BRATISLAVA LAW REVIEW

PUBLISHED BY THE FACULTY OF LAW, COMENIUS UNIVERSITY BRATISLAVA

ISSN (print): 2585-7088
ISSN (electronic): 2644-6359

THE MODIFICATION OF THE DUTY OF LOYALTY AND THE DUTY OF CARE AND THE CONSEQUENCES OF THEIR BREACH BY MEMBERS OF ELECTIVE BODIES OF STOCK COMPANIES / Lucie Josková, Petr Tomášek

JUDr. Lucie Josková, Ph.D., LL.M.,
Assistant Professor
Department of Business Law,
Faculty of Law, Charles University
nám. Curieových 7
116 40 Staré Město, Czechia
joskova@prf.cuni.cz
ORCID: 0000-0003-1450-2864

JUDr. Petr Tomášek, Ph.D.,
Assistant Professor
Department of Business Law,
Faculty of Law, Charles University
nám. Curieových 7
116 40 Staré Město, Czechia
tomasekp@prf.cuni.cz
ORCID: 0000-0002-7871-0112

This contribution was prepared within the grant project of GAČR No. 18-04757S: "Fiduciary Duties (Primary duties of the administrators of matters of others)".

Abstract: *There are two leading duties that react to the agency problem in the corporate regulation – duty of loyalty and duty of care. The purpose of this paper is to answer the question whether, under what circumstances and on what grounds, it would be permissible to modify the two general duties either on the basis of an exception presumed by the law, or upon an agreement between a company and its director. With this purpose in mind, the authors analyse the respective legal regulation in three countries, namely Germany, Great Britain and the Czech Republic. While the modification of obligatory loyalty has been understood by the analysed legal systems within certain boundaries, they deal with the decreasing of the standard of care in a more positive way, whether through a direct modification of the standard of care or indirect modification through determining the role of an elective body member.*

Key words: *duty of loyalty; duty of care; modification; elective body; board; supervisory board; board member; stock company; limited liability company, commercial law*

Suggested citation:
Josková, L., Tomášek, P. (2022). The Modification of the Duty of Loyalty and the Duty of Care and the Consequences of Their Breach by Members of Elective Bodies of Stock Companies. *Bratislava Law Review*, 6(1), 69-84. https://doi.org/10.46282/blr.2022.6.1.282

Submitted : 16 March 2022
Accepted : 18 June 2022
Published : 30 June 2022

1. DUTY OF LOYALTY, DUTY OF CARE AND THEIR MODIFICATION

There is a basic principle in most legal systems that a member of an elective body (a director) of a business company[1] is obliged to act loyally (primarily perceived as

[1] This paper focuses on stock companies (as understood under Czech law), i.e. a limited liability company or a joint-stock company. The term *company* is sometimes used as a linguistically simplified designation of either one.

a fiduciary duty) and with due care. Such duties are a natural response to the fact that a director is employed to administer the matters of another person (a company); for that purpose, the director has wide ranging autonomy in terms of decision-making and representation powers (the so-called principal-agent problem or *agency problem;* see also Kershaw, 2012, p. 171 et seq.). The duty of loyalty and the duty of due care are presumed to ensure that any director is to proceed duly when governing the company interests and that no harm would be caused as a result of the director´s execution of office (under ordinary circumstances). Although these duties comprise just one of the possible instruments[2] to react to the *agency problem*, they form part of all corporate regulations within the European Union.[3]

Duty of loyalty and *duty of (due) care* mean that the member of an elective body is subject to requirements in two directions: the director is obliged (a) to protect the interests of the company[4] (duty of loyalty), and (b) to act with certain competence (duty of care). This is how two types of risk to which a company may be exposed, are prevented: the member of an elective body can be active and can have sufficient knowledge and experience, but he or she need not use the abilities in order to support the interests of the company; alternatively, the director may be loyal to the company´s interests, but in an absolutely incompetent way (Davies and Worthington, 2012, p. 517).

Although the distinction between the duty of loyalty and the duty of care may seem obvious, it is not always the case (Engert, 2016, p. 404 et seq.). But a general consensus applies at least to the meaning and substance of both duties.

The meaning of the loyalty duty is to ensure that a director prefers the interest of the company over his or her personal interest (or the interests of a third party). In that context, individual legal systems contain, in addition to the general loyalty duty, more detailed instruments in order to ensure that the company´s interests can be duly protected, such as regulation of conflicts of interest, which is considered by many authors as the core of the loyalty duty (Gold, 2014, p. 178),[5] prohibition of competition, prohibition to resign from office at improper time,[6] etc.

The duty of care imposed upon members of elective bodies means for them to proceed with the defined standard of conduct (care) which is used by the legislature to determine the desirable (expectable) mode of performing particular activities. Although the duty of due care has often been specified as various individual partial duties (see for example Fleischer, 2022, n. 19 ff.), its substance consists of a duty to preserve a certain quality of the way of acting or progressing in a course of action (standard of care).

The purpose of this paper is to answer the question whether, under what circumstances and on what grounds, it would be permissible to modify the two general

[2] For possible strategies to decrease agency costs see Armour, Hansmann and Kraakman (2009, p. 37 et seq.)

[3] This applies despite the fact that these are not always regulated as autonomous duties (see Gerner-Beuerle, Paech and Schuster, 2013, pp. 75–78, 118–125).

[4] We do not tackle the definition of what the interest of a company may be as the debate on this issue has been far from concluded.

[5] Also, a comparative study compiled for the purposes of the European Union dealing with the rights and liabilities of directors of stock corporations in individual EU countries states that "*The duty of loyalty, broadly understood, addresses conflicts of interest between the director and the company*." (Gerner-Beuerle et al., 2013, p. xi). For Czech law see, for example, Krtoušová Novotná (2019, p. 41).

