Accountability For Flawed Corporate Culture

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We thank David Hess, Don Langevoort, participants in workshops and seminars at Goethe University, King's College London, University of Cambridge, University of Leeds, University of Sheffield, Monash University, and Bar-Ilan University for their helpful comments. Alma Katzri, Mitheran Selvendran, Omar Shalbi, Chen Sternhall and Victoria Xiong provided excellent research assistance. Shapira acknowledges generous support from the Ackerman Center for Corporate Governance. Hill thanks Monash University for providing funding for this project under a Networks of Excellence (NoE) Research Grant on the topic, 'Enhancing Corporate Accountability.'

Abstract

Flawed corporate culture has been at the root of the largest corporate debacles in recent years, such as Wells Fargo's fraudulent accounts, Volkswagen's emissions cheating, and Boeing's 737 Max crashes. In this type of case the corporation in question boasts a well-funded compliance program, a well-constituted board of directors, and a well-crafted code of ethics. Still, without an ethical corporate culture that emphasizes high integrity as much as it does high performance, all the observable markers of corporate governance matter little. There is a consensus among practitioners and academics that corporate culture matters greatly, both in creating financial value and in mitigating compliance risks. Yet there exists relatively little research on the types of legal mechanisms that can influence corporate culture. The extant legal literature focuses on addressing flawed cultures through criminal law and regulatory mandates. But public enforcers find it hard to assess a given corporate culture. As a result, such regulatory mandates too often result in corporations adopting a check-the-box "cosmetic" compliance program instead of meaningfully focusing on improving their behavior. This Article spotlights the underexplored role of corporate law in addressing flawed corporate culture. In recent years, corporate law's oversight duty doctrine has been recalibrated. That recalibration has made the doctrine adept at holding officers and directors accountable for how they shape the information flows, economic incentives, and in-group norms. To be sure, corporate law alone cannot fix corporate culture, but with the right design it can complement other legal mechanisms and incentivize officers and directors to set the right tone at the top. The Article conducts a comparative institutional analysis of different legal fields (criminal versus civil) and different legal systems (the US private litigation model versus Australia's public enforcement model and the UK market discipline model), to assess the relative strengths and weaknesses of various legal instruments to address flawed corporate culture. In the process, the Article makes the following three contributions. First, the Article highlights just how pivotal a role corporate culture plays in shaping corporate behavior. Second, the Article delineates the pros and cons of different legal tools to foster accountability for flawed corporate culture. Finally, the Article generates concrete recommendations for practitioners and policymakers. For directors, key lessons include the need to rethink board structures. For judges, key lessons include reassessing prefiling discovery doctrines, and coming up with tools to infer scienter in large organizations.

Keywords: Corporate Culture, Compliance, Corporate Governance, Corporate Law, Oversight Duties, Organizational Wrongdoing, Comparative Corporate Law, Corporate Crime, Fiduciary Duties

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ACCOUNTABILITY FOR FLAWED CORPORATE CULTURE

JENNIFER G. HILL & ROY SHAPIRA

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INTRODUCTION

The two biggest global trends in corporate governance over the past decade have been ESG and compliance. Companies these days are facing increased societal and regulatory demands.[1] In response, companies are pouring billions of dollars into compliance programs meant to prevent and detect wrongdoing by their employees.[2] Yet, in one major corporate debacle after another, companies that boasted an elaborate compliance program are caught engaging in elaborate wrongdoings and cover-ups.[3] The culprit is often flawed corporate culture. Even the best and most intricate compliance policies and value statements matter little when the unwritten norms of "how we do things around here" are unethical. Flawed corporate culture can inflict enormous harm on shareholders, communities, the environment, and society at large.

To illustrate, consider Wells Fargo's phony accounts scandal. Up to when news about the scandal broke, the banking giant enjoyed a stellar reputation for sound management.[4] It was praised as weathering the 2008 financial crisis better than its peers, its CEO was named "Banker of the Year," and the company was ranked among the top ten of the "Most Respected Companies."[5] Pertinently, while the fraudulent sales practices were raging at Wells Fargo, the company had the trappings of a great compliance system. It issued a "Vision and Values" statement that read: "We start with what the customer needs – not with what we want to sell them."[6] Its employee handbook stated that "opening multiple accounts for the purpose of increasing potential incentive compensation is considered a sales integrity violation."[7] Its ethics programs clearly instructed employees on how to spot and address conflicts of interest.[8] And, it established a whistleblower hotline to notify senior managers of violations.[9] Finally, Wells Fargo even designed the remuneration packages of

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[1] *See* Leo E. Strine, Jr., Kirby M. Smith, & Reilly S. Steel, Caremark *and ESG, Perfect Together: A Practical Approach to Implementing an Integrated, Efficient, and Effective Caremark and EESG Strategy*, 106 IOWA L. REV. 1885, 1886 (2021).
[2] Eugene Soltes, *Evaluating the Effectiveness of Corporate Compliance Programs: Establishing a Model for Prosecutors, Courts, and Firms*, 14 N.Y.U. J. L. & BUS. 965, 969 (2018) (estimating aggregate compliance costs).
[3] *See generally* Benjamin van Rooij & Melissa Rorie, *Measuring Compliance: The Challenges in Assessing and Understanding the Interaction between Law and Organizational Misconduct*, *in* MEASURING COMPLIANCE: ASSESSING CORPORATE CRIME AND MISCONDUCT PREVENTION (Benjamin van Rooij & Melissa Rorie, eds., 2022) (providing evidence for systemic failures of compliance).
[4] *See* Brian Tayan, The Wells Fargo Cross-Selling Scandal (Stan. U. Bus. Sch. Res. Paper no. 17-1, 2019), https://ssrn.com/abstract=2879102 (detailing the reputational laurels of the bank).
[5] *Id*.
[6] *See* U.S. Dept. of Justice, *Wells Fargo Agrees to Pay $3 Billion to Resolve Criminal and Civil Investigations into Sales Practices Involving the Opening of Millions of Accounts without Customer Authorization* (Feb. 21, 2020) (detailing the investigation's findings).
[7] *Id*.
[8] *Id*.
[9] *Id*.

senior managers to minimize compliance risks, such as by promising bonuses for instilling the abovementioned values and including numerous triggers for clawbacks of bonuses in those cases where bonuses were inappropriately earned.[10]

Ultimately, all these structural protections were not enough to curb wrongdoing on a mass scale, which ended up causing enormous damage to customers, employees, and the company itself. The problems that led to the opening of phony accounts were simply too systemic and intractable for these structural protections to prevent.[11] In other words, the problems stemmed from flawed corporate culture. Similar dynamics appear in virtually every major corporate debacle these days, from Walmart's involvement in the opioid crisis, to Boeing's safety woes, to Volkswagen's emissions test cheating scandal.[12] Without a strong corporate culture that translates proclaimed values into clear prescriptions on how things are done on the ground, even well-budgeted compliance programs and grandiose value statements fail to curb corporate wrongdoing.[13]

Once one recognizes that corporate culture matters greatly, the key question becomes how to address problems with corporate culture. Thus far lawyers have focused almost exclusively on *criminal* law as a tool to regulate corporate culture. For example, the Department of Justice weighs the corporation's "culture of compliance" when determining leniency.[14] However, public enforcers find it hard to assess a given corporate culture.[15] As a result, such regulatory mandates often result in corporations adopting a check-the-box "cosmetic" compliance program instead of meaningfully focusing on improving their behavior.[16]

This Article offers a more comprehensive assessment of the different tools to assess corporate culture and to deliver accountability for flawed culture. In particular, the Article highlights the understudied role of corporate law. Corporate law imposes oversight duties on directors and officers. Public shareholders can therefore sue directors and officers derivatively (on behalf of the corporation) for not doing enough to monitor, prevent, and remedy lawbreaking by others in the organization. On paper, the oversight duty doctrine is a natural candidate for holding directors and officers accountable for flawed

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[10] *Id*.
[11] Shaev v. Baker, 2017 U.S. Dist. LEXIS 68523, *39.
[12] Veronica Root Martinez, *More Meaningful Ethics*, U. CHI. L. REV. ONLINE (2020), https://lawreview.uchicago.edu/online-archive/more-meaningful-ethics [Hereinafter Root Martinez, *More Meaningful Ethics*] (noting that these scandals invoke "fundamental concerns about the strength of each firm's ethical culture").
[13] *See, e.g.*, Mihaela Constantinescu, *Organisational Integrity and Responsibility*, *in* RESEARCH HANDBOOK ON ORGANISATIONAL INTEGRITY 394, 407 (2024) (using the GM ignition switch scandal to illustrate how an unethical culture can undermine even the best written procedures: there, GM's own safety requirements for the ignition switch were not respected in practice).
[14] Section II.B *infra*.
[15] *Id*.
[16] *Id*.

culture. Historically, however, the doctrine has been irrelevant in practice.[17] The standard was set high, and derivative actions against directors for failure of oversight were summarily dismissed.[18] That situation has changed over the past couple of years.[19] In a string of recent cases corporate law courts have shifted their approach to oversight duties. Courts have been willing to scrutinize directors' oversight efforts, and to provide public shareholders with access to internal company documents to investigate potential failures of oversight.[20]

The evolving recalibration of oversight duties carries the potential to mitigate the problem of flawed corporate culture. To advance a failure-of-oversight claim, shareholders must prove bad faith on the part of the company's directors.[21] The courts have delineated three scenarios that give rise to an inference of bad faith, namely, that directors either (1) failed to implement systems that monitor and report on compliance with central risks (an "Information System" claim), or (2) ignored clear warnings of pervasive lawbreaking (a "Red Flags" claim), or (3) knowingly approved a business strategy that prioritizes profits over compliance (a "Business Plan" claim). This Article shows that each one of these scenarios implicates the involvement of directors in their company's culture and enhances directors' accountability for flawed culture. To illustrate, let us consider one example from each scenario.

An information system claim can effectively mitigate the problem of *willful blindness*. Corporate directors have strong incentives to remain ignorant about decisions that prioritize profits over everything else.[22] Prioritizing profits is good for directors who receive substantial stock-based compensation. And remaining ignorant about how profits were obtained is good for directors' ability to maintain plausible deniability and escape accountability in criminal law.[23] The new mode of oversight duty litigation counters these dynamics by emphasizing *culpable ignorance* (faulting directors for what they should have known) and *proper documentation* (incentivizing more upward flows of information). To illustrate, when Boeing's directors claimed that there were no indications that they were warned in real time of the Max 737 problems, the court held that the lack of such indications can itself serve as an indication that the directors breached their oversight duties.[24] If you are a director of an airplane

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17 *See generally* Marc T. Moore, *Redressing Risk Oversight Failure in UK and US Listed Companies: Lessons from the RBS and Citigroup Litigation*, 18 EUR. BUS. ORG. L. REV. 733 (2017) (explaining why past iterations of the oversight duty doctrine, whether in the US or in the UK, failed to generate accountability for pervasive corporate misconduct).

18 *See* Elizabeth Pollman, *Corporate Oversight and Disobedience*, 72 VAND. L. REV. 2013 (2019) (providing a comprehensive overview of *Caremark* claims up until 2019).

19 Roy Shapira, *Max Oversight Duties: How* Boeing *Signifies a Shift in Corporate Law*, 48 J. CORP. L. 119, 121 (2022) [hereinafter Shapira, *Max Oversight Duties*].

20 *Id*.

21 Stone v. Ritter, 911 A.2d 362, 370 (Del. 2006).

22 *See* Samuel W. Buell, *The Responsibility Gap in Corporate Crime*, 12 CRIM. L. & PHIL. 471, 490 (2018) [Hereinafter Buell, *The Responsibility Gap*].

23 *Id*.

24 *In re* Boeing Co. Deriv. Litig., 2021 WL 4059934 (Del. Ch. Sep. 7, 2021).

manufacturing company, and there is no record of you discussing potential safety issues of a new airplane model, it probably means that you were not trying hard enough to oversee compliance (or that you concealed evidence of damning information).[25]

A red flags claim can effectively mitigate the problem of *recidivism*. Recidivism is one of the clearest syndromes of flawed corporate culture, yet public enforcers are deficient at targeting it. This is because regulatory enforcement is disparate and uncoordinated, with each enforcer having a narrow, circumscribed authority. Further, public enforcers are incentivized to allocate their scarce resources to working new cases rather than policing old settlements.[26] The revamped oversight duty doctrine treats pervasive past problems as "red flags" that put the directors on notice. Consequently, directors who wish to avoid personal liability must ensure that the company fixes defects in its culture of compliance over time.

A business plan claim can effectively mitigate the problem of *cosmetic compliance*. Directors and officers of giant corporations are rarely cynical or imprudent enough to explicitly order employees to prioritize profits by breaking the law and harming others. But recent court decisions have drawn inferences based on the incentive plans that the higher-ups install throughout the corporation. To illustrate, consider the 2023 case of Walmart's involvement in the opioid epidemic. Walmart's directors and officers claimed in their defense that the company had in place a compliance program meant to detect and prevent unauthorized distribution of opioids. Yet the court looked beyond the mere existence of a program, and ultimately ruled against the defendants based on the incentives in place: the company provided supercharged bonuses for pharmacists who attracted opioid customers, while significantly underbudgeting compliance monitoring efforts.[27]

Across all these claims, corporate law litigation serves to focus attention on the role of those at the top of the corporate hierarchy. Directors and officers shape corporate culture by setting economic incentives, establishing information flows, and supplying personal examples. Indeed, researchers have long recognized that the "tone at the top" is crucial for creating and maintaining ethical corporate culture.[28] Yet public enforcers rarely hold top individuals in giant corporations accountable, if only because the fragmentation of knowledge inside such corporations makes it harder to prove culpability at the top.[29]

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[25] *Id*. at *86–87.
[26] Andrew K. Jennings, *Follow-up Enforcement*, 70 DUKE L.J. 1569, 1574 (2021).
[27] Ontario Provincial Council of Carpenters' Pension Trust. v. Walton, 2003 Del. Ch. LEXIS 92 (Del. Ch. Apr. 26, 2023) ("Walmart II"), at *97–98, 122.
[28] *See, e.g.*, Lynn S. Paine, *Managing for Organizational Integrity*, HARV. BUS. REV. (Mar.–Apr. 1994), at 106 ("Ethics has everything to do with management"); D. Daniel Sokol, *Policing the Firm*, 89 NOTRE DAME L. REV. 785, 814 (2013); Melvin A. Eisenberg, *Corporate Law and Social Norms*, 99 COLUM. L. REV. 1253, 1270 (1999); Elise Bernlohr Maizel, *Illegal Corporate Cultures*, DUKE L.J. (forthcoming), https://ssrn.com/abstract=5134979, manuscript at 11.
[29] Roy Shapira, *The Challenge of Holding Big Business Accountable*, 44 CARDOZO L. REV. 203, 232 (2022).

Instead, public enforcers typically opt to focus their enforcement at the entity level and settle early for what large corporations often write off as the small costs of doing business.[30] Derivative suits in corporate law, by contrast, provide superstrong incentives for private actors (shareholders and their attorneys) to extract damning information about what exactly top individuals knew and when they knew it. In the *Boeing* case, for example, the plaintiff attorneys scoured over 44,000 internal documents related to how directors and officers handled air safety issues.[31] For their success in holding Boeing's directors accountable, the attorneys received an award of almost $40 million (out of a $240 million settlement).[32]

To be sure, it is far from certain that corporate law will reach its abovementioned potential to address flawed cultures. The oversight duties doctrine suffers from at least three limitations in that regard. First, the standard for proving breach remains high: judges try to avoid hindsight bias and err on the side of underenforcement. Second, the "enforcers" in these cases are shareholders and their plaintiff attorneys, whose narrow incentives do not always align with social welfare (under certain conditions, shareholders can benefit from unethical corporate culture). Finally, the "targets" in these cases are corporate directors, who may be too removed from the ground to affect real change in corporate culture.

This Article therefore does not proclaim that the oversight duty doctrine is a panacea for flawed corporate culture. Our aim here is more modest, namely, to delineate the circumstances under which corporate law can (or cannot) supply the defects of other legal mechanisms for promoting ethical corporate behavior. Indeed, recent changes to Delaware corporate law may end up rendering US-style private litigation less suitable for generating accountability for flawed culture, because of how these changes limit shareholders' ability to inspect internal company communications.

To further our understanding of what legal mechanisms work best under certain conditions, the Article compares not just different liability modes (criminal versus civil) but also different legal systems. For example, while civil liability in the US is based on an aggressive private litigation mode, civil liability in Australia for corporate behavior emanating from flawed culture is predominantly based on a public enforcement mode, and in the UK accountability for flawed culture comes mainly from market discipline. The comparative analysis helps us identify both the promise and the perils of addressing flawed corporate culture via corporate law, and to generate concrete policy implications.

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[30] *Id*.
[31] Boeing, 2021 WL 4059934, at n.1.
[32] Kevin LeCroix, *Largest Derivative Lawsuit Settlement*, D&O DIARY, https://www.dandodiary.com/2014/12/articles/shareholders-derivative-litigation/largest-derivativelawsuit-settlements/.

A few words on terminology and methodology are in order at the outset. We use "corporate culture" here to denote the implicit, unwritten norms that create expectations for how people in the corporation will behave. A vast literature documents just how pivotal a role culture plays in shaping corporate behavior. But culture can be studied from various perspectives, such as how it contributes to innovation or to teamwork.[33] We focus here on the integrity dimension of corporate culture. In that sense, we use "corporate culture" to denote the shared beliefs inside a corporation about how important legal compliances and ethics are relative to other pressures and goals. Unless noted otherwise, references to "corporate law" are to Delaware corporate law. Most large corporations are governed by Delaware law, and other states tend to follow its lead.[34]

"Accountability" is another fuzzy concept that we rely on here. It is normally used as shorthand for various types of efforts to address problems with the exercise of power. We use it here mostly in the sense of generating answerability for past misconduct to deter future misconduct. In other words, when we talk about accountability for flawed culture, we ultimately have in mind pathways for improving corporate behavior. If directors are more answerable to flawed culture, they will change the way that they shape their company's culture, or so the thinking goes. We are thus concerned not just with how to deliver accountability, but also with how accountability delivers a change in corporate behavior.

The reason legal scholars have understudied corporate culture and corporate law's role in promoting ethical culture is not because they find these issues unimportant, but rather because they find these issues to be lacking in data and hard to capture in neat models.[35] To overcome this tractability problem, we triangulate between different methods: not just traditional doctrinal analysis, but also rich case studies, and content analysis of media coverage and law firm memos. To illustrate, we searched for every mention of "culture" in oversight

[33] Luigi Guiso, Paola Sapienza, & Luigi Zingales, *The Value of Corporate Culture*, 117 J. FIN. ECON. 60, 64 (2015).

[34] *See* Charlotte Morabito, *Here's Why More Than 60% Of Fortune 500 Companies Are Incorporated in Delaware*, CNBC (Mar. 13, 2023), https://www.cnbc.com/2023/03/13/why-more-than-60percent-of-fortune-500-companies-incorporated-in-delaware.html (on how most large companies incorporate in Delaware); Kevin LaCroix, *Cardinal Health Opioid-Related Derivative Suit Settled for $124 million*, D&O DIARY (May 30, 2022), https://www.dandodiary.com/2022/05/articles/shareholders-derivative-litigation/cardinal-health-opioid-related-derivative-suit-settled-for-124-million/ (an example of out-of-Delaware developments that mimic the trends described here). As of this writing, some practitioners and scholars are questioning whether Delaware's incorporation position will be secured going forward, especially in the light of well-publicized cases such as over Elon Musk's Tesla pay package. Zohar Goshen & Tomer S. Stein, Leaving Delaware? The Essential Role of Specialized Corporate Court (ECGI working p. 837/2025), https://ssrn.com/abstract=5200668.

