

THE DUTY OF CARE IN CZECH COMPANY LAW

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Abstract: The duty of care is a core instrument to incentivise directors to act diligently and in the best interest of the company. The article seeks to answer the following questions concerning the duty of care in company law; 1) who is obliged to exercise it, 2) to whom, 3) what is the content of the duty of care, 4) what place does it occupy among other standards of care, 5) what is its nature, and 6) how does the duty of care differ between a director of a company and director of other legal persons of private law.

Keywords: duty of care; director; company

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1. INTRODUCTION

The duty of care is a legal instrument closely related to managing someone else's property and the regulation of legal persons. Its purpose is to set an expected standard of care from the manager of someone else's property and a board member of a legal person, who is also the manager of someone else's property in a broad sense.¹ The additional purpose is to distinguish this standard from other standards with which private law operates because of the predictability of legal consequences and, therefore, the protection of everyone who participates in legal relations. In this sense, standards of conduct firstly motivate persons to behave following them. Secondly, they help in dealing with cases arising from incomplete contracts.² Finally, they are general clauses of desirable behaviour, with the result that their interpretation and application may change over time and adapt to social developments.³ This paper focuses on the regulation of the duty of care in company law so that the conclusions drawn from it are comparable

¹ The question of the relationship between the management of someone else's property and the performance of the function of a board member of a legal person is dealt with further in the text of the paper.

² SITKOFF, R. H. The Economic Structure of Fiduciary Law. *Boston University Law Review*. 2011, No. 91, p. 1044.

³ HANSMANN, H. – ARMOUR, J. – KRAAKMAN, R. in: KRAAKMAN, R. – ARMOUR, J. – DAVIES, P. – ENRIQUES, L. – HANSMANN, H. – HERTIG, G. – HOPT, K. – KANDA, H. – ROCK, E. *The Anatomy of Corporate Law: a Comparative and Functional Approach*. 3rd ed. New York: Oxford University Press, 2017, pp. 32–33.

to those of other national reports (Austria, Hungary, Poland, Romania, Slovakia), which are published in this monothematic journal issue, too.

The basic definition of the duty of care is in § 159(1) of the Civil Code (CC). There it is defined as the obligation of each director⁴ of a private law legal person, not only of the company, to perform their function correctly with the required due care.⁵ Czech law requires the directors to exercise their functions with due care (*péče řádného hospodáře*). This is a duty of care in a broader sense, as it includes not only the component of the duty of care in the narrower sense, but also the component of loyalty.⁶ The Civil Code specifies several relationships which the duty of care applies. In the first place, a manager of someone else's property shall be mentioned.⁷ Additional particular cases of management of someone else's property are, e.g., parents in the case of care of a minor child's property,⁸ guardian *ad litem*,⁹ the pledgee in care of the surrendered pledge,¹⁰ executor of the will,¹¹ and proxy (*prokurista*).¹²

The duty of care of a director of a business corporation is regulated by the Civil Code and by the Business Corporations Act (BCA).¹³ The Business Corporations Act governs the issue of the duty of care in general for all business corporations and does not provide for any exceptions for particular forms of business corporations. In light of other national reports, as I mentioned above, and in the interest of comparability, I focus on limited liability companies (*společnost s ručením omezeným*) and joint-stock companies

⁴ Further, I use the term *director* in the sense used by EMCA (European Model Companies Act) as equivalent to a board member of a business corporation. Under sec. 1.02(5) EMCA director is a member of the management body or of the supervisory body of a company.

⁵ Under § 20(2) CC, the rules relating to private law legal persons under the Civil Code shall also apply to public law legal persons in the absence of a particular regulation if the particular rule of the Civil Code is compatible with the nature of public law legal person.

⁶ It is difficult to choose the correct English equivalent for the Czech concept of due care. The official translation of the Civil Code into English translates the notion "*péče řádného hospodáře*" as due managerial care (see <https://www.cak.cz/assets/pro-advokaty/mezinarodni-vztahy/civil-code.pdf>). However, the literature use only a notion of the duty of care, not the duty of managerial care.

If we compare the content of the rule under § 159(1) CC with sec. 174 UK Companies Act 2006, then Czech law works with the concepts of necessary knowledge, necessary care, and loyalty when defining the concept of the duty of managerial care of a director, whereas the UK legislature works with the concepts of reasonable care, skill, and diligence when defining the duty of care of a director. The main difference is an element of loyalty, whether it is or not the part of the duty of care. I use the notion of duty of care under Czech law in broad sense.