[6] Such explicit prohibition was contained in the Czech Business Corporations Act ("ZOK") as applicable before 31 December 2020. It may be assumed that similar prohibition continues to result from the general duty of loyalty of a director. See the similar conclusion by Štenglová (2020, p. 196). For consequences of resignation from office at improper time see Supreme Court of the Czech Republic, No. 27 Cdo 3367/2018 (20 November 2019).

duties either on the basis of an exception presumed by the law, or upon an agreement between a company and its director.[7]

In order to find an answer to the above posed question, we have analysed the respective legal regulation in three countries; Germany, Great Britain and the Czech Republic (for the reasons for this choice see below). Furthermore, based on the findings, we have formulated general principles for modifying the duty of loyalty and the duty of care. For the sake of clarity, modification is understood as both the alteration of the content of the duty itself (loyalty duty, duty of care), and private law consequences of their violation.[8] Extremely significant consequences include liability to damages,[9] where *ex ante* or *ex post* exemption from liability to damages can be considered, and also changes of conditions in liability insurance regarding the performance of office (*D&O Insurance*).[10]

2. AN OUTLINE OF FOREIGN REGULATION

To provide a comprehensive overview of foreign regulation in a limited amount of space, one representative of both the continental and common law legal system have been chosen. The continental law is represented by Germany as regulation of the most populous European country, moreover with crucial impact on the regulation of further European countries (e.g. Austria and, due to the historical reasons, the Czech Republic as well). Great Britain stands for the common law system as a traditional representative of this legal family. Finally, the regulation of the Czech Republic is introduced as a state which belongs among continental jurisdiction, however, where common law principles are followed thoroughly and where different aspects of common law system are incorporated.[11]

2.1 Germany

German law imposes upon members of the board of directors and supervisory board of a joint-stock company and upon directors of a limited liability company a duty to act with due care (*Sorgfalt eines ordentlichen und gewissenhaften Geschäftsleiters*,[12] or *Sorgfalt eines ordentlichen Geschäftsmannes*).[13] The duty of loyalty is not explicitly regulated by legislation regarding those persons; however, both literature and case-law uniformly rely on the presumption that members of elective bodies of both joint-stock companies and limited liability companies owe also the duty of loyalty (*Treuepflicht*) (see, for example, Hüffer and Koch, 2022, n. 10–11; Fleischer, 2022, n. 147 ff.). Explicit

[7] This paper is based upon the text of co-author L. Josková entitled "Možnosti modifikace povinnosti postupovat s péčí řádného hospodáře" published in *Dvořák, J. a kol.* Soukromé právo 21. století. Praha: Wolters Kluwer ČR, 2017, pp. 63 – 75. The content of the original text has been substantially changed and its conclusions adapted after debates with P. Tomášek.

[8] Sanctions under Czech public law include, for example, disqualification (exclusion from the position). Czech law provides that a member of the governing body may be excluded from the performance of office if he or she has repeatedly or seriously violated duties during the last three years (section 63 (1) ZOK). In British law, see the Company Directors Disqualification Act 1986.

[9] Other penalties are also possible such as to render benefit acquired (for Czech law see section 53 (1) ZOK).

[10] Insurance is considered as one of the instruments to restrict liability (see, for example, Gerner-Beuerle et al., 2013, p. xiii).

[11] Since 2014, it has been possible to form joint stock company with both two-tier (traditional) system and one-tier system. At the same time, the business judgment rule was introduced [see Sec § 51 (2) ZOK].

[12] Provisions of section 93 (1) AktG for the members of the board of directors, and section 116 AktG for the members of the supervisory board.

[13] Section 43 (1) GmbHG for directors of a limited liability company.

DOI: 10.46282/blr.2022.6.1.282

statutory expressions of the loyalty duty are prohibition of competition and non-disclosure duty; in addition, some rules for conflicts of interest are also regulated.

Prohibition of competition applies to members of the board of directors of a joint-stock company (section 88 AktG), who must not, without the permission of the supervisory board, carry out certain activities and/or occupy a certain position. The supervisory board can issue permission only regarding certain activities unless harm has been caused to the interests of the company (for example, double mandates within the holding are permissible). Members of a supervisory board are not subject to the prohibition of competition; this approach has been justified by their looser relation with the company (and a more restricted loyalty duty) (Kumpan, 2014, p. 117; Habersack, 2019, n. 47; Spindler, 2022a, n. 81). On the other hand, it has been generally accepted that the prohibition of competition applies to the governing director of a limited liability company although the law does not explicitly stipulate so (Raiser and Veil, 2006, p. 517; currently e.g. Leuering and Rubner, 2020, p. 719).

Members of the board of directors and supervisory board of a joint-stock company are obliged to preserve the non-disclosure duty (section 93 (1), section 116 AktG). The same duty is owed by the governing director of a limited liability company, although the law does not explicitly impose the non-disclosure duty upon them (Oetker, 2021a, n. 19–21).

The Stock Act regulates the protection of a company against consequences of a conflict of interest in its section 112 AktG;[14] it governs the rules for representation of a company by the supervisory board where negotiations with the board of directors are at issue. The recent case law and literature suggest that those provisions apply not only to the existing members of the board of directors but also to its former members (Spindler, 2022b, n. 17). Even contracts concluded within common business transactions do not create an exception to such rule.[15] The Limited Liability Company Act is free from any similar provision; this is why the general rule of the Civil Code should apply in relevant cases (section 181 (1) alt. 1 BGB). However, in practice, governing directors of limited liability companies are frequently released from such restriction in the respective memorandum of association (Fleischer, 2003, p. 1052). The general regulation is complemented with rules regarding specific legal transactions. Thus, the Stock Act regulates the rules for providing loans to the members of the board of directors (section 89 (1) AktG); the same applies to providing security for a transaction (Fleischer, 2003, p. 1054). The provision of a loan to the governing director is regulated by the Limited Liability Company Act (section 43a GmbHG), although the main purpose in such cases is the protection of the registered capital (Oetker, 2021b, n. 1).

The doctrine treats in a different way possible modifications of the duty of loyalty and the duty of care, or the consequences of their breach, with respect to either form of the company.

The approach of the doctrine to permissibility of a modification of the duty of care for members of elective bodies of stock company appears to be uniform. German

[14] Section 112 AktG reads: "*Vorstandsmitgliedern gegenüber vertritt der Aufsichtsrat die Gesellschaft gerichtlich und außergerichtlich. § 78 Abs. 2 Satz 2 gilt entsprechend.*", i.e. the supervisory board represents the company against the board of directors in judicial proceedings and also externally.