[35] *Cf.* David Hess, *Ethical Infrastructure and Evidence-Based Corporate Compliance and Ethics Programs: Policy Implications from the Empirical Evidence*, 12 N.Y.U. J. L. & BUS. 317, 368 (2016) (explaining that although many regulators and scholars "have recognized the importance of a corporation's culture for controlling unethical behavior," there continues to be "a wide-spread lack of understanding" of how culture affects compliance).

duty cases and corporate governance blog, and analyzed how the media and legal advisers to corporate boards covered those judicial opinions and regulatory guidelines that mention "corporate culture."[36] The idea was to provide a comprehensive assessment of how corporate directors and their legal advisors perceive the role of corporate law in promoting ethical corporate culture.

The Article proceeds in four parts. Part I explains what corporate culture is and why it matters. The Part uses case studies to illustrate how unethical corporate culture can undermine well-intentioned and well-constituted corporate governance structures, thereby creating grave consequences for the company in question and for society at large. Part II canvasses the well-studied legal mechanisms to regulate culture, with an emphasis on criminal enforcement and its limits. Part III explores the understudied role that corporate law can play in shaping corporate culture, with an emphasis on recent developments in oversight duties. The Part shows how corporate law litigation affects not just the expected legal sanction but also the expected nonlegal (reputational) sanction for directors and officers. Part IV highlights the pros and cons of other methods of holding individuals accountable for flawed culture, such as public enforcement or soft law, building on the accumulated experience in other legal systems. Part V derives concrete implications for practitioners and policymakers. A short conclusion then clarifies the Article's original contributions by juxtaposing them with the extant literature and acknowledges the Article's limitations.

I. BACKGROUND: CULTURE MATTERS

What are the main forces that shape behavior within corporations? Corporate legal scholars have traditionally approached this question by focusing on "hard" factors, such as the structure of executive pay, the number of independent directors, or the separation of chairperson and CEO.[37] But decades of empirical studies have generally failed to find a reliable impact of such salient and measurable factors on corporate performance.[38] Instead, studies suggest that often the harder-to-measure "soft" factors are the ones making the most impact on corporate behavior.[39] No concept captures these soft factors better than

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[36] We searched legal databases ("Lexis" and "Westlaw") for every case that cites the oversight duty precent of *Caremark* and mentions "culture." Practically speaking, this means that every oversight duty case from 1996 (when *Caremark* came out) onwards that invokes the concept of corporate culture is part of our analysis. And we searched Harvard Corporate Governance Forum for every blog post that mentions "culture." As *infra* Section I.A illustrates, we also searched for every mention of "culture" in different countries' corporate governance codes.

[37] *See* Roy Shapira & Yaron Nili, *Specialist Directors*, 41 YALE J. REGUL. 652, 664 (2024).

[38] *See, e.g.*, David F. Larcker & Brian Tayan, *Governance Gone Wild: Epic Misbehavior at Uber Technologies*, STAN. U. CLOSER LOOK SERIES (2017).

[39] Constantinescu, *supra* note 13, at 407 (summarizing the body of empirical literature thusly: "it is more likely that individuals follow the informal organizational culture or climate rather than the formal structure"); Kelly D. Martin & John B. Cullen, *Continuities and Extensions of Ethical Climate Theory: A*

corporate culture, which denotes the unwritten norms of "how we do things around here."[40] Culture shapes the preferences and behaviors of individuals inside the corporation.[41] Two companies can have the same number of independent directors or the same structure of executive pay, yet one company will behave very differently than the other because of different cultures. Scholars in other fields, such as organization science and finance, have increasingly found ways to study the hard-to-quantify aspects of corporate culture.[42] It is time for more legal scholars to enter the fray: without studying corporate culture, corporate legal scholars would not be able to effectively describe corporate misbehavior and prescribe ways to address it.

This Part provides the backdrop for our discussion of legal tools to address corporate culture. Section A delineates what corporate culture is, just how much it matters, and why it matters. Section B delves more specifically into our subject matter, namely, what are the typical causes, symptoms, and consequences of a deeply flawed corporate culture. Section C spotlights the role of directors and officers in allowing a flawed culture to develop.

A. *How Corporate Culture Matters*

Corporate culture is a slippery concept that does not lend itself to a standard definition.[43] For our purposes, we can define culture broadly as the "shared set of values or assumptions that reflects the underlying mindset" of the company.[44] Culture, in that sense, denotes "the way that things are done around here," or "the corporation's DNA."[45]

Meta-Analytic Review, 69 J. BUS ETHICS, 175 (2006) (presenting a meta-analysis of relevant literature); Muel Kaptein, *Understanding Unethical Behavior by Unraveling Ethical Culture*, 64 HUM. REL.'S, 843 (2011) (same); Hess, *supra* note 35, at 350 ("With respect to influencing behavior, the more deeply embedded system is the more influential system. Thus, the formal system is weaker than the informal system").

[40] *See* Steve W. Klemash et al., *Five Ways to Enhance Board Oversight of Culture,* HARV. L. SCH. F. ON CORP. GOVERNANCE (Sep. 18, 2024), https://corpgov.law.harvard.edu/.

[41] *See generally* Geoffrey M. Hodgson, *Corporate Culture and the Nature of the Firm*, *in* TRANSACTION COSTS ECONOMICS AND BEYOND 249 (John Groenewegen ed. 1996); Ernst Fehr, *Behavioral Foundations of Corporate Culture,* 7 PUB. PAPER UBS INT'L CENT. ECON. SOC'Y (2018).

[42] *See, e.g.*, Donald C. Langevoort, *The Effects of Shareholder Primacy, Publicness, and "Privateness" on Corporate Culture*, 43 SEATTLE U. L. REV. 377, 377 (2020) (noting the explosion of academic interest in corporate culture) [hereinafter Langevoort, *The Effects of Shareholder Primacy*].

[43] *See, e.g.*, Dan Awry et al., *Between Law and Markets: Is There a Role for Culture and Ethics in Financial Regulation*, 38 DEL. J. CORP. L. 191, 205 (2013); Justin W. Schulz, *Tapping the Best That is Within: Why Corporate Culture Matters*, 42 MGMT. Q. 29, 32 (2001).

[44] *See, e.g.*, Gary B. Gorton et al., *Corporate Culture*, 14 ANN. REV. FIN. ECON. 535 (2022 (providing an excellent survey); Benjamin E. Hermalin, Economics and Corporate Culture (working paper, 1999), https://ssrn.com/abstract=162549 (same); John Price, *Culture and Conduct*, Austl. Inst. Co. Dir. (Sep. 1, 2015), https://www.aicd.com.au/organisational-culture/business-ethics/issues/culture-and-conduct.html (a Chairman of the Australian's corporate regulator, espousing a similar definition). *See also* John M. Conley et al., *Can Soft Regulation Prevent Financial Crises?: The Dutch Central Bank's Supervision of Behavior and Culture*, 51 CORNELL INT'L L.J. 773, 787–88 (2019) (elaborating on the origins of said definition).

[45] *See, e.g.*, Barak Orbach, *D&O Liability for Antitrust Violations*, 59 SANTA CLARA L. REV. 527, 535 (2020); David Roth, *Creating a Great Corporate Culture – Your Company's Foundational DNA*, FORBES (May 29,

While there is not a consensus on how to define it, there is a consensus among practitioners, scholars, and regulators that corporate culture matters greatly.[46] Practitioners were the first to recognize the importance of corporate culture, and to this day managers and investors consistently rank corporate culture as the number one driver of corporate value,[47] as well as a major risk factor.[48] Scholars were historically deterred by the "fuzzy" nature of culture but have increasingly devised clever research designs to produce large-N statistical evidence on how much culture matters. For example, one study linked how employees view the integrity of senior management with the company's financial performance: when upper management is viewed as committed to a culture of integrity, the company performs better.[49] Another study showed that companies with a strong culture weathered the Covid-19 crisis better than their peers.[50]

Pertinently for our purposes, corporate regulators around the world have recently joined practitioners and scholars in acknowledging the importance of corporate culture.[51] To illustrate, one need simply look at the evolution of national corporate governance codes over time.[52] In 2019, Australia's code introduced a provision stating that public companies should "instil a culture of acting lawfully, ethically, and responsibly."[53] In 2018, the British code unambiguously stated that corporate directors must establish a culture of integrity.[54] The 2016 Dutch code explicitly outlined the roles of upper

2012), https://www.forbes.com/sites/davidroth/2012/05/29/creating-a-great-culture-your-companys-foundational-dna/; Mark Bonchek, *How to Discover Your Company's DNA*, HARV. BUS. REV., (Dec. 12, 2016); Carey Oven et al., *Corporate Culture Risk and the Board*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Apr. 20, 2018), https://corpgov.law.harvard.edu/2018/04/20/corporate-culture-risk-and-the-board/.

[46] *See, e.g.*, John Wilcox & Morrow Sodali, *Corporate Purpose and Culture*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Feb. 21, 2020), https://corpgov.law.harvard.edu/2020/02/21/corporate-purpose-and-culture/ (calling culture "one of the most important and one of the most difficult to explain" factors that shape corporate behavior).

[47] *See, e.g.*, John R. Graham et al., *Corporate Culture: Evidence from the Field*, 146 J. FIN. ECON. 552 (2022) (presenting evidence on how executives perceive corporate culture).

[48] *See, e.g.*, *Survey of Institutional Investors Reveals Urgent Need,* EDELMAN (Nov. 29, 2018), https://www.edelman.com/news-awards/survey-institutional-investors-reveals-urgent-need-public-companies-societal-issues-build-trust.

[49] Guiso et al., *supra* note 33.

[50] Kai Li et al., *The Role of Corporate Culture in Bad Times: Evidence from the COVID-19 Pandemic*, 56 J. FIN. & QUANTITATIVE ANALYSIS 2545 (2021).

[51] Donald C. Langevoort, *Cultures of Compliance*, 54 AM. CRIM. L. REV. 933, 943 (2017) [hereinafter Langevoort, *Cultures of Compliance*] (noting that culture has "expanded from an academic obsession to a regulatory one"); Emily Glazer & Christina Rexrode, *As Regulators Focus on Culture, Wall Street Struggles to Define It*, WALL ST. J. (Feb. 1, 2015), https://www.wsj.com/articles/as-regulators-focus-on-culture-wall-street-struggles-to-define-it-1422838659.

[52] *See generally* Marie-Fleur Lobrij et al., *What National Governance Codes Say about Corporate Culture*, 20 CORP. GOVERNANCE 903 (2020); Jennifer G. Hill, *Shifting Contours of Directors' Fiduciary Duties and Norms in Comparative Corporate Governance*, 5 U. C. IRVINE J. INT'L TRANSNAT'L & COMP. L. 163, 165 (2020).

[53] ASX Corporate Governance Council, *Corporate Governance Principles and Recommendations* (Feb. 2019), at Principle 3.

[54] FINANCIAL REPORTING COUNCIL, THE UK CORPORATE GOVERNANCE CODE, 4 (2018), at Principal B.

management and the supervisory board in creating and maintaining a healthy corporate culture.[55] Other examples abound.[56]

All these academic studies, practitioner-based surveys, and regulatory guidelines agree not just that corporate culture matters, but also on *how* and *why* it matters. A strong corporate culture can align values and behaviors, and facilitate higher employee morale, better employee engagement, more innovation, and stronger performance. A weak corporate culture, by contrast, can create a gap between professed values and actual behavior, and lead to low retention of talent and weak safety records. In other words, there is by now a consensus that creating and maintaining a healthy corporate culture is key for both value creation and risk mitigation.[57]

This Article focuses more on the latter: not on how a healthy culture can create value, but rather on how an unhealthy culture can create significant risks for both the corporation and society at large. Let us therefore delve into the causes, symptoms, and consequences of a deeply flawed corporate culture.

B. *The Causes and Consequences of Flawed Corporate Culture*

To understand how to address deeply flawed corporate culture, one first needs to understand what deeply flawed culture looks like. It is easy to attribute every corporate debacle to a flawed culture in hindsight. But in reality, many debacles are the result of less deep-seated and more mundane factors.[58]

Take for example large-scale debacles that are caused by specific technical failures, such as NASA's Challenger disaster.[59] Postmortem analysis revealed that defective O-ring seals and a series of unfortunate decisions taken under pressure led to the disaster, rather than an inherently flawed culture at NASA.[60] Similarly, the catastrophic Exxon Valdez oil spill (where the grounding of an oil tanker led to massive pollution in Alaska) was primarily attributed to one-off human errors, such as the tanker captain's decision to leave the bridge and the failure of the crew to properly navigate the vessel.[61] To be sure, one can argue that had the company in question installed better

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[55] CORPORATE GOVERNANCE CODE MONITORING COMMITTEE, THE DUTCH CORPORATE GOVERNANCE CODE, 25–26 (2016), at Principal 2.5.

[56] *See, e.g.*, Klemash et al., *supra* note 40 (noting how the Japanese corporate governance code similarly emphasizes the importance of defining, measuring, and engaging in oversight of culture).

[57] *See* Oven et al., *supra* note 45; Ning Chiu et al., *State Street and Corporate Culture Engagement*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Feb. 4, 2019), https://corpgov.law.harvard.edu/2019/02/04/state-street-and-corporate-culture-engagement/ (a leading institutional investor advising corporate directors to focus on corporate culture as a key value driver)

[58] *See* Donald C. Langevoort, *Opening the Black Box of 'Corporate Culture' in Law and Economics*, 162 J. INSTITUTIONAL & THEORETICAL ECON. 80, 82 (2006)

[59] WILLIAM P. ROGERS, REPORT OF THE PRESIDENTIAL COMMISSION ON THE SPACE SHUTTLE CHALLENGER ACCIDENT 40, 73 (1986).

[60] *Id*. at 40–70. *See also The Shuttle Findings: A Long Series of Failures; Key Portions of Commission Report on Challenger Accident,* N. Y. TIMES, Jun. 10, 1986, at C10 (for a concise explanation of the causes).

[61] *See* N.T.S.B., No. Mar-90/04, MARINE ACCIDENT REPORT: GROUNDING OF THE U.S. TANKSHIP EXXON VALDEZ 122–26 (1990).

management practices or better safety protocols the disaster would not have occurred.[62] Yet such an argument does not really advance our understanding of how to address corporate misbehavior. After all, even companies with healthy corporate culture can suffer from operational failures that cause massive harms; trying to prevent such harms by imposing liability for flawed corporate culture may even be counterproductive.

At the risk of oversimplifying, let us offer several rules of thumb to decide when it makes sense to address a problem by focusing on corporate culture. In one typical scenario, the company in question almost never violates rules. When misconduct is a one-off isolated event, there is little purchase in speaking about flawed culture. In another typical scenario, the company's entire business model is predicated on violating rules, and corporate misconduct is the norm. Take for example online black markets or offshore tax havens and shell companies. In this scenario as well, there is little to be gained from speaking about flawed culture. After all, the entire business model and "hard" incentives in such companies are structured to facilitate law evasion. Accordingly, it makes more sense to discuss straightforward tools such as straight bans or asset seizures or criminal prosecutions of the directly involved individuals, rather than seeking accountability for flawed culture.

The typical scenario where it makes sense to focus on flawed culture is when the company in question has many legitimate business activities and boasts a well-funded compliance program, yet is somehow still a perennial recidivist. In such cases, discussion of flawed culture becomes productive, since there is evidently something about the informal norms that undermine the impressive formal policies and programs. To identify when a given case fits into that category, one can examine three factors that keep surfacing in postmortem analyses of large corporate debacles.

The first and most obvious sign of flawed culture is the *pervasiveness* of misconduct.[63] When news about corporate misconduct surfaces, companies' spokespersons usually try to attribute the problem to a "few bad apples."[64] Closer inspection, however, may reveal that the problem is more of the "rotting barrel" type, in which case there is reason to suspect that the corporate culture

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[62] *See, e.g.*, LaRue Tone Hosmer, *Lessons from the Wreck of the Exxon Valdez*, BUS. ETHICS. Q. 109, 115 (1998).
[63] *See* Hess, *supra* note 35, at 330 (noting that the United States' Attorney's Manual encourages prosecutors to look at the pervasiveness of misconduct as an indication of unethical culture).
[64] *See, e.g.*, Lucinda Shen, *Former Wells Fargo Employees to CEO John Stumpf: It's Not Our Fault*, FORTUNE (Sep. 19, 2016) (describing the Wells Fargo phony accounts scandal) https://fortune.com/2016/09/19/former-wells-fargo-employees-to-ceo-john-stumpf-its-not-our-fault/; DE NEDERLANSCHE BANK, SUPERVISION OF BEHAVIOUR AND CULTURE: FOUNDATIONS PRACTICE AND FUTURE DEVELOPMENTS 27–28 (2015) (describing the 2013 LIBOR scandal, by a bank that was involved in illegally fixing the London Interbank Offered Rate interest rate); Luciana Magalhaes & Rogerio Jelmayer, *Former Petrobas CEO Weighs in on Corruption Probe*, WALL ST. J., Feb. 11, 2015, at B3 (describing systemic fraud at Brazilian oil giant Petrobas).

is flawed.[65] Wells Fargo is a case in point. Management initially blamed the phony account scandal on a few overzealous low-level employees.[66] But investigations revealed that the company fired more than 5,300 employees in real time (2011–2016) for creating unauthorized accounts, including many whistleblowers who tried to alert management to the problems.[67] Eventually, one of Wells Fargo's Chief Operating Committee members admitted that the company had a deep-seated problem of not being able "to recognize right from wrong."[68] In such scenarios, it makes sense to explore what the unwritten norms in the company were, why these unwritten norms took hold, and who allowed them to go unchecked.

A second recurring theme in postmortem analyses of large corporate debacles is *perverse economic incentives*.[69] At the bottom of the corporate hierarchy, one often finds overly aggressive sales targets.[70] To revisit the Wells Fargo example, bank tellers who earned an average hourly wage of $12.40 could not afford to lose their job if they failed to meet aggressive sales targets, and so the tellers ignored ethical considerations.[71] At the top of the corporate hierarchy, one often finds performance-based pay packages that are too short-term oriented.[72] When those at the top stand to earn a lot to from short-term performance indicators, they may underinvest in long-term ethics policies and monitoring systems.[73] In Volkswagen's emissions scandal, for example, the

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[65] *See generally* Susan S. Silbey, *Rotten Apples or a Rotting Barrel: How Not to Understand the Current Financial Crisis*, XXI MIT FAC. NEWSL (2009) https://web.mit.edu/fnl/volume/215/silbey.html (offering the distinction).

[66] Shen, *supra* note 64.

[67] *See* Renae Merle, *Wells Fargo Fired 5,300 Workers for Improper Sales Push. The Executive in Charge is Retiring with $125 Million*, WASH. POST (Sep. 13, 2016), https://www.washingtonpost.com/news/wonk/wp/2016/09/13/wells-fargo-fired-5300-workers-for-illegal-sales-push-executive-in-charge-retiring-with-125-million/; Stacy Cowley, *Wells Fargo Whistle-Blower Wins $5.4 Million and His Job Back*, N.Y. Times (Apr. 3, 2017).

