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FRANKLIN A. GEVURTZ*

Disney in a Comparative Light

This article uses a comparison of the recent Delaware Supreme Court decision in the Disney litigation and the recent German Federal Supreme Court decision in the Mannesmann case as a launching point to explore six important differences between Delaware and German corporate law, including the different degrees to which Delaware and German courts defer to the business judgment of corporate directors; the greater suspicion in German versus Delaware law of the ability of so-called disinterested directors to protect the corporation in dealing with other directors; the impact of employee representation on the corporate board under German law when it comes to board decisions dealing with executive compensation; the very different legal and societal attitudes toward compensation of senior executives in Germany versus the United States; the far lesser ability of shareholders to waive fiduciary obligations under German law than under Delaware law; and the potential unintended impact of various procedural rules that make shareholder suits less viable in Germany than in Delaware.

Is there something wrong with this picture: recently, Delaware courts exonerated directors of The Walt Disney Company from liability for damages—despite the directors having paid Michael Ovitz around $130 million in exchange for a year accomplishing little as the number two executive at Disney. At about the same time, the German Federal Supreme Court held that directors of the German company, Mannesmann AG, breached their duty to the company when they awarded a bonus of approximately $17 million to the outgoing CEO—whose actions apparently played an important role in gaining over $50 billion for the Mannesmann shareholders. As a result, the Mannesmann directors ended up paying a multi-million euros settlement for having rewarded success, while their counterparts at Disney avoided liability for paying eight times as much to reward failure.

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Incongruities in judicial decisions are nothing new, even within a single jurisdiction. Moreover, it is always possible to point to specific factual differences upon which to reconcile seemingly incongruous judicial decisions, or to ask whether a particular judicial decision, or pair of judicial decisions, might be aberrational. Nevertheless, one important utility from the comparative study of the laws in different nations lies in the opportunity it provides to ask whether different results in particular cases reflect some more fundamental differences in law and policy, and, if so, then to explore the implications of those differences. Addressing this question, and exploring these implications, in the context of the cases involving Disney and Mannesmann, provides the objectives for this article.

This article will proceed in two parts. The first provides a background discussion of the Delaware court decisions in In re The Walt Disney Company Derivative Litigation ("Disney"), and the German Federal Supreme Court decision in the Mannesmann Case ("Mannesmann"). The next part of this article will ask whether these two decisions reflect some significant differences in Delaware and German corporate law and policy, and, if so, what are the implications of those differences.

In fact, the challenged actions by the defendant directors in Disney and Mannesmann occurred in different contexts—the former involving termination pay provided for under an employment contract, while the latter involved a gratuitous bonus. Moreover, both cases involve fairly extreme facts, which place them on the cusp of culpable conduct. Even taking such facts into account, however, it is difficult to shake the conclusion that had Disney been a German corporation, or Mannesmann been incorporated in Delaware, the results would have been different. This conclusion flows from six highly significant contrasts between Delaware and Germany in the area of corporate law and policy, which these two cases illustrate.

To begin with, these cases illustrate the different degree to which Delaware and German courts defer to the business judgment of corporate directors; specifically, German courts, both in Mannesmann and more generally, seem more willing to second guess directors than are Delaware courts, both in Disney and in innumerable other cases. Compounding this difference, German law, in situations not limited to Mannesmann, is more suspicious of the ability of so-called disinter-

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ested directors to protect the corporation in dealing with other directors than is Delaware law, in situations not limited to Disney. A difference in the composition of the Disney and Mannesmann boards arose out of the German law that mandates employee representation on the board (so-called co-determination). The facts of the Mannesmann case provide an opportunity to address the impact of employee representation when it comes to board decisions dealing with executive compensation. More broadly, comparing Mannesmann with Disney illustrates very different legal and societal attitudes toward compensation of senior executives in Germany versus the United States. These cases also demonstrate the far lesser ability of shareholders to waive fiduciary obligations under German law than under Delaware law. Finally, the fact that Mannesmann was a criminal prosecution, while Disney was a shareholder derivative action, illustrates the potential unintended impact of various procedural rules that make shareholder suits less viable in Germany than in Delaware.

It is interesting to match these differences in Delaware and German law and policy with a list of some of the more contentious issues in corporate law and corporate law scholarship in the United States during the last quarter century. Such a list would surely include: What is the appropriate level of deference to the business judgments of directors? Can we trust so-called disinterested directors to protect the corporate interest in transactions with other directors? Is there a problem with excessive compensation for senior corporate executives? Should shareholders be able to contract out of fiduciary du-


ties? Is there a need for further rules curbing potentially meritless derivative suits? It is probably not a coincidence that these issues parallel five of the six differences in Delaware and German law and policy illustrated by comparing Disney and Mannesmann. Moreover, even if not a particular source of contention in the United States, the remaining difference (employee representation under co-determination) is a source of contention in Europe. Hence, comparing Disney and Mannesmann achieves more than simply a look at a couple of fascinating cases; it allows us to revisit some of the important fault lines in corporate law and corporate law scholarship.

I. Some Background on Disney and Mannesmann

A. The Disney Case

Disney's dealings with Michael Ovitz arose out of the death, in 1994, of Frank Wells—Disney's then president, second highest executive, and heir apparent to its CEO, Michael Eisner. Eisner decided to ask Michael Ovitz to fill the vacancy. Eisner and Ovitz had been close friends for around 25 years. Ovitz was a founder and the majority owner of a talent agency (Creative Artists Agency, or CAA). CAA was extraordinarily successful, resulting in Ovitz receiving substantial remuneration ($20 million in a year) and becoming one of the most powerful persons in Hollywood.
In August of 1995, Eisner and Ovitz reached an agreement for Ovitz to become the president and number two executive at Disney. Disney’s board appointed Ovitz president, effective October 1, 1995. Ovitz also was elected to Disney’s board. Approval of Ovitz’ compensation package fell to the compensation committee of Disney’s board. The committee consisted of an entertainment lawyer (Irwin Russell, who was also Eisner’s personal attorney), a movie star (Sidney Poitier), the editor-in-chief of the largest Spanish language newspaper in Los Angeles (Ignacio Lozano, who also served on a number of other corporate boards), and the chair of the Disney board’s executive committee (Raymond Watson, who also served on a number of other corporate boards).9

A key feature of Ovitz’ employment contract was downside protection demanded by Ovitz, who would be giving up ownership in CAA to join Disney. Under Ovitz’ five-year employment contract, if Disney terminated Ovitz other than for gross negligence or malfeasance, Ovitz would receive (1) his base salary for the reminder of the contract, (2) three-quarters of the maximum annual bonus which he might have received had he stayed with Disney for the reminder of the contract (these two sums modestly discounted to reflect their immediate receipt by Ovitz), (3) immediate vesting of all stock options to which he would have been entitled for the five years of his contract, and (4) $10 million in lieu of the stock options to which he would have been entitled had the contract been extended for a second five year period.

Within a year after Ovitz’ appointment as president, Eisner decided that Ovitz was not working out. On December 12, 1996, Disney terminated Ovitz’ employment, but, critically, did so without claiming cause within the meaning of Ovitz’ employment contract. As a result, Ovitz became entitled to the amounts provided for under the contract in the event of termination without fault. The value of this package was over $130 million. Word of what Ovitz received upon termination at Disney sparked negative publicity and, in turn, derivative lawsuits by some Disney shareholders.

The claims of the shareholder plaintiffs in *Disney* revolved around two decisions: the compensation committee’s approval of the downside protection provision in Ovitz’ employment contract,10 and the decision to terminate Ovitz without claiming cause within the meaning of the contract. In both instances, the plaintiffs challenged the substantive merits of the decisions (claiming the decisions amounted to “waste”), and the process by which the directors reached

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10. The highly positive stock market reaction to the announcement of Disney’s hiring Ovitz precluded much of a claim that the directors made a mistake simply in hiring Ovitz.
the decisions. Essentially, the plaintiffs claimed that the termination provision in Ovitz' contract amounted to waste, because Ovitz actually would do better by losing his job (so long as he did not commit gross negligence or malfeasance) than by keeping his job—which is not the incentive a company desires to create. The plaintiffs claimed that the decision to let Ovitz depart without claiming fault constituted waste, because Ovitz had given Disney grounds to terminate him for cause, thereby avoiding payment under the termination provision. With respect to process, the plaintiffs asserted that the board (or the compensation committee) simply had deferred to Eisner—rather than carefully considering the impact of the termination provision (in approving Ovitz' employment contract), or without actually even deciding upon the matter (when it came to terminating Ovitz without claiming fault).

In almost a decade of litigation, the Disney case spawned five published court opinions—three from the Delaware Chancery Court and two from the Delaware Supreme Court. In the first opinion,\(^{11}\) the Delaware Chancery Court dismissed the plaintiffs' complaint for failure to plead either that the plaintiffs had made a demand upon Disney's board, or that such a demand would be futile. While acknowledging that the large size of the payout had sparked media interest, the Chancery Court viewed the situation as an unremarkable exercise of business judgment. On appeal, however, the Delaware Supreme Court showed more concern. It expressed the view that the sloppy processes allegedly followed by Disney's board, and the sheer size of the payout to Ovitz, rendered "this a close case" both on the process and on the waste claims.\(^{12}\) In the end, the Supreme Court affirmed the dismissal of the plaintiffs' complaint due to its "deficient pleading," but, in an important post script, instructed the Chancery Court to grant the plaintiffs leave to amend.

After following the Supreme Court's advice to seek more facts through the exercise of shareholder inspection rights, the Disney plaintiffs returned with an amended complaint. This new complaint painted a picture of the Disney board virtually abdicating any real decision-making role in the company's dealings with Ovitz. The new complaint turned out to be enough for the Chancery Court—whose attitude toward the case seems to have undergone a shift (as evident in the Court's critical asides about the possible impact of the friendship between Eisner and Ovitz on the favorable treatment that Ovitz received). This picture of a board passively abdicating decisions to the CEO not only provided the sort of detailed factual pleading of wrongful conduct by most of the board necessary to excuse demand, it

\(^{11}\) In re The Walt Disney Company Derivative Litigation, 731 A.2d 342 (Del. Ch. 1998).
\(^{12}\) Brehm v. Eisner, 746 A.2d 244, 249 (Del. 2000).
also was sufficient, in the view of the Chancery Court, to get the plaintiffs past the formidable obstacle they faced because of a liability waiver provision contained in Disney's certificate of incorporation.\textsuperscript{13} This provision prevented the corporation from recovering monetary damages from its directors for breach of their duty of care, but was inapplicable if the directors did not act in good faith or engaged in intentional misconduct.