[15] Literature in such cases recommends that a resolution of the supervisory board be adopted that would authorize company employees to enter into everyday transactions with the members of the board of directors Fleischer (2003, p. 1052).

stock law is based upon the principle *Satzungsstrenge*,[16] under which provisions of the Stock Act are considered to be peremptory. Therefore, a prevailing part of the specialist literature on this subject contends that the duty of care or the consequences of the breach thereof could not be modified, i.e. neither made stricter (Hopt and Roth, 2015, p. 126) nor softer (Hopt and Roth, 2015, p. 125; Hüffer and Koch, 2022, p. 613; Krieger and Sailer-Coecani, 2015, p. 1437). Should there be any deviations from statutory regulation of the duty of care or consequences of its violation stipulated in the by-laws or any agreement between the company and a member of its elective body, such provisions would be considered as non-existent *ab initio* (*Nichtigkeit*) (Hopt and Roth, 2015, p. 126). Although recently part of the German literature and practice requires that the modification of the duty of care (not the loyalty duty) should be permissible[17], particularly regarding the restriction of the scope of compensation for damage caused due to the breach of the duty of care (see Grunewald, 2013, p. 813 et seq.; Habersack, 2015, p. 1297 et seq.), any agreement in this respect is still missing[18] and no recent amendment of the Stock Act has introduced such a possibility.

As for the duty of loyalty for members of elective bodies of stock companies, the possibilities of its restriction or exclusion have received only marginal mention in the literature. Opinions regarding that issue tend to conclude that the duty of loyalty as a whole cannot be excluded again with respect to the principle *Satzungsstrenge*.[19] In another words, the duty of loyalty is considered to be peremptory and no modification is allowed.

As for the legal rules applicable to a company taking insurance in order to secure a director against risks resulting from his or her position there is a requirement of coinsurance in the amount of at least 10% of the damage, but not less than 1.5 multiple of the fixed annual remuneration of the board member.[20] However, it is not excluded that a board member also takes individual insurance to cover any potential duty of coinsurance, which has been used frequently in practice (Wagner, 2014, p. 235).

Regarding a limited liability company, part of the literature admits that certain modification of the duty of care, or the restriction of the duty to compensate the damage caused as a result of the breach of that duty, can occur.[21] However, these issues have been generally considered as controversial (e.g., Fleischer, 2016, n. 298). The basic argument of supporters of permissibility of modification of the duty of care is based upon

[16] Under section 23 (5) AktG, the by-laws of a joint-stock company can deviate from the statute only if such deviation is explicitly permitted in the statute. As a result, provisions of stock law are considered as peremptory. The principle *Satzungsstrenge* is based upon the decision of the Reich Court of Justice of 25 September 1901, file n. I 142/1; the decision became part of case law and was not questioned in the literature for a long time. However, it has been recently subject to criticism more and more frequently.

[17] The reason is relatively recent proceedings for damages instituted by members of elective bodies of joint-stock companies where the volume of damage was such that it significantly exceeded the insurance taken and compensation of such damage by the members would be for them liquidating. In this respect, there is a "model" case of Dr. Breuer, former board member of Deutsche Bank AG, who, along with the Bank, was sued for damages in the amount of 3.5 billion Euro, since he had expressed doubts regarding the creditworthiness (*Kreditwürdigkeit*) of Kirch empire (summary under Grunewald, 2013, p. 813).

[18] For a critical opinion see for example Fleischer (2005, pp. 914–915).

[19] See for example A. Hellgardt, whose opinion regarding the exclusion of the loyalty duty is quite tolerant (2010, p. 784).

[20] Section 93 (2) third clause, reads: "*Schließt die Gesellschaft eine Versicherung zur Absicherung eines Vorstandsmitglieds gegen Risiken aus dessen beruflicher Tätigkeit für die Gesellschaft ab, ist ein Selbstbehalt von mindestens 10 Prozent des Schadens bis mindestens zur Höhe des Eineinhalbfachen der festen jährlichen Vergütung des Vorstandsmitglieds vorzusehen*."

[21] The cornerstone in that respect was laid by the decision of the Federal Court of Justice (BGH), which allowed for the shortening of the limitation period (decision of 16 September 2002, file n. II ZR 107/01).

DOI: 10.46282/blr.2022.6.1.282

the existence of wide powers of company members regarding their right to claim damages against the governing director.[22] This leads to a deduction that if limited liability company members may decide whether and to what extent they wish to enforce the claims of the company against its governing director having breached his or her duties, the same approach should apply to waiving such claims in advance (Paefgen, 2014, p. 1255). An example of potential modification of the duty of care, or consequences of the breach thereof, includes the right to restrict the liability of a governing director for certain types of conduct,[23] or to agree on a maximum scope of damages; another possibility is to make stricter the requirements giving rise to liability for the damage caused (Paefgen, 2014, p. 1254). Such restrictions are considered efficient even if they negatively affect the creditors (e.g. the performance regarding the claim for damages is required in order to satisfy the creditor) (Paefgen, 2014, p. 1255).[24]

Regarding the duty of loyalty of the governing director, it has to be said that the relevant literature makes minimal reference to the exclusion of the loyalty duty. However, at the same time, some authors admit that the duty of loyalty as a whole may be excluded (Hellgardt, 2010, p. 785 et seq.).

2.2 *Great Britain*

British regulation of business companies has traditionally been based upon the so-called monistic principle which means that a company has just one elective body – *board of directors*. The regulation of duties of its members was historically developed by case-law; a relatively complex statutory regulation was introduced by the Companies Act 2006.[25] Although this legislation does not contain explicit subdivision of duties of a member of the board of directors into the duty of care and duty of loyalty, such classification is presumed to be relevant today as it corresponds with the historical development of both duties (Davies and Worthington, 2016, p. 478).

Section 174 CA can be considered as a codification of the duty of care; a member of the board of directors is obliged to exercise reasonable care, skill and diligence to such an extent that would be expected of a person carrying out the functions of a director in relation to the company. The doctrine then infers that it would depend on the situation of a particular company and that it could not be expected in every single case that every member of any board of directors would be able to act as a professional member of the board (Davies and Worthington, 2016, pp. 480–481; Girvin, Frisby and Hudson, 2011, p. 336). In this context, some authors conclude that - with regards to the liability of non-executive directors who are not qualified or experienced in a discipline relevant to company administration – CA prescripts nothing relevant (Wild and Weinstein, 2016, p.

