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Officers and Directors of Failed Federally Chartered Financial Institutions Will Be Held to a Gross Negligence Standard of Liability

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governing standards. The court suggested two alternative standards of care: 1) a case-by-case basis where juries would apply the reasonable person standard; or 2) a judicially created standard of care. The court rejected the first alternative, explaining that this open-ended rule would compel manufacturers to package all their nonprescription drugs with warnings in multiple foreign languages which would add to the costs and environmental burdens of the packaging. The court also declined to declare a particularized standard of care since the judiciary lacks the procedures and the resources to make relevant inquiries. Thus, the court concluded that the administrative and statutory standards provided the best standard of care.

Although it did not foreclose the possibility of tort liability premised upon the content of foreign-language advertising, the court held that manufacturers do not have a duty to warn that is broader in scope and more onerous than that currently imposed by applicable statutes and regulations because the associated problems and costs would be too great. The court adopted the FDA's position that "it is in the best interest of the consumer, industry, and the marketplace to have uniformity in presentation and clarity of message" in the warnings provided with nonprescription drugs. The court reasoned that to preserve this uniformity and clarity, to avoid the problems and costs of foreign-language requirements, and to defer to the legislature, it adopted the legislative standard of care that required nonprescription drug warnings only in English. Thus, the court held as a matter of law that Plough was not liable for failing to warn Ramirez in Spanish about the dangers of Reye's syndrome.

The court also denied recovery on the plaintiff's alternative theories. Ramirez also argued that the labeling was defective because it should have warned against the use of SJAC for children with colds. The court stated that because the plaintiff's mother conceded that she had not read the label, plaintiff's injury could not have been caused by the labeling. In his other theory, Ramirez also asserted that Plough should not have distributed SJAC at all since the dangers of Reye's syndrome outweighed any benefits of SJAC. The court, however, rejected this theory, stating that Plough was not liable for keeping its product in the market when plaintiff's mother bought it. At that time, the FDA had not determined whether Reye's syndrome was caused by aspirin, and therefore, the FDA had concluded that product warnings were sufficient.

Concurrence Addresses Potential Liability of Foreign-Language Advertising

Justice Mosk wrote separately to address the issue posed but not answered by the majority: the potential liability arising from foreign-language advertising based on tort theories of recovery. The concurrence agreed, however, that if a nonprescription drug manufacturer gave reasonable notice of possible side effects in a foreign language to a consumer whose purchase was induced in that language, the manufacturer would meet the standard of reasonable conduct. ❖

Kathie Yoo

Officers and Directors of Failed Federally Chartered Financial Institutions Will Be Held to a Gross Negligence Standard of Liability

In ***Resolution Trust Corp. v. Gallagher***, 10 F.3d 416 (7th Cir. 1993), the United States Court of Appeals for the Seventh Circuit held that Section 1821(k) of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) preempts federal common law and establishes a gross negligence standard of liability for officers and directors of failed federally chartered financial institutions. However, the court purposefully chose not to reach the issue of whether Section 1821(k)'s gross negligence standard preempts state law, cautioning that federalism concerns require greater evidence of congressional intent to preempt state law than federal common law.

District Court Dismisses All RTC Claims

In 1990, the Resolution Trust Corporation (RTC) placed the Concordia Federal Bank for Savings (Concordia), a federally chartered and insured thrift, into receivership. On February 14, 1991, the RTC brought suit against Concordia's former directors and officers, seeking to recover losses for alleged negligence, breach of fiduciary duty, gross negligence, and breach of contract. The RTC maintained that the defendants' conduct caused Concordia to incur substantial losses, resulting in the thrift's failure. The defendants, under Fed. R. Civ. P. 12(b)(6), filed motions to dismiss for failure to state a claim.

The District Court for the Northern District of Illinois dismissed the negligence, breach of fiduciary duty, and breach of contract claims, holding that

Section 1821(k) preempted all previously existing federal common law and created a federal cause of action solely for gross negligence. However, it held that Section 1821(k) did not preempt either state statutory or common law. Despite this finding, the court ruled that no state law claims could be successfully prosecuted against the defendants because Concordia was a federally chartered and regulated thrift, organized under federal law.

