

MAX OVERSIGHT DUTIES: HOW *BOEING* SIGNIFIES A SHIFT IN CORPORATE LAW

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ABSTRACT

In September 2021, the Boeing 737 Max debacle turned into an important moment in corporate law. A Delaware court allowed a derivative lawsuit brought by Boeing shareholders to proceed, based on the theory that Boeing's directors breached their oversight duties by not doing enough to monitor, prevent, and react to fatal airplane safety issues. This Essay explains what the *Boeing* decision means for director oversight duties going forward, and uses it as a springboard to discuss broader trends in corporate law. Specifically, the Essay makes the following five contributions.

First, the Essay delineates the contours of a new era of heightened oversight duties. Corporate law courts are increasingly willing to designate certain compliance risks as "mission critical," thereby activating an enhanced scrutiny mode. *Boeing* suggests that practically all directors of manufacturing companies are operating in or around the mission critical zone these days, and illustrates just how enhanced the scrutiny is once in this zone. Second, the Essay fleshes out a shift in focus: from scrutinizing compliance with regulations meant to protect investors (such as financial reporting), to scrutinizing compliance with regulations meant to protect broader societal interests (such as product safety). *Boeing*, for example, faults directors for focusing on restoring corporate profitability and image instead of putting consumer safety front and center. Third, the Essay uses *Boeing* to show how corporate law guides behavior not just directly, through legal sanctions, but also (and indeed more so) indirectly, through shaping norms and reputations in the business community. *Boeing* did not end in a verdict in favor of the plaintiffs: it was instead settled quickly after the motion to dismiss. Still, the case created significant changes in the advice that lawyers give their director clients, and in the volume and tone of media coverage, which in turn created reputational fallout. Fourth, the Essay evaluates the desirability of the *Boeing* development. On one hand, the development holds the promise of mitigating incentives to remain ignorant, and improving accountability. On the other hand, *Boeing* may have gone too far in removing corporate law's guards against hindsight bias. Finally, the Essay spotlights two big questions that *Boeing* left unanswered: *officer* oversight liability, and director liability for oversight of *nonlegal* requirements.

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INTRODUCTION

Two Boeing 737 Max airplanes crashed within months of each other, killing all 364 passengers and crew members aboard. The crashes ignited a heated discussion over airplane safety regulation.¹ Then, a year and a half later, the Max debacle turned into an important moment in corporate law. In September 2021, a Delaware court allowed a derivative lawsuit brought by several Boeing shareholders to proceed, finding it reasonable to infer that Boeing’s directors had breached their oversight duties by not doing enough to monitor, prevent, and react to the 737 Max safety issues.² The *Boeing* case signifies a shift in the way that corporate law treats the protection of broader societal interests. For decades, corporate law has remained relatively silent on issues of product safety and corporate compliance more generally. Yet, over the past two years, a chain of successful failure-of-oversight claims (dubbed “*Caremark*” claims, after Delaware’s leading precedent) has signaled a new era in director oversight duties.

The *Boeing* case perfectly illustrates the two pillars of this new *Caremark* era: willingness to apply enhanced scrutiny of board oversight efforts, and willingness to

¹ Niraj Chokshi, *House Report Condemns Boeing and F.A.A. in 737 Max Disasters*, N.Y. TIMES (Sep. 16, 2020) (describing a House Report condemning the lack of regulatory oversight on the part of the Federal Aviation Administration (FAA)); Natalie Kitroeff, *Boeing Underestimated Cockpit Chaos on 737 MAX, N.T.S.B Says*, N.Y. TIMES (Sep. 26., 2019) (describing a National Transportation Safety Board’s report, hearings in congress, letters by the United States Office of Special Counsel, and so on).

² *In re Boeing Co. Derivative Litig.*, C.A. No. 2019-0907-MTZ, 2021 Del. Ch. LEXIS 197 (Del. Ch. Sep. 7, 2021) (hereinafter: *Boeing*).

grant shareholders access to internal company documents in order to investigate potential failure-of-oversight claims.

First, *Boeing* shows just how much Delaware courts are willing to designate certain compliance risks as “mission critical.” Not all potential risks are created equal from a board-oversight-duties perspective. Risks that implicate the core business of the company and are externally regulated earn the mission critical designation, which means that the courts will scrutinize board oversight of them more rigorously.³ While many past *Caremark* cases scrutinized compliance with regulations meant to protect investors qua investors (such as financial reporting requirements), nowadays courts increasingly scrutinize compliance with regulations meant to protect broader societal interests (such as product safety). The *Boeing* decision, in particular, faults directors for managing the Max crisis with a focus on restoring profitability and image concerns, instead of putting consumer safety front and center.⁴ Further, while other recent cases have applied enhanced scrutiny of product safety in the context of smaller companies whose existence depends on one product line, *Boeing* applies it in the context of a giant company with many subunits.⁵ Following *Boeing*, arguably all directors of manufacturing companies operate in or around the mission critical zone.⁶

Second, *Boeing* shows just how much outside shareholders can utilize their inspection rights to hold directors accountable for failures of oversight. Shareholders have always enjoyed a qualified right to inspect their company’s “books and records,” nestled in Delaware’s Section 220.⁷ But in recent years the courts have liberalized their interpretation of Section 220’s requirements, so that they now order provision of documents in more cases, and order provision of more types of documents.⁸ From this vantage point, the most important part in the *Boeing* decision is footnote 1. Vice Chancellor Zurn tells us there that the entire case rests on a prior Section 220 request, which provided plaintiffs with access to over 44,000 internal documents containing

³ *Marchand v. Barnhill*, 212 A.3d 805, 822 (Del. 2019).

⁴ *Boeing*, at *48.

⁵ See also *Teamsters Loc. 443 Health Servs. & Ins. Plan v. Chou*, No. 2019-0816-SG, 2020 WL 5028065 (Del. Ch. Aug. 24, 2020) (applying the enhanced oversight duties mode in a context of violations of law that happened in one tiny subsidiary of a giant pharmaceutical company).

⁶ Roy Shapira, *A New Caremark Era: Causes and Consequences*, 98 WASH. U. L. REV. 1857, 1866 (2021) (“one could provocatively maintain that everything is regulatory mission critical these days”); Stephen Bainbridge, *After Boeing, Caremark is No Longer “The Most Difficult Theory in Corporation Law upon Which a Plaintiff Might Hope to Win a Judgment,”* PROFESSORBAINBRIDGE.COM (Sep. 8, 2021), <https://www.professorbainbridge.com/professorbainbridge.com/2021/09/after-boeing-caremark-is-no-longer-the-most-difficult-theory-in-corporation-law-upon-which-a-plainti.html> (“After all, how many products these days come without safety warnings? How many production lines are not extensively regulated? Zurn’s approach leaves every manufacturer vulnerable to *Caremark* claims”).

⁷ DEL. CODE ANN. tit. 8, § 220 (2021).

⁸ Shapira, *supra* note 6, at 1872-77. On a similar trend in M&A litigation see generally Roy Shapira, *Corporate Law, Retooled: How Books and Records Revamped Judicial Oversight*, 42 CARDOZO L. REV. 1949 (2021).

630,000 pages about Boeing's oversight of airplane safety. Such richness of detail allows outside shareholders to plead with particularity facts about what corporate insiders knew, when they knew it, and what they did or did not do to address problems in real time. Armed with such a powerful *pre-filing* discovery tool, plaintiffs these days are more likely to be able to show that the board never even discussed a critical compliance issue, or that the board was notified of a critical issue yet failed to make efforts to remedy it.

The combination of enhanced scrutiny and liberalized inspection rights allows shareholders to regularly overcome what once seemed like an insuperable pleading hurdle in oversight cases. The chain of recent successful *Caremark* claims is therefore a trend, and *Boeing* signals that the trend is only intensifying. This Essay uses *Boeing* as a springboard to delineate the contours of this new mode of heightened oversight liability, evaluate its desirability, and generate implications for academics and policymakers.

The Essay proceeds in three parts. Part I describes the *Boeing* case: from the corporate governance problems behind the Max debacle, to the unique procedural aspects of the court decision.

Part II explains what *Boeing* means for director oversight duties going forward, and what it tells us about how Delaware corporate law works more generally. *Boeing* expands the zone of enhanced scrutiny of board oversight so that it now applies to more boards. It also evidences how enhanced the scrutiny is once a board is in the zone, along the following two dimensions: (1) scrutinizing directors not just for what they knew but also for what they should have known; and (2) scrutinizing directors not just for doing nothing but also for not doing enough. More generally, *Boeing* illustrates how corporate law guides behavior even in the absence of verdicts reached after a full trial. Part II analyzes the content of law firm memos and media coverage following *Boeing*, to highlight how even a decision in a preliminary stage (motion to dismiss) can reshape the legal advice that corporate directors receive, and reshape the reputations of said directors and their companies.