[22] Under section 46 n. 8, GmbHG, the annual meeting by its simple majority decides whether the claim against the governing director would be raised. In addition, the company may waive the claim or agree on its composition. This does not apply if the provision of section 43 (3) GmbHG has been violated, i.e. the provision prohibiting the payment of means in order to sustain the registered capital (s. 30 GmbHG), or the provision limiting the acquisition of one´s own shares (s. 33 GmbHG), and the amount is necessary to satisfy creditors (s. 9b GmbHG). Should the general meeting declare that no claim would be raised against the governing director regarding any damage already sustained, it means the waiver of any right to damages (s. 46 n. 5 GmbHG).

[23] Nevertheless, it is impossible to exclude the liability of a governing director for intentional breach of a duty, section 276 (3) BGB.

[24] Paefgen adds that although peremptory regulation of a director´s liability for the breach of a duty could be politically desirable it can be inferred neither from the systematics, nor the wording of the Limited Liability Company Act (2014, p. 1255).

[25] Hereinafter referred to as "CA".

198). In our opinion, such an approach opens the door to indirect modification of the duty of care, depending on the tasks a member of the board is entrusted with.

On the other hand, sections 171 through 173 and 175 through 177 can be considered as codification of the loyalty duty and relating good faith as basic fiduciary duties.[26] Those provisions stipulate that a director must act within his or her powers, must promote the success of the company, exercise independent judgment, avoid conflicts of interest (or notify the company of his or her interest in certain transactions), and must not accept benefits from third parties.

As for thoughts regarding possible modifications of the duty of loyalty, British law traditionally offers to company members a wide range for their autonomous regulation of internal issues of the company (see Davies and Worthington, 2016, p. 356), and the statutory regulation should be considered peremptory except for cases where the statute itself provides for certain deviation. Under section 173 (2) CA, the company´s constitution can stipulate under what circumstances the director is not obliged to exercise fully independent judgment (but his or her own judgment). Such special regulation can be used, for example, in subsidiary companies (see also Boyle, Birds et al., 2014, p. 610), which would be established for "servicing" purposes to fulfil objectives of their parent company or other companies within the same group. However, even in these circumstances, the director has a responsibility to their company as a whole. Thus, they must not force a subsidiary out of business just because it suits the parent company to do so, nor must the director be guided solely by the interests of the group as a whole (Loose, Griffiths and Impey, 2015, p. 241).

Another statutory exception applies to conflicts of interest. Under section 175 (1) CA, a director of a company must avoid a situation in which he or she has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company (on conflict rule). However, subsection (3) stipulates that such duty does not apply to a conflict of interest arising in relation to a transaction or arrangement with the company relating to an unessential volume of company assets.[27] Furthermore, section 180 (4) b) CA provides that company members may, at the general meeting, adopt their own rules relating to conflicts of interest (Hannigan, 2016, p. 539), which makes the statutory regulation default than rather mandatory.

In addition, the no conflict rule is expanded by the no profit rule[28] which precludes a director of a company from benefiting personally from the position of a director. The no profit rule covers any inducement or incentive type of payment to a director or non-monetary type inducement as well.

As for a possible agreement between the company and its director to exclude private law consequences of the breach of the duty of care and the loyalty duty, section 232 CA prevents it ex ante as it stipulates that any provision is void that purports to exempt a director of a company from any liability for the breach of duty in relation to the company (Loose et al., 2015, p. 362 et seq.). However, subsequent approval (ratification) of conduct of a company director amounting to the breach of duty is possible (section 239 CA); it should be made by resolution of the members of the company adopted by qualified or simple majority depending on the respective form of the breach of duty (Loose et al., 2015, p. 355 et seq.).

---

[26] As for a fiduciary nature of such duties see also section 178 (2) CA. Cf. For a different opinion regarding section 171 CA see Hannigan (2016, p. 316).

[27] Section 191 CA stipulates that an asset is a substantial asset in relation to a company if its value— (a) exceeds 10% of the company's asset value and is more than £5,000, or (b) exceeds £100,000.

[28] See sec. 176 CA.

The limitation of the maximum extent to which a company director may be released from liability for a breach of their duties is rarely covered in literature. However, the doctrine infers that there can be such breaches that could not be subject to subsequent ratification, such as misappropriation of corporate property (Davies and Worthington, 2016, p. 574 et seq.).

It should be added that, despite the existence of section 232 CA, British regulation explicitly provides that a company can purchase, for a director of the company, insurance against the consequences of the breach of his or her duties (section 233 CA). Unlike in German regulation, no minimum co-insurance to be taken by a company director is required in Britain. Although such provision (in the case of taking insurance in the widest possible extent) can seem to remove all preventive effects regarding statutory duties of company directors, the issue can be seen also from another perspective, namely that insurance serves as a means to smoothly compensate the damage caused by a director and to protect the company and its creditors (Davies and Worthington, 2016, p. 579).

2.3 *The Czech Republic*

Czech legislation imposes the duty to act with loyalty[29] and due care upon the members of elective bodies of all companies (including limited liability companies and joint-stock companies). The loyalty duty and the duty of care are covered, by the general duty to act with due managerial care.[30] These duties are considered to be peremptory.[31] However, as is obvious from the text below, the regulation is in fact semi-peremptory as the tightening of the duties is allowed.

The possibility of making the duty of due managerial care (i. e. both duty of loyalty and duty of care) stricter is undoubted, as the law prohibits only mitigation of it.[32] Thus, a company and a member of its elective body can enter into an agreement that the member of the elective body must perform their role with due professional care.[33] The limit for this tightening is liability for a result as this is considered to be unacceptable (Čech and Šuk, 2016, p. 159).[34]

On the other hand, the duty to act with due managerial care (i. e. both duty of loyalty and duty of care) can be mitigated neither by agreement between a member of an elective body and the company nor in any constituting document of the company (there are exceptions mentioned below which limit partial loyalty duties) (Dědič and Lasák, 2021,

[29] It should be mentioned that a company director is obliged to act with necessary loyalty, which may give rise to consideration that such loyalty is lower as to its intensiveness compared to unlimited loyalty. P. Čech and P. Šuk argue that "*A member of a company body cannot be required, for example, to work 24 hours a day and seven days a week.*" (2016, p. 159).