Although it dismissed the RTC's claims, the district court granted its petition to certify for interlocutory review the question of whether Section 1821(k) preempted federal common law and created a cause of action solely for gross negligence. On November 30, 1992, the Seventh Circuit agreed to hear the interlocutory appeal.

FIRREA's Plain Language Preempts Federal Common Law

The preemption issue as certified was one of first impression in the Seventh Circuit. Moreover, no other circuit court had directly addressed this question. A majority of district courts, however, have held that Section 1821(k) preempts federal common law.

In its analysis, the Seventh Circuit first recognized the limited role federal common law plays in areas where Congress has legislated. The court observed that federal common law applies only in those situations where Congress has not addressed a particular issue and there exists a significant conflict between a federal interest and state law. In resolving the issue of whether Congress spoke directly to the issue of the standard of liability governing suits brought by the RTC against officers and directors of failed federally chartered financial institutions, the court turned to the plain language of the statute. Section 1821(k) provides as follows:

A director or officer of an insured depository institution may be held personally liable for monetary damages in any civil action by, on behalf of, or at the request or direction of the Corporation . . . for gross negligence, including any similar conduct or conduct that demonstrates a greater disregard of a duty of care (than gross negligence) including intentional tortious conduct, as such terms are defined and determined under applicable State law. Nothing in this paragraph shall impair or affect any right of the Corporation under other applicable law.

From its reading of the statute, the Seventh Circuit determined that Congress spoke directly to the issue in question. Moreover, it concluded that the plain language of Section 1821(k) established a gross negligence standard of liability for officers and directors of failed financial institutions, holding that federal common law must yield to Congress' clear statement on the matter.

RTC Disagrees with Court's Analysis

The RTC disagreed with the district court's conclusion that Section 1821(k) speaks directly to the question of the standard of liability governing suits brought by it against directors and officers of failed federally chartered financial institutions. Turning to the language of the statute, the RTC first argued that because Section 1821(k) states an officer or director *may* be held liable for gross negligence or intentional torts, instead of *may only*, Congress did not intend to displace the federal common law standard of liability.

The Seventh Circuit rejected the RTC's reading of Section 1821(k). It found that "may" when read in the context of the statute, referred to the RTC's right to bring suit under this section. Furthermore, the court observed that the word "may" cannot be read to qualify the gross negligence liability standard and thus is irrelevant to the substance of the provision.

The RTC then argued that the savings clause contained in Section 1821(k) allows actions under federal common law. This savings clause specifically provides that "nothing in this paragraph shall impair or affect any right of the Corporation under other applicable law."

The Seventh Circuit again rejected the RTC's argument. It declared that if the RTC's reading of FIRREA was correct, the general language of the savings clause would override the statute's specific language establishing a gross negligence standard of liability. Such an interpretation would violate a fundamental principle of statutory construction that holds the reading of a statute should not render any part inoperative. In addition, the court noted that a better reading of the savings clause was one that would preserve the RTC's ability to take other regulatory actions based on simple negligence. Any other reading would diminish its previous powers, such as the power to remove directors and issue "cease and desist" orders for simple negligence.

Finally, the RTC contended that the legislative history of Section 1821(k) failed to support preemption of federal common law. In its argument, the RTC relied heavily on the Senate report accompanying the statute. However, the Seventh Circuit found the Senate report unpersuasive as it was not available when the Senate initially voted on FIRREA. Rather, the court turned to the conference report for more authoritative evidence of congressional intent in drafting the statute.

The conference report stated that Section 1821(k) preempts state law and permits the FDIC to pursue claims for gross negligence or any conduct that demonstrates a greater disregard of a duty of care. From this reading, the court concluded that Congress intended for officers and directors to be held liable for gross negligence or conduct indicating a greater disregard of a duty of care.

Furthermore, the court noted that key proponents of the bill supported a higher level of liability than simple negligence. They recognized the need for a higher standard of liability in order to attract high quality officers and directors. Moreover, the court observed that two subsequent attempts to modify the statute and replace the gross negligence standard with a standard of simple negligence failed.

