst comes to worst, courts will resort to the implied duty to perform in good faith.

**Chancellor Chandler:** If I might add one thought, professor, since Justice Jacobs mentioned the culture and tradition of an equity court: I've long believed that the greatest strength of the judges on the Court of Chancery is not in their knowledge or skill in applying the statutory commands of the Delaware Corporation Law. Rather, I think it is in knowing when and how not to apply the literal statutory commands, when principles of equity and fairness should trump those commands. The hard part isn't in knowing how to apply the statutory default rules, or the literal terms of the agreement that the parties have fashioned. It's having the feel or intuition for when it's inappropriate to apply it, based on the actions of the parties and the surrounding circumstances in a particular case.

**Judge Ambro:** Let me add onto that. When you are presented with a dispute not of your making, but by the parties before you, there are different ways of attempting to resolve the dispute, and you have to decide in a particular case which you wish to go with.

Let me give you an example. There was an article written around 1994 dealing with the Supreme Court. And it said that, with regard to the then-makeup of the United States Supreme Court, while you read in the newspapers that there are liberals and conservatives, that's not really how it works. What goes through
those justices' minds, this person posited, was about four things, three of which I'll mention now.

There are those who are primarily believers that one must follow the text, whether it be the Constitution or a federal law. This person put into that camp Justices Scalia and Thomas.

There are those who believe that perhaps the motivating forces for their decision-making are the consequences of what they do. And this person, this author put into that camp Justices O'Connor and Kennedy. And then there are those who—like many perceive the old Warren Court—ask themselves, “Is what we are doing fair?” And in that camp this person put Justices Ginsberg and Stevens.

So when you go before judges with your case, think about what is it that you believe, from that judge's past decisions, are the things that motivate that judge to decide. It may be the text; it may be simple fairness or equity, as in the Schnell v. Chris-Craft case. Or it may be the consequences.