[30] Section 159 (1) of the Czech Civil Code 2021 reads: "(1) *A person who accepts the office of a member of an elected body undertakes to discharge the office with the necessary loyalty as well as with the necessary knowledge and care. A person who is unable to act with due managerial care although he must have become aware thereof upon accepting or in the discharge of the office and fails to draw conclusions for himself is presumed to act with negligence.*"

[31] Supreme Court of the Czech Republic, No. 31 Cdo 4831/2017 (11 April 2018). In literature see e.g. Janů (2019, p. 229).

[32] As section 53 (2) ZOK explicitly excludes any limitation (or even exclusion) of liability it may be inferred that stricter rules may apply. Such conclusion corresponds with the purpose of the provision, namely to protect the company and its members and creditors.

[33] The standard of professional care is generally considered to be stricter than the standard of due managerial care.

[34] As for case-law, for example, see Supreme Court of the Czech Republic, No. 29 Cdo 2363/2011 (29 April 2013); Supreme Court of the Czech Republic, No. 29 Cdo 935/2012 (19 December 2013); Supreme Court of the Czech Republic, No. 29 Cdo 662/2013 (18 September 2014).

pp. 393–394). According to the law,[35] this is applicable to both the regulation of the duty itself and the consequences of its breach. The quoted provision undoubtedly applies to the *ex ante* modification of the duty to act with due managerial care and/or the liability for its breach.[36] However, it is disputed, whether an agreement between a company and a member of an elective body regarding limitation of damages, or – as the case may be – giving up of the compensation by the company after the causation of damages (*ex post)* is allowed. It should be noted that this part of the doctrine acknowledges both possibilities (similarly Dědič and Lasák, 2021, pp. 394–396).

As suggested in the introduction, the loyalty duty in Czech law is indicated in individual provisions of the Act. There is detailed regulation of the rules for conflicts of interest[37] and the prohibition of competition. The loyalty duty partly covers duties not explicitly regulated by the statute, such as non-disclosure (Lasák, 2022, p. 599). There are conditions regulated within the framework of individual partial duties, the fulfilment of which does not result in the infringement of statutory prohibition. For example, a member of an elective body who intends to enter into a contract with the company (e.g. to purchase one of the company´s immovables) has the right to conclude the contract with the company despite the existence of a conflict of interest, providing he or she informs all members of both the governing body and supervisory body of the intended purchase in advance of the conditions under which such contract is to be concluded. Nevertheless, it is emphasised by law that the notification of conflict of interests does not remove the duty of the member of the elective body to act in the interests of the company. As far as matters within the frame of common business transactions are concerned, the Act does not require any notification of a conflict of interest.[38] A possibility to deviate from the statutory regulation of the prohibition of competition is presumed by the Act itself as it explicitly permits that acts constituting the company can contain rules derogating from the statutory definition of the prohibition of competition.[39]

Specific regulation of liability insurance for the performance of office is absent in the Czech legal system. However, in practice, such insurance is commonly taken without being considered as a limitation of liability of a member of an elective company body.[40]

3. PRINCIPLES FOR THE MODIFICATION OF THE LOYALTY DUTY AND THE DUTY OF CARE

3.1 *Duty of Loyalty*

Across all three countries studied, there is a unifying presumption that duty of loyalty is an obligation intrinsically connected with the role of a member of an elective body and applies irrespective of whether the duty of loyalty is regulated by the law explicitly (the Czech Republic); through a set of duties (Great Britain) or – as the case may be – is not part of the written law at all (Germany).

[35] Section 53 (2) ZOK reads: "*Legal acts of a business corporation restricting the responsibility of a member of its bodies are disregarded*."

[36] Section 53 (3) 4 ZOK provides for the settlement of damages arisen due to the breach of the duty to act with due managerial care, but it is quite controversial in the literature whether only an agreement on another equivalent manner of settlement is permissible, or a partial waiver of compensation of damage caused is also possible (e.g., Čech and Šuk, 2016, p. 176).

[37] See sections 54 through 57 ZOK.

[38] Section 57 ZOK.

[39] Sections 199, 441 (4), 451 (4) and section 459 (4) ZOK.

[40] In this sense, for example, see Csach (2015, p. 198). An exception is the view of R. Pelikán, who considers insurance as an impermissible limitation of the liability of an elective body member (2012, p. 116).

DOI: 10.46282/blr.2022.6.1.282

Further, it seems that the legislative core of the duty of loyalty is usually understood as the statutory regulation of the conflicts of interest (and their regulatory displays) and – in some cases – as the regulation of the prohibition of competition. At the same time, it is obvious that the analysed regulations also reflect that it could be necessary to partially derogate certain rules to enable the practical functioning of businesses (e.g. in case of group of companies). It is also obvious that in the German and Czech law the modification of the duty of loyalty is discussed rather reluctantly and only in connection with the regulation of conflict of interests and prohibition of competition, whereas British law stipulates multiple exemptions from the statutory regulation of the duty of loyalty. Moreover, any modification of the duty of loyalty or any statutory exemptions does not deprive a member of an elected body of his or her duty to act in the interests of the company (explicitly in the Czech regulation), or to – at least – bear these interests in mind.

In a general sense, we agree that it is inherent in every person's nature that they protect their interests against, and prioritise them over, the interests of others.[41] Therefore, the duty of loyalty imposed on a member of an elective body obliges them to prefer the interests of the company to his or her own interests (or interests of the allied person). Thus, the duty of loyalty creates the pillar of the relationship between a company and a member of its elective body (i.e. the relationship between two different persons).

However, contrary to the analysed jurisdictions, we do not think that conflict of interests and prohibition of competition are core elements of the duty of loyalty. We agree that the basis of obligatory loyalty is the general prohibition of self-enrichment to the detriment of the company or to use the powers entrusted for one´s personal benefit or for the benefit of an allied person.[42] This duty (prohibition to enrich yourself to the detriment of the company) cannot be modified by agreement between a company and a member of an elective body or given up by the company as this would be contrary to the substance of the relationship between the company and the member of an elective body.