⁷ § 1411 CC.

⁸ § 896(1) sentence 1 CC.

⁹ § 949 CC.

¹⁰ § 1356(1) sentence 2 CC.

¹¹ § 1554(1) sentence 1 CC.

¹² § 454 CC.

¹³ Act No. 90/2012 Sb., on Commercial Companies and Cooperatives, whose short title is Business Corporations Act (*zákon o obchodních korporacích*). The Business Corporations Act regulates not only companies as partnership, limited partnership, limited liability company, and joint-stock company, but also a cooperative. A cooperative under Czech law is a capital business corporation which can be established for business or another purpose. Cooperatives have certain particular characteristics which could be relevant in the analysis of particular issues related to the duty of care of their directors, in particular the fact that they do not have to be established for the purpose of business (e.g., housing cooperatives) and that only members of the cooperative can be director. A small cooperative is thus limited in the choice of its director by the qualities, skills, and abilities of its own members. However, these issues have not been discussed deeply in Czech doctrine yet.

(akciová společnost).¹⁴ However, the conclusions presented also apply *mutatis mutandis* to the cooperative, although I do not explicitly mention it.

The Civil Code has regulated the management of someone else's property (§ 1400 et seq. of the Civil Code) and the duty of care of the director of private law legal persons since the recodification of private law, i.e., since 2014.¹⁵ The doctrine has not been able to agree on whether or not regulation of the management of someone else's property is also applicable to directors of a business corporations by way of a subsidiary. The intention of the legislature is not clear. Under § 59(1) *in fine* of the Business Corporations Act, the rules concerning managing someone else's property do not apply to directors. Instead, the regulation on mandate shall apply complementarily. However, the purpose and sense of this rule do not clear. This rule may be a lawmaker's mistake. Doctrine accepts that a director manages the company's property.¹⁶ If the regulation of legal persons does not exclude it, the rules of management of someone else's property may also apply to the directors of legal persons, including companies.¹⁷

As I have already stated, the Civil Code requires all directors of legal persons to exercise their functions with the duty of care. Under § 159(1) of the Civil Code, whoever accepts the office of a member of an elected body¹⁸ undertakes to perform it with the necessary loyalty and with the knowledge and care needed. A person is deemed negligent if they are not capable of exercising such care, although they must have discovered

¹⁴ I leave aside the public partnership and the limited partnership for two reasons. First, there are very few of them in the Czech Republic. Secondly, the doctrine is not uniform as to whether a director is obliged to exercise their function with due care. The reason for this doubt is that a director is a shareholder and becomes a director *ex lege*, not by election, appointment, or other calling to office. See LÁLA, D. *Povaha členství ve statutárním orgánu osobní společnosti aneb je člen statutárního orgánu osobní společnosti členem voleného orgánu ve smyslu občanského zákoníku?* [Nature of membership in the Board of directors of a partnership or is a director of a partnership a member of an elected body within the meaning of the Civil Code?]. *Obchodněprávní revue*. 2018, Vol. 10, No. 4, p. 106 ff. Conversely NOVOTNÁ KRTOUŠOVÁ, L. *Odpovědnost členů statutárních orgánů právnických osob* [Liability of directors of legal persons]. Praha: Wolters Kluwer, 2019, p. 10; LASÁK, J. *Commentary to § 159 CC*. In: LAVICKÝ, P. et al. *Občanský zákoník I: obecná část (§ 1–654): komentář* [Civil Code I: General Part (§ 1–654): Commentary]. 2nd ed. Praha: C. H. Beck, 2021, p. 598 (m. 7). However, in my opinion, it is also true that they manage the company's assets, not their own, and therefore they should also act with due care when exercising their functions as a director. See HAVEL, B. in: HAVEL, B. – ŽITNANSKÁ, L. (eds.). *Fiduciární povinnosti orgánů společnosti na pomezí korporálního, insolvenčního a trestního práva* [Fiduciary duties of company bodies at the interface of corporate, insolvency and criminal law]. Praha: Wolters Kluwer ČR, 2020, p. 152.

¹⁵ Before the recodification of private law, there was no general regulation of the management of someone else's property and the management of all private law legal persons. Even the Commercial Code (Act No. 513/1991 Sb.) did not regulate this issue in general terms, but for each form of company it stipulated that directors were obliged to perform their functions with due care. In detail see NOVOTNÁ KRTOUŠOVÁ, *Odpovědnost členů statutárních orgánů právnických osob*, p. 6 ff.

