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Changes in Legal Protections for Officers of Delaware Corporations

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It is critical for companies with operations in the United States to understand the customary benefits and protections afforded by corporate officers in US companies to ensure they can attract and retain the best executive talent. In addition to offering competitive compensation and employee benefits packages that will attract such talent, companies looking to attract US executives should also ensure that the legal protections afforded to such executive officers are consistent with market standards. While most US C-suite executives will require indemnification agreements as part of their terms of employment, the extent to which an employer can provide certain key legal protections is subject to applicable state law. The corporation statutes of US states attempt to balance each state's conflicting interests in allowing companies to attract and protect their executive officers, while also protecting the shareholders from unreasonably bearing the burden of an executive's failure to fulfill his duties. One recent change in the Delaware corporation law increases the permissible protections for corporate officers. It is likely to be widely adopted by companies incorporated in Delaware as they seek to attract and retain executive officers.

The duty of care is one of the two fundamental fiduciary duties owed by an officer to a corporation, requiring the officer to exercise care and act in an informed manner when acting for the corporation and making decisions on its behalf. Before August 2022, a Delaware corporation could only limit or eliminate monetary liability for breaches of duty of care for its directors but not for its officers. On August 1, 2022, amendments to the Delaware General Corporation Law came into effect that allow Delaware corporations to include exculpation provisions in their certificate of incorporation to eliminate or limit monetary liability for their officers for breaches of the duty of care. Very importantly, this exculpation will not be allowed to protect officers where: (i) the breach of a duty of care also implicates a breach of the duty of loyalty, (ii) the acts or omissions of the officer were not in good faith or involved intentional misconduct, or a knowing violation of law, or (iii) the officer received an improper personal benefit from the transaction in question. In addition, the language of the amended Delaware statute also prohibits the corporation from including exculpation provisions protecting the officer against any actions by the corporation itself (or a derivative action on its behalf).

As it is common amongst Delaware corporations to provide exculpation to their directors to the full extent permitted by Delaware law, most corporations employing sophisticated executives will likely elect to extend this protection to their officers in response to the change in Delaware law. Clients seeking to retain or attract sophisticated management talent in the United States would be well-served to review and update the legal protections they provide to their officers and directors.