This conclusion does not mean that the statutory regulation of conflicts of interest and the regulation of the prohibition of competition are not important rules connected with the duty of loyalty. On the contrary, they represent crucial devices to ensure that the duty of loyalty is fulfilled properly. However, they must follow the aim: to ensure that a member of an elective body does not enrich themselves at the expense of the company; not to prohibit every situation where interests of a company and a member of an elective body differ. Thus, if the analysed jurisdictions enable partial derogation of these rules, they reflect the functioning of businesses and do not alter the above-mentioned conclusion that the core duty of loyalty cannot be modified. Furthermore, the rules for conflicts of interest should solve situations when the interest of a company and interest of a member of an elected body are different. At the same time, they must prevent the situation when their strict observance would be to the detriment of the company. A typical example may be that it turns out to be exigent to admit, under set circumstances, that a contract should be concluded between the company and an elective body member. For example, if the member owns property that is needed by the company for its future expansion, the exclusion of such purchase with reference to its absolute prohibition would finally result in the detriment to the interests of the company. Similarly, it would make no sense if an elective body member would have to provide notification of every transaction with the company irrespective of its significance and risks for the company;

[41] For details regarding the existence of one´s own interest as a condition for legal personality see Pelikán (2012, p. 58 et seq.).
[42] For details regarding this issue see Engert (2016, p. 406 et seq.).

an example would be an elective body member of a company operating a chain of petrol stations who wishes to fill their car's fuel tank under regular business conditions.

We argue that the rules governing conflicts of interest should, rather than to provide for the general prohibition, mean primarily the regulation of procedures to resolve conflict satisfactorily, including providing exceptions to the general rules.

Conflicts of interest have been inevitably designated as a symptom of our times.[43] Thus, business practice has to deal not only with conflicts of interest between a company and its elective body member, but also between several companies with the participation of the same elective body member. Those situations are usually subject to the statutory regulation of prohibition of competition. An example of a justified exception to the prohibition of competition may be the possibility to hold a position on an elective body for several companies which are interconnected and where the interest of a particular company is subordinate to another interest (e.g. that of the holding).

To sum up, the above outline indicates that it may be desirable in some situations where the loyalty duty is to apply, that the restriction or exclusion of certain aspects of obligatory loyalty may be admitted; but only under the condition that the prohibition of self-enrichment to the detriment of the company is respected. The legal systems under consideration consider that such situations must be somehow resolved; as a result, they allow, within the defined scope, for certain mitigation of selected aspects of the duty of loyalty.[44] It is important that such intervention is practicable only to the extent and under conditions justified by another prevailing and legitimate interest. However, such considerations should be left only to a restrained legislature due to the significance of the loyalty duty and the actual imbalance between a company and an elective body member; the more so in the case of a company composed of several members where there is a potential threat of outvoting the minority.

On the other hand, the situation is perceived the other way around if the obligatory loyalty duty is made stricter. Should an agreement between a company and a member of its elective body replace the legal requirement to act in the necessary interest of the company in such a way that the elective body member would be obliged to act in the best interests of the company we would see no risk in such regulation as the statutory standard of acting would be higher and the protection of the company strengthened. Similar reasons lead us to have no objections against strengthening the rules on conflicts of interest and the prohibition of competition (whether applicable to substance or time). Nevertheless, it should always be thoroughly considered if such rules do not affect the company´s interest in undesirable ways (see above). Moreover, it should always be kept in mind that a company can act against its elective body members as a stronger party; as a result, the actual negotiating power of an elective body member should be considered and any excessive conditions prevented by means of the principles of private law.[45]

[43] As for conflicts of interest see Hopt (2004, pp. 1–52).
[44] See, for example, exceptions to the prohibition of competition in the German Stock Act (section 88 AktG), or the rules for transactions during conflicts of interest in British law (section 175 CA).
[45] Those would include, for example, an agreement under which a member of an elective body would bind him or herself not to accept the position of an elective body member in another company with the same objects of business.

DOI: 10.46282/blr.2022.6.1.282

3.2 Duty of Care

The members of the elective bodies are obliged to perform their duties with due care in all three jurisdictions under consideration. This duty is – unlike the duty of loyalty – was found to be explicitly regulated by law.

Whereas the possibility of modification of obligatory loyalty within the analysed legal systems is rather narrow, the changes to the duty of care seem to be more acceptable. It seems that raising the standard of care (e.g. to require due professional care) is generally allowed, unless a member of an elective body should be responsible for the outcome. Of the analysed jurisdictions, only the German regulation of stock companies explicitly forbids tightening of the duty of care referring to the principle of *Satzungsstrenge*. The decrease of the standard of care is demanded by the doctrine as it is believed to be required by the reality of business life (across all three jurisdictions). One possible way of decreasing the standard of care which has been suggested is restricting the duty to compensate for damage caused by the breach of the duty of care. There, analysed regulations distinguish between *ex ante* limitation (which is considered problematic) and *ex post* limitation (which could be allowed). Such an open approach is presumed to be based upon an idea that decreasing the standard of care or restricting the consequences of the breach of duty to act with such standard of care; can ensure that candidates would be more willing to take respective positions and be subject to reasonable risk in the course of their duties. Another important idea is that it is not legitimate to expect that all members of the board of directors would act with the same standard of care as they have different tasks to perform. On the other hand, opponents object that any limitation of the duty of care would have negative impact on the preventative nature of this duty.

Based on the findings, it can be stipulated as follows.

Companies by their nature have a primary role to protect their interests; they allow the modification of duty of care or legal consequences of its breach only if it proves to be advantageous for them.

Thus it can be presumed that a company permits the reduction of the standard of care (e. g. by limiting the consequence of its breach) only if it rationally evaluates, with sufficient evidence, that decreasing the standard of care, or limiting or excluding the consequences of the breach thereof, is more beneficial for the company than to adhere to the duty of care within the statutory regime (Hellgardt, 2010, p. 771).[46] This can be case if the reduction of the duty of care helps the company to secure a better candidate for the position of the member of an elective body. However, it is necessary to keep in mind that protecting the company´s own interests inevitably covers its implementation, i.e. ensuring the further existence of the company. This is possible only if interests of both the company members and its creditors are taken into account.[47] Not respecting the interests of creditors results in the company´s bankruptcy and further promotion of the company's interests becomes impossible (Pelikán, 2012, p. 59). In other words, contractual autonomy of parties must not be without limits when the standard of care is to be reduced. Thus, contractual autonomy should not only take into account the

[46] An example may be that a candidate makes the acceptance of the position conditional upon the limitation of the duty of care (such as by restricting the scope of compensation for damage in the case of the breach of that duty); and the authorized person would come to the conclusion that the risk potentially caused as a result of the reduction of the statutory standard would be counter-balanced by the benefits to be brought in by the candidate.