[68] *Notice of Charges for Orders of Prohibition and Orders to Cease and Desist and Notice of Assessment of a Civil Money Penalty*, OCC notice N20-001 ¶ 62c, at 9 (Jan. 23, 2020).

[69] *See* Hess, *supra* note 35, at 330 (noting that the United States' Attorney's Manual encourages prosecutors to look at history of past misconduct as an indication for unethical culture).

[70] Root Martinez, *More Meaningful Ethics*, *supra* note 12 (citing research on how aggressive sales quotas lead to unethical conduct).

[71] *See Wells Fargo Agrees to Pay $3 Billion to Resolve Criminal and Civil Investigations into Sales Practices Involving the Opening of Millions of Accounts Without Customer Authorization* OFF. PUB. AFF.: PRESS RELEASE (Feb. 21, 2020), https://www.justice.gov/opa/pr/wells-fargo-agrees-pay-3-billion-resolve-criminal-and-civil-investigations-sales-practices (describing how "onerous sales goals and accompanying management pressure led thousands of its employees to engage in unlawful conduct"); Shen, *supra* note 64. *See also* Jennifer Hill, *What Do Colonialism and Pizza Delivery Policies Have to Do with the Wells Fargo Scandal*?, OXFORD BUS. L. BLOG (Nov. 2, 2016), https://blogs.law.ox.ac.uk/business-law-blog/blog/2016/11/what-do-colonialism-and-pizza-delivery-policies-have-do-wells-fargo.

[72] *See* Lucian A. Bebchuk & Jesse M. Fried, *Pay without Performance: Overview of the Issues*, 20 ACAD. MGMT. PERSP. 5, 21 (2006).

[73] *See* Jennifer Arlen & Marcel Kahan, *Corporate Governance Regulation through Nonprosecution*, 84 U. CHI. L. REV. 323, 355–58 (2017); John Armour et al., *Taking Compliance Seriously*, 37 YALE J. ON REGUL. 1, 5 (2020).

CEO at the time had supercharged financial incentives tied to growth and was at the final year of his tenure.[74]

There is a broader point at play here about the main difference between the culture of business entities and the culture of other types of groups. A business entity itself "wants" to shape individual behavior in ways that increase the entity's profits.[75] The entity does that by providing individuals with supercharged economic incentives (such as stock options), which in turn shape the entity's culture.[76] To be sure, incentives could help bolster a healthy corporate culture, such as when employees' bonuses are linked to safety performance metrics, or when executive remuneration packages are contingent on achieving concrete environmental targets.[77] But incentives can also fuel an unethical culture that harms shareholders (when incentives are short-term oriented and shareholders are long-term oriented) and society at large (when the incentives push insiders to externalize costs on others).[78]

The third overarching theme in postmortem analyses of large corporate debacles is the glaring gap between stated values and on-the-ground norms.[79] At the same time that the fraudulent sales practices were raging, Wells Fargo issued a "Vision and Values" statement that read: "We start with what the customer needs – not with what we want to sell them."[80] To generalize, the point is that mere proclamations of values do not suffice to improve behavior in an environment with supercharged economic incentives. For virtuous statements to matter they must be married to the right tone at the top and the right incentives at the bottom.[81]

[74] John Armour, *Volkswagen's Emissions Scandal: Lessons for Corporate Governance? (Part I)*, OXFORD BUS. L. BLOG (May 17, 2016), https://blogs.law.ox.ac.uk/business-law-blog/blog/2016/05/volkswagen%E2%80%99s-emissions-scandal-lessons-corporate-governance-part-1; John Armour, *Volkswagen's Emissions Scandal: Lessons for Corporate Governance? (Part 2)*, OXFORD BUS. L. BLOG (May 18, 2016), https://blogs.law.ox.ac.uk/business-law-blog/blog/2016/05/volkswagen%E2%80%99s-emissions-scandal-lessons-corporate-governance-part-2.

[75] Rafael Rob & Peter Zemsky, *Social Capital, Corporate Culture, and Incentive Intensity*, 33 RAND J. ECON. 243, 249 (2002). For a criticism of this "functional" approach to corporate culture see Luigi Guiso et al., Embedded Culture as a Source of Comparative Advantage (NBER working p. no. 33268, 2024), https://www.nber.org/papers/w33268.

[76] *Id*.

[77] *See, e.g.*, Anat Keller & Andreas Kokkinis, *The Senior Managers and Certification Regime in Financial Firms: An Organisational Culture Analysis*, 22 J. CORP. L. STUD. 299, 312 (2022) (noting that the right remuneration design can bolster a healthy corporate culture). *But see* Adam B. Badawi & Robert P. Bartlett, ESG Overperformance? Assessing the Use of ESG Targets in Executive Compensation Plans (Stan. L. & Econ. Olin Working Paper n. 592, 2024), https://ssrn.com/abstract=4941016 (showing evidence suggestive of the room for manipulation in ESG-based pay).

[78] *See, e.g.*, *In re* Gen. Motors Co. Derivative Litig, 2015 WL 3958724, at 1–2 (Del. Ch. Jun. 26, 2015).

[79] *See, e.g.*, Denise Lee Yohn, *Company Culture is Everyone's Responsibility*, HARV. BUS. REV. (Feb. 8, 2021), https://hbr.org/2021/02/company-culture-is-everyones-responsibility ("At many organizations there is a gap between the existing culture and the 'desired' culture"); Graham et al., *supra* note 47.

[80] *Supra* note 71 and the accompanying text.

[81] *See* Fehr, *supra* note 41 ("the mere proclamation of abstract values […] does not suffice. Values need to be translated into clear and simple behavioral prescriptions that are integrated into everyday behaviors that are encouraged and enforced by both management and the employees themselves"); Arthur H. Kohn et al., *With the Benefit of Hindsight: The Wells Fargo Sales Practices Investigation Report,* HARV. L. SCH. F. ON

These three recurring themes teach us important lessons not just about the indicators of flawed corporate culture (how to identify it when we see it), but also about the drivers of corporate culture (what we need to do to fix it). In a nutshell, the main drivers are misaligned economic incentives and in-group norms. The combination of strong economic incentives and in-group norms can push individuals who behave morally in their everyday lives to prioritize high performance over high integrity in their corporate lives. Reward systems that focus solely on outcomes, without considering the means used to achieve those results, numb employees to the ethicality of their behaviors. Further, companies can prime employees with the importance of working together for the common goal of increasing profit and growth, thereby diluting the power that societal-level norms (such as do not degrade the environment, or do not jeopardize your customers' safety) have on the employees.[82]

The key question then becomes, who shapes the economic incentives and in-group norms? And the answer is upper management.[83] To understand what causes flawed culture and how to address it, we therefore need to understand the role of those at the top of the corporate hierarchy.

C. *How Directors and Officers Affect Corporate Culture*

Following Enron's collapse in the early 2000s, a committee headed by William Powers (then dean of the University of Texas School of Law) investigated at length what caused the collapse.[84] The final report emphasized the role that board oversight failures played.[85] On paper, Enron had a well-constituted board full of savvy independent businesspersons, and a great "corporate social responsibility" program that won the company many accolades right up to its demise.[86] In reality, however, the board had not adequately implemented internal controls, did not ensure that information flow upward, and failed to respond promptly when serious issues started surfacing.[87] When a board behaves like that, flaws in corporate culture persist and worsen.

CORP. GOVERNANCE (May 16, 2017), https://corpgov.law.harvard.edu/2017/05/16/with-the-benefit-of-hindsight-the-wells-fargo-sales-practices-investigation-report/ (noting that "value statements and guidelines alone do not create an ethical culture" without the proper tone at the top).

[82] Jennifer Arlen, *The Compliance Function*, *in* THE OXFORD HANDBOOK OF CORPORATE LAW AND GOVERNANCE (Jeffrey N. Gordon and Wolf-Georg Ringe, eds., 2d ed., forthcoming).

[83] To be more precise, "upper management" is a large part of the answer. One could claim that other actors play some role as well. *See, e.g.*, Jeniffer G. Hill, *Good Activist/Bad Activist: The Rise of International Stewardship Codes*, 41 SEATTLE U. L. REV. 497, 501 (2018) (on the role of institutional investors in shaping corporate norms).

[84] WILLIAM C. POWERS, JR. ET AL., REPORT OF INVESTIGATION BY THE SPECIAL INVESTIGATION COMMITTEE OF THE BOARD OF DIRECTORS OF ENRON CORP (2002).

[85] *Id*.

[86] Roy Shapira, *Corporate Philanthropy as Signaling and Co-optation*, 80 FORDHAM L. REV. 1889, 1939 n.202 (2012).

[87] *See* Michael Peregrine et al., *Twenty Years Later: The Lasting Lessons of Enron,* HARV. L. SCH. F. ON CORP. GOVERNANCE (Apr. 5, 2021), https://corpgov.law.harvard.edu/2021/04/05/twenty-years-later-the-lasting-lessons-of-enron/.

In the two decades since the Powers Report, practitioners, scholars, and policymakers have increasingly acknowledged just how large a role directors and officers play in allowing a flawed corporate culture to develop.[88] Indeed, one of the clearest themes in the emerging literature on corporate culture is the importance of "tone at the top."[89] And advisors to boards have started emphasizing oversight of culture as a perennial topic on the board agenda, with many now ranking it as the number one issue that boards must address.[90]

Directors and officers shape corporate culture by setting economic incentives, setting information flows, and setting personal examples.[91] Managers are the ones setting sales targets and remuneration procedures for lower-level employees. Directors are the ones designing the executive pay packages, which could affect executives' time horizon and their inclination to invest in creating ethical cultures. Beyond these economic incentives, directors and officers also determine how information flows inside the organization. Managers can make it clear that they do not want to be bothered with details about how the employees are achieving, say, sales goals. Indeed, field work in large organizations has shown that information about unethical behavior tends to be pushed down the organizational ladder, while credit for success is claimed up the ladder.[92]

Finally, directors and officers affect the culture by example.[93] Employees tend to observe how directors and officers model either ethical or unethical behavior.[94] In other words, the behaviors of those at the top send cues to lower-level employees about which behaviors are unacceptable, which are tolerated, and which are rewarded.[95] Perhaps the best illustration of such dynamics came in recent years from companies with rampant sexual misconduct.[96] Prior to the #MeToo era (and in some cases even today), sexual

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[88] Langevoort, *The Effects of Shareholder Primacy*, *supra* note 42, at 386; Guiso et al., *supra* note 49 (finding that "a firm's board directors or CEO play a significant role in shaping its corporate culture").
[89] Langevoort, *Cultures of Compliance*, *supra* note 51.
[90] *See, e.g.*, Kerry Berchem et al., *Top 10 Topics for Directors in 2019*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Jan. 17, 2019), https://corpgov.law.harvard.edu/2019/01/17/top-10-topics-for-directors-in-2019/ (ranking corporate culture as the number one issue for boards); Martin Lipton et al., *Spotlight on Boards*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Jul. 18, 2023), https://corpgov.law.harvard.edu/2020/07/18/spotlight-on-boards-7/ (a prominent legal advisor imploring boards to "set the 'tone at the top' to create a corporate culture that […] gives priority to ethical standards, professionalism, integrity and compliance in setting and implementing both operating and strategic goals").
[91] *See* Veronica Root Martinez, *Complex Compliance Investigations*, 120 COLUM. L. REV. 249, 301 (2020) (citing studies from the behavioral ethics literature, finding that the example set by those at the top affects the entire corporation).
[92] *See* ROBERT JACKALL, MORAL MAZES: THE WORLD OF CORPORATE MANAGERS 20 (1988).
[93] *See* Hess, *supra* note 35, at 348 (noting that the tone at the top is set by leadership's actual behavior, rather than leadership's formal policies).
[94] *See* Robert C. Bird, *Caremark Compliance for the Next Twenty-Five Years*, 58 AM. BUS. L.J. 63, 113 (2021) ("Employees can readily spot hypocrisy in their leaders").
[95] *See* Donald Sull & Charles Sull, *How to Fix a Toxic Culture*, MIT SLOAN MGMT. REV. (2023) (calling "lack of leadership investment" the primary obstacle for improving corporate culture).
[96] *See, e.g.*, Samantha Cooney, *A Timeline of Sexual Harassment Allegations at Fox News*, TIME (May 2, 2017), https://time.com/4757734/timeline-sexual-harassment-allegations-fox-news/.

harassment by successful managers was often tolerated and kept under wraps via nondisclosure agreements.[97] Famous examples include the scandals at Fox News and CBS.[98] Usually in these cases, the board is willing to turn a blind eye or proactively assist the cover-up because the misbehaving managers are supposedly very valuable to the company.[99]

When employees observe that their managers regularly break the rules but are not disciplined, the employees perceive the corporate culture as prioritizing short-term yardsticks over integrity and compliance and are more likely to break the rules themselves.[100] In other words, the problem in such scenarios is not necessarily perverse economic incentives to engage in wrongdoing. The problem is rather inadequate policing of specific salient misbehavior, which reverberates throughout the organization, thereby making it likely that others will misbehave too.[101] When employees are viewing those at the top of the corporate hierarchy as making exceptions for themselves rather than applying compliance programs and ethics policies equally for all, these nice-sounding measures could lose their legitimacy and effectiveness.[102]

Still, even in cases where it is clear that directors and officers could have done more to root out problems, it is not clear that the legal system should hold them personally liable for flawed corporate culture. It is one thing to delineate best practices (aligning the incentives, ensuring information flows, and modeling ethical behavior), and another thing to legally mandate certain behaviors. The remainder of this Article explores the legal conduits for holding directors and officers accountable for flawed culture: Part II examines criminal liability in the US, Part III focuses on civil liability in the US, and Part IV highlights different enforcement models around the world.

II. CRIMINAL LIABILITY FOR FLAWED CORPORATE CULTURE

[97] *See*, *e.g.*, Alicia Adamczyk, *The Real Reason More Women Didn't Speak out against Ailes*, MONEY (Jul. 20, 2016), https://money.com/fox-news-roger-ailes-sexual-harassment-women-speak-out/; Emily Steel & Michael S. Schmidt, *O'Reilly Thrives as Settlements Add Up*, N.Y. TIMES, Apr. 2, 2017, at A1. To generalize, in the #MeToo era companies are relatively more likely to hold their directors and officers accountable for sexual misconduct. *See, e.g.*, Elahe Izadi & Travis M. Andrew, *Former CBS Chairman Les Moonves Fired for Cause, Will Not Receive Severance in the Wake of Sexual Misconduct Allegations*, WASH. POST (Dec. 18, 2018), https://www.washingtonpost.com/arts-entertainment/2018/12/17/former-cbs-chairman-les-moonves-fired-cause-will-not-receive-severance-wake-sexual-misconduct-allegations/.

[98] For a detailed analysis of US sexual harassment scandals *see* Daniel Hemel & Dorothy Shapiro Lund, *Sexual Harassment and Corporate Law*, 118 COLUM. L. REV. 1583 (2018). For similar examples elsewhere *see, e.g.*, Sally Patten, *Time up for Boards on Sexual Harassment*, AUSTRALIAN FIN. REV. (Aug. 26, 2020), https://www.afr.com/work-and-careers/workplace/time-is-up-for-boards-on-treatment-of-sexual-harassment-20200824-p55ov8 (detailing a high-profile sexual harassment scandal at a leading financial adviser in Australia). For the Fox example *see* Cooney, *supra* note 96.

[99] *See, e.g.*, Steel & Schmidt, *supra* note 97.

[100] Joseph E. Murphy, *Policies in Conflict: Undermining Corporate Self-Policing*, 69 RUTGERS U. L. REV. 421, 480 (2017); Arlen, *supra* note 82.

[101] *See, e.g.*, James Cook et al., *Uber Technologies, Inc.: Accountability in Corporate Culture*, 11 J. ORGANIZATIONAL BEHAV. EDUC. 33 (2018) (detailing the case of Uber).

[102] Hess, *supra* note 35, at 343.

Corporate culture has emerged as a priority for lawmakers around the world.[103] The theory behind lawmakers' interest in culture seems straightforward enough: well-designed legal interventions can help in setting boundaries, shaping norms of what is acceptable and what is not, and ensuring that there are consequences for those who flout the norms. But there is one thorny problem, namely, designing such "well-designed legal interventions."

This Article focuses on one category of legal interventions, namely, imposing liability for flawed culture. In other words, the Article examines what legal recourse is available once corporate debacles happen due to flawed culture. Within that category, we can think of four conduits for liability, which can be presented as a 2x2 matrix: what type of liability (criminal or civil), and to whom liability is attached (entity or individuals). This Part focuses on criminal liability at both the entity and individual levels, while Part III below focuses on civil liability.

Before we delve into these liability conduits, let us briefly note that there exist other categories that can promote ethical corporate culture more indirectly and before the fact. Take for example regulations that protect and incentivize whistleblowers.[104] Whistleblower protection laws purportedly promote a more open and ethical corporate culture, by encouraging employees to report misconduct. It can be argued, for example, that emboldening employees to voice their concerns early could reduce the risk that corporate culture will go down a slippery slope. We do not discuss these types of interventions here, if only because they are already thoroughly analyzed in the legal literature.[105] The different conduits for liability for flawed culture, by contrast, are underexplored.

A. *Individual-Level Interventions*

The most intuitive legal recourse is for law enforcers to prosecute the corporate employees who were directly involved in misconduct: those who handed out bribes, spilled toxic chemicals into rivers, cut corners in the manufacturing process, and lied to regulators. The prospect of facing jail time will deter individuals from engaging in such behaviors to begin with, or so the argument goes.

Such a method is effective in relation to certain types of corporate misbehavior but not in others. Imposing criminal liability on individuals can be effective when the misbehavior in question involves clear, deliberate actions taken by individuals with direct control over their conduct, such as

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[103] Nizan Geslevich Packin & Benjamin P. Edwards, *Regulating Culture: Improving Corporate Governance with Anti-Arbitration Provisions for Whistleblowers*, 58 WM. & MARY L. REV. ONLINE 41, 45 (2016).

[104] *Id* (treating Dodd-Frank's whistleblower protections as a part of the newfound regulatory emphasis on corporate culture).

[105] *See, e.g.*, David Freeman Engstrom, *Whither Whistleblowing? Bounty Regimes, Regulatory Context, and the Challenge of Optimal Design,* 15 THEORETICAL INQUIRIES L. 605 (2014) (a legal perspective on whistleblowing regimes); Alexander Dyck et al., *Who Blows the Whistle on Corporate Fraud?*, 65 J. FIN. 2213 (2010) (an economic perspective on whistleblowing).

embezzlement or insider trading. In these scenarios, the threat of personal criminal liability can be clear and realistic enough to alter the individual cost–benefit calculus and deter misbehavior.