Part III evaluates the desirability of these new developments in corporate law. Overall, the revamped approach to oversight duties seems desirable, as it holds the potential to balance the flaws of other enforcement mechanisms. Pertinently, the new *Caremark* era can mitigate the tendency toward *willful blindness*. Corporate directors have strong incentives to remain ignorant about decisions that prioritize profits over safety or skirt regulatory requirements more generally. Prioritizing profits is good for directors who receive substantial stock-based compensation. And remaining ignorant about *how* profits were obtained is good for directors' ability to maintain plausible deniability and escape accountability. The new mode of oversight duties litigation, as illustrated in *Boeing*, counters these dynamics, by emphasizing *culpable ignorance* (faulting directors for what they should have known), and *proper documentation* (incentivizing more upwards flows of information). Still, in some particular areas the

Boeing development may have strayed too far from well-accepted Delaware principles, and Part III details four aspects worth worrying about going forward. The *Boeing* development seemingly (1) removes some guards against hindsight bias, (2) disincentivizes investments in subsequent remedial measures, (3) creates perverse incentives for boards to be overly confrontational with management once crisis hits, and (4) too readily lets corporate *officers* off the hook.

A short Conclusion spotlights the big question that *Boeing* left unanswered, namely, whether we may expect the trend of heightened oversight duties to expand also to *nonlegal* requirements (ESG issues).

I. THE *BOEING* CASE

A. *Factual Background*

The technological explanation for the two crashes is relatively straightforward: in both cases, an anti-stall system named MCAS was triggered by a faulty sensor reading, constantly pushing the airplanes' nose down.⁹ For our purposes, the interesting question is the more complex one: how did the checks and balances inside Boeing fail to detect, prevent, and be fully transparent about such a fatal technological flaw?¹⁰ To answer this question we need to go back to how and why Boeing introduced Max into the market in the first place.

Facing intense competition with Airbus, Boeing announced in 2011 that it would introduce a new 737 model.¹¹ The new, Max model was supposed to answer clamoring from airline operators for more fuel efficiency. To achieve that, Max was designed with larger engines, which were placed further forward on the wings compared to earlier models. These differences in aerodynamics made the Max prone to pitching up. To fix the tendency to pitch up, Boeing installed the MCAS system, meant to automatically push the airplane's nose back down. But the activation of MCAS relied on a single sensor, thereby rendering it prone to faulty readings.¹² To make things worse, Boeing wished to downplay this late design change, portraying it as a minor modification to an existing system, rather than a new system.¹³ The end goal for Boeing was maintaining "commonality" between the new, Max model and the old, NG model: this way, Boeing could expedite regulatory certification and cut the costs of

⁹ Chokshi, *supra* note 1. MCAS stands for "Maneuvering Characteristics Augmentation System."

¹⁰ David Gelles, *Boeing's 737 Max is a Saga of Capitalism Gone Awry*, N.Y. TIMES (Nov. 24, 2020) ("the true cause of the crashes wasn't faulty software. It was a corporate culture gone horribly wrong").

¹¹ *Id.*

¹² Robert E. Rosen, *Critical Thinking and Regulation: Learning from Engineering Mistakes*, TRANS. L. J. (forthcoming, 2022), <https://ssrn.com/abstract=3932613> (manuscript at n.57).

¹³ Chokshi, *supra* note 1.

expensive pilot training.¹⁴ Boeing thus had strong cost-cutting incentives to downplay the role of MCAS. Pertinently, the company failed to fully share information about the new system with regulators and pilots.¹⁵

The first crash happened in October 2018, when MCAS on a Lion Air airliner activated shortly after takeoff, causing the plane to dive into the Java Sea, killing all 189 passengers and crew members on board. Boeing allegedly did not fully inform the Lion Air crew about how MCAS functioned.¹⁶ The second crash happened in March 2019, when MCAS similarly constantly pushed an Ethiopian Airlines airliner down. By then, the pilots were aware of the need to reverse the procedure, but were apparently swamped with a cacophony of alerts, and the plane crashed, killing all 157 passengers and crew members.¹⁷

The primary victims of the Max debacle are those 346 who died and the families they left behind.¹⁸ But from a corporate law perspective, it is notable that the crashes caused significant attendant harms to Boeing and its shareholders: a 20-month global grounding of its fleet, \$20 billion in non-litigation costs, several additional billions in litigation costs, long-lasting reputational fallouts, and so on.¹⁹

A couple of pension fund shareholders from New York and Colorado sought to investigate whether these harms are attributed to failure of oversight on the part of Boeing's directors and officers. To do that, the shareholders requested to inspect Boeing's books and records. Based on the information they gleaned from internal documents, they filed a consolidated derivative action against thirteen directors and eight officers, for harming the company by breaching their oversight duties.

¹⁴ Boeing, at *21. When an airplane company can show that the new model is substantially similar to the old model, it can conduct pilot training via a tablet computer instead of costly flight simulator training. Indeed, pilots testified that their entire training on moving from NG to Max boiled down to "little more than a one-hour session on an iPad," and that they did not realize that the new model contained changes in the flight-control system. Dominic Gates, *U.S. Pilots Flying 737 MAX Weren't Told about New Automatic Systems Change Linked to Lion Air Crash*, SEATTLE TIMES (Nov. 12, 2018).

¹⁵ See, e.g., *How "Boeing's Fatal Flaw" Grounded the 737 Max and Exposed Failed Oversight*, N.Y. TIMES (Sep. 13, 2021) (an investigative report detailing how competitive pressures influenced the efforts to bring 737 MAX to market and led to insufficient oversight and inadequate pilot training); Chokshi, *supra* note 1 (noting that during the Max development, Boeing's test pilots reported the difficulties of reversing an MCAS activation; and that the company had promised one of its key clients, Southwest Airlines, a \$200 million discount in its order of 737 MAXs if the FAA ended up requiring simulator training instead of tablet training); Jack Nicas et al., *Boeing Built Deadly Assumptions into 737 Max, Blind to a Late Design Change*, N.Y. TIMES (Jun. 1, 2019) (an investigative report detailing how "test pilots, engineers and regulators were left in the dark about a fundamental overhaul to an automated system that would ultimately play a role in two crashes").

¹⁶ Boeing, at *34.

¹⁷ Kitroeff, *supra* note 1.

¹⁸ Boeing, at *1.

¹⁹ *Id.* at *4; Gelles, *supra* note 10.

B. Legal Analysis

Defendants filed a motion to dismiss, claiming that plaintiffs did not make proper demand on the board.²⁰ To survive such a motion, plaintiffs effectively need to show that demand was futile because the majority of directors face a substantial likelihood of liability for their role in the event in question (and so we cannot trust their judgment regarding whether the company should pursue its claims).²¹ Accordingly, the court needs to evaluate, already in such a preliminary stage, the merits of the claims that the directors breached their oversight duties. The framework for evaluating such oversight claims is termed “*Caremark*”, after Delaware’s 1996 decision.²²

To convince the court of substantial likelihood of liability, plaintiffs need to plead with particularity facts that pertain to one of two alternative *Caremark* prongs: either that directors failed to implement *any* reporting system of control; or that directors implemented such a system, yet consciously failed to monitor it, such as by not responding to red flags.²³ For decades, academics and practitioners have considered this *Caremark* pleading hurdle to be virtually insuperable.²⁴ After all, it is extremely hard for outsiders to show not just that the corporate insiders breached their duties, but that they breached them *knowingly*. Many academics and practitioners have accordingly considered *Caremark* duties an irrelevant, toothless tiger.²⁵

The tide started to turn in June 2019, with *Marchand v. Barnhill*.²⁶ *Marchand* revolved around food safety issues at Blue Bell, a leading ice-cream manufacturer. A line of Blue Bell’s ice-cream products was contaminated with listeria, causing three deaths, massive recalls, and attendant financial, legal, and reputational costs to the company and its shareholders.²⁷ The Court of Chancery routinely dismissed the

²⁰ DEL. R. CH. CT. 23.1. Shareholder derivative litigation displaces the board’s usual authority to assert its company’s legal claims. The courts will allow such displacement only if shareholders can show that they made “a demand” on the board to pursue the company’s purported claims, or show that making such a demand would be futile.

²¹ *Rales v. Blasband*, 634 A.2d 927, 930 (Del. 1993); *United Food & Com. Workers Union & Participating Food Indus. Empls. Tri-State Pension Fund v. Zuckerberg*, 250 A.3d 862 (Del. Ch. 2020), *aff’d* at 2021 WL 4344361.

²² *In re Caremark Int’l Inc. Derivative Litig.*, 698 A.2d 959 (Del. Ch. 1996), *adopted by* *Stone v. Ritter*, 911 A.2d 362, 365 (Del. 2006).

²³ *Stone v. Ritter*, *id.* at 370.

²⁴ For a comprehensive overview see Elizabeth Pollman, *Corporate Oversight and Disobedience*, 72 VAND. L. REV. 1013 (2019).