[47] See also section 172 CA.

interests of creditors but also the interests of minority company members[48] and other stakeholders (such as employees).

The tightening of the duty of care seems to be less problematic. This is obviously based on the logical fact that making the key duties of an elective board member stricter contributes to a higher degree of protection of the company's interests.

The need for a higher protection of interests can be applicable to companies engaging in highly specific activities, and such protection is required by statute. Examples in Czech law cover companies doing business or providing services on capital markets,[49] where the legislature imposes a higher standard of professional care instead of the standard of due managerial care. However, a risk-laden activity should not be avoided, because it attracts very high levels of care. This can lead to an extreme risk aversion and reduce the scope of individuals willing to join an elective body, which may potentially be to the detriment of the company. Despite this, we can assume that the benefit (i.e. an increased protection of the interests of the company) would prevail over the negatives. Therefore, making the duty to act with due care stricter, e.g. in the direction of professional care, is essentially possible. Nevertheless, it should not lead to the situation where the elective body member is liable for the result of his or her activities; if any business success goes for the good of the company, it should also bear the risk of failure and should not transfer it to the elective body members. Such tightening would be contradictory to the relationship between an elective body member and the company, as the member is responsible for the due performance of their activities and not for its results.

4. CONCLUSIONS

The duty of loyalty imposes on a member of an elective body the obligation to prefer corporate interests over their own (or the interests of the allied person). Its core role doesn´t lie in regulation of conflict of interests, but in the prohibition self-enrichment to the detriment of the company. Regulation of the conflict of interests is only a device achieve it. Thus, the duty of loyalty represents the pillar of the relationship between a company and a member of its elective body. Therefore, the possibility of modifying the duty of loyalty (or legal consequences of its violation) is very limited and only under condition that the prohibition self-enrichment at the detriment of the company is respected.

Thus, the restriction or exclusion of certain aspects of duty of loyalty may be admitted, but only within the scope defined by law, as legislature should ensure that the interests of the company are protected properly. On the other hand, the tightening of duty of loyalty is allowed, as in this way, the protection of the company is strengthened.

The duty of care requires a member of an elective body to act with certain competence. It can be assumed that – as the company primarily protects its own interests – the modification of the duty of care (or legal consequences of its breach) is only allowed in cases where it is more advantageous for the company than to let duty of care remain within the statutory regime. Thus, it is possible that also reducing the

---

[48] The interests of minority company members may be put at risk even where the company produces profit as a result of its functioning, namely when the company generates profits but has insufficient cash flow in order to pay dividends without taking a loan.

[49] Traders in securities (section 11a, the Business on Capital Market Act 2004, "ZPKT"), investment brokers (section 32 ZPKT), organizers of a regulated market (section 41 ZPKT), administrators of an investment fund (section 18, the Act on Investment Companies and Funds 2013, "ZISIF"), etc.

DOI: 10.46282/blr.2022.6.1.282

standard of care is attractive to the company as it can increase the willingness of candidates to take up membership of the elective body or to take risky business decision. However, the interests of the creditors and shareholders must be taken into account as well. The tightening of the duty of care seems to be less problematic as it helps to protect company better. Nevertheless, there are also visible hazards for the interest of the company which should be taken into consideration.

BIBLIOGRAPHY:

Boyle, A. J., Birds, J., Clark, B., McCormack, G., Solinas, M., Varney, M. R., and Villiers, C. (2014). *Company Law* (9th Edition). Bristol: Jordan Publishing.

Čech, P., and Šuk, P. (2016). *Právo obchodních společností v praxi a pro praxi (nejen soudní)*. Praha: Bova Polygon.

Csach, K. (2015). Poistenie zodpovednosti za škodu sposobenú členmi orgánov obchodných společnosti. In K. Hurychová and D. Borsík (Eds.), *Corporate governance* (pp. 194–204). Praha: Wolters Kluwer.

Davies, P., and Worthington, S. (2012). *Gower & Davies: Principles of Modern Company Law* (9th Edition). London: Sweet.

Davies, P., and Worthington, S. (2016). *Gower´s Principles of Modern Company Law* (10th Edition). London: Sweet & Maxwell.

Dědič, J., and Lasák, J. (2021). § 53. In J. Lasák, J. Dědič, J. Pokorná, Z. Čáp et al. (Eds.), *Zákon o obchodních korporacích. Komentář*. (2nd Edition, pp. 392–401). Praha: Wolters Kluwer.

Engert, A. (2016). Private Macht im Gesellschaftsrecht: Die Macht der Verwaltung und ihre Kontrolle. In F. Möslein (Ed.), *Private Macht* (p. 404 et seq.). Tübingen: Mohr Siebeck.

Fleischer, H. (2003). Zur organschaftlichen Treuepflicht der Geschäftsleiter im Aktien- und GmbH-Recht. *Wertpapier-Mitteilungen, Zeitschrift Für Wirtschafts- Und Bankrecht*, (22), 1045–1058.

Fleischer, H. (2005). Haftungsfreistellung, Prozesskostenersatz und Versicherung für Vorstandsmitglieder – eine rechtsvergleichende Bestandsaufnahme zur Erhaltung des Managements. *Wertpapier-Mitteilungen, Zeitschrift Für Wirtschafts- Und Bankrecht*, (20), 914–915.

Fleischer, H. (2022). Commentary on sec. 93 AktG. In M. Henssler, G. Spindler, and E. Stilz (Eds.), *Kommentar zum Aktiengesetz. Grosskommentar.* München: C. H. Beck. Retrieved from www.beck.de.

Fleischer, H. (2016). Commentary on section 43. In H. Fleischer and W. Goette (Eds.), *Münchener Kommentar. GmbHG - Gesetz.* (2nd Edition, p. 1696). München: C. H. Beck.

Gerner-Beuerle, C., Paech, P., and Schuster, E. P. (2013). *Study on Directors´ Duties and Liability prepared for the European Commission DG Markt*. London: LSE Enterprise.

Girvin, S., Frisby, S., and Hudson, A. (2011). *Charlesworth's Company Law* (18th Edition). London: Sweet & Maxwell.