A couple more years and a long trial later, the Chancery Court delivered its third written opinion. The Chancery Court remained critical of the Disney directors in general, and Disney's CEO, Michael Eisner, in particular. Nevertheless, the Court concluded that the directors' conduct was not so bad as to fall outside the protections of the business judgment rule. In reaching this conclusion, the Court chose to accept the defendants' version of a number of disputed facts, at times despite seeming conflict with written records. For example, despite the failure of the minutes of the compensation committee to document much review of the no-fault termination provision in Ovitz' employment contract, the court accepted the testimony of members of the committee regarding their discussions of the contract. Similarly, despite memoranda by Eisner characterizing Ovitz as incompetent and dishonest, the Chancery Court accepted the defendants' position that Ovitz had not succeeded, either because of interference by Eisner and others at Disney (Ovitz' story), or because of the ("it's nobody's fault") failure of Ovitz to fit into Disney's corporate culture (the defendants' story), rather than because of Ovitz' gross negligence or malfeasance (the plaintiffs' story).

On appeal, the Delaware Supreme Court affirmed—not a surprising result given that the case seemingly had come down in large part to a factual dispute resolved against the plaintiffs by the trial court.\textsuperscript{14}

B. The Mannesmann Case\textsuperscript{15}

Mannesmann AG was a German "stock company"—roughly speaking, a public corporation. While Mannesmann traditionally had

\textsuperscript{13}. In re The Walt Disney Company Derivative Litigation, 825 A.2d 275 (Del. Ch. 2003).

\textsuperscript{14}. One interesting residual from the liability waiver in Disney's certificate of incorporation is that both the Chancery Court and Supreme Court opinions contain extended discussions of what it means for directors to not act in good faith. This all seems to be beside the point, given that both courts concluded the Disney directors did not even commit acts of gross negligence, let alone engage in the conscious acts of indifference that might equal bad faith. Nevertheless, as a final irony, these passages may end up being the most noted aspect of the Disney case from a doctrinal standpoint.

\textsuperscript{15}. The following description of the Mannesmann case draws upon a translation found in Franklin A. Gevurtz, Global Issues in Corporate Law 97-104 (2006) (portions of the opinion translated by David Donald, Alexander Klauser, Klaus Linke & Katherina Pistor). Additional factual background comes from Theodore Baums,
produced heavy machinery and the like, starting in 1990, Mannesmann became increasingly focused on operating a cell phone network. In the 1990s, Mannesmann expanded its cell phone activities beyond Germany through a program of increasing its holdings in other cell phone companies. Klaus Esser, Mannesmann’s Chief Financial Officer at the time, was instrumental in this program. In May 1999, Esser became Mannesmann’s CEO. Esser successfully continued Mannesmann’s expansion by acquiring other cell phone companies.

In November 1999, a British cell phone company, Vodafone plc, launched an effort to take over Mannesmann. After Esser rejected a friendly offer from Vodafone’s CEO—under which Mannesmann stockholders would have received stock in Vodafone with a market value of 203 euros for each surrendered share of Mannesmann—Vodafone made a hostile tender offer at 240 euros per share. Esser and Mannesmann’s board urged Mannesmann’s stockholders to reject the bid as inadequate. When it eventually became clear, however, that a majority of Mannesmann’s stockholders wanted to take the Vodafone offer, Esser yielded and negotiated a friendly takeover. The final deal, reached on February 3, 2000, valued Mannesmann stock at 360 euros per share—thereby gaining Mannesmann stockholders a total of 63 billion euros more in Vodafone stock than the original offer rejected by Esser. With respect to Esser himself, under the deal he would not, except for a short transitional period, continue to run Mannesmann, but, instead, would resign from Mannesmann’s management board effective July 31, 2000.

As a German stock company, Mannesmann had both a management board to run the company, and a supervisory board to supervise the management board—including setting compensation for members of the management board. Because Mannesmann had over 20,000 employees in Germany, German law required the supervisory board to have 20 members—half elected by employees and half by the stockholders.

Mannesmann’s supervisory board had delegated the task of setting compensation for members of the management board to an executive committee of the supervisory board, called the Präsidium. The Präsidium had four members: two members who had been elected to the supervisory board by the stockholders—Josef Ackerman (a senior executive, and now CEO, at Deutsche Bank) and Joachim Funk (Esser’s predecessor as CEO at Mannesmann)—and two supervisory board members selected by the Mannesmann employees—Jurgen...
Ladberg (chairman of the shop council for Mannesmann) and Klaus Zwickel (chairman of a labor union).

On February 4, 2000, two of the members of the Präsidium (Ackerman and Funk) met. Funk reported that another member of Mannesmann’s supervisory board (who was also a managing director of the largest stockholder in Mannesmann immediately prior to the takeover) had urged the committee to award Esser a £10 million bonus in recognition of Esser’s extraordinary accomplishments both before and after negotiating the takeover, with a similar amount to be shared among other members of Mannesmann’s senior management. Funk also reported that Vodafone’s management had agreed that this would be a good idea. Funk and Ackerman agreed to this bonus (labeled an appreciation award). Funk then called Zwickel. Zwickel thought Esser deserved something, but that the proposed £10 million bonus was too large. Nevertheless, because Zwickel felt that the bonus did not relate to employee concerns, and because he did not want to obstruct the bonus, he abstained—recognizing that his participation without a negative vote allowed the Präsidium to adopt the bonus.

When the German press heard about the bonus, the result was widespread and largely negative commentary. Employee reaction, both on and off of the board, to the bonus was negative. No effort was made to rescind the bonus, however, and, on March 28, 2000, Mannesmann paid Esser the bonus.

On March 7, 2000, a German attorney filed a criminal complaint with the Dusseldorf federal attorney’s office against Esser and others. Interestingly, this attorney’s clientele consisted of smaller German companies, at which, according to observers of the German scene, there has been considerable resentment toward the generous severance packages awarded to senior executives of larger corporations. On February 17, 2003, the federal attorney filed charges against Ackermann, Funk, Zwickel, Ladberg, Esser and Dietmar Droste (Mannesmann’s chief officer for personnel). The prosecutor charged that, in approving the bonus payment, Ackermann, Funk and Zwickel had violated Section 266 of the German Penal Code. This section provides:

Breach of Trust (Untreue)

(1) Any person who by law, administrative delegation or contract has dispositional power over the assets of others or power to commit these assets to a third party, abuses and breaches the duty laid on him by law, administrative delegation or trust relationship to protect the property interests of another, and in this way causes damage to the property interests that he should protect, shall be punished with arrest of up to five years or with a monetary fine.
The remaining defendants were charged with aiding the breach of trust.

The case was tried in a Dusseldorf criminal trial court in the first half of 2004. The trial court issued a judgment acquitting all of the defendants. The trial court concluded that, while the directors had breached their duty in awarding the bonus, they were not criminally liable. This was because, according to the trial court, there must be an "aggravated" breach of duty in order for a business judgment to violate Section 266 of the Penal Code. In this case, the trial court found the breach was not aggravated, because the company's profits were high and the continuity and the profitability of the company were never threatened, the decision was made diligently and in a transparent manner in accordance with the allocation of responsibility within the company, and the members of the Supervisory Board did not have an unlawful purpose.

The prosecution appealed the case to Germany's Federal Supreme Court, Criminal Division, which reversed the acquittal. The Supreme Court agreed with the trial court that the defendants had breached their duty in awarding the bonus—the reason being that there was no contractual obligation to award the bonus, and, in light of the change in control, Mannesmann could not gain anything by giving bonuses to departing employees. The Supreme Court disagreed with the trial court, however, that only an aggravated breach of duty violated the Penal Code. Having rejected this ground for acquittal, the Supreme Court returned the case for a retrial on a sort of "ignorance of the law" defense provided by the German Penal Code. Specifically, the defendants could escape conviction on retrial if it was established that, through unavoidable error, they did not know they were breaching their duty.

Before the retrial, the case settled. The defendants agreed to pay 5.8 million euros, and the prosecutor agreed to drop the prosecution.16

II. DIFFERENCES BETWEEN DELAWARE AND GERMAN CORPORATE LAW AND POLICY ILLUSTRATED BY COMPARING DISNEY AND MANNESMANN

Comparing Disney and Mannesmann illustrates six fundamental differences between Delaware and Germany when it comes to corporate law and policy. Perhaps not surprisingly, these differences go to some of the more contentious issues in corporate law and policy.

A. Judicial Deference to Directors, Generally

An evident divergence between Delaware law, as illustrated by Disney, and German law, as illustrated by Mannesmann, lies in the degree of deference that the Delaware and the German courts give to directors under the business judgment rule. The factual situations in the two cases are, of course, distinguishable. Nevertheless, the skepticism with which the German court in Mannesmann dissects the question of whether paying the challenged bonus could produce any offsetting advantage for the company seems at odds with the deferential way in which the Delaware courts accept the board's actions in Disney.

Both Disney and Mannesmann pay homage to the so-called business judgment rule—the idea that courts should be reticent to second guess the business decisions of disinterested directors. Hence, in Disney, the Delaware Chancery Court explained:

Because courts are ill equipped to engage in post hoc substantive review of business decisions, the business judgment rule "operates to preclude a court from imposing itself unreasonably on the business and affairs of a corporation." Similarly, in Mannesmann, the German Federal Supreme Court took care to point out:

Remuneration of officers is part of the executive and strategic tasks of the supervisory board and therefore generally open to a relatively wide margin of business judgment and discretion. Accepting such a margin of business judgment is called for because taking entrepreneurial decisions generally involves striking a balance between possible future risks and prospects and, due of their prospective nature, it is inherent ... that the quality [of such decisions] sometimes can only be known in hindsight. Hence no breach of duty can be found where a decision is based on a sense of responsibility, on diligent collection of all relevant data and is aimed solely toward furthering the company's best interests.