²⁵ See, e.g., Megan W. Shaner, *The (Un)Enforcement of Corporate Officers’ Duties*, 48 U.C. DAVIS L. REV. 271, 307 (2014); Mercer Bullard, *Caremark’s Irrelevance*, 10 BERKELEY BUS. L.J. 15, 44 (2013); Anne Tucker Nees, *Who’s the Boss? Unmasking Oversight Liability within the Corporate Power Puzzle*, 35 DEL. J. CORP. L. 199, 216 (2010); Charles M. Elson & Christopher J. Gyves, *In re Caremark: Good Intentions, Unintended Consequences*, 39 WAKE FOREST L. REV. 691, 692 (2004). See also Claire A. Hill & Brett H. McDonnell, *Reconsidering Board Oversight Duties after the Financial Crisis*, 2013 U. ILL. L. REV. 859 (arguing board monitoring duties should be expanded).

²⁶ *Marchand v. Barnhill*, 212 A.3d 805 (Del. 2019).

²⁷ *Id.* at 812–13, 822.

shareholders' failure-of-oversight claim, implying that they were not able to locate evidence linking the bad outcomes at the company level to bad intentions on the directors' part (no bad faith). Yet for Delaware's Supreme Court, the fact that there was no discussion of the listeria issues at the board level indicates, in itself, an utter failure of oversight.²⁸ If you are a director of a company that sells nothing but ice cream, and you do not allocate time and responsibilities to discussing potential food safety issues, you are not trying in good faith to oversee the company's operations, Chief Justice Strine reasoned, reversing the Court of Chancery's dismissal.²⁹ *Marchand* opened the door to other successful *Caremark* claims.³⁰ And so by 2021, when VC Zurn was facing the "substantial likelihood of liability" question in *Boeing*, she had a revamped, less director-friendly framework to work with.

In a rare feat, VC Zurn found pleading-stage indications of both *Caremark* prongs: directors completely failed to monitor air safety before the first crash (prong one), and then failed to respond to known safety risks after that crash (prong two).

Much of the decision focuses on the prong-one analysis. Closely following the *Marchand* framework, VC Zurn pointed to indications that the board did not even try in good faith to monitor air safety: the board did not have a committee specifically charged with airplane safety; the board as a whole discussed safety only in passing; the board received management reports on safety only ad hoc and passively, without probing further; and so on.³¹

Such indications of prong one were enough to reject the motion to dismiss. But VC Zurn continued to prong two, reaching pleading-stage inferences that directors failed to react to known problems (in *Caremark* lingo: ignored red flags). The decision specifically highlighted how the board treated the first crash mostly as a public-relations problem rather than a safety problem, and that the board supposedly publicly lied about its safety-monitoring efforts.³² VC Zurn clarified that the board's reaction cannot be considered merely a failed attempt to address red flags; there are pleading-stage indications the board was rather aware or had to be aware that their tepid response would fall short.³³

²⁸ *Id.* at 817.

²⁹ *Id.* at 824.

³⁰ *In re Clovis Oncology, Inc. Derivative Litig.*, No. 2017-0222-JRS, 2019 WL 4850188 (Del. Ch. Oct. 1, 2019); *Hughes v. Hu*, No. 2019-0112-JTL, 2020 WL 1987029 (Del. Ch. Apr. 27, 2020); Chou, *supra* note 5. See also *Inter-Mkt'ing Grp. USA v. Armstrong*, 2020 WL 756965 (Del. Ch. Jan. 31, 2020) (applying the *Marchand* framework and rejecting the motion to dismiss in the context of pipeline integrity issues at a master limited partnership). For an analysis of the *Caremark* cases up to 2020 see Shapira, *supra* note 6, at 1861-66.

³¹ *Boeing*, at *87. Compare *Marchand*, at 813.

³² *Boeing*, at *91.

³³ *Id.* at *96. Honest, failed attempts do not give rise to *Caremark* liability; bad-faith attempts do. See generally *Richardson v. Clark*, C.A. No. 2019-1015-SG (Del. Ch., Dec. 31, 2020).

The court thus rejected the motion to dismiss *Caremark* claims against the directors. At the same time, it granted the motion to dismiss two additional claims that did not pertain to director oversight duties. The court dismissed a “waste” claim against the board for allowing Boeing’s CEO at the time of the crashes to retire with full compensation (retaining unvested equity worth over \$38.6 million).³⁴ Plaintiffs claimed that such a decision amounts to a waste of shareholders’ money, as there is no rational justification for it aside from directors protecting their own narrow interests (making sure that the CEO remains silent about the directors’ role in the debacle).³⁵ The court disagreed, noting that ensuring that the CEO goes quietly may well be promoting the legitimate business objective of “avoiding further reputational and financial harm to the Company.”³⁶ Further, the court dismissed plaintiffs’ claims against Boeing’s officers. Here, the reasoning was more procedural: the plaintiffs supposedly did not argue that Boeing’s directors are beholden to or dominated by its officers, and so the court found no reason not to trust the directors’ judgment regarding whether to pursue claims against the officers.³⁷ In other words, demand could not be considered futile.

As the next Part shows, *Boeing* is more than just another link in the chain of recent successful *Caremark* claims; it also expands and puts an exclamation mark on a heightened mode of oversight liability.

II. WHAT *BOEING* TEACHES US ABOUT OVERSIGHT DUTIES AND CORPORATE LAW

This Part examines the potential outsized impact of the *Boeing* decision on corporate behavior. Section A explains how *Boeing* expands the zone of enhanced oversight duties. Section B details how *Boeing* illustrates the Section-220 turn in oversight litigation, and how it is likely to affect information flows inside large corporations. Section C uses *Boeing* to illustrate the way that Delaware corporate law works.

A. Boards Face More Rigorous Scrutiny

Boeing signifies the heightening of director oversight duties in two important ways: expanding the zone where the enhanced-scrutiny mode applies, and illustrating just how enhanced the scrutiny is inside that zone.

Following *Marchand*, *Boeing* designates product safety risks as “mission critical” for manufacturers operating in regulated industries (read: practically all industries³⁸).

³⁴ On the waste standard see *In re Citigroup Inc. S’holder Deriv. Litig.*, 964 A.2d 106, 136 (Del. Ch. 2009).

³⁵ *Boeing*, at *98.

³⁶ *Id.* at *100.

³⁷ *Id.* at *101.

³⁸ This was the reading that legal advisors to boards adopted. See, e.g., Paul E. Kalb & Holly J. Gregory, *Boeing Case Highlights Risk for Health, Life Sciences Boards*, ENHANCED SCRUTINY (Oct. 8,

But *Boeing* goes beyond *Marchand* by applying the “mission critical” designation even in the context of giant companies. Let us recall that the first successful *Caremark* cases invoked mission critical compliance in the context of “monoline” (single-product), smaller companies.³⁹ For a company that sells only ice cream, food safety is clearly critical;⁴⁰ for an upstart biotech company that has only one promising drug in its pipeline, following FDA protocols is clearly critical;⁴¹ and so on. Directors in giant companies, by contrast, have traditionally faced a *diluted* prospect of oversight liability. In the prior precedent of *Allis-Chalmers*,⁴² Delaware’s Supreme Court based its refusal to impose liability on the presumed inability to monitor misconduct in massive corporations.⁴³ In companies such as Allis-Chalmers (with over 30,000 employees and 24 plants), the inherent complexity and decentralized decision-making processes make it impracticable to expect directors to know when company employees engage in misconduct, or so the court reasoning implied.⁴⁴ In August 2020, the *Chou* court broke from this line of thinking, invoking “mission critical” for rule violations in a tiny subsidiary of a giant pharmaceutical company.⁴⁵ In *Boeing*, the company in question is by far the biggest ever to receive the “mission critical” treatment (Boeing has about 140,000 employees, compared to Allis-Chalmers’ 30,000).⁴⁶ The turning of the tide is thus complete: size is no longer a barrier for enhanced scrutiny of board oversight.

Beyond expanding the mission critical zone so that it applies to more boards, *Boeing* evidences how enhanced the scrutiny is once a board is in the zone. Consider the following two dimensions: (1) scrutinizing directors not just for what they knew but also for what they should have known; and (2) scrutinizing directors not just for doing nothing but also for not doing enough.

Historically, courts in *Caremark* cases refrained from telling directors what they *should have* known, and interfered based only on what directors actually knew about compliance failures.⁴⁷ Lack of documentation usually played in favor of defendants,

2021), <https://ma-litigation.sidley.com/2021/10/boeing-case-highlights-risk-for-health-life-sciences-boards/> (noting that all directors of companies in regulated industries should take notice of *Boeing*).

³⁹ *Marchand*, at 810-11.

⁴⁰ *Id.*

⁴¹ *Clovis*, at *12-13.

⁴² *Graham v. Allis-Chalmers Mfg. Co.*, 188 A.2d 125 (Del. 1963).

⁴³ *Id.* at 129.

