

March 22, 2000 #2000-2 Informal Opinion

Molly P. Lambert
Secretary
Agency of Commerce & Community Development
Montpelier, Vermont

Dear Secretary Lambert:

You have requested an opinion regarding the effect of the 1998 amendment to 11A V.S.A. § 8.30, the state statute that establishes the standard of conduct for directors of corporations. Prior to amendment, § 8.30 provided that a director "shall discharge his or her duties ... (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 the director reasonably believes to be in the best interests of the corporation." The 1998 amendment added a final sentence to this section:

In determining what the director reasonably believes to be in the best interests of the corporation, a director of a corporation which has a class of voting stock registered under section 12 of the Securities Exchange Act of 1934, as the same may be amended from time to time, may, in addition, consider the interests of the corporation's employees, suppliers, creditors and customers, the economy of the state, region and nation, community and societal considerations, including those of any community in which any offices or facilities of the corporation are located, and any other factors the director in his or her discretion reasonably considers appropriate in determining what he or she reasonably believes to be in the best interests of the corporation, and the long-term and short-term interests of the corporation and its stockholders, and including the possibility that these interests may be best served by the continued independence of the corporation

1997, No. 102 (Adj. Sess.), § 15a (codified at 11A V.S.A. § 8.30(a)(3)). Specifically, you have asked how this amendment changed the standard of conduct for corporate directors.

The Vermont Supreme Court has only infrequently addressed the duties of corporate directors. In Lash v. Lash Furniture Co., 130 Vt. 517, 522 (1972), the Court stated that "[t]he relationship of a director-stockholder to his corporation binds him to use the utmost good faith and loyalty for the furtherance and advancement of the interest of that corporation." The decision in Lash was primarily concerned with the duty of loyalty, as the defendant director in that case was found to have misused corporate assets and funds. *Id.* The Court has not addressed the statutory standard of conduct established by § 8.30, either prior or subsequent to the amendment. The absence of Vermont law on the subject makes it difficult to determine what effect the amendment has on the obligations of corporate directors.

The amendment may, however, be considered in light of the broader context in which it was enacted. This type of statute, often referred to as a "constituency statute," has been enacted in a majority of states over the past fifteen years. The wording of the statutes varies from state to state but generally the statutes specifically permit corporate directors to consider the interests of "stakeholders" or "constituencies" other than shareholders -- such as employees, suppliers, and local communities -- in determining the best interests of the corporation. See generally S.M.H. Wallman, "The Proper Interpretation of Corporate Constituency Statutes and Formulation of Director Duties," 21 Stetson L. Rev. 163 (Fall 1991) (collecting statutes).

Although there are few judicial decisions discussing these statutes, there is a substantial body of legal scholarship addressing the meaning of the statutes and the policy concerns that prompted legislatures to pass them. The statutes were a legislative response to the large number of hostile takeovers and takeover attempts during the 1980s. See L.J. Oswald, "Shareholders v. Stakeholders," 24 J. Corp. L. 1, 3-5 (Fall 1998). Generally, the statutes were aimed at least in part at protecting locally-based corporations from takeover attempts by out-of-state corporations -- and thus protecting local employees and communities. See Committee on Corporate Laws (American Bar Association), "Other Constituencies Statutes: Potential for Confusion," 45 Bus. Law. 2253, 2266 (Aug. 1990).

The legislative history of Vermont's constituency statute suggests that the Vermont legislature shared this goal. Passage of the amendment was urged by Ben & Jerry's Homemade, Inc., a Vermont-based corporation. Representatives of Ben & Jerry's testified before the Senate Finance Committee that the amendment would help the corporation remain independent.

What is less clear, however, is the practical effect that the amendment was intended to have. As noted, the Legislature did not act in response to any Vermont decisions on this issue. It may be presumed, however, that the Legislature was aware of both the widely-accepted norms of corporate law and the fact that many other states had already enacted constituency statutes.

Setting aside the relatively recent emergence of constituency statutes, courts have generally held that the duty of corporate directors to act in the best interests of the

corporation is defined by interests of corporation's shareholders. The best-known early decision on this point is Dodge v. Ford Motor Co., 170 N.W. 668 (Mich. 1919). Rejecting what it called "philanthropic and altruistic" sentiments expressed by Henry Ford, the Michigan Supreme Court held that "[a] business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end." Id. at 684.

More recently, the Delaware Supreme Court has adhered to the "basic principle that corporate directors have a fiduciary duty to act in the best interests of the corporation's stockholders." Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 955 (Del. 1985). (Decisions of the Delaware courts tend to be accorded substantial weight on corporate matters, in light of the extraordinary number of domestic corporations that are incorporated in Delaware.) The Unocal court did suggest that directors analyzing a takeover bid may consider as one factor "the impact on 'constituencies' other than shareholders (i.e. creditors, customers, employees, and perhaps even the community generally)." Id. In a later case, however, the court qualified this point:

Although such considerations [of other corporate constituencies] may be permissible, there are fundamental limitations upon that prerogative. A board may have regard for various constituencies in discharging its responsibilities, provided there are rationally related benefits accruing to the stockholders. However, such concern for non-stockholder interests is inappropriate when an auction among active bidders is in progress, and the object no longer is to protect or maintain the corporate enterprise but to sell it to the highest bidder.

Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 182 (Del. 1986).

Prior to the passage of the 1998 amendment to § 8.30, commentators and at least one court had characterized constituency statutes as a response to, and in effect an abrogation of, the Revlon decision. See Keyser v. Commonwealth Nat'l Financial Corp., 675 F. Supp. 238 (M.D. Penn. 1987); Wallman, 21 Stetson L. Rev. at 186; Committee on Corporate Laws, 45 Bus. Law. at 2265. The court in Keyser noted that Revlon and related cases "may stand for the proposition that once a corporation is up for sale, directors are obligated to get the best price. Pennsylvania law, however, permits directors to consider factors other than price ... and this factor [a constituency statute] apparently was not present in Revlon." 675 F. Supp. at 265. The Committee on Corporate Laws similarly suggested that "the principal effect of these statutes is to preserve this latitude [to consider other constituencies] after directors have made the decision to sell the company." 45 Bus. Law. at 2265.

The Legislature is generally presumed to act purposefully when it enacts legislation. Certainly by enacting this amendment to § 8.30, the Legislature intended to give corporate directors greater latitude to consider the interests of corporate constituencies other than shareholders. See Committee on Corporate Laws, 45 Bus. Law. at 2266 (suggesting that legislatures "intended to provide some support to

directors seeking to thwart unwanted offers” and “to accord directors more than the right they apparently have under existing corporation law to consider the interests of other constituencies in responding to takeover proposals”). It is also likely that the Legislature sought to ensure that directors had the discretion to consider those interests under all circumstances, including the circumstance in which a decision has been made to sell.

In the context of giving this opinion, however, it is not possible to further quantify the effect of the amendment on the obligations of corporate directors. As the court in Keyser noted, “[t]he extent to which price could be sacrificed for . . . social issues” turns on the specific factual context in which directors make a decision.

I hope that this is responsive to your concerns.

Sincerely,

Bridget C. Asay
Assistant Attorney General