¹⁶ See HAVEL, B. in: HAVEL – ŽITNANSKÁ, c. d., p. 152; DVOŘÁK, T. *Commentary to § 159 CC*. In: ŠVESTKA, J. – DVOŘÁK, J. – FIALA, J. et al. *Občanský zákoník: komentář. Svazek I (§ 1 až 654)* [Civil Code: Commentary. Volume I (§ 1 to 654)]. 2nd ed. Praha: Wolters Kluwer ČR, 2020.

¹⁷ HAVEL, B. – PIHERA, V. *Povaha funkce a odpovědnost členů orgánů obchodních korporací jako východisko racionální corporate governance* [The nature of functions and responsibilities of directors as a basis for rational corporate governance]. *Právní rozhledy*. 2019, Vol. 27, No. 23–24, p. 836 ff.

¹⁸ Under the 152(2) CC, elected bodies are those bodies to which a member is elected, appointed, or otherwise called. The duty of care thus does not apply to non-elected bodies, which include the supreme bodies of business corporations such as the general meeting of a joint-stock company.

this when accepting the office or exercising it and does not draw the consequences thereof.

The basic questions that I try to answer concerning the duty of care in company law are; 1) who is obliged to exercise it, 2) to whom, 3) what is the content of the duty of care, 4) what place does it occupy among other standards of care, 5) what is its nature, and 6) how does the duty of care differ between a director of a company and director of other legal persons of private law.

2. PERSONS SUBJECT TO THE DUTY OF CARE IN COMPANY LAW

The duty of care applies to directors, i.e., members of the board of directors and members of the supervisory board, the latter being mandatory in a joint-stock company with a two-tier board structure.¹⁹ The structure of boards of limited liability companies is one-tier unless the company decides to establish a supervisory board or a particular law requires a supervisory board (e.g., for securities traders, the Capital Market Undertakings Act requires the establishment of a supervisory board).

Under § 62 of the Business Corporations Act the duty of care applies to directors *de facto* and maybe to shadow directors.²⁰ The lawmaker also intends to extend the duty of care to the shadow directors,²¹ but the doctrine has doubts about whether the wording of the Act follows the lawmaker's intention.²² Despite these doubts however, it is accepted that a shadow director is an influential person and that they are liable to the company under § 71 of the Business Corporations Act for the damage caused by their influence, unless the influence has the quality similar to director's duty of care (arg. they will compensate for the damage unless they prove that they could reasonably have assumed in good faith that they were acting in an informed and defensible interest of the influenced person when they exercised their influence). Stanislava Černá and Lucie Josková add that the same standards which apply to the *de iure* director or *de facto* director shall apply to the shadow director who "*unofficially influences the management of the company so intensively that the influence is comparable to the content of decision-making in the performance of the function of the de iure director as to the de facto director if the only difference between them is the degree of transparency of their real influence*".²³

¹⁹ Czech joint-stock companies have the right to choose between one-tier and two-tier board structures and have the right to change the chosen structure. See §§ 395 and 396 BCA.

²⁰ Neither the *de facto* nor the shadow director is the *de iure* director. The difference between them is that the *de facto* director presents themselves externally as the director, while the shadow director is hidden from the public. Thus, a *de facto* director will regularly be a director whose term of office has expired and who nevertheless continues to hold the post. Whereas the shadow director is a controlling person who interferes so intensively in the management of the company that the *de iure* directors are probably just dummy.

²¹ Důvodová zpráva k zák. č. 33/2020 Sb., kterým byl novelizován zákon o obchodních korporacích [Explanatory report to Act No. 33/2020 Sb., which amended the Business Corporations Act].

²² LASÁK, J. – DĚDIČ, J. Commentary to § 62 BCA. In: LASÁK, J. – DĚDIČ, J. – POKORNÁ, J. – ČÁP, Z. et al. *Zákon o obchodních korporacích: komentář* [Business Corporations Act: Commentary]. 2nd ed. Praha: Wolters Kluwer ČR, 2021, p. 469.

²³ ČERNÁ, S. – JOSKOVÁ, L. in: HAVEL – ŽITŇANSKÁ, c. d., p. 42.