⁴⁴ Robert T. Miller, *Wrongful Omissions by Corporate Directors: Stone v. Ritter and Adapting the Process Model of the Delaware Business Judgment Rule*, 10 U. PA. J. BUS. & EMP. L. 911, 935 (2008).

⁴⁵ *Supra* note 5.

⁴⁶ Outside of Delaware, a California Federal court has already rejected a motion to dismiss a *Caremark* claim against the directors of an even bigger company, namely, Wells Fargo, for failure of oversight concerning the fake accounts scandal. *In re Wells Fargo & Co. S'holder Derivative Litig.*, No. 16-CV05541-JST, 2017 WL 4414304 (N.D. Cal. Oct. 4, 2017).

⁴⁷ *Citigroup*, *supra* note 34, at 127. See also Stephen M. Bainbridge, *Caremark and Enterprise Risk Management*, 34 J. CORP. L. 967, 986 (2009); Miller, *supra* note 44.

as an indication that directors were not aware of problems (did not act in bad faith). *Boeing* signifies a new *Caremark* era, in which lack of documentation is frequently viewed as evidence of lack of effort to implement reporting systems, and lack of needed response and follow-up to a red flag.⁴⁸

Additionally, historically, defendants in *Caremark* litigation could get off by showing any type of compliance efforts. Some compliance was enough compliance. *Boeing* shows that this is clearly not the case today. Consider the following examples:⁴⁹ Boeing's board agenda reflected allocating time to discuss safety, yet the court criticized them for allotting only five minutes. Boeing's board minutes invoked "safety" several times, yet the court criticized them for doing this only in passing and in the context of getting on the regulator's good side. The minutes also showed that management shared information on airplane safety with the board, yet the court faulted them for not treating information from management more critically. All in all, *Boeing* shows just how much courts are willing to scrutinize what directors should have known and how they should have reacted.

B. Shareholders Enjoy More Expansive Inspection Rights

To survive the *Caremark* pleading hurdle, it is not enough to show that the company has suffered a trauma; plaintiffs have to link the directors to the trauma. That is, plaintiffs have to plead with particularity facts about what directors knew and when they knew it. These are not the types of facts that one can readily glean from public documents.⁵⁰ To succeed in a *Caremark* claim, plaintiffs therefore need to be able to conduct thorough investigations *before* filing their lawsuit and reaching the discovery stage. One of the tools at hand to conduct pre-filing investigations is Delaware's Section 220,⁵¹ which provides shareholders with a qualified right to inspect their company's "books and records." Indeed, the courts themselves have long admonished plaintiffs to utilize their inspection rights before filing *Caremark* claims.⁵²

In recent years, Section 220 has become an especially powerful pre-filing investigatory tool. Aside from (some) plaintiff attorneys climbing the learning curve in utilizing Section 220, the change can be attributed to the courts increasingly liberalizing the Section's requirements. Courts now provide internal documents in more cases (liberalizing the "proper purpose" requirement),⁵³ and provide more types

⁴⁸ *Infra* note 58 and the accompanying discussion.

⁴⁹ *Boeing*, at *41-44.

⁵⁰ *South v. Baker*, 62 A.3d 1, 23 (Del. Ch. 2012).

⁵¹ DEL. CODE ANN. tit. 8, § 220 (2021).

⁵² *AmerisourceBergen Corp. v. Lebanon Cnty. Emps' Fund*, 243 A.3d 417, 426 (Del. 2020); *Wood v. Baum*, 953 A.2d 136, 143-44 (Del. 2008).

⁵³ *See, e.g., AmerisourceBergen, id.* at 437 (clarifying that credible suspicions of wrongdoing at the company level are proper purpose for inspection, regardless of whether directors were exculpated).

of documents (liberalizing the “permissible scope” requirement).⁵⁴ The expansion of shareholders’ inspection rights enabled the new *Caremark* era.⁵⁵ Shareholders and their attorneys are more likely to use Section 220 to extract internal documents that implicate directors’ mental state and awareness. Accordingly, they can more easily show that the board never even discussed a critical compliance issue, or knew about critical problems yet chose to ignore them.

Nowhere is this Section-220 turn in *Caremark* litigation clearer than in *Boeing*. Footnote 1 is key for understanding the entire decision: VC Zurn notes there that the plaintiffs carefully reviewed 630,000 pages of materials relevant to airplane safety oversight in Boeing, and maintains that one can reasonably infer that whatever “exculpatory information [is] not reflected” in this mountain of documents does not exist. The super-detailed Section 220 record allowed the court to infer that directors faced substantial likelihood of liability under both alternative *Caremark* prongs.⁵⁶

In the “what is not documented does not exist” department, the record shows no regular allocation of time to safety assessments prior to the crashes, and no documentation of directors seeking or receiving written information after the crashes about how Boeing dealt with regulators, the required amount of pilot training, or the risks of MCAS and the single sensor the system relied on. In the “tepid responses to red flags” department,⁵⁷ the record indicates that directors delayed an internal investigation, and that when they did come around to discussing safety, they allotted only five minutes to the subject.⁵⁸

The upshot is that even if the standard for oversight liability remains a high bar,⁵⁹ shareholders’ ability to meet this bar has improved. The combination of the courts’ increased willingness to scrutinize directors’ conduct in this context and plaintiffs’ increased ability to document directors’ conduct is likely to continue generating successful *Caremark* claims going forward.⁶⁰

⁵⁴ See, e.g., *In re Facebook, Inc. Section 220 Litig.*, No. 2018-0661-JRS, 2019 WL 2320842, at *18 n.185 (Del. Ch. May 30, 2019) (ordering Facebook executives to produce emails relating to data privacy issues, so as to investigate potential failure-of-oversight claims concerning the Cambridge Analytica scandal). See also, in the context of M&A litigation, *KT4 Partners LLC v. Palantir Techs. Inc.*, 203 A.3d 738 (Del. 2019); Shapira, *supra* note 8.

⁵⁵ This is the main argument in Shapira, *supra* note 6.

⁵⁶ The *Boeing* complaint also relied on a wealth of public information coming from investigative reporting and congressional hearings, which extracted their own fair share of internal documents.

⁵⁷ Here, red flags came in the form of the crashes themselves and the investigative reports that came thereafter. For more on how investigative journalism interacts with board oversight duties see Michael J. Borden, *The Role of Financial Journalists in Corporate Governance*, 12 FORDHAM J. CORP. & FIN L. 311 (2007).

⁵⁸ *Boeing*, at *43, 80-81, n.294.

⁵⁹ *Supra* note 33.

⁶⁰ Shapira, *supra* note 6.

C. Corporate Law Guides Behavior Indirectly, through Law Firm Memos and Reputational Fallout

Boeing did not end with a final verdict for the plaintiffs. Neither have the other successful *Caremark* claims. They were “successful” only in the sense of surviving the preliminary motion to dismiss. One could therefore argue that our portrayal of a new *Caremark* era is overblown: without final verdicts in favor of plaintiffs, there is no reason to believe that the new era will generate more compensation for shareholders or better deterrence.

In fact, such an objection misconstrues how Delaware corporate law works. In corporate law, in general, very few cases are ultimately decided in final verdicts.⁶¹ And even fewer are decided in favor of the plaintiffs (corporate decision-makers almost never pay out of pocket).⁶² To measure corporate law’s impact one cannot focus on the sanction imposed after a full trial. Corporate law’s impact on oversight instead comes from paying settlements *ex post* and planning how to avoid the risks and costs of litigation *ex ante*.

Boeing illustrates the three core conduits through which corporate law guides behavior: hefty settlements, law firm memos, and *nonlegal* sanctions.

Settlements. In November 2021, two months after VC Zurn rejected the motion to dismiss and before discovery even started, the parties reached a settlement. That settlement included a payment of over \$237 million: by far the highest ever in a *Caremark* case.⁶³ It also included commitments by Boeing to take prophylactic corporate governance measures, such as appointing a board member with expertise in airplane safety and hiring an ombudsman to handle internal safety complaints.⁶⁴ This is a recurring pattern: *Caremark* cases that survive the motion to dismiss tend to settle

⁶¹ To illustrate, during a five-year period, there have been only five final verdicts reached after a full trial in derivative or class actions. Lawrence A. Hamermesh & Michael L. Wachter, *The Importance of Being Dismissive: The Efficiency Role of Pleading Stage Evaluation of Shareholder Litigation*, 42 J. CORP. L. 597, 652 (2017).

⁶² To illustrate, during a twenty-five-year period, there have been only thirteen instances in which outside directors of public companies paid out of pocket. Bernard Black, Brian Cheffins, & Michael Klausner, *Outside Director Liability*, 58 STAN. L. REV. 1055, 1055 (2006).