Imposing criminal liability on corporate employees is less effective in deterring misbehaviors that are more systemic and driven by flawed corporate culture, such as pervasive regulatory noncompliance, or misconduct driven by unrealistic performance targets. In these scenarios, the lower-level employees who directly commit wrongs may feel powerless to resist pressures or incentives created by the company's leadership.[106] In fact, rank-and-file employees may perceive acquiescing to these pressures as being loyal to their colleagues and company.[107] For example, in Volkswagen's case, the judge who sentenced an engineer to jail for his role in the emissions scandal explicitly noted that the engineer had been "too loyal" to the firm.[108] When individuals interpret what they are doing not as a wrong but rather as promoting the greater good, they are unlikely to be deterred by the prospect of criminal liability.[109]

Another factor that dilutes the deterrent power of criminal liability is fragmentation of knowledge.[110] In large organizations, tasks are divided into numerous subtasks and spread across numerous subunits.[111] As a result, individual rank-and-file employees are unlikely to realize the full ramifications of the corporate conduct of which they are a part.[112] Multiple seemingly blameless actions by each individual employee can result in blameworthy corporate behavior. Individuals who do not realize that they are doing something criminal are less likely to be deterred by the prospect of criminal liability.[113]

To address corporate misbehavior that emanates from flawed culture it may therefore be more effective to focus on a different class of individuals: instead of prosecuting the low-level employees who committed the acts, prosecute the directors and officers who shaped the economic incentives, information flows, and prevalent norms.[114]

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[106] Langevoort, *Cultures of Compliance*, *supra* note 51, at 950.
[107] *See* John C. Coffee, Jr., *"No Soul to Damn: No Body to Kick": An Unscandalized Inquiry into the Problem of Corporate Punishment*, 79 MICH L. REV. 386, 396–97 (1981); Arlen, *supra* note 82 ("corporate culture provides employees with an other-regarding justification for the misconduct by priming them with the importance of working together towards the common goal of profit").
[108] Bill Vlasic, *Volkswagen Engineer Gets Prison in Diesel Cheating Case*, N.Y. TIMES, Aug. 26, 2017, at B2.
[109] Langevoort, *Cultures of Compliance*, *supra* note 51, at 950.
[110] *See* Diane Vaughan, *Toward Understanding Unlawful Organizational Behavior*, 80 MICH. L. REV. 1377, 1393 (1982) ("As organizations grow larger, specialized subunits result, each providing opportunities to engage in unlawful behavior on the organization's behalf").
[111] *See* DONALD C. LANGEVOORT, SELLING HOPE, SELLING RISK 40 (2016).
[112] *Id.*
[113] Constantinescu, *supra* note 39, at 404.
[114] Indeed, the guidelines for sentencing of organizations were recently updated to clarify that it is the "high-level personnel and substantial authority personnel of the organization" that "shall promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law." U.S SENT'G GUIDELINES MANUAL §8B2.1. (U.S SENT'G COMM'N 2018).

Here, however, settled concepts of criminal law get in the way.[115] To hold directors and officers criminally liable for flawed culture, prosecutors must typically prove beyond reasonable doubt the mental state of said decision-maker.[116] This may be a feasible task in small or mid-sized corporations, where directors and officers tend to be involved in key aspects of the business. In these smaller corporations, the evidential record is likely to contain traces that could indicate just how aware (or willfully blind) managers were of pervasive wrongdoing by others. In large corporations, by contrast, directors and officers are typically many steps removed from the actual wrongdoing, and therefore enjoy plausible deniability.[117] Prosecuting them for omission (not doing more to improve the corporate culture) is an uphill battle for prosecutors.[118]

Tellingly, not a single top executive has been prosecuted in some of the largest flawed-culture debacles, such as the opioid crisis or General Motors' faulty ignition switch scandal.[119] Public enforcers anticipate not only that it will be objectively difficult for them to disprove the ignorance of those at the top in such cases, but also that they will be "outlawyered" by defendants who spend enormous resources on fighting their cases.[120] Public enforcers lack the appetite for initiating such lengthy legal battles that would drain their resources and come with a relatively low win rate.[121] Top executives are aware of these dynamics, and as a result they too often opt to implement the minimum check-the-box compliance measures necessary for them to shift blame onto employees.[122]

Acknowledging these limits of prosecuting individuals for flawed culture has led to an emphasis on prosecuting the entity itself.[123] The theory

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[115] Buell, *The Responsibility Gap*, *supra* note at 22, 490.
[116] *Id*.
[117] *See* Assaf Hamdani & Alon Klement, *Corporate Crime and Deterrence*, 61 STAN. L. REV. 271, 296 (2008); Coffee, *supra* note 107, at 399; John Braithwaite, *Scaling up Crime Prevention and Justice*, 50 CRIME & JUST. 247, 255 (2021).
[118] *See* Jennifer Arlen & Samuel W. Buell, *The Law of Corporate Investigations and the Global Expansion of Corporate Criminal Enforcement*, 93 S. CAL. L. REV. 697, 700 n.8 (2020); Coffee, *id*; Mihailis E. Diamantis, *Functional Corporate Knowledge*, 61 WM. & MARY L. REV. 319, 341–42 (2019).
[119] *See* JOHN C. COFFEE, JR., CORPORATE CRIME AND PUNISHMENT: THE CRISIS OF UNDERENFORCEMENT 2–3 (2020).
[120] *See* Buell, *The Responsibility Gap*, *supra* note 22.
[121] *See* COFFEE, *supra* note 119; JESSE EISINGER, THE CHICKENSHIT CLUB: WHY THE JUSTICE DEPARTMENT FAILS TO PROSECUTE EXECUTIVES (2017) (describing the "fear-of-losing" culture among regulatory enforcers).
[122] *See* William S. Laufer, *Corporate Liability, Risk Shifting, and the Paradox of Compliance*, 52 VAND. L. REV.1341, 1403, 1418 (1999).
[123] Samuel W. Buell, *Criminal Procedure within the Firm*, 59 STAN. L. REV. 1613, 1625–26 (2007) [hereinafter Buell, *Criminal Procedure*]. The relevant doctrine here is *respondeat superior*, which allows holding corporations liable for the behavior of any employee with at least a partial intent to benefit the firm. Diamantis, *supra* note 118, at 338–39. Over the past decade, the policy of not going after senior managers has drawn many criticisms. *See, e.g.*, Jed S. Rakoff, *The Financial Crisis: Why Have No High-Level Executives Been Prosecuted?*, N.Y. REV. BOOKS (Jan. 9, 2014), https://www.nybooks.com/articles/2014/01/09/financial-crisis-why-no-executive-prosecutions/; Dorothy S. Lund & Natasha Sarin, *Corporate Crime and Punishment: An Empirical Study*, 100 TEX. L. REV. 285, 291 (2022) (noting the deterrence limitations of entity liability and stressing the need for enforcement agencies

seems promising: by imposing liability at the entity level, the legal system incentivizes the corporation to police individuals in its employ.[124] Managers will fear that the company whose stock options they own will suffer significant sanctions, and so they will create saner sales targets, instill a commitment to integrity and safety, and hire and promote ethical individuals, or so the argument goes. However, the accumulated experience of the past two decades suggests that focusing on the entity is not very effective in addressing flawed culture either.

B. *Entity-Level Interventions*

Perhaps the most familiar tool for regulating corporate culture is to seek lighter penalties (or to abstain from prosecution altogether) for corporations that have made efforts to improve their culture of compliance.[125] The US Federal Sentencing Guidelines for Organizations provide a classic illustration of this regulatory technique.[126] In the 1990s, the Guidelines sought to incentivize corporate investment in compliance by promising leniency for companies that have an effective compliance program. The key question then became, what counts as an *effective* compliance program? During the first years of implementing the Guidelines, it seemed as if too many companies superficially invested in external indicia of compliance just to gain credit, and that these external indicia did not serve the purpose of curbing corporate misbehavior.[127]

In response, public enforcers have updated the Guidelines and their policies to explicitly stress the need to evaluate not just the structural elements of compliance but also the company's *culture* of compliance.[128] Indeed, the current version of the Guidelines explicitly instructs enforcers to assess whether the company promoted a culture "that encourages ethical conduct and a commitment to compliance with the law." And virtually every public speech by a high-level public enforcer in recent times has emphasized just how much the assessment of culture matters to decisions on how to resolve enforcement

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to pursue "culpable individuals"). In response to the backlash, the DOJ released the Yates Memorandum, which outlined a shift in enforcement policy toward prioritizing prosecuting individuals. Memorandum from Sally Yates, U.S. Deputy Att'y Gen., to all U.S. Att'ys. (Sep. 9, 2015). But thus far the Yates Memorandum has not necessarily led to a meaningful change in prosecuting top-level individuals for flawed corporate culture. Brandon L. Garrett, *Declining Corporate Prosecutions*, 57 AM. CRIM. L. REV. 109, 135 (2020) (stating that the approach originally envisaged in the Yates Memorandum "seems not to have fully taken hold and has never produced its intended results"); COFFEE, *supra* note 119, at 69.

[124] *See* Buell, *Criminal Procedure*, *id*. at 1625–26.

[125] Langevoort, *Cultures of Compliance*, *supra* note 51, at 940–44.

[126] U.S SENT'G GUIDELINES MANUAL §8B2.1(a). (U.S SENT'G COMM'N 2010).

[127] Hess, *supra* note 35, at 330; Miriam Hechler Baer, *Governing Corporate Compliance*, 50 B.C. L. REV. 949, 950 (2009).

[128] Langevoort, *Cultures of Compliance*, *supra* note 51, at 934, 944; Hess, *id*. at 320.

actions.[129] Perhaps the best illustration of the newfound emphasis on culture comes from the 2023 version of the DOJ's Criminal Division guidance:

> "Beyond compliance structures, policies, and procedures, it is important for a company to *create and foster a culture of ethics and compliance* with the law at all levels of the company. The effectiveness of a compliance program requires a high-level commitment by company leadership to implement a culture of compliance from the middle and the top."

On paper, the fact that criminal law enforcers emphasize culture so much should have nudged corporate decision-makers to work harder on instilling and maintaining a culture of compliance. But in practice, the ability of these guidelines and policies to affect meaningful change in corporate culture is limited, if only because it is difficult for enforcers to follow through on their promises to emphasize culture.[130]

As outsiders to the company in question, enforcers find it hard to define with precision what counts as part of said company's culture, let alone to measure or quantify the level of ethicality in said culture (consider the difficulty of having to measure "the way things get done" within a large corporation that you are not a part of).[131] To operationalize instructions such as "assess the company's culture," enforcers therefore typically resort to focusing on more easily observable indicia such as whether the company in question has a compliance program in place or certain policies in its employee handbook. Corporate insiders are aware of these dynamics, and so they too direct most of their attention and resources to the easily observable indicia of compliance, rather than to the hard-to-verify aspects of ethical culture.[132]

Our story thus far has been a straightforward one: (1) public enforcers have increasingly recognized the central role of culture in preventing corporate misbehavior, but (2) they have struggled to operationalize this newfound emphasis on culture, given the inherent limitations of criminal procedure and

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[129] *See, e.g.*, Lisa O. Monaco, *Speech by Deputy Attorney General Monaco on Corporate Criminal Enforcement*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Nov. 8, 2021), https://corpgov.law.harvard.edu/2021/11/08/speech-by-deputy-attorney-general-monaco-on-corporate-criminal-enforcement/ (noting that a culture "that thumbs its nose at compliance leads to bad results"); Langevoort, *id*. at 935 ("In the last few years especially, lawmakers have increasingly invoked culture as something crucial to good compliance"); Bird, *supra* note 94, at 106–07 (compiling examples). Another manifestation of the outsized role that corporate culture plays in criminal law is the policy of settling enforcement actions with Deferred Prosecution Agreements (DPAs) and Non-Prosecution Agreements (NPAs). An ostensible goal of this policy is to pressure companies to transform their corporate cultures. Indeed, as part of DPAs and NPAs companies usually commit to reforming their policies, incentives, and sometimes even leadership, and many agreements also include an appointment of outside monitors to ensure that the promised reforms indeed happen. *See* Jennifer Arlen, *Prosecuting beyond the Rule of Law: Corporate Mandates Imposed through Deferred Prosecution Agreements*, 8 J. LEGAL ANALYSIS 191, 192 (2016) (noting the prevalence of NPAs and DPAs and their purported roles).

[130] Hess, *supra* note 35, at 335–36.

[131] *Id;* Root Martinez, *More Meaningful Ethics*, *supra* note 12.

[132] Laufer, *supra* note 122.

public enforcement.[133] Prosecuting the individuals who were directly involved in the crime does not change the culture. Prosecuting the individuals who shape the culture is an uphill battle given the settled concepts of criminal law, such as the need to prove mental state. And punishing companies whose culture is flawed is a tall task too, given the difficulties for outsiders to assess the unwritten norms within large corporations. Could the civil liability channel be better at generating accountability for flawed corporate culture?

III. CORPORATE LAW LIABILITY FOR FLAWED CORPORATE CULTURE

The board of directors is the corporate organ responsible for risk oversight. A flawed culture puts the company's critical assets – such as its brand reputation or high-end talent – at risk.[134] It is therefore clear that oversight of corporate culture risk should feature prominently on the board's agenda.[135] But it is far from clear that directors will be held personally liable for harms caused to their companies due to flawed culture. After all, settled concepts of corporate law, such as the business judgment rule, largely immunize directors from judicial scrutiny of their decisions, including decisions on how to design compliance systems and policies.[136] To delineate the conditions under which directors can be liable for flawed culture, this Part examines the resurgence of corporate law's oversight duty doctrine.

Section A provides the necessary background on the doctrine, and how it has evolved in recent years. Section B explains how this recent evolution has rendered the doctrine more adept at holding officers and directors accountable for flawed corporate culture. The doctrine as currently construed extracts information on how officers and directors set information flows, design incentives, and set the tone in ways that shape their company's culture. Section C highlights the flip side, namely, the limitations that sometimes prevent oversight duty litigation (even in its revamped form) from facilitating improvements in corporate culture. Section C also spotlights a recent overhaul of Delaware corporate law from March 2025, which may end up diluting the prospect of oversight duty litigation.

A. *Oversight Duties: A Primer*

In 1996, the *Caremark* decision shifted directors' role in compliance enforcement from passive to proactive: to meet their oversight duties, directors

[133] *Cf.* Cary Coglianese et al., *The Role of Government in Corporate Governance*, 1 N.Y.U. J. L. & BUS. 219, 235 (2004) (discussing the various limitations of criminal law in affecting change in corporate behavior).
[134] *See* Wilcox & Sodali, *supra* note 46 (noting that culture is the foundation that protects the company's most important asset, namely, its reputation).
[135] *See* Oven et al., *supra* note 45 (a prominent adviser to boards noting that "culture-related risk is a key risk that calls for board oversight").
[136] Stephen M. Bainbridge, *The Business Judgment Rule as Abstention Doctrine*, 57 VAND. L. REV. 83, 87 (2004).

cannot sit idle and wait for someone to flag problems to them.[137] Instead, directors must at a minimum (1) implement a system that collects information about potential problems and reports back to them, and (2) address warnings that said system generates.[138] Beyond installing a system and addressing red flags, directors must also (3) refrain from affirming a business plan that is based on making profits by skirting regulations.[139] These three requirements are often dubbed information system claims, red flags claims, and business plan (or *Massey*) claims, respectively.[140]

Yet, until 2019, all these claims and the oversight duty doctrine more generally lay dormant. The combination of the procedural stance and the standard of review in failure-of-oversight claims presented a virtually insuperable pleading hurdle for plaintiffs.[141] To survive the "demand" requirement in such cases,[142] plaintiffs must provide indications that directors abdicated their duties *in bad faith*.[143] Yet it is extremely hard for outside shareholders to show already at the pleading stage (before discovery) what directors knew, when they knew it, and what they did or did not do to stop the compliance failure in question. As a result, *Caremark* claims basically amounted to a parade of early dismissals and were widely perceived by academics and practitioners as a "toothless tiger."[144]

This state of affairs changed quickly following the 2019 *Marchand* decision.[145] Blue Bell, a leading ice-cream manufacturer, suffered a listeria outbreak in one of its product lines, causing three deaths, massive recalls, and attendant financial, legal, and reputational costs to the company.[146] Delaware's Court of Chancery routinely dismissed the shareholders' failure-of-oversight claim, reasoning that they failed to produce evidence linking the directors to the corporate trauma (no bad faith). Yet for Delaware's Supreme Court, the fact that

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[137] *In re* Caremark Int'l Inc. Deriv. Litig, 698 A.2d 959 (Del. Ch. 1996) *adopted by* Stone v. Ritter, 911 A.2d 362, 365 (Del. 2006).
[138] *Id*.
[139] *In re* Massey Energy Co., 2011 WL 2176479 (Del. Ch. May. 31, 2011).
[140] *In re* McDonald's Corp. S'holder Deriv. Litig., 289 A.3d 343, at 359–60 (Del. Ch. Jan 26, 2023) (McDonald's I).
[141] *See* Elizabeth Pollman, *Corporate Disobedience*, 68 DUKE L.J. 709, 756 (2019) (noting the paucity of successful cases); Jennifer G. Hill, *Deconstructing Sunbeam – Contemporary Issues in Corporate Governance*, 67 U. CIN. L. REV. 1099, 114-117 (1999) (analyzing the drawbacks of the doctrine as then construed).
[142] Shareholder derivative litigation displaces the board's usual authority to assert its company's legal claims. The courts will allow such displacement only if shareholders can show that they made "a demand" on the board to pursue the company's purported claims or show that making such a demand would have been futile. Del. Ch. Ct. R. 23.1; United Food & Com. Workers Union v. Zuckerberg, 250 A.3d 862 (Del. Ch. 2020), *aff'd*, 262 A.3d 1034 (Del. 2021). The practical way to show demand futility in oversight duty cases is to link the majority of directors to the trauma that the corporation suffered (showing that they may be held liable themselves, and so cannot be trusted to decide how to handle the derivative claims).
[143] *See Stone*, 911 A.2d at 370.
[144] *See, e.g.*, Anne Tucker Nees, *Who's the Boss? Unmasking Oversight Liability within the Corporate Power Puzzle*, 35 DEL. J. CORP. L. 199, 216 (2010).
[145] Marchand v. Barnhill, 212 A.3d 805 (Del. 2019).
[146] *Id*. at 812–13.

there was no discussion of potential listeria issues at the board level served in itself as an indication that directors were breaching their oversight duties.[147] If you are a director of a company that only sells ice cream and you do not allocate time and responsibilities to discussing potential food safety issues, you are probably not trying in good faith to oversee the company's operations.[148]

Marchand opened the doors to many other successful *Caremark* claims.[149] Within a couple of years, oversight duties transformed from being irrelevant to being highly relevant.[150]

The immediate cause for this shift is twofold.[151] First, courts these days are increasingly willing to apply heightened scrutiny to directors' compliance efforts.[152] Following *Marchand*, when the compliance failure in question concerns central compliance risks, courts are willing to view absence of proof that the board discussed the issue as a pleading-stage indication that the board breached its duties.[153]

Second, courts have been willing to grant shareholders access to internal company documents to investigate potential failure-of-oversight claims.[154] Shareholders have always enjoyed a qualified right to inspect their company's books and records, under DGCL §220.[155] But in recent years, courts liberalized their interpretation of Section 220's requirements,[156] so that they ordered provision of internal documents in more cases,[157] and ordered the provision of a broader scope of documents (not just formal board materials, but also informal electronic communications).[158] Shareholders thus enjoyed much better prefiling

[147] *Id.* at 821.
[148] *Id.* at 824.
[149] *See, e.g.*, *In re* Clovis Oncology, Inc. Derivative Litig., 2019 WL 4850188 (Del. Ch. Oct. 1, 2019); Hughes v. Hu, 2020 WL 1987029 (Del. Ch. Apr. 27, 2020); Teamsters Loc. 443 Health Servs. & Ins. Plan v. Chou, 2020 WL 5028065 (Del. Ch. Aug. 24, 2020); *In re* Boeing Co. Deriv. Litig., 2021 WL 4059934 (Del. Ch. Sep. 7, 2021).
[150] *See, e.g.*, Ann Lipton, *Possibly the Easiest Theory in Corporation Law*, BUS. L. PROF. BLOG (May 13, 2023), https://lawprofessors.typepad.com/business_law/2023/05/the-easiest-theory-in-corporation-law.html (the title inverts the oft-cited, but arguably outdated, notion that *Caremark* is "the most difficult theory in corporation law upon which a plaintiff might hope to win a judgment" (Caremark, 698 A.2d 959, 967)).
[151] Shapira, *Max Oversight Duties*, *supra* note 19.
[152] *Id*.
[153] Marchand, 212 A.3d 805, 821.
[154] Shapira, *Max Oversight Duties*, *supra* note 19, at 121.
[155] DEL. CODE ANN. tit. 8, § 220 (2021).
[156] Roy Shapira, *Corporate Law, Retooled: How Books and Records Revamped Judicial Oversight*, 42 CARDOZO L. REV. 1949, 1952 (2021) [Hereinafter Shapira, *Books and Records*]; Geeyoung Min & Alexander M. Krischik, *Realigning Stockholder Inspection Rights*, 27 STAN. J. L., BUS. FIN. 225, 233 (2022); James D. Cox et al., *The Paradox of Delaware's "Tools at Hand" Doctrine: An Empirical Investigation*, 75 BUS. LAW. 2123 (2020) (documenting the rise of Section 220 cases).
[157] *See, e.g.*, AmerisourceBergen Corp. v. Lebanon County Employees' Retirement Fund, 243 A.3d 417, 427 (Del. 2020) (clarifying that to demonstrate a "proper purpose" for inspection, shareholders do not need to show indications of an actionable claim against the directors).
[158] *See, e.g.*, *In re* Facebook, Inc. Section 220 Litig., 2019 WL 2320842, at *18 n.185 (Del. Ch. May 30, 2019) (ordering Facebook's high-ranking officers and directors to produce not just formal board materials, but also private emails).

discovery powers, which they utilized to plead with particularity facts about how the board never even discussed a critical compliance issue, or how they knew about critical problems but chose to ignore them. But there is a caveat here: in March 2025, Delaware's legislature arguably reduced the potency of these prefiling discovery powers, by making it harder for shareholders to gain access to informal company communications. It remains to be seen how courts will interpret the new language of Section 220. We return to this point in our context of accountability for flawed culture later in this Part.

