

PUBLICATION

Does the Business Judgment Rule Really Exist in Georgia?

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On April 21, 2014, the Georgia Supreme Court heard oral arguments in the case of FDIC v. Loudermilk to determine whether the Business Judgment Rule really exists in Georgia. Claiming contrary decisions on the Business Judgment Rule from various courts and contradictory statutes, Judge Thrash of the Northern District of Georgia has formally asked the Supreme Court of the State to determine whether the Business Judgment Rule protects the actions of bank directors and officers in Georgia.

For years, if not decades, officers and directors of Georgia's companies have relied on the Business Judgment Rule in support of motions to dismiss allegations of ordinary negligence in connection with corporate actions that result in losses for a company. While the Court of Appeals of Georgia has approved of the Business Judgment Rule, it has not been explicitly approved by the Supreme Court.

The Business Judgment Rule is a creation of case law that gives directors and officers a presumption that, in making business decisions, the directors and officers acted in a good-faith, informed manner, and that a business action was taken in the best interest of the company. The Business Judgment Rule protects corporate directors and officers from personal liability unless it can be proved that a director acted in bad faith, showed disloyalty, engaged in self-dealing or abused his or her discretion. Georgia's lower courts regularly invoke the Business Judgment Rule as a recognition that: (1) judges and juries should not be called upon to review business decisions made in the regular course of corporate operations; and (2) businesses should have the ability to take calculated risks. The Official Code of Georgia Section 51-1-2 describes simple or ordinary negligence as "the degree of care which is exercised by ordinarily prudent persons under the same or similar circumstances."

Despite this history, the Federal Deposit Insurance Corporation (FDIC) has repeatedly claimed in court filings that directors and officers may be sued for simple negligence in Georgia. As receiver for a failed financial institution, the FDIC may sue officers, directors and other professionals who played a role in the failure of an insured institution to maximize recoveries to the Deposit Insurance Fund (DIF).

The FDIC has been extremely active in asserting its claims against officers and directors of failed financial institutions for ordinary negligence. In fact, since 2007 the FDIC has authorized over 1,000 liability suits often claiming negligent actions by officers and directors that resulted in bank failures.

The FDIC's claims against the officers and directors of a failed bank has led one judge in the Northern District of Georgia to determine that the Business Judgment Rule's existence presents an unsettled question of state law in the banking context and certified the question to the Georgia Supreme Court for decision. The question certified for decision is: "Does the Business Judgment Rule in Georgia preclude as a matter of law a claim for ordinary negligence against the officers and directors of a bank in a lawsuit brought by the FDIC as receiver for the bank?"

In the Loudermilk case, the Federal District Court for the Northern District of Georgia refused to dismiss claims of ordinary negligence against the defendant directors and officers of a failed bank. The Federal District Court in Loudermilk concluded that, absent a clear statutory reference or an explicit ruling from the Georgia Supreme Court, Georgia law does not mandate application of the Business Judgment Rule to preclude ordinary

negligence claims against bank officers and directors. Further, the Loudermilk Court provided the Supreme Court with the ability to state that, even if the Business Judgment Rule exists in Georgia, it may not be available to bank directors and officers. The Supreme Court could reason that bank directors and officers should be held to a different standard than directors and officers of other business corporations because, according to the District Court, unlike a business corporation whose stockholders bear the loss if the corporation fails, the FDIC and ultimately taxpayers bear the financial loss when a bank fails.

The Georgia Supreme Court's answer to the certified question posed in the Loudermilk case will have a significant impact on directors and officers of Georgia's banks. Beyond that, the decision could have far-reaching consequences for directors and officers of all Georgia corporate entities and determine the future standard by which all corporate actions will be reviewed.

The Georgia Supreme Court has several options available to it in deciding the case. First, it could explicitly accept the Business Judgment Rule in Georgia and side with the defendants. Second, it could rule that the Business Judgment Rule only applies to directors and officers of institutions that are not insured by a government agency like the FDIC's DIF. Alternatively, the Georgia Supreme Court could determine that the Business Judgment Rule doesn't apply in Georgia, but that result is extremely unlikely due to the policy reasons outlined above. Finally, among other options, the Court could draft a narrowly-tailored decision and leave open the question for a future date. Regardless of the outcome, if the Georgia Supreme Court directly addresses the federal certification, the decision could impact the conduct of thousands of boards of directors and officers of businesses that operate in the state.