

Updates From Delaware

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Officers' Duty of Oversight

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Oversight Duties Extend to Officers

In re McDonald's Corporation Stockholder Derivative Litigation, 289 A.3d 343 (Del. Ch. 2023)

- McDonald's stockholders brought suit alleging that the company's Chief People Officer ("CPO"):
 - breached his fiduciary <u>duty of oversight</u> by allowing a corporate culture to develop that condoned sexual harassment and misconduct; and
 - breached his fiduciary duty of loyalty by engaging personally in acts of sexual harassment.
- The Court denied the officer's motion to dismiss and rejected the argument that Delaware law does not recognize an oversight claim against corporate officers:

"This decision clarifies that corporate officers owe a duty of oversight."

- Like directors, officers owe a "context-driven" duty to:
 - (i) implement "information systems and controls," and
 - (ii) "identify red-flags and either address them or report upward."

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Scope of Officers' Duty of Oversight

"Although the CEO and Chief Compliance Officer likely will have company-wide oversight portfolios, other officers generally have a more constrained area of authority."*

Officers' Information Systems Duty

- "With a constrained area of responsibility comes a constrained version of the duty that supports an Information-Systems Claim."
- The Court provided examples:
 - The CFO "is responsible for financial oversight and for making a good faith effort to establish reasonable information systems to cover that area."
 - The CLO "is responsible for legal oversight and for making a good faith effort to establish reasonable information systems to cover that area.

Officers' Duty to Address or Report Red Flags

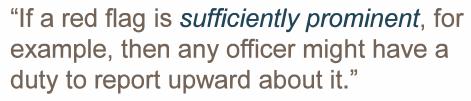
 Similarly, "officers generally only will be responsible for addressing or reporting red flags within their areas of responsibility, although one can imagine possible exceptions."

* Emphasis in quotations is added by presenter unless otherwise specified.

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McDonald's Corporation Stockholder Derivative Litigation



For example, "[a]n officer who receives credible information indicating that the corporation is **violating the law** cannot turn a blind eye and dismiss the issue as 'not in my area.'"

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Officer Red-Flags Claim

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To plead a "**red-flags claim**" that will survive a Rule 12(b)(6) motion, a plaintiff must plead facts supporting an inference that the fiduciary:

- knew of evidence of corporate misconduct; and
- consciously failed to take action in response.
- The bad faith requirement for director duty of oversight claims applies to officer claims: "This decision concludes that oversight liability for officers requires a showing of bad faith."
 - "The pled facts must support an inference that the failure to take action was sufficiently sustained, systematic, or striking to constitute action in bad faith. A claim that a fiduciary had notice of serious misconduct and simply brushed it off or otherwise failed to investigate states a claim for breach of duty."

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