Despite its recognition of the business judgment rule, however, the court in Mannesmann held that the directors breached their duty to the corporation in approving the bonus. The court based this hold...
ing on the assertion that the bonus could yield no advantage for the company. Essentially, this is the same as a waste claim in the United States. To reach this result, the court went through three steps. First, the court pointed out that Mannesmann's outgoing CEO (Klaus Esser) had no legal claim to the award, having received all he was entitled to under his employment contract. If the court had stopped there, the case might have stood for nothing more than an inability to find benefit to the corporation in anything other than contractually bargained exchange; a viewpoint sometimes found in archaic cases in the United States. The court's rationale, however, was not so limited. Instead, recognizing that a gratuitous bonus might benefit the corporation by providing incentives for future performance—either by the recipient or by other employees—the court next asserted that Esser's expected departure meant that Mannesmann could not benefit from giving him an incentive to perform well on behalf of the company in the future. Finally, and most critically, the court responded to the possibility that the bonus could provide an incentive for other employees. Here, the court asserted that, because Vodafone was taking over management of Mannesmann, Mannesmann could gain no advantage in terms of incentives for its executives in the future by developing a reputation as a firm that rewards good results.

It is in this final step that the court in Mannesmann shows a willingness to second guess business judgments under circumstances in which a more deferential court might find a rational basis sufficient to uphold the directors' decision. Specifically, the court's assumption as to the irrelevance of Mannesmann's internal management after the Vodafone takeover would seem subject to debate—particularly given the court's insistence on treating Mannesmann as a separate corporation when it came time to reject the defense that Vodafone approved the bonus. Moreover, even if one accepts the court's assumption, then it becomes evident that the court's analysis ignores the possible incentive impact of the award on Vodafone executives, in whose hands the court assumes Mannesmann's fate will thereafter rest. Vodafone's executives might calculate that the award of the bonus, which Vodafone had approved, heralded a similar policy of rewarding good results by them.

21. E.g., Adams v. Smith, 275 Ala. 142, 153 So.2d 221 (1963). A wag might note that this view of gratuities as constituting waste would be consistent with the fact that Germans traditionally did not tip waiters and waitresses.
22. Interestingly enough, the Mannesmann litigation produced an allegation that there was a more immediate benefit, at least for the Mannesmann shareholders who wanted to sell, obtained by paying the bonus. There was some evidence, albeit contested, to suggest that the representative of the holder of the largest block of Mannesmann stock going into the takeover, whose urging ultimately led the executive committee to award the bonus, had offered the bonus to Mannesmann's CEO during
By contrast, the Delaware Chancery and Supreme Courts in Disney were much more willing to accept the conduct of the Disney directors. A couple of examples illustrate the point.

To begin with, the Chancery Court expressed considerable displeasure with the conduct of Disney’s CEO, Michael Eisner, in connection with the process by which Disney hired Ovitz. The court pointed out that Eisner “failed to keep the board informed as he should have,” and that Eisner “prematurely issued a press release that placed significant pressure on the board to accept Ovitz and approve his compensation package in accordance with the press release.”23 The court stated that “a reasonably prudent CEO . . . would not have acted” in this manner, and that Eisner’s conduct did “not comport with how fiduciaries of Delaware corporations are expected to act.”24 Nevertheless, because Eisner was not uninformed, and because he subjectively believed that his actions were in the best interest of Disney, the court refused to find Eisner liable. As a result, the fact that Eisner acted unreasonably, and that this unreasonable conduct “infected and handicapped the board’s decisionmaking abilities,”25 escaped legal consequences.

Another example of the Delaware courts’ deference to the Disney directors comes from the courts’ reaction to the decision to let Ovitz walk away with a no-fault termination. The Disney plaintiffs argued that the defendants should have fired Ovitz for cause, thereby precluding his receipt of the generous compensation package provided by his employment contract in the event of a no-fault termination of his services. Indeed, Ovitz had not accomplished much during his year at Disney, and Disney’s CEO, Michael Eisner, had penned some rather scathing critiques of Ovitz during Ovitz’ tenure at Disney.26
In rejecting the no-fault termination claim, the Delaware courts pointed to the conclusion of expert witnesses, who testified that Ovitz' conduct did not fall so low as to meet the contractual criteria (gross negligence or malfeasance) for termination for cause. Yet, a more skeptical court, ala Mannesmann, might have asked whether this conclusion was so inescapable that normal business practice would not have called for at least attempting to negotiate a reduction in Ovitz' rights on termination. Instead of exploring such a possibility, the Delaware courts simply point out, as part of the factual background, that Disney's general counsel stated that such a negotiation would be unethical, expose Disney to a lawsuit, and hurt Disney's reputation—as if hardball negotiations were foreign to Hollywood. Yet, lost in this is the Chancery Court's reaction to the plaintiff's no-fault termination claim during earlier stages of the Disney litigation. Specifically, the Disney plaintiffs' allegation that the defendants had breached their duty by not firing Ovitz for cause had survived the demanding pleading standards facing a derivative suit plaintiff. Moreover, the defendants in the case had not disposed of this claim on summary judgment. Finally, no one had imposed sanctions on the Disney plaintiffs or their attorneys for having raised the claim concerning the no fault termination. Hence, it cannot be said that Ovitz' right to a no-fault termination was such a "slam dunk" that Disney would have been asserting a frivolous legal position by threatening to fire Ovitz for cause. This, in turn, suggests that the defendants gave up, without compensation, a colorable right to save $130 million. Indeed, even if one assumes that Disney had only a ten or twenty percent chance of prevailing in any litigation with Ovitz, that chance still had a $13 or $26 million value.

The critical point in all of this is not that the German court is wrong in its conclusion about the impact of the bonus for Mannesmann's outgoing CEO, or that the Delaware courts are wrong in their conclusions about the actions of the Disney directors. Rather, the discussion above simply illustrates the ability of courts to reach different results in reviewing these sorts of questionable board decisions depending upon the degree of skepticism versus deference which the court brings to the review. Disney and Mannesmann reached different results because the courts differed in the degree of skepticism versus deference which they brought to the examination.

27. 825 A.2d at 289.
28. E.g., Donohue, supra note 26 (discussing extensive evidence that Ovitz should have been fired for cause, the failure of the Disney directors to carefully consider this evidence, and the limited factual basis, years after the fact, for the Chancery Court to conclude that no cause existed for firing Ovitz).
This difference between Disney and Mannesmann, in turn, raises two questions: Are these cases aberrational, or do they typify a difference between Delaware and German law when it comes to deference to the directors' business judgment? If they do typify such a difference, what are the normative implications?

The deference accorded by the Delaware courts in the Disney case appears quite typical of Delaware courts' application of the business judgment rule.29 Indeed, in Zapnick v. Goizueta,30 the Delaware Chancery court applied a highly deferential interpretation of the business judgment rule in order to uphold the sort of bonus, based upon extraordinary past accomplishment, condemned by Mannesmann. Similarly, the greater willingness to second-guess board decisions demonstrated by the German court in Mannesmann finds parallels both in other German court decisions and in the German corporate statute.

A good example, beyond the Mannesmann case, of German judges showing less deference to directors than do judges in Delaware comes the very court opinion sometimes cited31 as importing the business judgment rule (or something like it) into German law. In the ARAG/Garmenbeck case,32 the German Federal Supreme Court (Civil Division) dealt with an action brought by a couple members of a supervisory board of a German insurance company (ARAG). These board members challenged the decision by the board's majority declining to bring an action against the chairman of the company's management board. The dissenting directors argued that the chairman had violated his duty of care when he lost company funds by becoming the victim of a pyramid scheme (involving a company named Garmenbeck). A regional court found merit in the dissenters' complaint, but an intermediate appellate court—in an opinion marked by language about the need for courts to grant directors “decision-making prerogative”33—ruled that the complaint should be

29. E.g., Zapnick v. Goizueta, 698 A.2d 384 (Del. Ch. 1997) (liability for a disinterested decision is very rarely established by a shareholder plaintiff, because judicial inquiry ends if any reasonable person might conclude that the deal made sense); Gagliardi v. TriFoods Intl., Inc., 683 A.2d 1049 (Del. Ch. 1996) (there have been no awards of money damages in Delaware against corporate officers or directors based upon the theory that their decision was so egregious as to fall outside the protection of the business judgment rule); Stein v. Meyer, 1995 WL 441999 (Del. Ch. 1995) (decisions by disinterested directors that would be sufficiently one-sided as to constitute waste are so rare that they may, like “Nessie” [the Loch-Ness monster], be nonexistent). 30. 698 A.2d 384 (Del. Ch. 1997).


32. 175 Entscheidungen des Bundesgerichtshofs in Zivilsachen [BGHZ] 135, 244 (Bundesgerichtshof [Federal Court of Justice], F.R.G. 1997).

33. Translation in Gevurtz, supra note 15, at 81 (from a translation in Andreas Cahn & David C. Donald, COMPARATIVE COMPANY LAW (forthcoming)).
dismissed. The dissenter then appealed to the German Federal Supreme Court.

At first, the German Supreme Court’s opinion in the ARAG/Garmenbeck case sounds not dissimilar from what one would expect out of a Delaware court. The court recognized the need to give management board members “a wide range of free discretion” in making business decisions, by imposing liability “only when a manager goes significantly beyond the limits of a business judgment characterized by responsible management oriented solely towards the good of the corporation and based on a careful evaluation of the relevant facts.”

Nevertheless, when it came down to the specific decision of whether the company should bring an action against the chairman of the management board, the court showed little deference. This began by the court deciding that an evaluation of the merits of the likely claim against the chairman was a matter upon which directors had no special expertise. Hence, evaluating the merits was not a business decision calling for deference to the directors. Neither, it turns out, is any particular deference due to the board on the question of whether the interest of the corporation calls for refusing to prosecute a potentially viable claim. Instead, the court explained that only in extraordinary circumstances could the supervisory board refuse to prosecute an apparently well-grounded claim against managing directors. Rather than deferring to the directors’ evaluation of whether such extraordinary circumstances exist, the directors must establish them for the court, which will then “perform a detailed evaluation and balancing of the considerations for and against prosecuting the claim.”