The duty of care is also applicable to the director's representative if the director is a legal person. Under Czech law, a legal person can be a board member (or the only board member) of limited liability or a joint-stock company. However, under § 46(3) of the Business Corporations Act, legal person, which is a director, is obliged to authorise without undue delay, a single natural person. The representative of a legal person shall fulfil the statutory requirements and prerequisites for a director. A legal person without a representative cannot be entered as a director in the Commercial Register;²⁴ upon the termination of the authorisation, the legal person is obliged to authorise a new representative.²⁵ A representative of a legal entity has the exact legal requirements as a director, including the obligation to act with due care.²⁶ If the representative is not entered in the Commercial Register within three months from the establishment of the function of the legal entity, the office of the legal entity shall cease.²⁷ The same rule applies in the case of a termination of the authorisation of the previous representative.²⁸

3. BENEFICIARY

The question to whom the directors owe the duty of the care is complex. On the one hand, the company can sue the directors for breach of their duty. On the other hand, a breach of the duty of care leads to many legal consequences.

The duty of care serves to fulfil the company's purpose, i.e., the achievement of the benefit (not necessarily profit) defined by the shareholders in the articles of association. The definition of the purpose determines the basic framework of the company's interest.²⁹ In interpreting the company's interest, a main distinction is made among the shareholder value approach, the stakeholder value approach and the enlightened shareholder value approach.^{30, 31} Although the company's interest is defined in the Civil Code and the Business Corporations Act without other details, resp. attributes,³² the doctrine

²⁴ § 46 (6) BCA.

²⁵ § 46 (8) BCA.

²⁶ § 46 (5) BCA.

²⁷ § 46 (7) BCA.

²⁸ § 46 (8) BCA.

²⁹ PELIKÁN, R. *Právní subjektivita* [Legal personality]. Praha: Wolters Kluwer, 2012, p. 62.

³⁰ EMCA, p. 213; HAVEL, B. *Obchodní korporace ve světle proměn* [Business corporations in the light of changes]. Praha: Auditorium, 2010, p. 109 ff; PATAKYOVÁ, M. – GRAMLÍČKOVÁ, B. in: HUSÁR, J. – CSACH, K. (eds.). *Konflikty zájmů v práve obchodních společností* [Conflicts of Interest in Company Law]. Bratislava: Wolters Kluwer, 2018, pp. 37–41.

³¹ The expert discourse seeking to define the notion of company interest and company beneficiary cannot be limited to these three selected models which I choose because they are the most frequently mentioned in the Czech literature and EMCA also works with them; there are more models, e.g., the team production model. KAUFMANN, A. – ENGLANDER, E. A Team Production Model of Corporate Governance. *The Academy of Management Executive* (1993–2005). 2005, Vol. 19, No. 3, pp. 9–22.

³² The definition of a company's interest in EMCA, which was inspired by the UK Companies Act, can be seen as a definition of an interest with "attributes". Under sec. 9:04 EMCA "[d]irectors must act in the way they consider, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole. In doing so the director should have regard to a range of factors such as the long-term interests of the company, the interests of the company's employees, the interest of company's creditors and the impact of the company's operations on the community and the environment". Under sec. 172 (1)

concludes that the enlightened shareholder value approach is to be considered in a particular situation.³³ In other words, a director should not be in breach of their duties if they not only consider the company's purpose but also the interests of employees, the protection of the environment, etc. in a particular case, because these interests are consistent with the long-term sustainability of the company, i.e., the long-term achievement of the defined purpose.

Third parties whose interest under the doctrine is to be taken into consideration in determining the company's interest cannot sue the directors directly for a breach of that duty. However, third parties may have a right of action for damages against a member under the general rule of tort liability.³⁴

Creditors may also claim damages against members by statutory liability for the company's debts. Under § 159(3) of the Civil Code if a director fails to compensate a legal person for damage caused by a breach of their duty, although they were obliged to do so, they shall be liable to the creditor for the debt to the extent that they have not compensated the damage unless the creditor is unable to enforce performance against the legal person.³⁵ This rule, which applies to all directors of all legal persons, also leads to doubt whether non-business legal corporations (e.g., foundations) can be negotiated with a limitation of damages with the director to the extent generally permitted in contractual relationships.³⁶ The limit of damages is forbidden to business corporations by the Business Corporation Act (see below).