Taken together, the court found that the legislative history of FIRREA is consistent with its interpretation that the plain language of the statute establishes a gross negligence standard of liability for officers and directors of failed financial institutions.

Seventh Circuit Finds Precedent for Preemption

In further support for its holding, the Seventh Circuit found the United States Supreme Court's decision in *City of Milwaukee v. Illinois*, 451 U.S. 304 (1981) (*Milwaukee II*), required a finding of preemption in the case at bar. In *Milwaukee II*, the issue before the Court was whether the Federal Water Pollution Control Act Amendments of 1972 preempted an existing federal common law action for abatement of a nuisance caused by interstate water pollution. The Court held that the 1972 amendments preempted federal common law as Congress occupied the field, establishing a comprehensive regulatory program overseen by an expert administrative agency. Identifying similar factors in the instant case, the Seventh Circuit determined that the analysis employed in *Milwaukee II* was appropriate in the current situation.

First, the court explained that FIRREA established a comprehensive regulatory scheme as it expanded federal authority over the activities of officers and directors of federally insured financial institutions. For example, FIRREA broadened the power of federal banking agencies to require officers and directors, subject to a "cease and desist" order, to make restitution or provide reimbursement if they were unjustly enriched by reckless disregard for the law or regulations.

Second, the court found that FIRREA created several expert agencies to supervise and administer the comprehensive regulatory scheme. In addition, FIRREA also created the RTC to assist failed thrift institutions.

From its analysis of the plain language of Section 1821(k), its legislative history, and the Supreme Court's decision in *Milwaukee II*, the Seventh Circuit concluded that Congress intended to preempt federal common law and establish a gross negligence standard of liability for officers and directors of failed federally chartered financial institutions. However, the court emphasized that it chose not to address the issue of whether Section 1821(k) preempts state law. In so doing, it noted that federalism concerns require greater evidence of congressional intent to preempt state law than federal common law and that a court must start with the assumption that federal statutory law cannot supersede a state's police power in the absence of clear and manifest congressional intent. ❖

Joyce E. Raupp

Federal Airline Deregulation Act Not Preempted by State Claims for Breach of Contract

In ***Wolens v. American Airlines, Inc.***, 626 N.E.2d 205 (Ill. 1993), the Supreme Court of Illinois held that state law claims for breach of contract based on an airline's retroactive modification of a frequent flier program are not preempted by the Federal Airline Deregulation Act, 49 U.S.C. Section 1305(a)(1) (1988), (Deregulation Act). The court found the plaintiffs' state law claims for money damages to be too removed from airline activities to invoke Section 1305(a)(1), which prohibits a state from enacting or enforcing a law relating to the rates, routes, or services of an air carrier. Nonetheless, the plaintiffs' attempt to obtain an injunction to prevent the airline from retroactively modifying the rules of the frequent flier program fell within the constraints of the Deregulation Act and was preempted.

American Offers Frequent Flier Program

American Airlines offers discounted flights and other travel benefits to customers participating in their "AAdvantage" frequent flier program. This marketing device encourages greater use of American's services by the general public and by frequent fliers. Benefits are awarded to participants based upon accumulated mileage credits, which a member earns by flying on American or by doing business with one of American's affiliates.

Prior to May 18, 1988, AAdvantage members were entitled to redeem their travel award certificates for free air travel on any available date and on any available seat in the class of service provided. As of May 18, 1988, however, American retroactively altered the terms of its AAdvantage program by instituting various restrictions on previously earned AAdvantage credits.

Class Action Filed

In response to the changes in the frequent flier program, plaintiffs, representing AAdvantage members, filed a class action in the Circuit Court of Cook County. The complaint alleged that American's retroactive modification of the rules of the AAdvantage program constituted a breach of contract with members who joined the frequent flier program prior to May 1988. The complaint also claimed violations of the Illinois Consumer Fraud and Deceptive Business Practices Act, Ill. Comp. Stat. ch. 815, para. 505/1 (West 1987), (Consumer Fraud Act). The plaintiffs, who sought