⁶³ Ellen Bardash, *Proposed \$237.5M Boeing Deal Could be Largest ‘Caremark’ Settlement in Delaware History*, LAW360 (Nov. 8, 2021), <https://www.law.com/delbizcourt/2021/11/08/proposed-237-5m-deal-with-boeing-could-be-largest-caremark-settlement-in-delaware-history/>. Those interested in Delaware litigation’s inside baseball will note that the *Boeing* settlement is the second ever in Delaware after *Activision*, and that the same four-attorney firm of Friedlander & Gorris was behind both cases. Tom Hals, *Judge OKs Activision \$275 MLN Shareholder Settlement, \$72 MLN for Lawyers*, REUTERS (May 21, 2015), <https://www.reuters.com/article/activision-settlement-idUSL1N0YB2TS20150520>.

⁶⁴ Linda Chiem, *Boeing Board Inks \$238M Deal to End 737 Max Derivative Suit*, LAW360 (Nov. 5, 2021).

quickly and for hefty amounts, as defendants attempt to avoid prolonged legal battle and discovery.⁶⁵

Still, we cannot assume that such settlements do a good job in guiding corporate compliance ex ante, as payments (in *Boeing* and elsewhere) tend to come not out of directors' pockets but out of insurers' pockets.⁶⁶ The impact that corporate law has on behavior therefore tends to come from two other mechanisms, namely, law firm memos and the risk of reputational fallout.

Law firm memos. Following big cases, legal advisors send their clients memos explaining what the court decision means for them going forward.⁶⁷ Elsewhere I detailed how the first quadfecta of successful *Caremark* cases (*Marchand*, *Clovis*, *Hu*, *Chou*) created a wave of law firm memos, calling on boards to put compliance issues on the agenda, and properly document compliance deliberations and efforts.⁶⁸ The *Boeing* case created its own tsunami of legal advice, this time with emphasis on the need to adopt *structural changes* to board oversight.⁶⁹ Law firm memos following *Boeing* started by reemphasizing the existing themes: place compliance on top of your agenda, and make sure you properly document it.⁷⁰ They then highlighted new points

⁶⁵ *Marchand*, for example, was settled for \$60 million. Chris Brummer & Leo E. Strine, Jr., *Duty and Diversity*, 75 VAND. L. REV. 1, 74 (2022).

⁶⁶ For a classic discussion on why insurance cannot be counted on to promote better corporate governance see Tom Baker & Sean J. Griffith, *The Missing Monitor in Corporate Governance: The Directors' & Officers' Liability Insurer*, 95 GEO. L.J. 1795 (2007). For a recent discussion with a concrete policy recommendation see Andrew Verstein, *Changing Guards: Improving Corporate Governance with D&O Insurance Rotations*, VA. L. REV. (forthcoming, 2022), <https://ssrn.com/abstract=3660571>. For a view from within the industry see Kevin LaCroix, *Mandating D&O Rotation? A Critique*, D&O DIARY (Aug. 23, 2020), <https://www.dandodiary.com/2020/08/articles/d-o-insurance/a-critique-of-requiring-mandatory-do-insurer-rotation/>.

⁶⁷ On the importance of law firm memos see Edward B. Rock, *Saints and Sinners: How Does Delaware Corporate Law Work?*, 44 UCLA L. REV. 1009, 1070-71 (1997).

⁶⁸ *Shapira*, supra note 6. See also Robert C. Bird, *Caremark Compliance for the Next Twenty-Five Years*, 58 AM. BUS. L.J. 63, 86-102 (2021).

⁶⁹ David A. Katz & Laura A. McIntosh, *Board Structure is Key to Oversight*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Sep. 27, 2021), <https://corpgov.law.harvard.edu/2021/09/27/board-structure-is-key-to-oversight/>. See also Gail Weinstein et al., *Boeing: Rejecting Early Dismissal of Claims against Directors for Inadequate Risk Oversight*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Oct. 21, 2021), <https://corpgov.law.harvard.edu/2021/10/21/boeing-rejecting-early-dismissal-of-claims-against-directors-for-inadequate-risk-oversight/>; Jim Ducayet et al., *Delaware Chancery Court Affirms Importance of Director Oversight in Wake of Boeing Crashes*, ENHANCED SCRUTINY (Oct. 13, 2021), <https://ma-litigation.sidley.com/2021/10/delaware-chancery-court-affirms-importance-of-director-oversight-in-wake-of-boeing-crashes/>; Kalb & Gregory, supra note 38; Marie Larsen et al., *Recent Delaware Decision Highlights Heightened Board Oversight Requirements in Caremark Cases*, HOLLAND & KNIGHT (Oct. 1, 2021), <https://www.hklaw.com/en/insights/publications/2021/09/recent-delaware-decision-highlights-heightened-board-oversight/>; Stephen A. Radin & Joshua Glasser, *Weil Gotshal Discusses Boeing Decision and Board Oversight of Product Safety Risks*, CLS BLUE SKY BLOG (Sep. 20, 2021), <https://clsbluesky.law.columbia.edu/2021/09/20/weil-gotshal-discusses-boeing-decision-and-board-oversight-of-product-safety-risks/>.

⁷⁰ Katz & McIntosh, *id.*; Weinstein et al., *id.*; Radin & Glasser, *id.*

of emphasis: delegate specific risks to board committees and do so explicitly in the company's corporate governance documents; map potential mission critical risks with special attention to product safety, and incorporate a protocol for management to regularly report to you about these risks; and make sure your company's whistleblowing process includes the board.⁷¹

The upshot for our purposes is that a final verdict reached after a full trial is not necessary in order to change the legal advice that corporate boards receive. Apparently, well-reasoned decisions in the motion to dismiss such as *Boeing* are enough. We will have to wait a couple of years to fully assess the extent to which boards actually adopt these recommendations. But it is plausible to assume that when virtually all top legal advisors to boards prompt directors to adopt certain measures, change is already underway.⁷²

Reputational Fallout. Finally, and perhaps most importantly, corporate law deters misbehavior not just by imposing legal sanctions or shaping legal advice, but also by producing information that facilitates *nonlegal* sanctions.⁷³ Corporate decision-makers fear the process of litigation in itself regardless of its legal outcomes, because the process digs out damning information about them and makes it public for all market participants to see. That is, corporate litigation facilitates reputational sanctioning of market actors whose behavior falls below market norms.⁷⁴

Boeing illustrates these reputational-fallout dynamics perfectly. The decision starts with a sixty-page exposé of the facts. Such a detailed narrative of what and how things went wrong with Boeing is great fodder for journalists.⁷⁵ And indeed, the *Boeing* decision attracted media coverage that was voluminous in scope and unfavorable in tone.⁷⁶ The media specifically emphasized three particular frames from the decision: (1) profits over safety, (2) dishonesty, and (3) individual culpability.

Regarding profits over safety, many stories quoted at length VC Zurn's admonition that "rather than prioritizing safety, defendants lent their oversight authority to

⁷¹ *Id.* See also Kevin LaCroix, *Del. Court Substantially Denies Boeing Duty of Oversight Claim Dismissal Motion*, THE D&O DIARY (Sep. 9, 2021), <https://www.dandodiary.com/2021/09/articles/shareholders-derivative-litigation/del-court-substantially-denies-boeing-duty-of-oversight-claim-dismissal-motion/> (similar advice coming from a prominent directors & officers insurance blog).

⁷² Further, the memos warn directors that if their peers adopt such measures and they do not, the court will look on it negatively. Radin & Glasser, *supra* note 69.

⁷³ For theoretical and empirical examinations of such reputation-through-litigation dynamics see ROY SHAPIRA, *LAW AND REPUTATION: HOW THE LEGAL SYSTEM SHAPES BEHAVIOR BY PRODUCING INFORMATION* 35–74 (2020).

⁷⁴ *Id.* For a specific application to fiduciary duty litigation see Roy Shapira, *A Reputational Theory of Corporate Law*, 28 STAN. L. & POL'Y REV. 1 (2015).

⁷⁵ See generally Roy Shapira, *Law as Source: How the Legal System Facilitates Investigative Journalism*, 37 YALE L. & POL'Y REV. 153 (2018) (providing empirical evidence for just how much journalists utilize information from litigation).

⁷⁶ *Infra* notes 78–80.

Boeing's agenda of rapid production and profit maximization.⁷⁷ Some added the quote about directors "turning a blind eye" once problems started surfacing.⁷⁸ Regarding dishonesty, almost all stories directly quoted VC Zurn's admonition that "the Board publicly lied about if and how it monitored the 737 MAX's safety."⁷⁹ Regarding individual culpability, almost all media stories picked up the parts in the decision where VC Zurn calls out one director in particular, David Calhoun, for repeatedly making misstatements in his public interviews following the crashes in 2019.⁸⁰ The media seemed to be subtly (or not so subtly) pointing out the irony to their readers: the one director who is singled out by the court (Calhoun) is the one that Boeing has since decided to promote to CEO.