The German statute governing stock companies also suggests a less deferential standard for reviewing board decisions. Interestingly enough, the German statute contains a provision making directors liable only in the event they are grossly negligent—which sounds a lot like the Delaware version of the business judgment rule—but this applies just when individual creditors assert the corporation's claim against directors. By comparison, in marked distinction from the business judgment rule in Delaware, the statute governing the liability of the directors of German stock companies places the burden of proof on directors to establish their due care. Most recently, in 2005, the German legislature amended the law governing stock

34. Id. at 83.
35. Id. at 84.
36. Aktiengesetz [AktG] [Stock Corporation Act] § 93(5). For an English translation of the Stock Corporation Act, see Wirth et al., supra note 8.
39. AktG § 93(2).
companies to codify a business judgment rule along the following lines:

There will be no breach of duty when a member of the management board, in making a business decision, could reasonably assume, on the basis of appropriate information, that the member was acting in the interest of the corporation.\textsuperscript{40}

The notion that the directors will be liable unless they "reasonably" assume they are acting in the interest of the company, however, seems closer to traditional standards of negligence than it does to Delaware's version of the business judgment rule.\textsuperscript{41}

This brings the discussion to the normative implications of the different degrees of deference accorded by Delaware and German law to the business judgments of directors. One could argue that the greater apparent willingness of German judges to second guess business decisions is symptomatic of the statist tendencies in German political and economic philosophy, which, from the days of Bismarck, often has endorsed an active role for government bureaucracy in managing economic matters.\textsuperscript{42} By contrast, the deference of Delaware courts is consistent with a philosophy more willing to put trust in private ordering and markets.\textsuperscript{43}

In any event, whether viewed in these macro terms of different economic and political philosophy, or in micro terms of how directors might be expected to react to a greater or lesser degree of judicial oversight, one might ask whether there has been any demonstrated impact on the performance of Delaware and German corporations as a result of this difference in the application of the business judgment rule. If there is such an impact, no one has yet put together a convincing study to demonstrate it.\textsuperscript{44} Of course, the fact that German

\begin{enumerate}
\item AktG § 93(1), para. 2, as added in 2005 (translation in Gevurtz, \textit{supra} note 15, at 85).
\item \textit{E.g.}, Gevurtz, \textit{supra} note 3, at 298-300.
\item \textit{E.g.}, Harold Baum, \textit{Change of Governance in Historic Perspective: The German Experience, in Corporate Governance in Context: Corporations, States, and Markets in Europe, Japan, and the U.S.} 6-8 (Klaus J. Hopt, Eddy Wymeersch, Hideki Kanda & Harold Baum eds., 2005).
\item It might be tempting to find evidence of a negative impact for the German approach to the business judgment rule in the relatively poorer economic performance in Germany versus the United States in recent years. Such an assertion, however, begs the question of whether earlier periods of higher economic growth in Germany (the 1950s through the 1980s) were the aberration, or whether the recent period of more stagnant growth (following the costly absorption of formerly Communist East Germany) is the aberration. Interestingly enough, Germany recently passed the United States to become the world's largest exporter. \textit{Come in Number One, Your Time is Up}, \textit{The Economist} 12 (Apr. 14, 2007). More fundamentally, one would need to disentangle the impact of judicial review of business decisions from a host of more
\end{enumerate}
law, as discussed later, is much less hospitable to shareholder litigation than Delaware law may offset seemingly more onerous substantive liability standards and thus result in a rough functional equivalence between Delaware and Germany as far as the actual likelihood of corporate directors facing liability. Still, the difference between Delaware and Germany in applying the business judgment rule should give one pause before assuming Delaware courts have come upon the optimal version of the rule. This should not be surprising, since, even within the United States, different state courts over the years have come to very different positions as to the appropriate level of judicial scrutiny of the directors’ business judgments.

B. Attitudes toward Directors Dealing with other Directors

As just discussed, the contrast between Disney and Mannesmann seems broadly indicative of a greater willingness of German judges, than Delaware judges, to second guess business decisions. There is, however, a narrower way to view the German court’s willingness to second guess the directors specifically in Mannesmann. German law seems implicitly to reflect greater skepticism toward the ability of so-called disinterested directors to protect the corporate interest when making decisions impacting other directors, than does Delaware law in cases like Disney.

The German skepticism of the ability of directors to deal objectively with other directors shows up most clearly in the requirement that a German stock company (an Aktiengesellschaft or AG) have a two-tier board. In such an arrangement, the company must have a management board empowered to manage the company, and a supervisory board—none of whose members can be on the management board or otherwise be a senior executive of the company—to supervise the management board. Of central importance for present purposes, the obligations of the supervisory board encompass representing the company in dealing with members of the management board—which includes setting the compensation of the members of the managing board. In other words, a critical notion behind

likely explanations for German economic and corporate performance. See, e.g., Edmund S. Phelps, Entrepreneurial Culture, Wall St. J., Feb. 12, 2007, at A15 (essay by a Nobel Prize winning economist, which attempts to explain lagging economic performance in Western Europe, including Germany).

45. See infra text accompanying notes 112 through 120.
47. E.g., Gevirtz, supra note 3, at 290-303 (outlining four variations of the business judgment rule).
48. AktG § 76(1).
49. AktG § 105(1).
50. AktG § 111(1).
51. AktG § 112.
requiring a two-tier board is that there should be an organizational wall that separates the directors empowered to approve conflict-of-interest transactions, including executive compensation, from serving with the managers whose transactions and compensation they must approve.\textsuperscript{52}

By contrast, Delaware law allows members of a single board to approve transactions between the corporation and other directors,\textsuperscript{53} including setting compensation for any directors that also act as senior managers of the corporation—such as Eisner and Ovitz at Disney. Corporations might attempt to create a rough approximation of the separation entailed in the German two-tier board by having a board composed entirely of outside directors, or by delegating compensation decisions to a committee of outside directors; but there is no requirement in Delaware law that corporations do either.\textsuperscript{54}

Of more direct relevance when comparing Disney and Mannesmann is the attitude of German and Delaware judges toward reviewing transactions in which some directors have a conflicting interest. Despite the insulating impact of a two-tier board, German courts, as exemplified by Mannesmann, have not given the supervisory board the same degree of deference in dealing with the management board that the Delaware courts routinely give to so-called disinterested directors, who approve transactions involving fellow members of unitary boards. In part, this reflects, as discussed earlier, a generally less deferential approach to reviewing the directors' business judgment that appears to exist under German law. It is worth noting, however, that the principal German cases exhibiting this lack of deference involve supervisory board decisions in which members of the management board had a financial stake. Specifically, Mannesmann involved compensation for members of the management board.\textsuperscript{55}

\textsuperscript{52} See, e.g., Klause J. Hupt, Corporate Governance in Germany, in \textit{Capital Markets and Company Law} 394 (Klauss J. Hupt & Eddy Wymeersch, eds., 2003).

\textsuperscript{53} \textit{E.g.}, Del. Code ann., tit. 8 § 144.

\textsuperscript{54} \textit{Id.} Delaware law in this regard stands in contrast not only with German law, but also with stock exchange listing requirements. \textit{E.g.}, \textit{New York Stock Exchange Listed Company Manual} § 303A.05(a) (companies listed on the New York Stock Exchange must have a compensation committee composed entirely of independent directors).

\textsuperscript{55} Moreover, among the recipients of the bonuses approved by Mannesmann's executive committee apparently was one member of the committee itself (the predecessor to Mannesmann's CISO at the time of the takeover). \textit{E.g.}, Kolli, \textit{supra} note 32, at ¶ 9. The fact that this conflict-of-interest left only one disinterested director voting to approve the transaction, with the other disinterested directors either abstaining or not present, presumably would have tipped the scale under Delaware law against application of the business judgment rule. See, e.g., Del. Code ann., tit. 8 § 144(a)(1) (during a conflict of interest if a majority of the disinterested directors approve the transaction). The key passages of the \textit{Mannesmann} opinion, however, ignore the conflict-of-interest of this one committee member—suggesting skepticism even as to a transaction involving just members of the management board.
while ARAG/Garmenbeck, as discussed above,\textsuperscript{56} involved the decision of whether to sue the chairman of the management board.

By contrast, Delaware court decisions potentially limit judicial review of transactions involving board members to the deferential standard of the business judgment rule when such transactions receive approval from a majority of the so-called disinterested directors on the board.\textsuperscript{57} Indeed, the Delaware courts in Disney gave—as described above—great deference to the decisions of the defendant directors despite commenting unfavorably throughout the litigation on personal relationships that may have influenced those decisions. For example, the Delaware Chancery Court wrote:

\begin{quote}
Eisner stacked his (and I intentionally write “his” as opposed to “the Company’s”) board of directors with friends and other acquaintances who, though not necessarily beholden to him in a legal sense, were certainly more willing to accede to his wishes and support him unconditionally than truly independent directors.\textsuperscript{58}
\end{quote}

In fact, among Disney’s directors were Eisner’s personal attorney, the administrator of a private school attended by three of Eisner’s children and to which Eisner had made substantial contributions, and the president of a university upon whose board Eisner served and to which he had made a $1 million contribution. Eisner, in turn, had been close friends with Ovitz for around 25 years.

The deference shown in Disney in the face of reasons to question the objectivity of so-called disinterested directors is very typical of Delaware jurisprudence.\textsuperscript{59} For example, in Beam v. Stewart,\textsuperscript{60} the Delaware Supreme Court refused to excuse the shareholder plaintiff from making a demand on the board of directors of Martha Stewart Living Omnimedia, Inc. before bringing a derivative action against Martha Stewart.\textsuperscript{61} The plaintiff claimed that Martha Stewart—whose criminal conviction allegedly undermined the brand name—had breached her duty to the company, and that a majority of the board members were not independent of Martha Stewart so as to be

\textsuperscript{56} See supra text accompanying note 32.

\textsuperscript{57} E.g., Cinerama v. Technicolor, Inc., 663 A.2d 1156 (Del. 1995) (business judgment rule will apply unless a majority of the board are interested in the transaction or are dominated or controlled by the interested directors, or the interested directors do not disclose the conflict); Oberly v. Kirby, 592 A.2d 445, 467 (Del. 1991) (approval by a board, the majority of whose members are disinterested and independent, brings a conflict-of-interest transaction within the scope of the business judgment rule).

\textsuperscript{58} 907 A.2d at 760.


\textsuperscript{60} 845 A.2d 1040 (Del. 2004).

\textsuperscript{61} For a discussion of the requirement under Delaware law that the plaintiff in a derivative lawsuit must either first make a demand upon the board, or else plead that such a demand would be futile, see infra text accompanying notes 122-24.
able to consider the corporation's interest in bringing a suit against her. One might have thought that the allegations that Stewart controlled over 94 percent of the voting stock—meaning that all of the directors served at her sufferance—and that the directors were longtime friends of Stewart, would have been enough to create a reason to doubt the directors' ability to consider independently the corporation's interest in bringing a suit against Stewart. This was not enough, however, for the Delaware courts. Instead, the Delaware Supreme Court affirmed the Chancery Court's dismissal of the complaint for failure to make a demand—thereby effectively leaving the decision as to whether to sue Stewart to the board.