Each shareholder in the limited liability company and qualified shareholder in the joint-stock company have the right to bring an *actio pro socio* on behalf of the company against the (former) director for damages caused to the company by the breach of due care.³⁷ The plaintiff in such a case is the company itself, the (qualified) shareholder is

UK Companies Act 2006 “a director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to

(a) the likely consequences of any decision in the long term,

(b) the interests of the company's employees,

(c) the need to foster the company's business relationships with suppliers, customers, and others,

(d) the impact of the company's operations on the community and the environment,

(e) the desirability of the company maintaining a reputation for high standards of business conduct, and

(f) the need to act fairly as between members of the company”.

³³ See HAVEL, B. in: HAVEL – ŽITŇANSKÁ, c. d., p. 153; PATĚK, D. in: ČERNÁ, S. – ŠTENGLOVÁ, I. – PELIKÁNOVÁ, I. et al. *Právo obchodních korporací* [Law of Business Corporations]. 2nd ed. Praha: Wolters Kluwer ČR, 2021, p. 184.

³⁴ Under § 2914 sentence 1 CC “[a] person who, in his activities, uses an agent, employee or another helper shall provide compensation for the damage caused by such a person as if he caused it himself”. This rule is interpreted as the common liability of person and their agent. Directors are classified as a non-independent agent (helper) within the meaning of this rule and may therefore be liable for damage caused to third parties in the performance of their duties for the company. See FLÍDR, J. *Deliktní odpovědnost člena statutárního orgánu obchodní korporace vůči třetím osobám* [Tort liability of a director of a business corporation towards third parties]. Praha: Wolters Kluwer ČR, 2021.

³⁵ This liability is limited by damage caused to company.

³⁶ Under § 2898 sentence 1 CC an agreement which excludes or limits in advance the obligation to compensate for injury to a person's natural rights or caused intentionally or by gross negligence shall not be considered; nor shall an agreement which excludes or limits in advance the right of the weaker party to compensate for any injury be considered.

³⁷ See §§ 157 and 371 ff BCA.

only its special representative. In addition however, Czech law has an institute of reflexive damages, where under certain circumstances, the shareholder themselves may sue the director on their own behalf for damages to the value of their share caused by a breach of the director's duties. In such disputes, however, the court has the right to decide, even without a particular motion, that the director as the one who caused the damage shall compensate the company for the damage, not the shareholder directly, if it is sufficiently apparent that such measure will also pay for the damage to the devalued share (see § 213 CC).³⁸ Not all problematic issues are resolved, including the relationship of procedural rules to substantive law.³⁹

4. CONTENT OF THE DUTY OF CARE

The duty of care has two parts – the duty of loyalty and duty of care in a narrower sense. The two duties are closely linked and overlap. The conclusion that it is not appropriate to strictly distinguish the duty of loyalty and the duty of care from each other had already been reached by pre-codification doctrine and case law,⁴⁰ and the lawmaker followed up on these conclusions by combining the two duties in defining the duty of care in § 159(1) of the Civil Code.⁴¹ Lucie Josková describes the interrelationship of these two components very precisely when she states, “*if a person is imposed a duty of loyalty and at the same time a duty to act with a certain standard of care, the duty of loyalty is necessarily reflected in the duty to act with care. Acting in the interests of the person entitled will be the framework within which the person's competence under an obligation to act will be judged. A director will fulfil his or her duty to act with due care only if, in the exercise of his or her functions, s/he acts with the knowledge, skill and care required in the particular case by the company's interests.*”⁴²

³⁸ The adjustment of reflective damage is a new phenomenon and therefore raises a lot of questions. For example, there are questions whether the *actio pro socio* excludes the possibility for a shareholder to claim reflexive damages. In other words, if a shareholder is able to bring an *actio pro socio* on behalf of the company, they are not entitled to bring an action for reflexive damages. LASÁK, J. Commentary to § 213 CC. In: LAVICKÝ, P. et al. *Občanský zákoník I: obecná část (§ 1–654): komentář* [Civil Code I: General Part (§ 1–654): Commentary]. 2nd ed. Praha: C. H. Beck, 2021, p. 842 (m. 3).

³⁹ HRABÁNEK, D. Commentary to § 213 CC. In: PETROV, J. – VÝTISK, M. – BERAN, V. et al. *Občanský zákoník: komentář* [Civil Code: Commentary]. 2nd ed. Praha: C. H. Beck, 2019, p. 286 (m. 10); LASÁK, J. Commentary to § 213 CC, p. 848 (m. 30, 31).

⁴⁰ HAVEL, *Obchodní korporace ve světle proměn*, p. 155 ff.

