



LUIGA MODY HÄÄL BORENIUS

## **To be or not to be a board member**

*by Helen Tulve, attorney at law  
Luiga Mody Hääl Borenius*

The decision on whether to become a board member of an Estonian undertaking should not be made hastily. It is recommended to learn beforehand what are the rights, obligations and liabilities involved. Board members, unlike executive directors or financial directors who work based on an employment contract, that are entered into the Commercial Register can have unlimited liability toward the company and its creditors. A board member may be held liable in case of damages to the full extent of his property.

### Obligations of management board members

General obligations of a board member include acting within the duty of loyalty with respect to the company and exercising the necessary level of care and diligence commensurate with the nature of the duties and position of the board member. A board member shall perform the duties to the maximum benefit of the company in light of and according to the board member's knowledge and abilities, and shall prevent any damage to the company's property.

The specific obligations of a board member are set out in the Commercial Code, the agreement concluded between the company and the board member, and the articles of association of the respective company. These obligations usually include conducting the everyday business, organising the accounting and reporting to higher bodies of the company. The board member should be aware of his exact obligations since a failure to act may also bring liability.

### Civil liability of management board members

Although the provisions governing civil liability of board members have been included in the Commercial Code since its adoption in 1995, relatively few cases have reached courts. In cases that have reached the Supreme Court, the Court has emphasised that board members' rights shall be exercised, and obligations shall be performed in good faith. The foregoing obligation involves the requirement for a board member to be diligent and sufficiently informed for making decisions, and not to take unreasonable risks for the company. In case a board member does not act with the diligence that a reasonable person in a similar position would apply in similar conditions, the board member may be regarded to have breached the duty of care, which in turn may result in personal liability.

It should be noted that complying with resolutions of higher bodies could release the board members from liability. However, since the obligations of the board members only include adhering to the lawful orders of higher bodies, acting in accordance with any unlawful order

*Advokaadibüroo Luiga Mody Hääl Borenius Attorneys at Law Luiga Mody Hääl Borenius*

**Tallinn** Kawe Plaza, Pärnu mnt 15, Tallinn 10141, Estonia Tel +372 6651 888 Fax +372 6651 899 [www.lmh.ee](http://www.lmh.ee)

**Helsinki** Attorneys at law Borenius & Kempainen Ltd, Yrjönkatu 13 A, FI-00120 Helsinki, Finland Tel +358 9 615 333 Fax +358 9 6153 3499 [www.borenius.com](http://www.borenius.com)

**Riga** Attorneys at Law Liepa, Skopiņa / Borenius, Lacplesa 20a, LV-1011 Riga, Latvia Tel +371 6 7201 800 Fax +371 6 7201 801 [www.borenius.lv](http://www.borenius.lv)

**Vilnius** Attorneys at law Foigt & Partners / Regija Borenius, J. Jasinskio str 16 A, 8<sup>th</sup> floor, LT-01112 Vilnius, Lithuania Tel +370 5264 9555 Fax +370 5260 8327 [www.regija.lt](http://www.regija.lt)



shall not preclude liability. Thus, board members should constantly evaluate the lawfulness of resolutions of higher bodies, and notify higher bodies of any resolutions contradicting the laws or economic interests of the company.

#### Criminal liability of management board members

In Estonia, board members may also be held criminally liable for their wrongful acts. Based on the Penal Code, a board member is considered an “official.” Thus, committing acts such as negligence related to office and misuse of official position are crimes applicable to the board members.

Additionally, the Penal Code establishes criminal punishments for several offences that are connected to violation of obligations of board members, such as the failure to call a general meeting of shareholders if the net assets do not comply with the requirements of law; failure to submit a bankruptcy petition if such obligation were to arise as set forth by law; fraudulent miscalculation of taxes, and other such acts.

#### Imposing liability

According to the Commercial Code, the statute of limitations for claims against a board member is five years, unless the articles of association or the agreement with the board member stipulate otherwise. However, the articles and the referred agreement may not reduce the five year limit, and can only specify a longer period of liability.

Releasing board members from liability upon annual approval by shareholders of financial results is an accepted practice. Additionally, entering into service agreements between board members and companies, and establishing limitations of liability in favour of board members to avoid subsequent claims that may be filed on behalf of the companies are also recommended. However such limitations on liability are valid only internally. External liability is liability towards creditors, which is derived mainly from the law and is unlimited.

As a rule, if a board member has acted in good faith and can also prove that, then liability toward the company or its creditors shall not follow, even if the company’s economic position has deteriorated or is damaged in any other way.