For now, let us note that these two changes – willingness to sanction directors for what they did not know and willingness to grant shareholders access to internal communications – make the oversight duty doctrine more adept at generating accountability for flawed culture. In information system claims, litigation revolves around the question of whether the board ensured that adverse information about central compliance risks flows up the corporate hierarchy. In red flags claims, litigation revolves around the two-pronged inquiry of whether past warnings were imminent (namely, connected to the current trauma), and what directors did to address said warnings. And in business plan claims, litigation revolves around the question of whether directors proactively prioritized profits over compliance. Litigation of each one of these claims therefore implicates directors' involvement in their company's culture of compliance and ethics.

Before the next Section elaborates on how exactly each one of these claims generates accountability for flawed culture, let us take a step back and clarify how corporate law works more generally. In corporate law, very few cases are ultimately decided in final verdicts.[159] And when cases are decided, directors almost never pay out of pocket.[160] Corporate law affects behavior less through sanctions imposed after a full trial, and more through the early stages of the process. Corporate decision-makers are deterred from the prospect of paying settlements ex post and planning how to avoid the risks and costs of litigation ex ante. Importantly, the costs of litigation that defendants try to avoid are also nonlegal, such as the emotional stress of having to go through depositions, or the reputational fallout from having damning information about you dug out for everyone in the market to see.[161] The upshot for our purposes is that when trying to assess how oversight duties shape corporate culture, we need

[159] Lawrence A. Hamermesh & Michael L. Wachter, *The Importance of Being Dismissive: The Efficiency Role of Pleading Stage Evaluation of Shareholder Litigation*, 42 J. CORP. L. 597, 605 (2017) (finding that during a five-year period, only five final verdicts were reached after a full trial in derivative or class actions).
[160] Bernard Black et al., *Outside Director Liability*, 58 STAN. L. REV. 1055, 1055 (2006) (finding that during a twenty-five-year period, there were only thirteen instances in which outside directors of public companies paid out of pocket).
[161] Edward B. Rock, *Saints and Sinners: How Does Delaware Corporate Law Work?*, 44 UCLA L. REV. 1009 (1997) (on the social sanctions that come with corporate law litigation); Margaret M. Blair & Lynn A. Stout, *Trust, Trustworthiness, and the Behavioral Foundations of Corporate Law*, 149 U. PA. L. REV. 1735, 1747–49 (2001) (on the moral sanctions that come with corporate law litigation); Roy Shapira, *A Reputational Theory of Corporate Law* 26 STAN. L. POL'Y REV. 1 (2015) (on the reputational sanctions).

to look at (1) settlements, (2) memos that law firms send to their clients following important judicial decisions in the preliminary stages of litigation, and (3) the framing of media coverage of corporate debacles before and after corporate law litigation.

As the next Section shows, the revamped mode of oversight duty litigation has already affected how directors and officers view their roles in corporate culture through all these channels: ramping up settlement amounts, leading to a flurry of law firm memos imploring their corporate clients to put oversight of the company's culture of compliance squarely on the agenda, and generating reputational fallouts for directors who do not address flawed culture.

B. *How the Oversight Duty Doctrine Can Counteract Flaws in Corporate Culture*

In its revamped form, oversight duty litigation holds directors accountable for their various roles in shaping the corporate culture. For concreteness, let us consider the three roles that we mentioned earlier, namely, how directors and officers set the information flows, design economics incentives, and lead by example. Oversight duty litigation often revolves around questions that directly implicate each one of those roles.

First, the revamped oversight duty doctrine holds directors and officers accountable for how they set information flows, through the "mission critical" designation. When it comes to central compliance risks, directors and officers cannot use the "I didn't know" gambit: the court insists that not being informed on central risks constitutes a breach of fiduciary duty. The most important question therefore becomes what compliance risks count as central. It can be argued that a flawed culture counts as a central risk for virtually every large company. After all, companies have been facing increased regulatory and societal demands, including growing pressures from the ESG movement to treat their stakeholders better. In such an environment, boards that do not put oversight of the company's culture of compliance on their agendas are doing so at their company's peril (exposing it to both legal and reputational sanctions).[162] Directors can therefore be held accountable for not doing enough to inform themselves about the unwritten norms of compliance in their company.

As such, the oversight duty doctrine mitigates the incentives of directors and officers to remain *willfully blind* about the unwritten norms in their company. Corporate directors have strong incentives to remain ignorant about

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[162] *Cf.* Stavros Gadinis & Amelia Miazad, *The ESG Information System*, 47 SEATTLE U. L. REV. 695, 696 (2024). This observation is reflected in numerous recent law firm memos. *See, e.g.*, Michael W. Peregrine et al., "*Operation Codebreaker" and the Culture of Compliance*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Mar. 4, 2020), https://corpgov.law.harvard.edu/2020/03/04/operation-codebreaker-and-the-culture-of-compliance/ (imploring boards to ask "How often and how does the company measure its culture of compliance? How does the company's hiring and incentive structure reinforce its commitment to ethical culture?").

decisions that skirt regulatory requirements and prioritize profits over everything else. Prioritizing profits is good for directors who receive substantial stock-based compensation.[163] And remaining ignorant about *how* profits are obtained is good for directors' ability to maintain plausible deniability and escape accountability.[164] Indeed, in virtually all the flawed culture debacles, directors' first line of defense is "we did not know." For example, in Wells Fargo's phony accounts scandal, the board supposedly never knew that 5,300 employees had been terminated for sales practice violations until this information became public.[165]

Both facets of the new *Caremark* era – increased willingness to give weight to culpable ignorance, and increased willingness to grant shareholders access to internal communications – enhance the quantity and quality of information that flows up to the board. Indeed, following the recent string of *Caremark* cases, virtually every large law firm circulated memos advising their corporate clients to put thorny compliance issues on the agenda and to emphasize proper documentation of discussions of said issues.[166] As a result, directors are more likely to ask others in the organization to prepare written materials for them, which in turn undercuts the kind of "don't ask, don't tell" norms that are prevalent in flawed corporate cultures.[167]

Second, the oversight duty doctrine holds directors accountable for how they set incentives. Specifically, oversight duty litigation is programmed to extract information about the disjunction between what directors and officers are saying and how they are incentivizing employees, thereby attacking attempts to engage in *cosmetic compliance*.[168]

With information system claims, courts look at the company's professed values as an indication of what counts as mission critical for purposes of activating heightened scrutiny. When a company's mission statement, for example, declares a certain issue or value as a priority of the company, the court will treat lack of board discussions of said issue as a pleading-stage indication of a breach of oversight duties.[169] To illustrate, the *McDonald's* decision opens by highlighting that the fast-food giant prides itself on being "America's best first job," that fifty-five percent of entry-level workers are women, and that the company's code of conduct stresses the need to cultivate "respectful

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[163] *See generally* Armour et al., *supra* note 73.
[164] Miriam H. Baer, *Too Vast to Succeed*, 114 MICH. L. REV. 1109, 1112 (2016).
[165] Kohn et al., *supra* note 81.
[166] On these law firm memos see Roy Shapira, *A New Caremark Era: Causes and Consequences,* 98 WASH. U. L. REV. 1857, 1881–83 (2021). *See generally* Stavros Gadinis & Amelia Miazad, *The Hidden Power of Compliance*, 103 MINN. L. REV. 2135 (2019) (arguing that the open lines of chief compliance officers to the board and the documentation of their reports to the board incentivize board risk oversight).
[167] Walmart II, 2003 Del. Ch. LEXIS 92, at *147 ("Driving adverse information to the board-level thus becomes the mechanism for improved compliance").
[168] Kimberly D. Krawiec, *Cosmetic Compliance and the Failure of Negotiated Governance*, 81 WASH. U. L.Q. 487, 491 (2003) (coining the term and describing the phenomenon).
[169] Ontario Provincial Council of Carpenters' Pension Trust. v. Walton, 294 A. 3d 65, 86 (Del. Ch. Apr. 12, 2023) ("Walmart I").

workplaces."[170] The decision then concludes that "the court does not have to infer that sexual harassment and misconduct constituted a mission critical risk. The company said it."[171] As a result of such decisions, companies are more likely either to tone down their value statements or make sure that they walk the talk to begin with.

With red flags claims, courts determine whether directors addressed warning signs by distinguishing between superficial efforts and genuine efforts. In *AmerisourceBergen¸* for example, the court reprimanded directors for responding to warnings of opioid diversion and theft by adopting superficial measures, while saving more potent recovery measures as a bargaining chip in future settlements with regulators (i.e., as a settlement currency to obtain a global release).[172] *Chou*, to use another example, admonished the board for paying an outside law firm to identify weaknesses in the company's compliance program but not taking actual steps to remedy the weaknesses.[173]

In business plan (*Massey*) claims, courts explicitly look for cases where managers set incentives throughout the organization to prioritize profits over everything else. In *Walmart*, for example, the fact that managers set unrealistic sales targets and understaffed compliance officers led the courts to conclude that the instances of opioid diversion were not isolated incidents but rather symptomatic of a broader issue within the company's culture, and that the board proactively decided to prioritize profits over compliance.[174]

Third, the oversight duty doctrine holds directors and officers accountable for how they set the tone and lead by example. To illustrate, consider corporate law's role in the #MeToo movement. The movement turned a spotlight on sexual misconduct in the workplace and made it a key corporate governance issue.[175] Companies responded quickly by writing new policies and sending all employees to training sessions.[176] Nevertheless, in some companies, workplace harassment remains endemic, because the tone at the top encourages a misogynistic (or simply lawless) culture.[177] Too often directors and other gatekeepers prefer to overlook such misconduct by charismatic executives who are valuable to the company.[178]

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[170] *In re* McDonald's Corp. S'holder Derivative Litig., 291 A.3d 652, 664 ("McDonald's II").
[171] *Id*. at 681.
[172] Lebanon County Employees' Retirement Fund v. Collis, 2022 Del. Ch. LEXIS 358 (Del. Ch. Dec. 22, 2022), at *49.
[173] *Chou*, 2020 WL 5028065, at *10.
[174] Walmart II, 2003 Del. Ch. LEXIS 92, at *100–05 (noting that while Walmart's directors created the paperwork necessary for nice-sounding compliance programs and policies, they undermined the actual implementation of the program by underfunding the internal compliance team and purchasing a limited amount of database capacity).
[175] Hemel & Lund, *supra* note 98, at 1585–87.
[176] Rachel S. Arnow-Richman, James Hicks, & Steven Davidoff Solomon, *Do Social Movements Spur Corporate Change? The Rise of "MeToo Termination Rights" in CEO Contracts*, 98 INDIANA L.J. 125, 129 (2022).
[177] *Id*. at 170.
[178] *Id*.

In the past, *Caremark* cases did very little to police such behavior. In 2018, pre-*Marchand*, Professors Hemel and Lund conducted a thorough analysis of the corporate law implications of sexual misconduct and concluded that the *Caremark* channel is unlikely to hold directors and officers accountable.[179] They illustrated their claim with the *American Apparel* case, where the court dismissed a *Caremark* claim even though the serial sexual misconduct of the company's CEO had been widely reported in major newspapers for many years.[180]

The situation today is very different. In several recent cases that ultimately settled, such as the *Victoria's Secret* case, the court was willing to grant shareholders access to internal company documents, the media was quick to pick up and extensively cover the shareholders' complaints, and the defendants were quick to settle and commit tens of millions to prophylactic measures designed to eradicate their misogynistic cultures.[181] And in 2023, *McDonald's* explicitly held that the company's Chief People Officer can be held liable for not doing enough to root out a culture of rampant sexual misconduct.[182] Setting bad examples is therefore yet another type of behavior that is now being addressed head on in oversight duty cases.

Beyond inquiring about how directors have shaped the company's culture by setting information flows, economic incentives, and personal examples, oversight duty litigation also generates accountability for flawed culture by addressing the most common excuses and blame-shifting tactics used in such scenarios.

The fourth way in which the oversight duty doctrine generates accountability for flawed corporate culture is by *exposing the fact that the culture is deeply flawed*, and not letting directors get away with the "just a few bad apples" excuse. Indeed, in most all large corporate debacles, upper management initially tries to attribute misbehavior to a few rogue low-level employees rather than to a pervasive unethical culture. Volkswagen's upper management, for example, steadfastly argued that the emissions scandal was simply the work of "a couple of software engineers."[183] Once shareholders sue

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[179] Hemel & Lund, *supra* note 98, at 1646.

[180] *In re* Am. Apparel Shareholder Derivative Litig., 2012 U.S. Dist. LEXIS 146970 (C.D. Cal., July. 31, 2012), at * 100 ("the bare allegation that [the CEO's] sexual proclivities were widely known is insufficient to support a lack of oversight claim").

[181] Sierra Jackson, *L Brands Inks Deal with Shareholders to Exit Workplace Harassment Cases*, REUTERS (Jul. 30, 2021), https://www.reuters.com/legal/litigation/l-brands-inks-deal-with-shareholders-exit-workplace-harassment-cases-2021-07-30/ (reporting on the large settlement); Kellie Ell & Sindhu Sundar, *L Brands Founder Leslie Wexner Faces New Complaints about "Culture of Misogyny" at Victoria's Secret*, YAHOO! FINANCE (Jan. 15, 2021), https://finance.yahoo.com/news/l-brands-founder-leslie-wexner-202839664.html (reporting on the detailed complaint); Catherine M. Clarkin & Melissa Sawyer, *ESG Trends and Hot Topics*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Aug. 25, 2021), https://corpgov.law.harvard.edu/2021/08/25/esg-trends-and-hot-topics/ (advising corporate clients to take seriously their oversight obligations in that regard).

[182] McDonald's I, *supra* note 140, at 370.

[183] *See*, *e.g.*, *Top U.S. VW Exec Blames "A Couple of Software Engineers" for Scandal*, REUTERS (Oct. 8, 2015).

directors derivatively for breach of oversight duties, litigation can override the corporation's narrative by revealing just how pervasive the misconduct was.

To illustrate, consider how a typical red flags claim will be adjudicated. When the court conducts its red flags analysis, it considers the scale of the misconduct and its pervasiveness. If the problems accumulated over time and were systemic, it is unlikely that directors did not see the warning signs (unless they willfully chose not to see them).[184] In other words, showing that the company was a perennial recidivist will bolster plaintiffs' chances of proving a red flags claim, and in the process will reveal evidence about how the problem was one of flawed culture rather than one of rogue employees.[185] In business plan claims, these dynamics are even more pronounced: to show that directors proactively approved a plan predicated on profiting from violating the law, plaintiffs must extract information on how the problems were not accidental but rather part of the plan.[186]

The fifth way in which oversight duty litigation generates accountability is by not allowing the company in question to diffuse guilt across the entire industry.[187] To revisit the Volkswagen example, upper management sought to frame its emissions scandal as something that all other car manufacturers do.[188] By convincing the world that "everybody else was doing it too," the company hoped to reduce not just the expected legal sanction (how culpable can it be to do something that the entire industry is doing?), but also the expected reputational sanction. After all, reputational sanctioning is the process of market actors learning about something bad that company X did and taking their business to X's competitors; but if X's competitors are just as bad, there is no reason for market actors to stop doing business with X.[189]

Oversight duty litigation counteracts these dynamics by comparing the conduct of the company in question to that of its industry peers. The recent opioid decisions against Walmart and AmerisourceBergen, for example,

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[184] *See, e.g.*, *in re* Countrywide Financial Corp. Derivative Litigation, 554 F. Supp. 2d 1044, 1065 (C.D. Cal. 2008) ("the idea that a Company-wide culture that encouraged unchecked deviations from underwriting standards in a way which would fatally affect the Company's continued financial performance went unnoticed by a Board of Directors simply does not square").

[185] The following quote from the *Wells Fargo* case provides a good example: "Defendants ignore the bigger picture by addressing each of these red flags in piecemeal fashion. While any of these red flags might appear relatively insignificant to a large company like Wells Fargo when viewed in isolation, when viewed collectively they support an inference that a majority of the Director Defendants consciously disregarded their fiduciary duties despite knowledge regarding widespread illegal account-creation activities, and therefore, that there is a substantial likelihood of director oversight liability." Shaev v. Baker, 2017 U.S. Dist. LEXIS 68523, at *45.

[186] See Massey 2011 Del. Ch. LEXIS 83, at *70 (noting that the problems were "caused not by a freak and unavoidable accident, but instead by a corporate culture premised on the view that the company's management knew better than the law about what was necessary to run safe mines").

[187] Langevoort, *Cultures of Compliance*, *supra* note 51, at 961 (noting that "everybody does it" is one of the most used excuses by companies that get caught misbehaving).

[188] *See* Patrick McGee, *Car Emissions Scandal: Loopholes in the Lab Tests*, FIN. TIMES (Aug. 6, 2018), https://www.ft.com/content/2a123e88-9582-11e8-b747-fb1e803ee64e.