Curiously, the lesser apparent scrutiny applied by Delaware, as opposed to German, judges in reviewing board decisions in which senior executives have a personal interest seems to be upside down. After all, given the greater structural protection against bias presumably built into the two-tier board, one would think that it would be the German judges that ought to apply less scrutiny than the Delaware judges. The likely explanation for this apparent anomaly is that legislative and judicial responses to a problem often work like a magnifying glass, rather than like a teeter-totter. In other words, rather than courts viewing protective legislation as a reason to reduce their own protective scrutiny, both legislation and judicial decisions constitute a lens through which one can see society's attitudes toward the need for protection. Hence, both the German statute and the German court opinions reflect the attitude of a society which appears suspicious of the ability of fellow board members to protect the corporation from each other. By contrast, both the Delaware statute and Delaware court opinions reflect a philosophy willing to place much more trust in the so-called disinterested director.

What then is the normative implication of this difference between Delaware and German law with respect to the trust accorded to disinterested directors in dealing with other directors? Perhaps in light of that nation's history it is not totally surprising that German law would seem particularly attuned to the dangers of group think to which so-called disinterested directors on a unitary board might be prone. Indeed, the German saying "one crow does not gouge out the other crow's eye" may explain why German courts apparently remain suspicious even of actions of the supervisory board impacting members of the management board. The facts in *Disney* suggest that the Germans are right to question the ability of disinterested direc-

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tors to act objectively in protecting the corporation's interest in transactions with senior management.

C. Employee Representation on Corporate Boards

Comparing the events in Disney and Mannesmann provides an opportunity to consider the impact of another difference between Delaware and German law. Two major attributes constitute defining characteristics of corporate governance under German law. The previous discussion mentioned one attribute—the two-tier board. A second defining attribute is mandatory employee representation on corporate supervisory boards under a system known as co-determination. Such employee representation is a concrete manifestation of the stakeholder, as opposed to the shareholder primacy, model of corporate governance followed in Germany, under which those charged with management of the corporation should serve the interests of shareholders, employees, creditors and even the community at large, as opposed to being exclusively, or even primarily, concerned with maximizing profits for the shareholders.64

Under a 1952 law, German firms with more than 500 employees must have a board, one-third of whose members are elected by the employees of the firm who work in Germany.65 A 1976 Act goes further and requires all German firms with more than 2000 employees to allow the employees working in Germany to elect half of the members of the supervisory board (the size of which depends, under the Act, upon how many persons the company employs).66 The ability to elect half the board under the 1976 Act does not quite give parity to employees, however, since the representatives of the shareholders on the board can elect the chair, who has the power to cast a tie-breaking vote. As mentioned earlier, because Mannesmann had over 20,000 employees in Germany, the 1976 Act required Mannesmann to have a 20-person supervisory board, half of whose members were selected by the employees. Following the same ratio, half of the members of the four-person executive committee, which approved the bonus to the outgoing CEO, were employee representatives.

Looking at the matter from an ex post standpoint, there is no evident indication that the German court was any less deferential to the Mannesmann directors, or that the Delaware courts were any more deferential to the Disney directors, because of the presence or absence of employee representatives among the defendants. True,

65. Betriebsverfassungsgesetz [Works Council Constitution Act] § 76. See also Wirth et al., supra note 8, at 103.
66. Mitbestimmungsgesetz [Co-determination Act] §§ 1, 7 27, 29. See also Wirth et al., supra note 8, at 103.
the German Supreme Court was probably not very impressed with the efforts of the employee representatives to have it both ways—complaining about the bonus, but not taking all available steps to prevent its adoption or implementation. Indeed, the court rejected the argument that there was no breach of duty in an employee representative’s abstaining from voting on, rather than voting to approve, the bonus. Still, this was not central to the German court’s condemnation of the bonus. Moreover, the decision-making process at Disney was, as commented upon by the Delaware courts, hardly free from fault.

What may be more interesting is to look at the matter from an ex ante perspective. Specifically, did the presence of employee representatives on the Mannesmann board, or their absence on the Disney board, impact either board’s actions?

Looking at the events in Mannesmann, it appears at first glance that co-determination was unhelpful in the board’s dealing with the bonus. As described earlier, the two shareholder representatives on the executive committee decided upon the bonus at a session without the two employee representatives. Following this session, the two shareholder representatives contacted one of the employee representatives (a union official). The union official agreed to be “present” and essentially to abstain—thereby allowing the committee to approve the bonus. He did so, despite qualms about the large size of the bonus, based upon the rationale that the bonus did not relate to “employee concerns.” Generalizing from this experience, one might fear that co-determination can weaken the ability of the supervisory board to deal with executive compensation, since employee representatives may take a hands-off attitude toward such non-employee concerns.

Other events surrounding the Mannesmann case, however, may point to a different conclusion. Specifically, following public disclosure of the bonus, the Mannesmann employees and employee representatives on the board provided a locus of opposition to the bonus. This suggests that employee representation in Germany may help keep executive compensation in check, in a manner that is missing in the United States as illustrated by the compensation package in Disney.

While the events in Mannesmann provide conflicting evidence regarding the impact of employee representatives on executive compensation decisions, there are several reasons to suspect that employee representatives will be more conservative in approving executive compensation than are other directors. In part, as captured by the remarks the union official on the executive committee of Mannes-

67. See supra text at page 461.
mann's board, a reluctance to approve multimillion compensation packages can be the expected response from persons for whom multimillion dollar compensation packages are largely foreign from the life experiences of themselves and persons they know. Moreover, employee representatives are likely to be attuned to a comparison of executive compensation to compensation of rank-and-file employees. Not only does such a comparison reflect simple, but powerful, jealously, this focus may also reflect the perception that more pay for the senior executives means less for the rank-and-file. True, senior executives might argue that such an attitude assumes a zero-sum game, whereas attracting the best senior management can actually increase pay for the rank-and-file by producing superior business performance. Acceptance of this argument, however, is likely to run into the self-validating psychology of workers, who might, accurately or not, be inclined to assume that their efforts are the key to business success (often in spite, rather than because, of senior management). Finally, to the extent that higher compensation commonly results from tying pay to stock price or to net-profit oriented performance incentives, employee representatives might quite rationally assume that such pay is counter to their interests insofar as it may motivate efforts to reduce labor costs.

Regrettably, the impact of co-determination in Germany on executive compensation is one aspect of co-determination upon which there apparently has been no empirical study. There is some anecdotal evidence, however, to support the conclusion that employee representatives tend to oppose more generous executive pay. For example, in 1996, Daimler-Benz's supervisory board confronted the issue of whether to introduce a stock option plan for managers. Like Mannesmann, the Daimler-Benz supervisory board had 20 members, half of whom were employee representatives. Nine of the ten employee representatives voted against the stock option plan, which passed only by a vote of eleven to nine. Actually, one suspects that the impact of co-determination on executive compensation will rarely manifest itself in an actual vote. Instead, it is more likely that knowledge of possible opposition by employee representatives is factored into the choice of how generous a pay package to present to the board. In any event, there is also some evidence from the United States that employee representatives will oppose more generous ex-

68. The union official purportedly made the comment that "a lady would have to knit a heck of a lot" to make so much money.
70. The "Dilbert" cartoon strip humorously captures this attitude.
71. E.g., Cheffins, supra note 69, at 515.
72. See Gerum & Wagner, supra note 8 (discussing the various empirical studies of the impact of co-determination in Germany).
73. E.g., Cheffins, supra note 69, at 515.
ecutive pay. Specifically, many of the shareholder proposals made pursuant to Securities Exchange Act Rule 14a-8, which seek to limit executive pay, come from union and public employee pension plans.

By contrast, typical directors on the boards of Delaware companies, or indeed other public companies formed within the United States, have a background that will make them much less conservative in approving executive pay. In this regard, it is useful to look at the members of Disney's compensation committee, who approved Ovitz' pay package. The committee members consisted of an attorney, who specialized in the entertainment industry and thus likely was comfortable with multimillion dollar compensation packages, a renowned movie actor, who presumably has received significant compensation packages on various movie deals, and two other individuals, who served on the boards of a number of corporations that probably paid well their senior executives. More broadly, the habit of filling boards of Delaware corporations with the CEOs of other companies hardly seems like a recipe for restraint in executive pay.

What then is the normative implication of the possible impact of co-determination on executive pay? At first glance, one's view of the utility of having employee representatives on the board when it comes to executive pay might seem to depend upon one's view as to whether executive compensation has become too large: if one believes that executive compensation has become too large, then having employee representatives as a source of opposition would be useful. Even if one is agnostic about the overall level of executive compensation, however, an argument can be made for having employee representatives involved in setting executive pay. After all, such representatives can bring a different, and useful, perspective on the issue. Not only might such representatives have a different sense of the value of money, but they might also bring an insight into the effectiveness of management from those who see its impact on a daily basis. Of course, the possible impact on executive compensation is only one factor to consider in weighing the advantages and disadvantages of co-determination. Given the conflicting and uncertain evi-

74. 17 CFR 240.14a-8. This regulation, promulgated by the Securities Exchange Commission, gives shareholders in listed companies the right to demand that corporate management include, in the corporate proxy statement, proposals that the shareholders intend to make at the shareholders meeting.

75. E.g., William J. Holstein, Raising Labor's Hand at Annual Meetings, N.Y. TIMES, Oct. 26, 2006, at 3-1; (interview with one of the architects of organized labor's effort to use corporate proxy machinery to alter compensation to CEOs); David A. Katz & Laura A. McIntosh, Corporate Governance: Institutional Investors Ready Proxy Season 'Wish Lists,' 236 N.Y.L.J., Nov. 10, 2006, at 5 (describing proxy proposals from union pension funds aimed at executive compensation).

ence that exists on the broader impact of co-determination, however, the utility of the practice with regard to disciplining executive compensation is worth taking into account.