From a reputation-management perspective, such media coverage is likely to have an outsized impact on the reputations of all those involved.⁸¹ At the company level, consider that Boeing, like other giant companies that find themselves in a product-safety crisis, has poured vast resources into getting in front of the narrative and conveying a message that the crashes are not indicative of Boeing's safety culture. At first, they seemed to be succeeding. Indeed, a content analysis of the first ten months of media coverage following the crashes concluded thusly:

"[T]he mainstream media served primarily as a Boeing's loudspeaker. Critical tones were rare... The media's client (the mass audience) was tuned to seeing Boeing's side of the story narrowly focused on two allegedly smaller technical problems. The story covered Boeing's management as being stable... the company working hard on technical fixes, and the airlines expecting a quick return to service of the 737 MAX. Reality of 'all is under control' was mediated overwhelmingly"⁸²

Several investigative reports then started introducing different narratives, such as that of Boeing "duping" the regulators and prioritizing profits over safety.⁸³ But by the

⁷⁷ Boeing, at *8.

⁷⁸ Andrew Tangel, *Boeing Board to Face 737 MAX Lawsuit*, WALL ST. J. (Sep. 8, 2021); Victoria Bryan, *Boeing Faces Lawsuit over MAX Crashes from Shareholders*, AEROTIME HUB (Sep. 8, 2021), <https://www.aerotime.aero/28824-boeing-max-lawsuit-shareholders>.

⁷⁹ Dominic Gates, *Boeing Board Agrees to \$237.5 Million Settlement of 737 MAX Shareholder Lawsuit*, SEATTLE TIMES (Nov. 6, 2021); Tangel, *id.*

⁸⁰ Jeff Feeley & Julie Johnson, *Boeing Board Members Will Have to Face Lawsuit Over 737 Max Crashes*, FORTUNE (Sep. 8, 2021); Ai Heping, *Boeing Board Faces Suit by Investors over MAX*, CHINA DAILY (Sep. 9, 2021); Tangel, *id.*; Gates, *id.*

⁸¹ See also Claire A. Hill, *Caremark as Soft Law*, 90 TEMP. L. REV. 681 (2018) (explaining that *Caremark* litigation is an area where the legal and reputational realms strongly affect each other).

⁸² Bob Travica, *Mediating Realities: A Case of the Boeing 737 MAX*, 23 INFORMING SCI. INT'L J. EMERGING TRANSDISCIPLINE 25, 34 (2020).

⁸³ Boeing, at *37. See also Yaron Nili, *Board Gatekeeper Independence* (working paper, 2022) (on file with author), manuscript at 5 (detailing the finger-pointing toward Boeing's directors after the crashes).

second half of 2021, the Max debacle was seemingly in the rearview mirror from Boeing's reputation-management perspective: the Federal Aviation Administration (FAA) had lifted the ban and the Max fleet was flying all over the world; the Department of Justice (DOJ) had settled the criminal charges without requiring Boeing to admit wrongdoing or appoint a safety monitor; and media interest in the debacle had started to peter out.

Then, the court decision happened, reigniting the media's attention to Boeing's deep-seated problems. For a giant company like Boeing, the expected reputational fallout from being embroiled in an airplane safety debacle often dwarfs any expected legal sanction.⁸⁴ *Caremark* litigation can undermine companies' reputation-management efforts, thereby creating strong incentives for companies to invest in compliance to begin with.

At the individual level, the reputational ramifications for Calhoun from having his integrity so blatantly questioned are clear. But the (reputational) buck rarely stops at a single decision-maker. The reputational fallout extended to Boeing's officers, even though the lawsuit against them was dismissed.⁸⁵ And it even extended to Boeing's directors who were not mentioned by name in the court decision. To illustrate, consider the case of Boeing director Lynn Good, who is also the well-respected CEO of Duke Energy. In September 2021, Good received the prestigious Yale School of Management's Leadership Award, for her efforts in transforming Duke into a clean energy provider.⁸⁶ Yet, media coverage of her award was marred with references to the *Boeing* decision from earlier that month, noting that the board that Good served on prioritized profits over safety, and misled regulators and the public.⁸⁷ The not-so-subtle subtext was questioning Yale's decision to award a prize for "effective leadership and strong personal character" to someone who was supposedly a part of the Boeing board's failures.⁸⁸

The upshot is clear: in *Caremark* litigation, the process (starting with pre-filing Section 220 requests) *is* the punishment. It is through the combination of both the expected nonlegal costs of going through the process and the legal advice (law firm memos) on how to avoid the process that Delaware corporate law effectively guides behavior, even in the absence of a final verdict reached after a full trial.

⁸⁴ SHAPIRA, *supra* note 73, at 19 (compiling references).

⁸⁵ Rose Krebs, *Abrams & Bayliss Says Chancery Must Clarify Boeing Ruling*, LAW360 (Sep. 14, 2021).

⁸⁶ Eda Aker, *Lynn Good Wins SOM Leadership Award While Facing Negligence Lawsuit for Time at Boeing*, YALE DAILY NEWS (Oct. 7, 2021)

⁸⁷ *Id.*

⁸⁸ *Id.*

III. IS THE *BOEING* DEVELOPMENT DESIRABLE?

It is one thing to recognize that *Boeing* evidences a new *Caremark* era, in which more failure-of-oversight claims advance, and another to conclude that such a development is desirable from a societal perspective. One could claim, for example, that expanding pre-filing discovery comes with its own set of costs; or that aspirations to protect broader societal interests via derivative litigation inevitably clash with the reality of such litigation being driven by plaintiff attorneys.⁸⁹ Section A offers reasons to think that the development that *Boeing* has brought about will prove desirable from an overall societal perspective, given how nicely it balances the flaws of other institutions that attempt to curb corporate wrongdoing. Section B spotlights areas where the *Boeing* development may have gone too far, letting Delaware's self-imposed guards against hindsight bias down, and creating perverse incentives for directors to overinvest in some compliance measures and underinvest in others.

A. *The Good: Balancing the Flaws of Other Enforcement Systems*

Boeing signifies corporate law's newfound emphasis on director oversight duties, and we have ample reason to believe that this newfound emphasis will prove desirable from a societal perspective. The new, Section 220-driven mode of *Caremark* litigation can help balance the flaws of other enforcement mechanisms: from internal corporate governance, to external regulation, to market discipline.

First and most importantly, the new *Caremark* era can mitigate the tendency toward *willful blindness*. Corporate directors have strong incentives to remain ignorant about decisions that prioritize profits over safety or skirt regulatory requirements more generally. Prioritizing profits is good for directors who receive substantial stock-based compensation.⁹⁰ And remaining ignorant about *how* profits were obtained is good for directors' ability to maintain plausible deniability and escape accountability.⁹¹

The two pillars of the new *Caremark* era can potentially reverse such willful-blindness incentives. First, expanding the mission critical zone gives *more weight to culpable ignorance*, as directors can now face liability not just for what they knew, but also for what they *should* have known. Second, expanding shareholders' inspection rights while emphasizing the need for proper documentation *incentivizes more upward flows of information* inside large organizations, thereby making it less plausible to

⁸⁹ See, e.g., Stephen M. Bainbridge, *Don't Compound the Caremark Mistake by Extending it to ESG Oversight*, BUS. LAW. (forthcoming, 2022).

⁹⁰ See generally John Armour, Jeffrey Gordon & Geeyoung Min, *Taking Compliance Seriously*, 37 YALE J. REG. 1 (2020). With *Boeing*, the chair of the House Transportation Committee explicitly attributed the Max debacle to how the company has aggressively tied its executives' pay to stock performance. Gelles, *supra* note 10. See also Dov Fischer et al., *Was Boeing's Compensation Committee Sufficiently Independent in Judging the Business Risk of the 737 Max?*, (working paper, 2019), <https://ssrn.com/abstract=3370066> (suggesting same).

⁹¹ Miriam H. Baer, *Too Vast to Succeed*, 114 MICH. L. REV. 1109, 1112 (2016); Assaf Hamdani & Alon Klement, *Corporate Crime and Deterrence*, 61 STAN. L. REV. 271, 297 (2008).

maintain deniability.⁹² Going forward, directors and their legal advisors in all likelihood will attempt to create a proper record of their efforts to monitor and address safety issues. This, in turn, will force directors to ask others in the organization to prepare written materials for them, thereby bringing thorny issues to the fore.