[189] Assaf Jacob & Roy Shapira, *An Information-Production Theory of Liability Rules*, 89 U. CHI. L. REV. 1113, 1115 (2022).

repeatedly emphasized that other distributors fared much better in terms of identifying and reporting suspicious opioid orders.[190]

Note that the abovementioned five conduits for accountability for flawed culture may sometimes exist outside of oversight duty litigation, such as in securities fraud cases in federal courts. Indeed, in recent years there has been a resurgence in "ESG securities fraud" cases.[191] The Securities Exchange Act prohibits fraudulent or misleading statements in connection with the sales of securities.[192] And because public companies have been disclosing more and more information about their ESG performance, they have been opening themselves up to claims that they inflated their ESG efforts in ways that affect the value of their stock. In other words, shareholders can bring a securities law claim to hold the company accountable for ESG-related organizational hypocrisy. For example, when a company claims that it is committed to environmental sustainability, while at the same time increasing its carbon emissions, it potentially becomes a target for securities fraud litigation.[193] Such cases resemble oversight duty cases in several ways, most notably with their high pleading hurdle: here as well, plaintiffs need to plead with particularity facts indicating scienter.[194] On paper, then, these securities fraud cases could similarly implicate issues involving willful blindness, cosmetic compliance, and whether misconduct was one-off or pervasive and caused by flawed culture.[195]

In practice, however, two differences between oversight duty cases and securities fraud cases make the latter less adept at generating accountability for flawed corporate culture. First, from a substantive standpoint, securities fraud cases focus on whether *the entity* misled investors, whereas oversight duty cases focus on the individuals who set the tone at the top. Second, from a procedural standpoint, unlike plaintiffs in oversight litigation, plaintiffs in securities litigation cannot file "books and records" actions to compel the company to give them access to internal communications.[196] Plaintiffs in securities cases therefore must resort to more limited investigatory tools, such as hiring private investigators and attempting to solicit whistleblowers from within the defendant

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[190] Walmart I, *supra* note 169, at 81.
[191] *See generally* Emily Strauss, *Is Everything Securities Fraud?*, 12 UC IRVINE L. REV. 1331 (2022) (describing the trend).
[192] 17 C.F.R. § 240.10b-5.
[193] *See generally* James J. Park, *ESG Securities Fraud*, 58 WAKE FOREST L. REV. 1149 (2023) (on the proliferation of such claims).
[194] Roy Shapira, *Mandatory Arbitration and the Market for Reputation*, 99 B.U. L. REV. 873, 896 (2019).
[195] *See, e.g.*, Chau v. Musk, 1:22-CV-0592-DAE (W.D. Tex. Jul. 21, 2023) (trying to hold the company accountable for claiming that they are committed to diversity while having an anti-diversity corporate culture); Robert B. Thompson & Hillary A. Sale, *Securities Fraud as Corporate Governance: Reflections upon Federalism*, 56 VAND. L. REV. 859, 860 (2003) (identifying the role that securities fraud litigation plays in regulating corporate governance).
[196] The Securities Litigation Uniform Standards Act of 1998 (SLUSA) precludes securities class actions from being litigated in state courts, thereby limiting the ability to use state-backed rights to inspect the books. Pub. L. No. 105-353, 112 Stat. 3227.

company.[197] As a result, these cases are less likely to proceed past the motion to dismiss and to generate meaningful information on directors' involvement in their company's culture.

C. *The Limits of Oversight Duties*

The previous Section spotlighted the promise of the oversight duty doctrine as a tool for addressing flawed corporate culture. This Section shifts focus to the doctrine's limitations. At least three factors may prevent the oversight duty doctrine from affecting meaningful change in corporate culture.

The first limitation concerns the courts. Even in its revised version, courts in *Caremark* litigation still employ a largely deferential mode of review.[198] The courts tend to focus on the procedures that the board has adopted, and (often justifiably) refrain from second-guessing concrete decisions on what to discuss or how to address thorny issues. As a result, directors and officers might emerge unscathed as long as they ensure that the company puts in place the right procedures. In other words, putting in place a functioning compliance program might effectively shield directors from liability, even if their company doesn't emphasize ethical behavior.[199]

In theory, the courts can overcome this limitation by adopting a less deferential mode, probing more deeply into directors' oversight of culture and seeing through sophisticated sounding compliance programs. However, a more aggressive mode of judicial review comes with its own set of costs. Corporate law in general has always guarded against the danger of judicial hindsight bias. And in our context, the specter of hindsight bias looms especially large. After all, culture is not a tractable concept. As a result, judges' assessments of the prevalent culture and what any individual did to shape it are likely to be more art than science, and to be heavily influenced by the judges' own priors and biases.[200] Furthermore, even if judges manage to probe accurately (that is, to be proactive while somehow neutralizing their biases), they still probe according to a bad-faith standard. Good-faith efforts that fail and yield unhealthy corporate culture are not legally actionable.[201]

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[197] Shapira, *Books and Records*, *supra* note 156; Gideon Mark, *Confidential Witnesses in Securities Litigation*, 36 J. CORP. L. 551, 554 (2011). This is yet another factor that may be changing now, following Delaware's overhaul of Section 220.

[198] Jennifer Arlen, *Evolution of Director Oversight Duties and Liability under Caremark: Using Enhanced Information-Acquisition Duties in the Public Interest*, *in* RESEARCH HANDBOOK ON CORPORATE LIABILITY 194 (Martin Petrin & Christian Anton Witting, eds., 2023).

[199] Root Martinez, *More Meaningful Ethics*, *supra* note 12.

[200] *Cf.* Langevoort, *The Effects of Shareholder Primacy*, *supra* note 42, at 390 (discussing the biases involved in researching corporate culture).

[201] *Cf.* Hess, *supra* note 35, at 323 (explaining why even good-faith efforts often yield paper compliance programs). To be sure, the new mode of *Caremark* litigation partially ameliorates this problem. Because pleadings these days tend to be very detailed (based on expansive pre-filing discovery and information coming from preexisting regulatory enforcement actions), the courts can better distinguish between genuine and not-so-genuine commitment to a culture of compliance. In the *Walmart* case, for example, the court

The second limitation concerns the plaintiffs. Plaintiffs in corporate law litigation do not necessarily seek to fix corporate culture.[202] Derivative actions are driven by entrepreneurial plaintiff attorneys, who seek to maximize the return on their investment. These "bounty hunters" cannot be trusted to fight for ethical culture and enforce broader societal concerns, or so the argument goes. Plaintiff attorneys may opt not to pursue certain types of corporate misbehavior, such as those where the company gets away with externalizing costs on others (provided no harm is done to shareholders). When plaintiff attorneys do select a case to pursue, they may opt to settle it early and confidentially, in ways that dilute individual accountability for flawed culture.

The key to overcoming this limitation is to calibrate the plaintiff attorneys' incentives so that they receive large bounties only when promoting the overall level of corporate governance. In that regard, the revamped mode of *Caremark* litigation seems to be heading in the right direction: plaintiff attorneys get to collect hefty fees only if they conduct thorough prefiling investigations that yield new information tying the directors to the corporate trauma. In the *Boeing* example, the plaintiff attorneys received a nice share of the largest settlement ever in such cases, but not before they scoured 630,000 pages of internal documents and painstakingly detailed the roles of specific directors and officers in allowing a flawed culture of integrity that led to the debacle.[203] In other words, the plaintiff attorneys collected large bounties only after they promoted individual accountability on the part of directors and officers.[204]

The third limitation of oversight duty litigation concerns the defendants. The defendants in these cases have traditionally been mostly nonexecutive directors, whose influence on corporate culture may be limited.[205] Nonexecutive directors tend to be removed from on-the-ground operations.[206] They merely attend periodic board meetings, where they eat what they are fed by management. As a result, even a perfectly calibrated oversight duty doctrine

emphasized how the same compliance program that failed to catch opioid diversion was far more successful in relation to its internal anti-theft program (while the former externalizes costs on society, the latter saves costs for the company). Walmart II, 2003 Del. Ch. LEXIS 92, at *103.

[202] *See* Stephen M. Bainbridge, *Don't Compound the Caremark Mistake by Extending It to ESG Oversight*, 77 BUS. LAW. 651, 673 (2022).

[203] Shapira, *Max Oversight Duties*, *supra* note 151.

[204] Boeing could also serve as a case study for how holding top individuals accountable in derivative litigation may not be enough to fix a flawed corporate culture. As of this writing, Boeing is again embroiled in a series of events implicating its safety culture. Maizel, *supra* note 28,

[205] David R. Beatty, C.M., O.B.E., *Field Visits by Directors,* HARV. L. SCH. F. ON CORP. GOVERNANCE (Feb. 15, 2018), https://corpgov.law.harvard.edu/2018/02/15/field-visits-by-directors/ ("You can understand nothing, absolutely nothing, about the operating culture of any company by sitting around the boardroom table"); Maizel, *id*.

[206] *Cf. un re* Countrywide Fin. Crop. Derivative Litig., 554 F. Supp. 2d 1044, 2008 U.S. Dist. Lexis 40754, at *52–53, *102–04 (distinguishing for *Caremark* purposes between inside and outside directors).

may not be enough to nudge these directors to do something that they cannot do (root out flawed culture).[207]

Nevertheless, we should not overstate this limitation. As with many other aspects of corporate behavior in which they are involved, directors need not be on the plant's floor to make an impact: they can set the tone for managers in ways that nudge the latter to commit to a culture of compliance.[208] And by probing managers about the corporate culture, outside directors can ensure upward information flows, thereby countering the "willful blindness" and "fragmentation of knowledge" dynamics that we discussed earlier.[209]

Further, several 2023 corporate law cases clarified that oversight duties apply to corporate *officers* too.[210] In *McDonald's*, for example, the underlying issue was a "party" culture in the worst sense (rampant sexual misconduct). The court held that the company's Chief People Officer, whose remit is to ensure that the work environment does not become toxic, may face liability for not doing enough to address a toxic culture. Following *McDonald's*, more plaintiffs have started collecting information on officers' oversight efforts and naming officers as defendants. And while there exist some important differences between the likelihood of officers' oversight liability and that of directors' oversight liability,[211] for our purposes what matters is that the prospect of officers' oversight liability is likely to improve officers' commitment to a culture of compliance.

To these three general limitations of addressing flawed culture via corporate law litigation, one must now add developments from 2025, which could dilute the prospect of such litigation. The backdrop to this development, in brief, is that prominent corporate insiders decried the Delaware Court of Chancery's recent tendency to hold insiders accountable. Some of these insiders, such as Elon Musk, reincorporated their company out of Delaware or threatened to do so. Responding to this, in March 2025 the Delaware legislature passed a sweeping overhaul to its corporate law, supposedly to curtail the threat of exiting Delaware (DExit). Two aspects of this development are pertinent for our purposes of corporate law's ability to generate accountability for flawed corporate culture. First, as Section A above mentioned, Delaware's senate bill from March 2025 cabined shareholders' inspection rights in ways that may limit outside shareholders' ability to hold corporate insiders accountable for how they

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[207] *Corporate Governance Panel Question: Do You Think Corporate Culture Has Any Role to Play in Effective Governance?* PROFESSORBAINBRIDGE.COM (Oct. 30, 2023), https://www.professorbainbridge.com/professorbainbridgecom/2023/10/corporate-governance-panel-question-do-you-think-corporate-culture-has-any-role-to-play-in-effective.html ("while I agree with those who would argue that 'tone from the top' is crucial for creating effective and ethical corporate cultures, I suspect that the 'top' for this purpose is the C-suite"); Bird, *supra* note 94, at 110 ("Any culture change, and especially one that aspires to integrity-based principles, cannot happen merely through a board mandate").
[208] *Cf.* Bird, *id*. at 103 ("Effective boards both direct and set an example for executives to follow").
[209] *See, e.g.*, Walmart II, 2003 Del. Ch. LEXIS 92, at *147 ("Driving adverse information to the board-level thus becomes the mechanism for improved compliance").
[210] McDonald's I, *supra* note 140, at 370.
[211] Roy Shapira, *Conceptualizing Caremark*, 100 IND. L. J. 465, 521-22 (2025).

set information flows, incentives, and norms. Second, the competition between states over incorporations may create a race between the states over which state provides the most effective protection to corporate insiders from the need to ensure legal compliance.[212]

Regardless of how this recent development plays out, the upshot is that just like with criminal law, corporate law's oversight duty doctrine cannot fix all culture-related flaws on its own. Our argument here should therefore be read more modestly: we do not claim that corporate law is categorically better than criminal law in generating accountability for flawed corporate culture. We simply claim that the oversight duty doctrine as currently construed is better suited to hold individuals accountable for flawed culture relative to the doctrine's prior versions. More importantly, we claim that oversight duties should be looked at as another tool in the toolbox of enforcement mechanisms that improve flawed culture. The strengths and weaknesses of the corporate law channel counterbalance the strengths and weaknesses of the criminal law channel.

The next two Parts elaborate on this point of differential effectiveness. Part IV examines how other legal systems employ diverse legal mechanisms, which differ from the private litigation mode of US corporate law. Part V explores the pros and cons of the civil law channel relative to the criminal law channel, and considers policy implications.

IV. COMPARATIVE LESSONS: HOLDING INDIVIDUALS ACCOUNTABLE FOR FLAWED CULTURE WITHOUT PRIVATE LITIGATION

The previous Part focused on one corporate law channel for holding directors accountable, namely, oversight duty litigation under Delaware's *Caremark* model. But outside the US, the prospect of such derivative litigation is largely irrelevant, and accountability for flawed culture comes from other mechanisms. To illustrate the variation, this Part focuses on two examples of countries with similar common law legal systems to the US, namely, Australia and the UK.

In the UK, a plethora of procedural hurdles render litigation largely irrelevant. Accountability for flawed corporate culture in the UK seemingly stems mainly from a combination of soft law (such as codes of corporate governance and best practices guidelines), and institutional investor power. In Australia, accountability for flawed corporate culture comes predominantly from public enforcement by a dedicated corporate regulator. Learning from the accumulated wisdom on what works and what does not in these two different models could inform our understanding of how to better calibrate mechanisms to address flawed corporate culture going forward.

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[212] William J. Moon, Havens for Corporate Lawbreaking, WASH. U. L. REV. (forthcoming), https://ssrn.com/abstract=5148347 (analyzing the ramifications of the current state corporate law competition).

A. *Enforcement Lessons from the UK*

On paper, the threat of directors' liability for flawed corporate culture appears much higher in the UK than it does in the US. For one thing, UK courts measure the care and diligence required of directors against a more demanding standard (closer to regular negligence) relative to US courts (gross negligence).[213] Further, UK corporate law does not formally recognize the business judgment rule abstention doctrine, nor does it permit exculpation clauses in the way that US corporate law does.[214] And, significantly for claims implicating flawed corporate culture, UK corporate law explicitly requires directors to consider a range of stakeholder interests in fulfilling their duties.[215]

In practice, however, British directors and officers face a lower risk of oversight duty litigation than their US and Australian counterparts.[216] Unlike in the US, procedural factors such as a loser-pays rule make British shareholders wary of initiating derivative actions unless they are confident of their success.[217] As a result, private enforcement actions are "close to zero."[218] And unlike in the Australian system (which is discussed further in the next section), there is no enforcement of directors' duties by a dedicated corporate regulator in the UK.[219] Most recently, the 2023 *ClientEarth* decision poured even more cold water on the prospect of oversight duty litigation.[220] The plaintiff there claimed that a series of omissions and actions by Shell's directors regarding oversight of climate change risk constituted a breach of directors' duties.[221] The court ruled in favor of the defendants, reasoning that the proper forum for holding directors

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[213] Under UK law, the most apposite duty for assessing oversight breaches is the duty of care, skill and diligence. Companies Act 2006*,* §174 (UK); Re D'Jan of London Ltd [1993] B.C.C. 646; Norman v Theodore Goddard [1991] BCLC 1028.
[214] Companies Act 2006*,* §232(1) (UK).
[215] *Id.* at §172(1).
[216] *See* Moore, *supra* note 17. *See also* John Armour et al., *Private Enforcement of Corporate Law: An Empirical Comparison of the United Kingdom and the United States*, 6 J. EMPIRICAL LEGAL STUD. 687, 699–700, 710 (2009) (finding evidence for the relative dearth of private litigation over directors' failures in the UK); Joan Loughrey, *The Director's Duty of Care and Skill and the Financial Crisis*, *in* DIRECTORS' DUTIES AND SHAREHOLDER LITIGATION IN THE WAKE OF THE FINANCIAL CRISIS 12, 12–13 (Joan Loughrey ed., 2013) (lamenting how even in the wake of the global financial crisis, where blame could relatively easily be traced to board policies, there were no legal repercussions against directors); Andrew Keay & Michelle Welsh, *Enforcing Breaches of Directors' Duties by a Public Body and Antipodean Experiences*, 15 J. CORP. LEGAL STUD. 255, 276–77 (2015) (noting same).
[217] *See* Armour et al., *id*; Richard Meeran, *Access to Justice for Victims of Transnational Corporate Human Rights Abuses: A UK Perspective*, 32 U. PA. J. INT'L L. 1, 45 (2010) (on the limited role of contingency fees arrangements, which also make shareholders wary of initiating high-stakes derivative suits).
[218] John Armour, *Enforcement Strategies in UK Corporate Governance: A Roadmap and Empirical Assessment*, *in* RATIONALITY IN COMPANY LAW 213 (John Armour & Jennifer Payne, eds., 2009).
[219] Keay & Welsh, *supra* note 216, at 276.
[220] ClientEarth v Shell plc [2023] EWHC 1137 (Ch).
[221] *Id*. at 4, 20–22.

accountable in such matters is the shareholders' annual meetings rather than the courtroom.[222]

British scholars and policymakers have long lamented these hurdles for private enforcement as creating an "accountability firewall."[223] And a 2025 study reaffirms just how rarely private enforcement of directors' diligence occurs.[224]

Could it be, then, that in the UK there is no conduit for holding directors accountable for flawed corporate culture? A closer look reveals, perhaps unsurprisingly, that the answer is more nuanced: the corporate governance ecosystem in the UK has developed several alternative accountability mechanisms. Consider the following four and their applicability to flawed culture: soft law, director disqualification proceedings, entity criminal liability, and reputational sanctions.