D. Attitudes toward Compensation of Senior Executives

Even before the results in Disney and Mannesmann, writers had pointed to major differences between executive compensation in the United States and in Germany. These differences may help explain the different results in Mannesmann and Disney, and the different results in Mannesmann and Disney might help explain these differences in executive compensation. Moreover, as just mentioned in considering the implications of co-determination’s impact on executive compensation, it is difficult to separate out entirely one’s normative view of the differences discussed thus far between German and Delaware corporate law, from one’s view regarding the level of executive compensation currently prevailing in the United States.

The obvious difference between executive compensation in the United States, versus in Germany, lies simply in the amounts of compensation in the two nations. Looking to the year 2000, in which Esser received his bonus, the average CEO in the United States received 531 times the pay of an average employee in his or her company, while, in Germany, the average CEO received only 11 times the pay of an average employee in his or her company. Admittedly, the greater number of larger corporations in the United States than in Germany might mean that the comparison above exaggerates to some extent the actual difference between CEO pay in like corporations. Nevertheless, a dramatic example of the disparity in like corporations received public attention in 1998, when Daimler-Benz took over Chrysler. It turned out that the number two executive at Chrysler received more in compensation during the prior year from his salary, bonus and stock options than the total compensation for that year of the top ten Daimler-Benz executives combined.

A difference in the nature of compensation in the United States versus Germany has magnified the disparity in the amounts that executives receive in the two countries. As illustrated by the package that Ovitz received from Disney, an increasing component of executive compensation in the United States comes from stock options and

77. E.g., Gerum & Wagner, supra note 8; Hopt, supra note 8.
78. E.g., Cheffins, supra note 69.
79. E.g., John C. Coffee, Gatekeeper Failure and Reform: The Challenge of Fashioning Relevant Reforms, 84 B.U. L. REV. 301, 330 n.86 (2004); Susan J. Stabile, Enron, Global Crossing and Beyond: Implications for Workers, 76 ST. JOHNS L. REV. 815, 829 n.63 (2002). While my focus in this article is on a comparison between the United States and Germany, a similar disparity in CEO compensation exists between the United States and other nations as well. Id.
80. E.g., Cheffins, supra note 69, at 508-09.
similar incentive pay. This reflects a variety of factors, including favorable tax treatment, and the notion that such compensation better aligns the incentives for executives with the interests of the shareholders. German executives, by contrast, have received far less in variable or incentive oriented compensation. While bonuses for German executives based upon profits are common enough, stock options or similar schemes that reward executives based upon the performance of the company’s shares on the stock market traditionally have been uncommon.

These differences in the amount and nature of executive compensation in United States versus Germany, in turn, may reflect a difference in attitudes toward executive compensation both within corporations and in the broader society. Writers have pointed out how German companies, like companies throughout continental Europe, “tend to have an equality-oriented civil service mentality.” This attitude within German corporations appears to mirror a broader political and social culture much more attuned to equality in wealth distribution than is the political and social culture in the United States.

So, what do these differences with respect to executive compensation tell us about Disney and Mannesmann? To begin with, these differences likely influenced the results in these two cases. From a doctrinal standpoint, it is extremely difficult to assess the appropriateness of an executive’s compensation without regard to prevailing levels. The need to compare the challenged compensation with prevailing levels is explicit in the fairness test applied under Delaware law:


82. See, e.g., I.R.C. § 162(m) (preventing corporations from deducting more than $1 million in compensation paid to a senior executive, unless paid as performance based compensation, such as stock options), § 422A (providing favorable tax treatment for incentive stock options under certain restrictions); Treas. Reg. § 1.83-7 (creating the prospect of deferral of tax upon receipt of options for which there is no ascertainable value).

83. E.g., Lubin & Thurm, supra note 76 (before 2003, “options remained a favorable tool for an important reason—they were essentially free, [in that] options granted at or above the market price of a stock did not have to be recorded as a company expense in financial results”).

84. E.g., Loewenstein, supra note 5, at 8 (“much of the dramatic increase in CEO compensation is a direct result of the increase in incentive compensation in the form of stock options, which, in turn, were implemented by corporate boards in response to demands that CEO compensation be more closely linked to shareholder returns”).

85. E.g., Stefan Prigge, A Survey of German Corporate Governance, in COMPARATIVE CORPORATE GOVERNANCE, supra note 8, at 943, 967.

86. Cath Blackledge, Euroland Bonanza, EUROPEAN, June 8, 1998, at 20. See also Cheffins, supra note 69, at 513-16; Kolla, supra note 22, at ¶ 15.

87. E.g., Umfrage: Gerechtigkeit vor Freiheit, Zeit online, Tagesspiegel, http://www.zeit.de/news/artikel/2006/12/02/83097.xml (Dec. 2, 2006) [hereinafter, Survey] (article reporting on a survey by the German newspaper, Welt am Sonntag, which found that a majority of Germans (58% versus 34%) prefer “social justice”—i.e., income equality—to economic freedom).
law to conflict-of-interest transactions that lack disinterested director approval. Even with disinterested director approval, such a comparison remains relevant in assessing the outer bounds of acceptable compensation under the business judgment rule in Delaware. So, had Ovitz’ termination rights not reflected what he gave up from leaving his existing position, it is likely that there would have been a different result in Disney. Admittedly, the court in Mannesmann put aside discussion of whether the amount of the bonus was unreasonable in relation to the recipient’s task and position; instead finding no benefit to the company that would justify any bonus. Yet, it is impossible to believe that the court would have condemned a more modest token of appreciation—the traditional gold watch, as opposed to a bonus of extraordinary size relative to German compensation levels—on the ground that the corporation could gain no benefit under the circumstances.

Moreover, influence between prevailing practices and legal rules flows in both directions. Not only do the prevailing levels of executive compensation exert a pull on judicial results, but the underlying law reflected in judicial results exerts an influence over executive compensation. Of course, being very recent decisions, the impact of Disney and Mannesmann themselves may yet to be fully felt. These decisions, however, reflect longer standing statutory and judicial doctrine and attitudes, which have had plenty of time to explain some of the difference in executive compensation in the United States and Germany. This article has already discussed the lesser deference apparently accorded by German, as compared with Delaware, courts toward directors’ decisions, particularly, as with executive compensation, when the decision involves other directors, as well as the possibly limiting influence that co-determination might have on executive compensation.

One additional difference particularly with respect to executive compensation in German, as opposed to Delaware, law comes from the fact that the German stock company law, unlike the Delaware

88. E.g., Wilderman v. Wilderman, 315 A.2d 610 (Del. Ch. 1974).
89. E.g., Lewis v. Vogelstein, 699 A.2d 327, 339 (Del. Ch. 1997) (“option grants to directors of this size seem . . . sufficiently unusual to require the court to refer to evidence before making an adjudication of their validity and consistency with fiduciary duty”); E. Norman Veasey, State-Federal Tension in Corporate Governance and the Professional Responsibilities of Advisors, 28 J. Corp. L. 441, 447 (2003) (it is a myth that there are no “limits” to executive compensation under the law).
90. 906 A.2d at 58 (“the [compensation] committee members knew that by leaving CAA and coming to Disney, Ovitz would be sacrificing ‘booked’ CAA commissions of $150 to $200 million—an amount that Ovitz demanded as protection against the risk that his employment relationship with Disney might not work out.”).
91. E.g., Andreas Ransiek, Anerkennungsprämien und Untreue – Das “Mannesmann”-Urteil des BGH, NJW (Neue Juristische Wochenschrift) 2006 Heft 12, p. 814 (traditional parting gifts to corporate officials remain acceptable under German law despite Mannesmann).
corporate statute, contains a provision specifically addressing limits on executive compensation. This section requires the supervisory board to ensure that the total compensation of each member of the management board is reasonable in relation to the tasks of the member and the situation of the company.\(^\text{92}\) Such an explicit statutory command that compensation be reasonable arguably empowers courts to review compensation with a greater degree of scrutiny than would more generalized notions of fiduciary duty, and might thereby operate to restrain executive compensation levels in Germany.\(^\text{93}\)

This brings the discussion to the normative implications of the difference in executive compensation between Delaware and German corporations as reflected in Disney and Mannesmann. In fact, there may be at least five implications one can draw.

To begin with, as others have pointed out already,\(^\text{94}\) this gap may say something about the question of whether compensation in the United States lacks sufficient relation to actual performance. Specifically, one must ask whether CEOs in the United States perform so much better than CEOs in Germany to require compensation over 500, versus over 11, times the average worker’s salary.

The situations in Mannesmann and Disney, however, raise a more difficult normative issue with respect to executive compensation: is there a social problem with huge executive pay packages, even if tied to performance? After all, in Mannesmann, Esser’s bonus may seem large in absolute terms (certainly by German standards), but was small in proportion to the added wealth realized by the Mannesmann shareholders in the Vodafone takeover. In Disney, Ovitz’ termination package, while huge in absolute terms, appears designed to compensate Ovitz for commissions he would give up by leaving his talent agency to join Disney—which commissions presumably reflected a percentage of the income he gained for the agency’s clients. The evident hope behind paying this to Ovitz was that he would make more money for Disney by coming up with blockbuster movie deals. Hence, in both cases, one might justify the pay package based upon the goal of wealth creation for the corporation or its shareholders; yet, in both cases, the result of such large pay packages seemingly is to increase inequality in income between those at the top and those in the middle of the corporate workforce. This fact, in turn, raises a fundamental philosophic question upon which United States and German societies differ: this being, is it more important to soci-

92. AktG § 87(1).
93. E.g., Cheffins, supra note 69, at 526.
94. E.g., Troy A. Paredes, Too Much Pay, Too Much Deference: Behavior Corporate Finance, CEOs and Corporate Governance, 32 Fla. St. U. L. Rev. 673, 707 (2005) (proponents of the view the U.S. senior executives are overpaid often point out that managers in Europe and Asia are paid much less than their U.S. counterparts and, the argument seems to imply, are sufficiently industrious).
ety to reduce inequality in wages, or to maximize wealth creation, if necessary, at the expense of greater inequality.95

Next, in an increasingly global economy, one must ask whether the large gap in senior executive pay between the United States and Germany can endure. Specifically, why have German executives not migrated in sufficient numbers to Delaware corporations so as to force an increase in executive compensation by German companies (or a decrease in executive compensation by Delaware corporations)? Indeed, some have suggested96 that Mannesmann may be best understood as a “finger in the dike” in an attempt to hold back an alignment already underway of the compensation of German senior executives to come closer to senior executive compensation levels prevailing in the United States.97 The corollary is to provide another example of the tension between globalization and the preservation of local social policies.