Gold, A. S. (2014). The Loyalties of Fiduciary Law. In A. S. Gold and P. B. Miller (Eds.), *Philosophical Foundations of Fiduciary Law* (p. 436). Oxford: Oxford University Press. DOI: https://doi.org/10.1093/acprof:oso/9780198701729.001.0001.

Grunewald, B. (2013). Haftungsvereinbarungen zwischen Aktiengesellschaft und Vorstandsmitgliedern. *Die Aktiengesellschaft*, (22), 813–818.

Habersack, M. (2015). Enthaftung des Vorstandsmitglieds qua Anstellungsvertrag? Kritische Bemerkungen zu Seibt, NZG 2015, 1097. *Neue Zeitschrift Für*

Gesellschaftsrecht, 18(33), 1297–1300.

Habersack, M. (2019). Commentary on sec. 116 AktG. In W. Goette, M. Habersack, and S. Kalss (Eds.), *Münchener Kommentar zum Aktiengesetz* (5th Edition). München: C. H. Beck. Retrieved from www.beck.de.

Hannigan, B. (2016). *Company Law* (4th Edition). Oxford: Oxford University Press.

Hellgardt, A. (2010). Abdingbarkeit der gesellschaftsrechtlichen Treuepflicht. In S. Grundmann, B. Haar, H. Merkt et al. (Eds.), *Festschrift für Klaus J. Hopt zum 70. Geburtstag am 24. August 2010. Unternehmen, Markt und Verantwortung* (pp. 765–794). Berlin: De Gruyter. DOI: https://doi.org/https://doi.org/10.1515/9783899496321.

Hopt, K. J. (2004). Interessenwahrung und Interessenkonflikte im Aktien-, Bank- und Berufsrecht. Zur Dogmatik des modernen Geschäftsbesorgungsrechts. *Zeitschrift Für Unternehmens- Und Gesellschaftsrecht*, (1), 1–52. DOI: https://doi.org/https://doi.org/10.1515/zgre.2004.002.

Hopt, K. J., and Roth, M. (2015). *Aktiengesetz. Großkommentar: AktG, Band 4/2: §§ 92 - 94*. (M. Habersack, K.J. Hopt, M. Roth, and M. Foerster, Eds.) (5th Edition). Berlin: de Gryuter.

Hüffer, U., and Koch, J. (2022). Commentary on sec. 84 AktG. In J. Koch (Ed.), *Aktiengesetz* (16th edition). München: C. H. Beck. Retrieved from www.beck.de.

Janů, P. (2019). In J. Petrov, M. Výtisk, V. Beran et al. (Eds.), *Občanský zákoník. Komentář.* (2nd Edition). Praha: C. H. Beck.

Kershaw, D. (2012). *Company Law in Context* (Second Edition). Oxford: Oxford University Press.

Kraakman, R., Armour, J., Davies, P., Enriques, L., Hansmann, H. B., Hertig, G., … Rock, E. B. (2009). *The Anatomy of Corporate Law: A Comparative and Functional Approach* (2nd Edition). Oxford: Oxford University Press.

Krieger, G., and Sailer-Coecani, V. (2015). In K. Schmidt and M. Lutter (Eds.), *Aktiengesetz – Kommentar*. Köln: Otto Schmidt.

Krtoušová, L. N. (2019). *Odpovědnost členů statutárních orgánů právnických osob*. Praha: Wolters Kluwer.

Kumpan, C. (2014). *Der Interessenkonflikt im Deutschen Privatrecht. Eine Untersuchung zur Fremdinteressenwahrung und Unabhängigkeit*. Tübingen: Mohr Siebeck.

Lasák, J. (2022). In P. Lavický et al. (Ed.), *Občanský zákoník I. Obecná část (§ 1–654). Komentář.* (2nd Edition). Praha: C. H. Beck.

Leuering, D., and Rubner, D. (2020). Das Wettbewerbsverbot des GmbH-Geschäftsführers. *Neue Juristische Wochenschrift – Spezial*, 17(23), 719–720.

Loose, P., Griffiths, M., and Impey, D. (2015). *The Company Director: Powers, Duties and Liabilities* (12th Edition). Bristol: Jordan Publishing.

Oetker, H. (2021a). Commentary on sec. 35 GmbHG. In M. Henssler and L. Strohn (Eds.), *Gesellschaftsrecht* (5th Edition). München: C. H. Beck. Retrieved from www.beck.de.

Oetker, H. (2021b). Commentary on sec. 43a GmbHG. In M. Henssler and L. Strohn (Eds.), *Gesellschaftsrecht* (5th Edition). München: C. H. Beck. Retrieved from www.beck.de.

Paefgen, W. G. (2014). In P. Ulmer, M. Habersack, and M. Löbbe (Eds.), *Gesetz betreffend die Gesellschaften mit beschränkter Haftung (GmbHG). Großkommentar, Band II. §§ 29 bis 52* (2nd Edition). Tübingen: Mohr Siebeck.

Pelikán, R. (2012). *Právní subjektivita*. Praha: Wolters Kluwer.

Raiser, T., and Veil, R. (2006). *Recht der Kapitallgesellschaften* (4th Edition). München: Franz Vahlen.

Spindler, G. (2022a). Commentary on sec. 116 AktG. In G. Spindler and E. Stilz (Eds.), *Kommentar zum Aktiengesetz* (5th Edition). München: C. H. Beck. Retrieved from www.beck.de.

Spindler, G. (2022b). Commentary on section 112 AktG. In M. Henssler, G. Spindler, and E. Stilz (Eds.), *Kommentar zum Aktiengesetz. Grosskommentar*. München: C. H. Beck. Retrieved from www.beck.de.

Štenglová, I., Havel, B., Cileček, F., Kuhn, P., and Šuk, P. (2020). *Zákon o obchodních korporacích. Komentář.* (3rd Edition). Praha: C. H. Beck.

Wagner, G. (2014). Organhaftung im Interesse des Verhaltenssteuerung – Skizze eines Haftungsregimes. *Zeitschrift Für Das Gesamte Handelsrecht Und Wirtschaftsrecht*, 178(3), 227–281.

Wild, C., and Weinstein, S. (2016). *Smith and Keenan´s Company Law* (17th Edition). Edinburgh: Pearson Education.