First, the UK is an international leader in the use of corporate governance codes.[225] While corporate codes do not promote accountability for failed governance ex post, they can create norms that improve the quality of governance ex ante, and, in some instances, may be more important than formal legal rules in affecting the behavior of corporate actors.[226] In the context of improving corporate culture, the UK Corporate Governance Code explicitly requires directors to "act with integrity, lead by example and *promote the desired culture*."[227] Specific financial regulators have similarly alluded to ethical culture: the Financial Reporting Council states that the board should "set the company's purpose, values, and strategy, and satisfy itself that these and its culture are aligned."[228] And the Financial Conduct Authority has instituted a Senior Managers Certification Regime, which provides a clear roadmap of the responsibilities of officers within financial institutions regarding their institution's culture.[229]

Still, while corporate governance codes can serve as a starting point for promoting ethical values, they are unlikely to be sufficient on their own to drive

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222 *Id*. at 6.
223 *See* Joan Loughrey, *Breaching the Accountability Firewall: Market Norms and the Reasonable Director*, 37 SEATTLE U.L. REV. 989, 989 (2014).
224 Jenifer Varzaly & Christopher Riley, Artificial Intelligence and Directors' Duties (working paper, 2025) (on file with the authors), manuscript at 33-35.
225 *See* Jennifer G. Hill, *Transnational Migration of Corporate Law and Norms in Corporate Governance: Fiduciary Duties and Corporate Codes*, *in* TRANSNATIONAL FIDUCIARY LAW 216, 225-35 (Seth Davis et al. eds., 2024).
226 *See* John C. Coffee Jr., *Do Norms Matter? A Cross-Country Evaluation*, 149 U. PA. L. REV. 2151, 2154 (2001).
227 FINANCIAL REPORTING COUNCIL, THE UK CORPORATE GOVERNANCE CODE, 6 (2024), Section 1, Principal B [emphasis added].
228 *Id*. *See also* Hess, *supra* note 35, at 322.
229 FINANCIAL CONDUCT AUTHORITY, THE SENIOR MANAGERS AND CERTIFICATION REGIME: GUIDE FOR FCA SOLO-REGULATED FIRMS (2019); Eleanore Hickman, *Is the Senior Managers and Certification Regime Changing Banking for Good?*, 85 MODERN L. REV. 1440, 1443 (2022) (describing the regime as a dramatic change in individual accountability). *See also* Keller & Kokkinis, *supra* note 77, at 314–18.

meaningful change in corporate culture.[230] Corporate culture is deeply ingrained and shaped by factors such as economic incentives, tone at the top, and longstanding informal norms. These are the kinds of factors that are not easily swayed by aspirational statements of best practices. Further, the abovementioned provisions tend to be broad and vague. As a result, even businesspersons who wish to follow them will have a hard time translating abstract hortatory appeals into practical day-to-day prescriptions on how to change behavior. To move the needle, codes must have some bite to them, in the sense of specific mechanisms that monitor, enforce, and incentivize ethical behavior.[231] Indeed, some UK codes of best practice and reform initiatives in the financial sector have been criticized for failing to fulfil their promise in helping improve culture, and for leading to companies "taking an unambitious tick-box approach to culture, reliant on quantitative metrics of doubtful value."[232]

A second possible accountability mechanism for flawed corporate culture is public enforcement. Several UK regulators, such as the Financial Reporting Council and the Financial Conduct Authority, can initiate enforcement actions on specified corporate governance issues.[233] Other regulators can initiate proceedings for court-ordered disqualification of company directors. This process prohibits directors who are found guilty of "unfit conduct" from serving as company directors for a specified period.[234]

While these public enforcement conduits are seemingly effective when the directors themselves are personally involved in wrongdoing, they are very limited in their ability to generate accountability for flawed corporate culture. The bar for disqualification is very high,[235] and the threat is rarely relevant for directors of publicly traded companies and nonexecutive directors.[236]

A third possible conduit for accountability is entity criminal liability. Unlike the US expansive vicarious liability approach, the UK has historically applied the much more limited *Tesco* identification doctrine.[237] *Tesco* effectively

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[230] *Cf.* Su-Ping Lu, *Corporate Codes of Conduct and the FTC: Advancing Human Rights through Deceptive Advertising Law*, 38 COLUM. J. TRANSNAT'L L. 603, 614–18 (2000) (compiling arguments for the inability of codes of conduct and best practices to affect meaningful change in corporate behavior in the context of human rights).

[231] *Cf.* Harvey L. Pitt & Karl A. Groskaufmanis, *Minimizing Corporate Civil & Criminal Liability: A Second Look at Corporate Codes of Conduct*, 78 GEO. L.J. 1559, 1630 (1990) (arguing that private corporate codes have little legal significance).

[232] Keller & Mokkinis, *supra* note 77, at 333.

[233] *See generally* John Armour, *Enforcement Strategies in UK Corporate Governance: A Roadmap and Empirical Assessment*, *in* THE LAW AND ECONOMICS OF CORPORATE GOVERNANCE: CHANGING PERSPECTIVES 213, 231 (Alessio M. Pacces, ed., 2010) (discussing public enforcement in the United Kingdom).

[234] Company Directors Disqualification Act 1986.

[235] Herbert Smith Freehills, *Insight: Directors' Duties Under Siege - The Status Quo Prevails* (Jun. 19, 2024), https://www.herbertsmithfreehills.com/insights/2024-06/directors-duties-under-siege-the-status-quo-prevails.

[236] John Armour et al., *Private Enforcement of Corporate Law: An Empirical Comparison of the United Kingdom and the United States*, 6 J. EMPIR. LEGAL STUD. 687, 716 (2009).

[237] Tesco Supermarkets Ltd v. Nattrass [1972] A.C. 153.

protected companies from criminal liability unless the wrongdoing was authorized by a senior officer or at the board level.[238] Such a test is typically irrelevant for large corporations. More recently, however, UK courts have sought different tests, such as a "failure to prevent" model of liability, which can be more relevant to the scenarios that we deal with here.[239] Still, the failure to prevent model is restricted to specified offenses such as bribery, tax evasion and, more recently, certain fraud offenses in large corporations.[240]

Finally, another conduit for accountability for flawed culture is nonlegal (reputational) sanctions. Indeed, corporate governance scholars have long suggested that reputational sanctions may be the most forceful deterrent in the UK corporate governance ecosystem.[241] Large institutional investors enjoy outsized influence in the UK, due to a combination of the ownership structure in capital markets and strong shareholder rights.[242] These repeat players therefore tend to enforce behavior according to market norms. While we are sympathetic to the reputational-discipline argument, we note that reputational discipline is limited to certain types of corporate misconduct: reputational sanctions are pronounced in misconduct against investors, but they are attenuated in misconduct affecting third parties (such as pollution).[243]

B. *Enforcement Lessons from Australia?*

Corporate culture has become "a dominant feature of the Australian commercial regulatory landscape."[244] But our question of how to hold those at the top accountable for flawed culture has not been completely answered there either. Much like in the US, Australian corporate law has long recognized that directors have an obligation to oversee risks,[245] and that as part of this obligation, directors must ensure that their company installs proper information systems that report to the board.[246]

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[238] *See* Jennifer G. Hill, *Corporate Criminal Liability in Australia: An Evolving Corporate Governance Technique?* J. BUS. L. 1, 10-14 (2003); Elise Bant, *Catching the Corporate Conscience: A New Model of "Systems Intentionally"*, LLOYD'S MARITIME AND COMMERCIAL L.Q. 467, 468-70 (2022).
[239] *See* Ross Grantham, *Attributing Responsibility to Corporate Entities: A Doctrinal Approach* (2001) 19 CO. & SEC. L.J. 168, 174-75.
[240] *See e.g.,* Bribery Act 2010, § 7 (UK); Criminal Finances Act 2017, Part 3, §§ 45, 46; Economic Crimes and Corporate Transparency Act 2023 (UK).
[241] *See* John Armour, Colin Mayer & Andrea Polo, *Regulatory Sanctions and Reputational Damage in Financial Markets*, 52 J. FIN AND QUANT. ANAL. 1429 (2017) (providing empirical evidence that reputational sanctions often dwarf legal sanctions).
[242] Armour, *supra* note 233.
[243] *Id*, 1430-1431.
[244] *See* Bant, *supra* note 238, at 480 (stating that this dominance reflects "foundational community expectations of Australian corporate citizens.")
[245] *See* Daniels v Anderson (1995) 37 NSWLR 438, 503–04; Australian Securities and Investments Commission v Adler (2002) 168 FLR 253, [372], (8).
[246] Adler, *id.* at 13. In fact, one could claim that the liability standard for breach of oversight duty is more exacting in Australia than it is in the US. *See generally* Geoffrey Nettle, *The Changing Positions and Duties of Company Directors*, 41 MELB. U. L. REV. 1402 (2018) (discussing the trajectory of the duty of care in Australia); Greg Golding, *Tightening the Screws on Directors: Care, Delegation and Reliance*, 35 UNSW

The main difference between the US and Australia is not in what the oversight duty standard is but rather in who enforces the standard. Australia predominantly relies on a *public* enforcement model.[247] The Australian Securities and Investments Commission (ASIC) is the corporate regulator bringing enforcement actions against directors who have supposedly breached their fiduciary duties, under a "civil penalty" regime.[248] These public enforcement actions (which operate alongside a private enforcement model) have traditionally focused on directors' breaches of the duty of care and enjoyed a relatively high success rate.[249]

While there has been a lively debate about the merits of such a model,[250] for our purposes it is noteworthy that the model is well-suited to holding directors accountable for flawed corporate culture. Indeed, in recent years the Australian regulator has been selecting cases for enforcement that (1) send a strong deterrent message; (2) increasingly emphasize the "public" aspects of directors' duties, thereby nudging directors to think not just about the company's short-term profits, and (3) increasingly rely on *Caremark*-style claims, thereby nudging directors to prioritize compliance.[251]

A good example of the emphasis on the social functions that directors' duties carry is the *Healey* case, which stressed that "the role of a director is

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L.J. 266, 270–71 (2012) (same). Further, the Australian version of the business judgment rule offers narrower protection than its US counterpart. *Corporations Act* 2001 (Cth.) s 180(2) (Austl.); Nettle, *id*; Jennifer G. Hill & Matthew Conaglen, *Directors' Duties and Legal Safe Harbours: A Comparative Analysis*, *in* RESEARCH HANDBOOK ON FIDUCIARY LAW 305 (D. Gordon Smith & Andrew S. Gold, eds., 2018).

[247] *See* Renee M. Jones & Michelle Welsh, *Toward a Public Enforcement Model for Directors' Duty of Oversight*, 45 VAND. J. TRANSNAT'L L. 343 (2012) (comparing the US and Australian enforcement models); Jennifer Varzaly, *The Enforcement of Directors' Duties in Australia: An Empirical Analysis*, 16 EUROPEAN BUS. ORG. L. REV. 281 (2015) (providing evidence that the dominant enforcement mode for breaches of directors' duties in Australian public companies is public enforcement by the business conduct regulator). *See also* Brian R. Cheffins & Bernard S. Black, *Outside Director Liability across Countries*, 84 TEXAS L. REV. 1385, 1438–41 (2006).

[248] *Corporations Act* 2001 (Cth.), Pt 9.4B; s 1317E(1) (Austl.). For a detailed analysis of ASIC's enforcement *see generally* VICKY COMINO, AUSTRALIA'S 'COMPANY LAW WATCHDOG': ASIC AND CORPORATE LAW REGULATION (2015).

[249] *See* Varzaly, *supra* note 247, at 285, 316 (noting that whereas public enforcement in Australia tends to focus on breaches of directors' duty of care and the duty to prevent insolvent trading, private enforcement is more likely to involve breaches of the duties of loyalty); Ian Ramsay & Benjamin Saunders, *An Analysis of the Enforcement of the Statutory Duty of Care by ASIC*, 36 CO. & SEC. L.J. 497, 510–11 (2019); Golding, *supra* note 246, at 273–74. We note that there have been criticisms directed at ASIC's enforcement record, particularly the regulator's heavy reliance on negotiated settlements prior to the 2019 Banking Royal Commission. *See, e.g.*, Vicky Comino, *ASIC and Civil Penalties – 30 Years On: Is it "Fit for Purpose"*, GRIFFITH L. REV. (forthcoming.

[250] *See, e.g.*, Varzaly, *supra* note 247, at 304 (providing empirical evidence on the differences between the Australian and the UK models); John C. Coffee, Jr., *Law and the Market: The Impact of Enforcement*, 156 U. PA. L. REV. 229, 281 (2007) (commenting on the similarities between the Australian model and SEC enforcement in the US).

[251] *See, e.g., Australian Securities and Investments Commission v Cassimatis (No 8)* [2016] FCA 1023 (Aug. 26, 2016) [455, 461, 480–83] (Austl.) (ruling that the "foreseeable risk of harm" to the company, which is a component of the statutory duty of care under Australia's Corporations Act, should not be construed as limited to financial harm, but can also include matters such as long-term reputational harms). *See also* Comino, *supra* note 246, 10-11 (noting ASIC's 2022 launch of civil penalty proceedings against the directors of Star Casino for breach of the duty of care after several inquiries into the casino's operations).

significant as their actions may have a profound effect on the community, and not just shareholders, employees and creditors."[252] More recently, Australian regulators and notable commentators have suggested that directors who do not proactively address climate change risks to their company could face personal liability for breach of the duty of care.[253] Such a perspective lends itself to addressing flawed culture that puts profits over safety or profits over environmental degradation.

The emphasis on the social aspects of directors' obligations was coupled with an emphasis on bringing more "stepping-stone" liability claims, which are akin to *Caremark* claims.[254] In a nutshell, stepping-stone claims consist of two steps: first, showing that the corporation contravened a law; and second, showing that directors failed to take care to prevent said contravention. Just like *Caremark*, the theory behind stepping-stone claims is that the board of directors is the organ required to engage in oversight of serious compliance risks. When the board allows others in the company to violate laws, it does so at its company's own peril, exposing the company to legal and reputational sanctions.[255] As Part III above just demonstrated, litigation of such claims often involves discovery and examinations of the ethicality of the corporate culture and tone at the top.

To be sure, the public enforcement channel is not the only accountability conduit: accountability for flawed culture in Australia also emanates from soft law measures, entity criminal liability, and reputational sanctions. The accumulated experience with these channels resembles that of the UK. Australia too boasts an influential corporate governance code. This code states that listed companies should "instil and reinforce a culture across the organisation of

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[252] *Australian Securities and Investments Commission v Healey* [2011] FCA 717 (27 June 2011) [14]. *See generally* Jennifer G. Hill, *Centro and the Monitoring Board – Legal Duties Versus Aspirational Ideals in Corporate Governance*, 35 UNSW L.J. 341 (2012).

[253] *See, e.g.*, THE CENTRE FOR POLICY DEVELOPMENT AND THE FUTURE BUSINESS COUNCIL, "CLIMATE CHANGE AND DIRECTORS' DUTIES," SUPPLEMENTARY MEMORANDUM OF OPINION (2021); John Price, Climate Change, Keynote address at Centre for Policy Development: Financing a Sustainable Economy (Jun. 18, 2018) (transcript available in ASIC) (a speech by then-ASIC commissioner); Geoff Summerhayes, Australia's New Horizon: Climate Change Challenges and Prudential Risk, Speech delivered at Insurance Council of Australia Annual Forum, Sydney (Feb. 17, 2017) (transcript available in Center for Policy Development) (a speech by then-APRA commissioner); *Is Your Organisation's Climate Risk Management up to Scratch?* AUSTL. INST. CO. DIR'S (Apr. 1, 2020), https://aicd.companydirectors.com.au/membership/company-director-magazine/2020-back-editions/april/is-your-organisations-climate-risk-management-up-to-scratch (stating that Australian regulators now "speak as one" in their view that directors may be liable in relation to climate-related risks).

[254] *See generally* Abe Herzberg & Helen Anderson, *Stepping-Stone: From Corporate Fault to Directors' Personal Civil Liability* 40 FED. L. REV. 181 (2012) (detailing the evolution of stepping-stone liability).

[255] Although some judges have expressed concern about stepping-stone liability being used as a backdoor means of imposing accessorial liability on directors, this type of liability has been increasingly favored by ASIC. *See generally Australian Securities & Investments Commission v Maxwell & ors* [2006] NSWSC 1052 (Oct. 10, 2006) [104]–[106] (Austrl.); *Australian Securities and Investments Commission, in the matter of Sino Australia Oil and Gas Limited (in liq.) v Sino Australia Oil and Gas Limited (in liq.)* [2016] FCA 934 (Aug. 11, 2016) [85]–[86] (Austrl.); *Australian Securities and Investments Commission v Cassimatis (No. 8)* [2016] FCA 1023 (Aug. 26, 2016) (Austl.). *See also* Ramsay & Saunders, *supra* note 249, at 519.

acting lawfully, ethically and responsibly," and explains that it is the board's role "to oversee an appropriate corporate culture."[256]

In the context of entity criminal liability, Australia introduced a novel criminal code in the mid-1990s. This code included significant "corporate culture" reforms, which were underpinned by the idea of organizational fault and blameworthiness.[257] But, just like in the UK, this state-of-the-art criminal liability model has rarely been used and its efficacy is in doubt.[258] The key corporate criminal provisions, for example, have been marginalized, via exclusion from a wide range of Commonwealth statutes that have particular relevance to corporations.[259]

Importantly, reputational sanctions through institutional investor pressure are a viable accountability mechanism in Australia. What makes this mechanism potent is that Australia, like the UK, has high levels of institutional shareholder ownership[260] and strong mandatory shareholder rights.[261] A good illustration of reputational discipline at work comes from a 2020 activist shareholder campaign against Rio Tinto, one of the world's largest mining companies.[262] Rio suffered a safety debacle that destroyed two 46,000-year-old Aboriginal cultural heritage sites. Postmortem analysis revealed deep-seated deficiencies in Rio's processes and work culture. In response, Australian pension funds collaborated with international institutional investors to mount a campaign that ended up forcing the company's CEO and other top executives to leave.[263] However, in less salient debacles, it is far from clear that investor pressure can consistently generate accountability for flawed culture.

Our comparative analysis of the UK and Australian models of enforcement demonstrates that no single accountability mechanism is a silver bullet when it comes to flawed corporate culture. Even the mechanisms that seem at first glance to be potent, such as the public enforcement model, receive

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[256] ASX Corporate Governance Council, Corporate Governance Council, *Corporate Governance Principles and Recommendations Consultation Draft*, 4th ed. (Feb. 2019), Principle 3.

[257] Criminal Code Act 1995 (Cth.), §12.3. *See* Vicky Comino, *'Corporate Culture' is the 'New Black' – Its Possibilities and Limits as a Regulatory Mechanism for Corporations and Financial Institutions?*, 44 UNSW L.J. 295, 301–303 (2021) (discussing how the "corporate culture" provisions of the Act overcame the narrow operation of the *Tesco* identification doctrine); BANT, *supra* note 235, at 480–81 (comparing the Act's "corporate culture" provisions with the concept of "systems intentionality").

[258] *See* AUSTRALIAN LAW REFORM COMMISSION, CORPORATE CRIMINAL LIABILITY—THE CASE FOR REFORM (2020), https://www.alrc.gov.au/news/corporate-criminal-responsibility-the-case-for-reform/ (noting that because the new construct has been so rarely used, there is limited judicial guidance on its application).

[259].*See e.g.*, *See* AUSTRALIAN LAW REFORM COMMISSION, CORPORATE CRIMINAL RESPONIBILITY, FINAL REPORT, ALRC REPORT 136 (2020), [2.78]–[2.83], https://www.alrc.gov.au/wp-content/uploads/2020/05/ALRC-CCR-Final-Report-websml.pdf; Comino, *supra* note 254, at 303.

[260] *See* generally Jenifer Varzaly, *The Effectiveness of Disclosure Law Enforcement in Australia*, 21 J. CORP. L. STUD. 135 (2021); TIM BOWLEY, ACTIVIST SHAREHOLDERS IN CORPORATE GOVERNANCE: THE AUSTRALIAN EXPERIENCE AND ITS COMPARATIVE IMPLICATIONS Chap. 3 (2024).

[261] *See generally* Jennifer G Hill, *Subverting Shareholder Rights: Lessons from News Corp's Migration to Delaware*, 63 VAND. L. REV. 1 (2010) (on the difference between Australia and the US in that regard).

[262] *See* Tim Bowley & Jennifer G. Hill, *The Global ESG Stewardship Ecosystem*, 25 EUR. BUS. ORG. L. REV. 229, 243-246 (2024).