Disney and Mannesmann also have normative implications with respect to what sort of achievement compensation packages should reward. The bonus in Mannesmann rewarded, for the most part, actions by the departing CEO that increased the price received by the Mannesmann stockholders upon the sale of the company to Vodafone, rather than increased corporate performance for the benefit of all stakeholders in the company. As mentioned earlier, for a variety of reasons, German corporations traditionally have been reluctant to provide stock options, or other executive compensation tied to maximizing value for the stockholders—which formed the bulk of Ovitz’ package. An issue raised in both situations is the extent to which German corporations should adopt incentive pay plans that reward maximizing wealth for the shareholders, as opposed to running the corporation for the benefit of all stakeholders.

One final aspect of the bonus in Mannesmann is that it presumably would not have violated the board’s duty had the CEO’s employment contract called for such a performance bonus. This, in turn, creates an incentive for contractual pre-commitment to bonus pay. Disney suggests the downside to such a contractual pre-commitment: Ovitz received a huge payout despite poor results. True, corporations can try to draft contracts only to reward good performance by the particular official, but that is not always easy. Stock options, for example, reward market performance regardless of the role of the par-

96. E.g., Kolla, supra note 22, at ¶ 2.
97. E.g., Cheffins, supra note 69, at 497-98.
ticular recipient. By contrast, the appreciation award in Mannesmann allowed the corporation to reward good results after seeing them, and without the burden of drafting a contract that ensured the corporation only paid off for what were good results attributable to the CEO. The comparison between Mannesmann and Disney thus shows how legal rules with respect to executive pay structures might sometimes create perverse effects.

E. Deferece to Shareholders

A fifth difference between Delaware and German law illustrated by comparing Disney and Mannesmann involves the ability of shareholders to waive claims against directors for breach of fiduciary duty: specifically, German law is far more restrictive of such shareholder power than is Delaware law.

One cloud that hung over the plaintiffs in Disney was a provision in Disney's certificate of incorporation containing the liability waiver allowed by Section 102(b)(7) of the Delaware General Corporation Law. Section 102(b)(7) authorizes Delaware corporations to include a provision in their certificate of incorporation that eliminates a director's liability for monetary damages to the corporation, or to its shareholders, for breach of fiduciary duty—except if the breach is of the duty of loyalty, is from acts that are not in good faith or involve intentional misconduct, is for improper issuance of a dividend, or involves a transaction in which the director obtained an improper personal benefit. Essentially, by virtue of agreeing to such a certificate provision, the Disney shareholders had thrown away the company's right to assert a straightforward claim that the board had been grossly negligent in breach of its duty of care. In the end, it turned out that the invocation of the business judgment rule by both the Chancery and Supreme Courts in Disney rendered Disney's charter waiver provision unnecessary to the outcome of the case. Still, all the attention paid by the litigants and courts to the question of whether the Disney directors had breached their non-waiveable duty of good faith, as opposed simply to acting in a grossly negligent manner, suggests that the waiver seriously complicated life for the plaintiffs.

100. Faced with the waiver, the plaintiffs in Disney concocted a series of arguments that barely, if at all, pass the straight face test. The first was to assert that proof of the defendants' gross negligence—even if ultimately futile in establishing liability because of the waiver—was nevertheless relevant because it would flip the burden of proof to the defendants to establish the fairness of Ovitz' contract. Only thereafter, once the defendants failed to prove the fairness of the contract, would the court need to deal with the waiver. Presumably recognizing, however, that this reasoning only delayed their need to overcome the liability waiver, the plaintiffs then sought to equate a lack of good faith with gross negligence. Acceptance of this equa-
In contrast to Delaware’s Section 102(b)(7), the German corporation statute significantly limits the ability of shareholders to waive even the company’s duty of care claims against its directors. Such a waiver can only occur for claims more than three years old; essentially operating as a sort of shareholder imposed statute of limitations. Moreover, shareholders cannot waive claims against the company’s directors if holders of at least ten percent of the stock object.  

The German lack of deference to the shareholders in matters of fiduciary duty is not limited to the German corporate statute. The court in Mannesmann took a hyper technical view of whether shareholder approval would nullify the directors’ breach. Vodafone—who was acquiring Mannesmann, and who, by the time of the payout, owned 98.66 percent of the outstanding stock in Mannesmann—approved the bonus. Reasoning from general principles that there is no criminal breach of trust if the owner of the entrusted assets approves the disposition in question, the court in Mannesmann conceded that stockholder approval of the transaction could have avoided liability for the defendants. Nevertheless, the court rejected the shareholder approval defense, because the stockholders never voted on the bonus, and Vodafone did not yet own all of the stock.

Admittedly, the notion that less than unanimous shareholder approval cannot save a transaction amounting to waste is consistent with basic Delaware corporate law doctrine. Yet, it is almost impossible to believe that a Delaware court would find a transaction approved by a 98.66 percent shareholder (so long as that shareholder had no conflict-of-interest) constituted waste in the first place.

What then are the normative implications of the difference between Delaware and German law with respect to the ability of shareholders to waive breaches of fiduciary duty by corporate directors? Underlying the restrictive German approach are potentially different
views from Delaware on a couple of policy questions raised by allowing shareholders to contract out of fiduciary duties.

To begin with, given Germany's embrace of the stakeholder model of corporate governance, one might guess that the German law's reluctance to allow shareholder waiver is based, at least in part, upon a concern that employees, creditors and others beyond the shareholders, who have a stake in the corporation, might be prejudiced (even in situations short of insolvency) by shareholders waiving corporate claims. In fact, however, the Mannesmann opinion seems to reject this notion. The German court explicitly states that stockholder approval—had it occurred in a formal stockholder meeting or by 100 percent of the outstanding stock—would have constituted approval of the loss of assets by the owner of the assets for purposes of precluding a prosecution for breach of trust.

Instead of reflecting the stakeholder model, it appears that the German law's reticence about stockholder waiver reflects a desire to protect stockholders from their own actions. This may, in part, again reflect a paternalistic view implicit in the statist traditions of German political and economic philosophy. It also, in part, may reflect the view implicit in the decision of the German Supreme Court in ARAG/Garmenbeck, which suggests that only in extraordinary circumstances would it make sense not to pursue a potentially viable legal claim in court.

Interestingly, the facts in Disney can shed some light on the concern that shareholder waiver of fiduciary duty might be ill considered. The failure of Disney's directors to ask for shareholder ratification of their actions regarding Ovitz makes one wonder if the Disney shareholders would have agreed to waive this claim at the time, and, in turn, raises the question of whether the shareholders truly appreciated the future impact of their action when they agreed to the liability waiver provision in Disney's charter.

F. Public versus Private Enforcement of Fiduciary Duties

The sixth difference between Delaware and German laws illustrated by the comparison of Disney and Mannesmann involves the mechanism for enforcing fiduciary duties: Disney was a shareholder derivative suit seeking corporate recovery, while Mannesmann was a criminal prosecution seeking fines or prison. This difference, in turn, raises two questions: the first is whether the difference is coinciden-

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104. See supra text accompanying note 42.
105. See supra text accompanying note 35.
106. Of course, the fact that the plaintiffs in Disney ultimately lost after an expensive trial might suggest that the Disney liability waiver was a wise provision; yet, the fact that the case went through the expensive trial despite the provision suggests that all the provision accomplished was to further complicate and thereby add to the expense of the litigation.
tal, or symptomatic of the way in which the two jurisdictions are likely to react to cases of this nature. The second question is whether this difference carries any normative implications.

Criminal prosecutions of corporate officials accused of enriching themselves at corporate expense occur in the United States. Indeed, the prosecution of the former Tyco CEO, Dennis Kozlowski, (in a case known for its $6000 shower curtains) provides a recent example.107 Nevertheless, such prosecutions in the United States, as illustrated by the Tyco case, tend to involve egregious misconduct, and they normally target the corporate officials who enriched themselves, rather than the directors who either approved, or did not prevent, the misappropriation.108 Interestingly enough by way of comparison, in the first trial in the Mannesmann case, the trial court exonerated the defendants based upon the lack of an “aggravated” breach of their fiduciary duty. Thus, the trial court attempted to limit criminal liability under German law to the same sort of egregious cases that prosecutors in the United States might pursue. The German Supreme Court, however, rejected this limitation.

The typical action in Delaware (and in the United States generally) against both corporate officers accused of receiving excessive compensation or otherwise gaining unfair advantage at corporate expense, and the directors who approved, or failed to prevent, such conduct, is a shareholder derivative suit109—as in Disney. Through such an action, a shareholder of the corporation, no matter how small the shareholder’s interest, can bring a lawsuit seeking recovery for the company.110 Of course, one might ask why a shareholder with a minuscule stake in the corporation would file a lawsuit seeking recovery for the company. A principal answer is the availability of attorney’s fees for the shareholder plaintiff’s lawyer in the event the shareholder plaintiff succeeds in obtaining some sort of recovery for the corporation.111

A variety of procedural impediments have rendered shareholder actions to obtain corporate recovery much less viable in Germany.

108. See, e.g., Bernard S. Black et al., Outside Director Liability, 58 Stan. L. Rev. 1055, 1131 (2006) (no criminal prosecution pursuant to federal securities laws has been brought against an outside director for oversight failures); Lisa M. Fairfax, Spare the Rod, Spoil the Director? Revitalizing Directors’ Fiduciary Duty through Legal Liability, 42 Hous. L. Rev. 393, 394 (2005) (over the last 20 years there has been a virtual elimination of legal liability, including criminal liability, on corporate directors who breach their duty of care).
The basic scheme in the German statute governing stock companies, like Mannesmann, looks to the supervisory board to represent the corporation in bringing a legal action against members of the management board. In addition, the German stock company statute allows a vote of the stockholders at the stockholders meeting to command a suit by the corporation against members of the management or supervisory board. The stockholders can command such a suit by a majority vote, or even by a vote of ten percent of the outstanding shares (so long as the owners of the ten percent held their stock at least three months).