Second, private enforcement of companies' compliance efforts via corporate law litigation could *complement what is often limited and inadequate regulatory enforcement*. Here as well, Boeing serves as a case in point. Before the crashes, even though Boeing had a history of safety violations,⁹³ the FAA granted the company "too much sway over its own oversight," and failed in certifying the 737 Max.⁹⁴ After the crashes, regulatory enforcement arguably failed again, this time in not generating enough accountability. The DOJ settled the criminal conspiracy investigation against Boeing for misleading the FAA with a deferred prosecution agreement. The agreement required Boeing to pay \$2.5 billion, but did not require it to appoint a monitor, did not charge any individual executive, and did not require any admission of wrongdoing. Professor John Coffee called the agreement one of the worst he has ever seen.⁹⁵

There exist various possible reasons for these regulatory failures, ranging from the benign (regulatory enforcers stymied by limited resources and information asymmetries and complexity), to the cynical (the Trump Administration pushing to get Boeing cleared and back to business at all costs), to the really cynical (a lead prosecutor in the case subsequently joining Boeing's corporate criminal defense firm Kirkland & Ellis).⁹⁶ Whatever the reasons for these regulatory failures are, the new mode of *Caremark* litigation can counteract some of them, and hold companies and individuals accountable for prioritizing profits over safety.⁹⁷ Derivative litigation provides strong incentives for "bounty hunters" (institutional investor plaintiffs and their attorneys) to find out what went wrong and how. *Caremark* litigation in particular places a premium on thorough pre-filing investigations. As a result, hunters can collect their bounty only when they add something to the mix of existing information (linking the directors to

⁹² Stavros Gadinis & Amelia Miazad, *The Hidden Power of Compliance*, 103 MINN. L. REV. 2135 (2019) (arguing that the increased role of chief compliance officers and their open lines of communication to the board incentivize better board oversight).

⁹³ Boeing, at *8-12.

⁹⁴ Chokshi, *supra* note 1 (quoting a House Report condemning the FAA).

⁹⁵ *Columbia Law Professor John Coffee Says Boeing Deferred Prosecution Agreement One of the Worst*, CORPORATE CRIME MONITOR (Feb. 23, 2021), <https://www.corporatecrimereporter.com/news/200/columbia-law-professor-john-coffee-says-boeing-deferred-prosecution-agreement-one-of-the-worst/>.

⁹⁶ *Id.*; *Lead Boeing Prosecutor Joins Boeing Corporate Criminal Defense Firm Kirkland & Ellis*, CORPORATE CRIME REPORTER (Jul. 20, 2021), <https://www.corporatecrimereporter.com/news/200/lead-boeing-prosecutor-joins-boeing-corporate-criminal-defense-firm-kirkland-ellis/>.

⁹⁷ To be sure, the complementarities work both ways: a DOJ settlement that may seem lenient when looked in isolation can make it much harder for corporate insiders to defend against a *Caremark* claim in subsequent corporate law litigation, given the type of information and admissions that the public enforcement action generates.

the corporate trauma).⁹⁸ Relatedly, the emphasis that *Caremark* litigation in its revamped mode puts on better paper trails can help regulatory enforcers hold individuals to account, by creating a traceable record of who knew what when.⁹⁹

Finally, as detailed in Section II.C below, the new mode of *Caremark* litigation contributes to the ability of the market to discipline itself. Legal scholars too often suffer from indefensible optimism about the operation of reputation markets, assuming that whenever bad news surfaces, the market will discipline the misbehaving entities.¹⁰⁰ In reality, reputations are noisy, with the result that the market systematically overreacts to some news and underreacts to other news.¹⁰¹ With Boeing, we recall, the framing in the media was initially controlled by the company, and blame was shifted to (supposedly) incompetent third-world airline operators.¹⁰² When left to its own devices, the market often has a hard time of discerning how things happened and whether past events are indicative of a rotten company culture or just one-off mistakes.

The new, Section 220-driven version of *Caremark* litigation helps the market by providing both “objective” internal documents to which market actors were not privy and “subjective” interpretations by well-respected independent arbiters (Delaware judges). It also provides Delaware judges with an opportunity to voice their opinions on how things ought to be. Put differently, the new *Caremark* era comes with the added benefits of shaping norms (how market actors ought to behave) and reputations (how specific market actors behaved in given instances) in the business community.¹⁰³

VC Zurn seems to have been well aware of this function: months before the decision in the motion to dismiss, she rejected defendants’ motion to keep information that was gleaned from the Section-220 request confidential.¹⁰⁴ In doing so, Zurn explicitly rejected the argument that the intense media coverage of the Max debacle had already sated the public’s interest.¹⁰⁵ To the contrary, VC Zurn insisted, notwithstanding the preexisting voluminous media coverage, the market had very little

⁹⁸ On the role of such “bounty hunters” in corporate governance see Holger Spamann, Indirect Investor Protection: The Investment Ecosystem and Its Legal Underpinnings, Harv. L. Sch. John M. Olin Working Paper No. 1046 (2021), <https://ssrn.com/abstract=3707249>. On bounty hunters regimes more generally see David Freeman Engstrom, *Whither Whistleblowing - Bounty Regimes, Regulatory Context, and the Challenge of Optimal Design*, 15 THEORETICAL INQ. L. 605 (2014).

⁹⁹ Cf. Ann M. Lipton, *Beyond Internal and External: A Taxonomy of Mechanisms for Regulating Corporate Conduct*, 2020 WIS. L. REV. 657, 673.

¹⁰⁰ SHAPIRA, *supra* note 73, at 2 (compiling references).

¹⁰¹ Roy Shapira, *Reputation Through Litigation: How the Legal System Shapes Behavior by Producing Information*, 91 WASH. L. REV. 1193, 1203-10 (2016).

¹⁰² *Supra* note 82.

¹⁰³ This has always been a key function of Delaware courts in other areas, but one that was nonexistent in oversight litigation, due to the parade of early dismissals. Armour et al., *supra* note 90, at 9. *Boeing* signifies a change in that aspect as well.

¹⁰⁴ *In re Boeing Co. Derivative Litig.*, 2021 Del. Ch. LEXIS 22, 2021 WL 392851.

¹⁰⁵ *Id.* at *6-7.

quality insight into what the board knew, when they knew it, and how they reacted to it.¹⁰⁶ The internal documents that corporate law litigation reveals thus help market actors better assess the intentions and abilities of key decision-makers.

B. The Questionable: Hindsight Bias and Perverse Incentives

Boeing also included some aspects worth worrying about. Consider the following four.

First and foremost, the decision should make us question whether the specter of hindsight bias looms over future *Caremark* cases. Chancellor Allen envisioned his landmark *Caremark* decision as a two-step maneuver: not just telling directors that they should be more proactive about corporate compliance, but also warning his fellow judges from interfering with the benefit of hindsight and concluding that directors should have done more to prevent misconduct by others.¹⁰⁷ In most types of corporate litigation, there is a well-tested mechanism to guard against hindsight bias, namely, the business judgment rule.¹⁰⁸ But the business judgment rule does not apply in oversight duties litigation, where the claim is one of omission.¹⁰⁹ The way that courts in oversight litigation have traditionally safeguarded against hindsight bias is by refraining from telling directors what information they *should* have collected leading up to the corporate trauma. Instead, courts have interfered only in the rare cases where they had indications that directors *actually knew* but neglected to act on that information.¹¹⁰

The Section 220 development in *Caremark* litigation poses a challenge to this strategy of maintaining a judiciable role. When sophisticated shareholders and their attorneys gain access to 44,000 internal documents (as in *Boeing*), they are bound to locate instances where board oversight is seen in a negative light. In turn, the super-detailed *Caremark* complaints are tempting: it is hard for judges to read them without passing judgment on the reasonableness of decisions to collect or react to information (especially when in hindsight we know that people have died¹¹¹).

A second aspect of *Boeing* worth debating is the (dis?) incentives it creates for future boards to invest in post-fact remedial actions. Following the second crash, Boeing's board took actions to supposedly shore up its commitment to safety: from establishing a specific committee tasked with overseeing airplane safety, to

¹⁰⁶ *Id.*

¹⁰⁷ Jennifer Arlen, *The Story of Allis-Chalmers, Caremark, and Stone: Directors' Evolving Duty to Monitor*, in *CORPORATE LAW STORIES* 323 (J. Mark Ramseyer ed., 2009). See also *Citigroup*, *supra* note 34, at 126 (applying said approach).

¹⁰⁸ See generally Stephen Bainbridge, *The Business Judgment Rule as Abstention Doctrine*, 57 VAND L. REV. 83 (2004). Under the "business judgment rule," courts give deference to disinterested, informed board decisions.

¹⁰⁹ *Id.* at 99.

¹¹⁰ Stone, *supra* note 23, at 370; Miller, *supra* note 44, at 932.

¹¹¹ LaCroix, *supra* note 71.

communicating among themselves the need to start putting safety front and center. VC Zurn inferred from these actions that the board had breached its oversight duties to begin with. For example, instead of viewing the creation of a new safety committee as an attempt to respond to safety red flags, VC Zurn took it as a prong-one indication that the board had no system of monitoring air safety prior to the crash.

From a policy perspective, one could question the use of remedial actions after harm occurred as evidence that directors could have done more before harm occurred. After all, Rule 407 of the Federal Rules of Evidence bars admission of such evidence. The two common justifications against using post-fact remedial actions are (1) not to disincentivize market actors from adopting steps that improve safety,¹¹² and (2) to guard against hindsight bias on the part of adjudicators.¹¹³ For our purposes, the question is the extent to which these general justifications apply also in the specific context of *Caremark* litigation.