[263] *See* Peter Ker, *CEO Blasted Out: Australia to Regain Rio Control*, AUSTL. FIN. REV. (Sep. 12, 2020).

their own share of criticisms.[264] Indeed, the relative effectiveness of each mechanism depends on various country-specific factors such as capital market structure, shareholder statutory rights, fee-shifting rules, and regulators' enforcement resources. We therefore do not proclaim that one mechanism is categorically better than others. Instead, we aim more modestly to highlight the different advantages and disadvantages of each mechanism, and to identify the conditions under which the mechanisms operate synergistically so that one mechanism's advantages balance the other's flaws.

V. IMPLICATIONS

Our story thus far has been straightforward: corporate culture plays a pivotal role in shaping the conduct of corporations. A flawed corporate culture can lead organizations to missteps, rule violations, and even corporate disasters. To address these flaws, one must first understand their origins. In today's world, where most large corporations already invest billions in compliance programs and boast exacting policies, the origin of flawed corporate culture usually lies at the top. When those at the top of the corporation promulgate perverse economic incentives, do not ensure that crucial information flows to the top, and set the wrong example, the corporate culture is likely to be unethical, regardless of how impressive the written policies and programs are. To address flawed corporate culture in large organizations, one must therefore hold those at the top accountable. Against this backdrop, we have analyzed different conduits for holding corporate decision-makers accountable for flawed corporate culture: from criminal law to corporate law's oversight duty litigation, to soft law, to public enforcement of corporate and securities law.

The next step in our analysis is to derive real-world implications. Section A takes stock of our comparative institutional analysis and highlights the relative pros and cons of the different methods for holding directors and officers accountable. Section B then generates concrete recommendations for practitioners and policymakers. For example, key lessons for directors include the need to map their company's central compliance risks and ensure that management escalates information on these risks to the board level. And for judges, a key lesson concerns the need to ensure that shareholders enjoy broad inspection rights to investigate directors' role in flawed corporate culture.

A. Taking Stock: Comparing the Different Conduits for Accountability

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[264] For example, one could criticize this model for blurring the traditional boundaries between criminal and civil law. On the boundaries *see generally* Kenneth Mann, *Punitive Civil Sanctions: The Middleground between Criminal and Civil Law*, 101 YALE L.J. 1795 (1992) (noting the traditional view that the role of criminal law is to punish, and the role of civil law is to compensate). On the blurring of boundaries *see generally* John C. Coffee, Jr., *Paradigms Lost: The Blurring of the Criminal and Civil Law Models—And What Can Be Done about It*, 101 YALE L.J. 1875 (1992).

Let us reiterate that our aim is not to portray the different legal conduits for addressing flawed culture as part of a horserace: there is little value in proclaiming that the criminal law channel is generally "better than" the corporate law channel or vice versa. Our goal here is rather to compare the differential effectiveness of each channel. Developing a better understanding of each channel's strengths and weaknesses is an important step before jumping to policy prescriptions. Such an understanding can help policymakers identify areas where one system's advantages counterbalance the other system's flaws, as well as areas where all existing systems suffer from similar flaws and so different types of legal interventions may be needed.

With that in mind, let us highlight several areas where the revamped mode of oversight duty litigation enjoys advantages over other ways to address flawed corporate culture. At the most basic level, our analysis here highlights the advantages of the post-2019 mode of *Caremark* litigation over its pre-2019 mode. In the old *Caremark* era, the message coming from courts was interpreted as "just do something."[265] Even if there existed evidence that the company chronically underspent on safety measures and remediation efforts, the court would historically dismiss the case against the directors unless there was smoking-gun evidence indicating that they discussed the problems in real time.[266] In other words, the old *Caremark* era did not necessarily view it as the responsibility of the board to monitor and root out a culture of lawlessness. By contrast, the new *Caremark* era has been described by one notable corporate law commentator as the result of expert judges noticing that "something is wrong with corporate culture" and rewriting the caselaw to address it.[267] In the new *Caremark* era, "just doing something" about compliance policies is not enough: the courts will investigate a firm's culture as an integral part of assessing directors' commitment to compliance.[268]

The revised mode of *Caremark* litigation adds value to the criminal law channel for accountability for flawed culture in at least three important ways, namely, (1) focusing on individuals, (2) relaxing evidentiary hurdles, and (3) providing concrete guidance.

First and most basically, the derivative action channel differs from the public enforcement channel by focusing on those at the top of the corporate hierarchy. Delaware corporate law provides sophisticated bounty hunters (institutional investors and their plaintiff attorneys) with powerful incentives and powerful tools to extract information on directors' involvement in a flawed

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[265] Langevoort, *Cultures of Compliance*, *supra* note 51, at 941.

[266] *See, e.g.*, *in re* GM Co. Derivative Litig., 2015 LEXIS 179, at 53 (Del. Ch., Jun. 26, 2015); Fischman v. Reed, 2017 U.S. Dist. LEXIS 47152, at 5, 15–19, 36 (S.D. Cal., Mar. 29, 2017).

[267] Jennifer Kay & Mike Leonard, *Delaware's Judge Laster is Making His Mark on Corporate America*, BLOOMBERG LAW (Jul. 31, 2023), https://news.bloomberglaw.com/us-law-week/delawares-judge-laster-is-making-his-mark-on-corporate-america (quoting professor Charles Elson).

[268] Walmart II, 2003 Del. Ch. LEXIS 92.

corporate culture.[269] Recall in that respect *Boeing*, where the plaintiffs received access to 630,000 pages of internal communications about Boeing's safety culture, and ultimately received an award of almost $40ml for their role in generating individual accountability for the MAX 737 debacle. The high bar of "bad faith" incentivizes plaintiff attorneys to extract information on how those at the top set information flows, promulgate economic incentives, and lead by example.

To be sure, one can argue that the incentives of private bounty hunters who drive corporate law litigation are less aligned with the public interest than the incentives of public enforcers who drive criminal law enforcement. But when it comes to holding those at the top of giant corporations accountable, one must also consider which of the channels is more susceptible to the risk of "regulatory capture." To illustrate, let us recast the Walmart opioid example: the retail giant managed to quash the indictment and fight back public enforcement by pulling all levers in Washington, including hiring former senior officers at the DOJ to conduct internal investigations.[270] By contrast, Walmart was not able to quash the private enforcement channel, and the *Caremark* case against its directors was upheld (leading the company to ultimately settle it for $123ml). In Facebook's Cambridge Analytica scandal, to use another example, Facebook was accused of agreeing to pay the Federal Trade Commission a much heftier fine ($5bl) in exchange for the regulator waiving personal liability for Mark Zuckerberg.[271] For a regulator trying to maximize the amount of fines collected, trading off individual accountability for a higher settlement award is a winning proposition. In the *Caremark* case against Zuckerberg and Facebook's directors, by contrast, plaintiffs sought an expansive inspection of Zuckerberg's and Sheryl Sandberg's personal emails, and the judge sustained their failure-of-oversight claims.[272]

A second advantage of corporate law litigation is that it relaxes some of the evidentiary hurdles that make criminal law litigation ill adept at promoting individual accountability for flawed corporate culture. In criminal law, proving mens rea of directors and officers is extremely tough given the fragmentation of knowledge in large organizations. To be sure, even in civil law it is extremely difficult to establish causation between a flawed corporate culture and a specific harmful outcome, or between a director's inaction and a flawed corporate culture. But oversight duty litigation, in Delaware specifically, comes with a

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[269] Recall that the "powerful tools" proposition is now under a question mark, as it remains to be seen how the courts will interpret Delaware's March 2025 amendment to shareholders' inspection rights. Section III.C *supra*.
[270] *Id*. at *129.
[271] Leslie A. Pappas, *Facebook Balks at Document Demand over $5 Billion FTC Settlement*, BLOOMBERG L. (Jun. 24, 2020, 4:44 PM), https://news.bloomberglaw.com/esg/facebook-balks-atdocument-demand-over-5-million-ftc-settlement.
[272] Kevin LaCroix, *Court Denies Dismissal Motion in Facebook User Data Privacy Derivative Suit*, D&O DIARY (May 14, 2023), https://www.dandodiary.com/2023/05/articles/shareholders-derivative-litigation/court-denies-dismissal-motion-in-facebook-user-data-privacy-derivative-suit/.

unique procedural stance that ameliorates these evidentiary issues. Recall that most of the action in Delaware litigation happens at the pleading stage, where the courts make all reasonable interpretations and inferences in favor of the plaintiffs.[273] As Section III.A clarified, this front-loaded version of litigation normally does not generate final verdicts in favor of the plaintiffs: the cases where plaintiffs win at the pleading stage because all inferences worked in their favor usually settle quickly after that. Still, this front-loaded version of litigation generates accountability for the defendants, by flushing out inside information on how the directors behaved.

Such a "relaxed" evidentiary stance matters greatly in cases that implicate accountability for flawed culture. In these cases, directors and officers typically play the "I didn't know" card, and try to protect themselves by invoking attorney–client and work–product privileges, and by heavily redacting internal documentation of compliance discussions. In the past couple of years, Delaware courts increasingly employed an antidote for such defense tactics, treating heavy redactions as indications (at the pleading stage) that directors never oversaw a flawed culture, or failed to properly address indications that the culture was flawed.[274] Legal advisors to corporate boards quickly reacted to these rulings by advising their clients to conduct more frequently (and document more meticulously) discussions of compliance risks.[275] This is yet another example of how decisions in the early stages of corporate law litigation can lead to real-world changes in how those at the top of the corporate hierarchy engage in oversight of corporate culture.

Finally, a counterintuitive advantage of oversight duty litigation is that it provides guidance for directors who wish to promote ethical cultures. To understand why this is an advantage, consider first how the criminal law channel operates. In their guidelines for prosecutors, criminal law enforcers have increasingly emphasized the need to assess corporate culture when determining leniency. Yet historically these guidelines did "not provide sufficient guidance to corporations – especially the executives and members of the boards of directors of those corporations"[276] – on what their role should be in promoting a culture of compliance and ethicality. In other words, criminal law sent a signal that culture matters, but it did not clarify for the intended audience (corporate directors) how exactly they can improve their company's culture. Granted, in recent years the DoJ started issuing a frequently updated memo on how to evaluate compliance program, which can help companies better understand what the DoJ looks for when evaluating a company's commitment to

[273] Walmart II, 2003 Del. Ch. LEXIS 92, at *6.
[274] *Id*.
[275] *See, e.g.*, Gail Weinstein et al., *Chancery Rejects Dismissal of Caremark Claims against Walmart's Officers and Directors*, HARV. L. SCH. FORUM ON CORP. GOV. (May 13, 2023), https://corpgov.law.harvard.edu/2023/05/13/chancery-rejects-dismissal-of-caremark-claims-againstwalmarts-officers-and-directors/.
[276] Hess, *supra* note 35, at 346.

compliance.[277] Still, corporate law litigation can provide a more case-specific, practical guidance relative to the very general insights that companies can glean from reading the DoJ's instructions to prosecutors.

The front-loaded mode of Delaware litigation provides ample opportunities for expert judges to comment on what is expected of directors in *specific* situations. The function of providing guidance on what the reasonable director should do is especially valuable in the context of expecting directors to promote ethical culture. By now, there exist well-developed industry standards and norms regarding what makes for an effective *compliance* program.[278] Directors of a large company therefore do not typically need the courts to tell them what compliance protocols should look like. However, there remains much uncertainty in the business world about the drivers of ethical *culture*.[279] Directors need all the guidance that they can get in that regard.

Aside from comparing the current version of corporate law litigation to its previous version or to criminal law enforcement, we can also borrow insights from the accumulated experience with different accountability mechanisms in the UK and Australia. Perhaps the most useful lesson from this cross-country comparison comes from the commonalities: all three legal systems have tried and largely failed to deal with flawed corporate culture via entity criminal liability. The lesson here is that tweaking the model of criminal liability may not be enough, because settled concepts of criminal law are simply not a good match for the intricate task of accountability for flawed culture.

Turning our attention to noncriminal channels, it seems that the Australian model is more promising than the UK one. In the UK, accountability for governance failures predominately rests on market discipline through institutional investors. Such a model may be effective at curbing simple agency problems (insiders tunneling away money from outsiders), but it cannot effectively curb the types of misconduct that stem from a culture that puts profits over, say, safety or environmental degradation. After all, institutional investors are shareholders too, and it is futile to count on them to curb behavior that benefits shareholders while externalizing larger costs on others. The Australian model could serve as a blueprint for those in the US who believe that (1) there should be individual accountability for flawed culture, but also believe that (2) the *Caremark*-private-litigation model is not a good fit for achieving broader societal goals. It seems that the only viable alternative to private oversight duty litigation is public enforcement of oversight duties via a dedicated regulator.

B. *Practical Recommendations*

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[277] Moon, *supra* note 212, manuscript at 46

[278] Root Martinez, *More Meaningful Ethics*, *supra* note 12.

[279] *Id*.

Existing discussions of corporate culture in the legal literature have focused mostly on implications for criminal law, such as advising prosecutors on how best to address culture when deciding whether to grant leniency.[280] This Article, by contrast, focuses on implications for corporate governance (practitioners) and corporate law (judges).

For practitioners, our overarching lesson is the need for boards to play a more active role in overseeing corporate culture. Directors must ensure that they set the right information flows, the right economic incentives, and the right personal examples. Concretely, the first thing that every board should do is identify the risks to corporate culture that are central to their company. Further, boards should allocate responsibility for each such risk to a specific board committee and set clear expectations for management on what information to escalate to the board level, such as indications from hotline calls and whistleblower investigations. The second thing that every board should do is assess how the company's compensation plan reinforces (or undermines) the company's purported culture.[281]

Boards should also think hard about how they can corroborate assertions of the right culture.[282] That is, in today's world most large companies already have in place nice-sounding programs and policies. Where boards can add value is by using new digital tools for board oversight to identify instances where on-the-ground behavior is incompatible with these aspirational proclamations.

For judges, our analysis underscores the importance of adopting liberal interpretations to prefiling discovery doctrines. Private litigation without access to internal communications is unlikely to fulfill its role of promoting ethical corporate culture. The prospect of bounty-hunting plaintiff attorneys searching through the company's internal communications pushes directors to be more active in oversight of culture risk from the start. The analysis here thus lends credence to the court's liberalization of the "proper purpose" and "permissible scope" prongs of Delaware's Section 220.[283]

Our analysis here can also help judges better incorporate culture into their own analysis. Thus far we have focused on how *Caremark* law can help in rooting out bad corporate culture. But the literature on corporate culture can help in revealing bad *Caremark* law too. One of the biggest challenges for judges in such cases is how to infer scienter in large organizations, where knowledge and responsibility is inherently fragmented and dispersed.[284] A deeper understanding of the insights from corporate culture literature could help judges better assess how organizational incentives, norms, and structures

[280] *See, e.g.*, Hess, *supra* note 35, at 367.
[281] *See* Oven et al., *supra* note 45.
[282] *Id*.
[283] Shapira, books and records, *supra* note 156.
[284] *See* Brent Fisse, *Reconstructing Corporate Criminal Law: Deterrence, Retribution, Fault, and Sanctions*, 56 S. CAL. L. REV. 1141, 1184, 1187-88, 1189; Bant, *supra* note 235, at 469, 495 (arguing in favor of a theory of Systems Intentionality to address the problem of "diffused responsibility").

influence behavior. This, in turn, could help judges be more attuned to patterns of behavior, internal communications, and incentive systems that foster willful blindness or tacit approval of misconduct.

For example, a better understanding of corporate culture can inform the judicial analysis of what count as red flags. To illustrate with the recent opioid cases, identifying the pervasiveness of historical patterns of small rule violations can help judges assess whether directors were merely going through the motions or were truly interested in eradicating a culture of profits over safety. Corporate culture can also enter the analysis also as an indicator of what counts as good-faith responses to existing red flags: if the board learns about a management culture of lawlessness and responds simply by rewriting some protocols, without aggressively correcting the incentive structure and information flows, judges could infer that directors were not interested in engaging in oversight of corporate culture.[285] In other words, a deeper understanding of corporate culture enables judges to evaluate not only explicit smoking-gun evidence but also the broader organizational context that signals culpability.[286]

CONCLUSION

In recent years, corporate governance practitioners and scholars have endlessly debated the notions of "corporate purpose" and ESG. As a corollary, these scholars and practitioners turned their attention to the role of corporate culture and its relationship with corporate compliance and ethicality.[287] But there remains a gap in our understanding of the legal tools that can shape corporate culture. This Article has sought to narrow this gap with a comparative assessment of different legal instruments. Thus far policymakers and scholars have approached the question of legal tools to address corporate culture by focusing mostly on criminal liability at the entity level. This Article highlighted a different possibility, namely, addressing flawed culture via corporate law liability at the individual level. The Article compared not just different liability modes (criminal versus civil) but also different legal systems (civil liability in the US private litigation model versus civil liability in Australia's public enforcement model and the UK market discipline model). This comparative

[285] Melbourne Mun. Firefighters' Pension Trust Fund v. Jacobs, 2016 Del. Ch. LEXIS 114, *31–32.

[286] Our argument here parallels an argument concerning the need to broaden the time frame for considering organizational blameworthiness, by recognizing "reactive", as well as proactive, corporate fault. *See, e.g.,* Brent Fisse, *Reactive Corporate Fault*, *in* THE CULPABLE CORPORATE MIND ch. 7 (Elise Bant, ed., 2023).

[287] *See, e.g.*, Madeleine J. Fuerst & Christoph Leutge, *Organisational Integrity and Success*, *in* RESEARCH HANDBOOK ON ORGANISATIONAL INTEGRITY 553 (2024) (arguing that because "today's society is increasingly sensitive to moral corporate behaviour," the stakes of maintaining an ethical corporate culture are especially high); Lipton et al., *supra* note 90 (a law firm memo highlighting the main lessons for directors heading into the 2020s, and emphasizing "the heightened focus of investors, special interest organizations and the public on 'purpose' and 'culture' and an expanded notion of stakeholder interests").

analysis revealed both the promise and the perils of addressing flawed corporate culture via corporate law, and generated concrete policy implications.

We acknowledge that corporate culture is a multifaceted concept that cannot be covered in a single article. For example, we focused on how to assign blame for a flawed corporate culture, but did not cover an equally promising channel, namely, how to accord praise to those who maintain an ethical corporate culture. As another example, we focused on how corporate boards affect their company's culture, but did not discuss how culture (at the societal level) affects board behavior.[288]

Perhaps the biggest limitation that we must acknowledge in an article about accountability for flawed culture is just how difficult it is, even for the most publicly spirited and expert director, to ensure that members of their organization are following the rules and behaving with integrity. Today's large corporations are astoundingly complex, and it is difficult to know just how pervasive problems are or what causes them. More generally, we must acknowledge that corporate culture cannot be "fixed" by simple legal interventions.

Still, there is no choice but to continue searching and recalibrating ways to generate individual accountability. Overcoming a flawed culture requires a continuous commitment from the company's leadership to cultivate an environment where doing the right thing is prioritized over check-the-box compliance. Against this backdrop, we highlighted corporate law's role, not as a panacea, but rather as part of a host of imperfect mechanisms that together could, if designed properly, avert the next big corporate debacle.

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[288] *See generally* Guiso et al., *supra* note 75; Amir N. Licht, *Culture and Law in Corporate Governance*, *in* THE OXFORD HANDBOOK OF CORPORATE LAW AND GOVERNANCE 129 (Jeffrey N. Gordon & Wolf Georg Ringe, eds., 2015) (on the role of cultural values in shaping directors' preferences).

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