Collective action problems, however, can render the ten percent requirement an insurmountable hurdle in a widely held corporation. This, in turn, led to a 1998 amendment to the German Stock Company Act. Under this amendment, holders of five percent, or 500,000 euros worth, of the company’s outstanding stock could petition the court to appoint a special representative upon a showing of facts that justify a strong suspicion of damage to the company from management improprieties or serious violations of the law or articles. The representative must bring an action on behalf of the company if the representative concludes that the action offers a reasonable prospect of success. Implicitly recognizing that even this five percent or 500,000 euros requirement has rendered shareholder suits impractical, a 2005 amendment allows stockholders with one percent, or 100,000 euros worth, of the outstanding stock to bring a lawsuit on behalf of a German stock company if evidence justifies the suspicion of illegal activities or a serious violation of the law or articles; albeit, the shareholders must first make a demand upon the board, and the board can have the suit dismissed if the board can show the court that not suing would be in the overriding interest of the company. This 2005 change, however, obviously postdates the events in Mannesmann.

Corporate law rules are not the only practical impediment to shareholders’ actions in Germany. As suggested above, rules governing attorneys fees are critical to whether a shareholder with a small stake in the corporation will bring an action on behalf of the

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112. AktG § 112.
113. AktG § 147(1).
115. AktG § 147(3).
117. AktG § 148. See also Baums & Scott, supra note 63, at 52.
corporation. German law, like much law outside of the United States, presents a significant barrier in this regard. Specifically, the loser pays rule followed by Germany places a significant financial risk upon the complaining shareholder, who, after all, personally recovers nothing if the action on behalf of the corporation succeeds, but stands to reimburse the defendants' attorneys fees (as well as the costs of the special representative appointed to prosecute the case on behalf of the corporation) if the defendants prevail. Moreover, German law prohibits the contingent fee arrangements used in the United States to shift the risk of unsuccessful litigation from the shareholder plaintiff to the plaintiff's attorney, in exchange for the attorney obtaining more generous compensation in the event of a successful prosecution of the case.

What are the normative implications of this difference in the viability of shareholder derivative actions in Delaware and Germany? Critics of the derivative suit in the United States commonly contend that all too many shareholder derivative suits are meritless claims, whose main consequence is to cost the corporation money. Disney might seem to present a case in point. The litigation took the better part of a decade; involved two trips to the Delaware Supreme Court; required a full blown trial lasting 37 days; after all of which the plaintiffs lost on every one of their claims. As a result, the Disney corporation will end up being obligated to indemnify the defendants for their undoubtedly large legal bills.

Under Delaware law, the main protection of the corporate interest in avoiding meritless derivative suits is the requirement that the plaintiff either make a demand on the board of directors to address the alleged misconduct, or else plead with particularity an excuse for not making such a demand. The basic excuse is that demand would be futile in that all or a majority of the board of directors either are the wrongdoers themselves or under the control of the wrongdoers. Put in the language of the Delaware courts' formulation, the plaintiff must plead with particularity facts that create a reasonable doubt that the directors are disinterested and independent or that their decision is otherwise protected by the business judgment rule.
What this rule essentially does is to grant Delaware courts fairly flexible control over the spigot through which derivative suits must flow. The court can nitpick to death pleadings in a case whose broad outlines suggest to the court that there is probably not much there, or take a more liberal approach to a case the court feels from its broad outlines ought to go forward. The application of this flexible approach is visible in Disney. In the litigation’s first visit to the Delaware Supreme Court, the court held that the pleadings were insufficient, but, in an unusual and perhaps telling act of liberality, instructed the Chancery Court to allow the plaintiffs an opportunity to amend. Thereafter, the Chancery Court, in an opinion marked by its aspersions of Disney’s management, denied the defendants’ motion to dismiss the plaintiffs’ amended complaint, and held that the plaintiffs adequately pled that demand was futile.

One obvious criticism of Delaware’s approach to the demand rule is that it presents a high risk of screening out ultimately meritorious claims, since the court is attempting to intuit the merits based upon pleadings, before the plaintiff has had a chance to take discovery. Disney presents a flip-side problem, in that the court did not screen out a case that ultimately completely failed at trial. Yet, to view the Delaware courts’ demand rule decisions in the early stages of the Disney litigation as simply an evaluation of the probable merits may take too narrow a view. These courts were confronted with a seemingly outrageous transaction that had garnered significant negative publicity. Under such circumstances, interests of institutional legitimacy might well call for a trial on the merits, rather than summary disposition. In this manner, all the facts, including those that ultimately served to exonerate the defendants, could become part of the public record. In this sense, the decision to permit the Disney

126. E.g., Aronson v. Lewis, 473 A.2d 805 (Del. 1984) (allegations that the board approved a compensation package, which amounted to waste because it paid the retired CEO even if he was unable to work, and that the board was not independent of the retired CEO, as evidenced by the facts that he owned 47 percent of the outstanding stock, picked each board member, and had received favorable treatment from the board, were insufficient to excuse demand); Levine v. Smith, 591 A.2d 194 (Del. 1991) (allegation that the directors “did nothing” to inform themselves prior to rejecting the plaintiff’s demand was insufficient to plead that the directors took no action to inform themselves prior to rejecting the plaintiff’s demand).

127. E.g., In re Ebay, Inc., 2004 Del. Ch. Lexis 4, (2004) (allegations that the corporation’s stock option plan gave the directors an incentive to retain their positions and thus made them beholden to prospective defendants, who held less than half of the outstanding stock, were sufficient to excuse demand in a case involving spinning of IPO shares); Parnes v. Bally Entertainment Corporation, 722 A.2d 1243 (Del. 1999) (allegation that various payments were made to the CEO in exchange for his support of a merger was sufficient to excuse demand).

128. 746 A.2d at 267.

129. 825 A.2d at 287-91.

130. E.g., Gevurtz, supra note 124, at 432.

case to proceed to trial—even if the defendants ultimately prevailed—provided a potentially salutary relief valve.

By contrast, the criminal prosecution in Mannesmann illustrates what can happen in a high profile transaction, perceived by the public as outrageous, in the absence of a viable opportunity for civil adjudication. In the United States, a corporate attorney, whose clientele were appalled by a bonus to an outgoing CEO, might have searched for a shareholder who could serve as the named plaintiff in a derivative suit. Without an economically realistic prospect of bringing such a suit, the Dusseldorf attorney outraged by the Mannesmann bonus filed a complaint with the German Federal Attorney’s office. With no visible shareholder civil litigation to meet the public demand for action, increased pressure existed for a criminal prosecution. This is not to say—as the prosecutions growing out of the Enron, Worldcom and similar scandals in the United States illustrate—that the prospect of civil actions precludes criminal prosecutions. It is simply to suggest that the absence of realistic civil alternatives makes criminal prosecutions more likely.

Looking at the impact of this difference, reasonable minds may disagree as to whether greater criminalization of breaches of fiduciary duty is necessarily a bad thing. Perhaps not surprisingly, this disagreement manifests itself in apparently differing attitudes prevailing in the United States versus Germany on the use of criminal sanctions for breach of duty. For Germans, the notion of criminalizing the failure diligently to protect corporate assets entrusted to one’s control seems to have provoked no dissent; the criticisms of Mannesmann in the German literature instead revolve around whether there was a culpable breach. By contrast, one suspects that the Ameri-

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132. See supra text at page 461.
133. E.g., Allan Hall, Defendants “Likely to be Let Off the Hook” in Mannesmann Trial, EVENING STANDARD, July 21, 2004, at 35 (quoting a German business consultant, who stated that the Mannesmann prosecution was in many ways politically motivated and supported by the German chancellor to appease the unions).
135. E.g., Brooke A. Masters, Ebber’s Prosecutors Questioned on Tactics, WASH. POST, Jun. 31, 2006, Business Section.
138. E.g., Kolls, supra note 22, at ¶ 3 (“although it would be a legitimate use of state power to criminalize excessively large executive salaries, the location of the line...
can readers of this article find the criminal prosecution in *Mannesmann* to be disproportionate to the purported wrongdoing, even assuming a breach of duty.

At any event, one should be wary of the unintended consequences of a system in which breaches of fiduciary duty are met more with public criminal prosecutions, as opposed to private civil actions. One additional possible explanation of the result in *Mannesmann* is that the opinion came from the German Federal Supreme Court’s criminal division, which was not as experienced in dealing with corporate law as the civil division. By contrast, shareholder derivative suits in Delaware fall within the jurisdiction of the highly knowledgeable Chancery Court. In addition, the German court’s readiness to resolve doubts against the Mannesmann directors, as compared to the Delaware courts’ willingness to give the Disney directors the benefit of the doubt, might, in part, reflect an unintended (and unexpected consequence) of *Mannesmann* being a criminal prosecution, while *Disney* was a shareholder derivative civil suit. At first glance, given the traditional high burden of proof in criminal actions (including in Germany), courts should be more willing to give the defendants the benefit of the doubt in criminal, as opposed to civil, actions. This, however, ignores an important psychological, as opposed to doctrinal, factor. Specifically, government prosecutors may well enjoy greater credibility than plaintiffs’ attorneys, who make a business out of bringing derivative suits on behalf of shareholders with a minuscule stake in the company in order to collect fees.

### III. Conclusion

Delaware and Germany have been two of the most influential jurisdictions when it comes to the export of corporate law. *Disney* and *Mannesmann* show how these two jurisdictions have reacted to common concerns with executive compensation in ways that reflect different positions on some of the more contentious issues in corporate law. These differences, in turn, carry a number of normative implications regarding the appropriate degree of deference to corporate directors; the degree to which disinterested directors should be trusted to protect the corporation in dealing with other directors; the utility of employee representation on corporate boards; the size and structure of executive compensation; the ability of shareholders to waive claims for breach of fiduciary duty; and the means by which to enforce fiduciary obligations.

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140. StPO § 261; BGH, NStZ (Neue Zeitschrift für Strafrecht) 1985, 15.
One final thought is whether this discussion can tell us anything about whether national laws will converge upon the most efficient answers to these questions, thereby bringing about an end of history for corporate law.\textsuperscript{141} The perseverance of the differences in corporate law and policy reflected in Disney and Mannesmann suggests the need for caution before predicting such convergence. This should not be too surprising, since these differences represent contentious issues concerning which there may be no one correct answer. Moreover, the myriad of factors leading to business failure and success may prevent forces of evolution necessarily determining the most efficient corporate law and policy. Indeed, before becoming too immersed in debate about whether Germany should import corporate law from Delaware or Delaware should import corporate law from Germany, it is useful to keep in mind that Japanese automobile corporations currently are outperforming both the Americans and the Germans.