My answer is: less forcefully. On justification (1), there is less reason to fear that using subsequent remedial actions as evidence will disincentivize directors from taking safety measures, if only because directors face the threat of being punished for *not* remediating safety problems that they become aware of. That is, directors face the stick of failing *Caremark*'s prong two (ignoring red flags), and so they are unlikely to forego adopting remedial actions even if they think such actions will be used as prong-one evidence against them.¹¹⁴ On justification (2), there is less reason to fear hindsight bias given that the adjudicators here are not jurors but rather the expert and experienced Delaware judiciary.¹¹⁵ Delaware judges are well-equipped to make case-by-case determinations of when and how it is proper to use such evidence, as a function of the information asymmetries and the credibility of the allegations at hand.¹¹⁶ I am therefore less worried about creating incentives not to invest in post-fact remedial measures.

A third aspect of *Boeing*, and one that I worry about more, is creating perverse incentives for directors to be overly confrontational with management once crisis hits. For example, VC Zurn apparently viewed the fact that, in the heat of the crisis, one director internally praised the CEO for his strong leadership as an indication that the board was not critical enough.¹¹⁷ But sometimes a cigar is just a cigar: in my opinion, words of encouragement to a CEO who is currently juggling numerous balls in the air

¹¹² Richard A. Posner, *An Economic Approach to the Law of Evidence*, 51 STAN. L. REV. 1477, 1485 (1999).

¹¹³ Jeffrey J. Rachlinski, *A Positive Psychological Theory of Judging in Hindsight*, 65 U. CHI. L. REV. 571, 617 (1998).

¹¹⁴ Dan M. Kahan, *The Economics – Conventional, Behavioral, and Political – of Subsequent Remedial Measures Evidence*, 110 COLUM. L. REV. 1616, 1644 (2010).

¹¹⁵ Rachlinsky, *supra* note 113, at 618 (on how the justification emanated from the context of jury trials).

¹¹⁶ Kahan, *supra* note 114, at 1631 (advocating against a categorical rule and for case-by-case determinations).

¹¹⁷ *Boeing*, at *85.

should not be used against the board as an indication that they knowingly breached their oversight duties.¹¹⁸ The previous precedent of *Allis-Chalmers* explicitly warns courts against creating incentives for boards to enter a mode of internal espionage and distrust inside the company.¹¹⁹ It is precisely in times in crisis that the board and management need to trust each other enough to be frank with each other and work in unison.

Finally, *Boeing* leaves open the question of the management's role. The decision painstakingly details how top management pushed Max to the market quickly, lied to the regulators, tried to shift blame to the (dead) pilots, and withheld information from their own board.¹²⁰ Yet when it comes to liability, the decision lets management off the hook. We noted earlier that VC Zurn bases her decision to dismiss claims against officers on the demand's futility aspects: because plaintiffs apparently have not argued that Boeing's directors are beholden to its officers, there is no reason not to leave the decision on whether the company should sue the latter to the former.

I find this outcome hard to reconcile with the facts of the case. If officers constantly told directors that the Max is safe and everything is under control, at minimum we would think that the former face liability for aiding and abetting the breach of oversight on the part of the latter. In other words, one could argue that a large part of why directors face *Caremark* liability is that management knowingly fed them too rosy, not-enough-focused-on-safety information. And it is hard to believe that we can trust directors with whether to pursue on behalf of the company an aiding and abetting claim against management, given that an integral part of such a lawsuit would be claiming that a predicate breach of oversight on the part of the directors themselves occurred. This is not to mention the possibility that was explicitly mentioned in the court decision, namely, that pursuing claims against management will make the latter release damning information on others in the company. Granted, it is hard to criticize *Boeing* in this aspect, given that a judge can only decide on what the sides before her argue. But going forward, it is important to address in oversight duties litigation the question of "fraud on the board" by management and its advisors.¹²¹

¹¹⁸ It should be noted that VC Zurn made her comment in the context of justifiably criticizing the board for being too supportive of the CEO's focus on a public-relations campaign, instead of demanding that the CEO will focus on investigating the root causes of the first crash. My argument here focuses on what future boards may take from Boeing: I suspect that they may treat it as a call to adopt a strictly-confrontational stance when dealing with management, so as "to be on the safe side."

¹¹⁹ *Supra* note 42, at 130.

¹²⁰ Boeing, at *82-83.

¹²¹ Cf. Joel Edan Friedlander, *Confronting the Problem of Fraud on the Board*, 75 BUS. LAW. 1441 (2020) (raising the "fraud on the board" problem in the context of deal litigation). For evidence on how Delaware corporate law too often lets officers off the hook see Megan W. Shaner, *Officer Accountability*, 32 GA. ST. U. L. REV. 357 (2016). For the particular procedural aspects mentioned above, which make it less likely to hold officers accountable, see Shaner, *supra* note 25, at 314 n.187.

CONCLUSION

Compliance has become a key corporate governance issue. With mounting regulatory requirements, and hundreds of billions spent on internal programs, it is crucial to get corporate compliance right. Yet, until recently, corporate law played only a limited role in holding directors accountable for compliance failures. This state of affairs seems to be changing fast. Over the past couple of years, a string of successful *Caremark* claims has revamped director oversight duties.¹²² *Boeing* puts a final stamp of approval on and further extends this trend. It illustrates the courts' increased willingness to apply an enhanced mode of scrutiny, and outside shareholders' increased ability to investigate failure-of-oversight claims. *Boeing* also illustrates how Delaware corporate law guides behavior even in the absence of verdicts reached after a full trial.

The next big question is whether directors face *Caremark* liability also for failure of oversight of *nonlegal* requirements.¹²³ Large corporations are facing increased societal demands, calling on them to treat their stakeholders and society at large better.¹²⁴ Could it be that the heightening of *Caremark* liability will expand also to nonlegal, ESG demands? Traditionally, courts allowed cases to proceed only upon showing of corporate illegality.¹²⁵ The tide may have started to turn, however. Delaware's former Chief Justice Leo Strine and his co-authors have recently argued that rising ESG demands coincide with *Caremark* duties in at least two ways.¹²⁶ In terms of internal corporate governance, companies can and should use the same *Caremark* processes to meet both regulatory (floor) and societal (ceiling) demands.¹²⁷ In terms of external legal requirements, a failure to install systems that report and monitor issues of diversity and inclusion could trigger *Caremark* duties, or so the argument goes.¹²⁸ To me, the only realistic scenario where *Caremark* liability extends to nonlegal demands is when a given nonlegal issue is clearly "mission critical," in the sense that not going beyond legal requirements will endanger the company's core business and operations. But when ESG issues rise to such prominence, they are

¹²² Shapira, *supra* note 6.

¹²³ I deal with this question extensively in a separate project: Roy Shapira, *Mission Critical ESG and the Scope of Director Oversight Duties* (working paper, 2022) (on file with author).

¹²⁴ Leo E. Strine, Jr., Kirby M. Smith, & Reilly S. Steel, *Caremark and ESG, Perfect Together: A Practical Approach to Implementing an Integrated, Efficient, and Effective Caremark and EESG Strategy*, 106 IOWA L. REV. 1885, 1886 (2021).

¹²⁵ *Citigroup*, *supra* note 34, at 131; Pollman, *supra* note 24.

¹²⁶ Strine et al., *supra* note 124; Brummer & Strine, *supra* note 65.

¹²⁷ Strine et al., *id.*

¹²⁸ Brummer & Strine, *supra* note 65. *See also* Daniel Hemel & Dorothy S. Lund, *Sexual Harassment and Corporate Law*, 118 COLUM. L. REV. 1583, 1646 (2018) (discussing the possibility of *Caremark* liability for failure-of-oversight of sexual misconduct); Sarah Barker, Cynthia Williams, & Alex Cooper, *Fiduciary Duties and Climate Change in the United States* (Commonwealth Climate and Law Initiative Paper, Oct. 2021), <https://ccli.ubc.ca/wp-content/uploads/2021/12/Fiduciary-duties-and-climate-change-in-the-United-States.pdf> (discussing same for climate-related risks).

usually already incorporated in some form of legal requirement, thereby making it possible for plaintiffs to couch their case as a more classic claim of noncompliance with legal requirements.

Post *Boeing*, however, the differences between these approaches to *Caremark* liability for oversight of nonlegal issues seem minor.¹²⁹ After all, *Boeing* faults directors for discussing operational and design issues prior to the crashes only in terms of meeting benchmarks for quick entry to market, and for discussing safety issues after the crashes only in terms of restoring the company's profitability and image. In other words, *Boeing* already faults directors for putting short-term shareholder returns ahead of consumer safety. In that sense as well, *Boeing* signifies a shift in our corporate law.

¹²⁹ Or, in an alternative framing: inches us closer to Strine's opinion. See also Jill E. Fisch & Steven Davidoff Solomon, *Should Corporations Have a Purpose?*, 99 TEX. L. REV. 1309, 1326-27 (2021); Stavros Gadinis & Amelia Miazad, *Corporate Law and Social Risk*, 73 VAND. L. REV. 1401 (2020).