⁴¹ ČECH, P. – ŠUK, P. *Právo obchodních společností: v praxi a pro praxi (nejen soudní)* [Law of Business Corporations: in practice and for practice (not judicial only)]. Praha: BOVA POLYGON, 2016, p. 165; NOVOTNÁ KRTOUŠOVÁ, *Odpovědnost členů statutárních orgánů právnických osob*, p. 9; ŠTENGLOVÁ, I. – ŠUK, P. Některé důsledky porušení péče řádného hospodáře (nejen) v judikatuře českých soudů [Some consequences of breach of the duty of care (not only) in the Czech case law]. *Obchodněprávní revue*. 2021, Vol. 13, No. 3, p. 153; Judgment of the Supreme Court of 25 April 2019, case no. 27 Cdo 2695/2018.

⁴² JOSKOVÁ, L. Je rozdíl mezi povinností loajality a povinností postupovat s péčí řádného hospodáře? [Is there a difference between the duty of loyalty and the duty to exercise due care?]. *Obchodněprávní revue*. 2019, Vol. 11, No. 11–12, p. 281 ff.

The duty of loyalty does not only mean the prohibition of enriching oneself at the expense of the company or to harm but also the duty to fulfil the purpose for which the company was established.⁴³

The duty of care then requires that the function be performed with a certain quality.⁴⁴ The propriety of the performance of the function is judged according to the particular circumstances, which may include the type of legal persons,⁴⁵ type and size of the business, the number of employees, the market situation, and the company's particular economic situation.⁴⁶ Other relevant circumstances may include whether the company has issued securities traded on a European regulated market, whether the director is a member of the managing or supervisory board, whether they are an executive or non-executive board member or whether the horizontal delegation of competence is made in the board. In short, all circumstances shall be evaluated.⁴⁷

The requisite standard of care is objectified in the corporate context because its observance is judged in terms of an imaginary “*reasonably careful*” director who “*must not be anxiously cautious (business is inherently risky – necessarily requiring some degree of ‘brave initiative’ or ‘entrepreneurialism’), nor, again, excessively adventurous or foolhardy (both extremes establish mismanagement)*”.⁴⁸

However, if the director is an expert in a particular field (lawyer, economist, engineer, etc.), it is possible for the company to agree with them to use that professional knowledge, skills, or abilities in their role as a director.⁴⁹ Czech doctrine calls this the raising of standard subjectification of the duty of care. The increasing of the standard of the duty of care can be done by the service contract, the articles of association, and by the factual situation, e.g., if a particular person is appointed to a specific position on the board in a horizontal delegation (essentially a tacit agreement to raise the standard of care following the objective expectations associated with a particular position). Thus, the statutory standard of the duty of care cannot be lowered by contract but can be raised. The limit is the requirement that the standard of the duty of care not be raised so that the director is not liable for the propriety of the performance but the result. Directors are not liable for the result; the company and shareholders bring the risk of (business) unsuccess⁵⁰ and this is a basic characteristic of companies which cannot be excluded by agreement concluded by company and director.

Doctrine and case law conclude that the objective standard is subjectified even if the director has particular expertise, skills, or abilities.⁵¹ In other words, it is concluded that if

⁴³ ČERNÁ – JOSKOVÁ, *c. d.*, p. 42.

⁴⁴ *Ibid.*, p. 42.

⁴⁵ Lucie Novotná Krtoušová rightly argues that it is necessary to differentiate very sensitively between different types of legal persons as to what the duty of care implies in their circumstances. (NOVOTNÁ KRTOUŠOVÁ, *Odpovědnost členů statutárních orgánů právnických osob*, p. 26).

⁴⁶ ČERNÁ – JOSKOVÁ, *c. d.*, p. 42.

⁴⁷ ŠTENGLOVÁ – ŠUK, *c. d.*, p. 153 ff.

⁴⁸ ČECH – ŠUK, *c. d.*, p. 161.

⁴⁹ HAVEL, *Obchodní korporace ve světle proměn*, p. 155.

⁵⁰ ŠTENGLOVÁ – ŠUK, *c. d.*, p. 153 ff.

⁵¹ BORSÍK, D. Péče řádného hospodáře a pravidlo podnikatelského úsudku bez legend [Duty of care and business judgement rule without myths]. *Obchodněprávní revue*. 2015, Vol. 7, No. 7–8, pp. 193–205; ČECH – ŠUK, *c. d.*, p. 162; PATĚK, *c. d.*, p. 187.

a director has specific professional knowledge, skills, or abilities, they are obliged to use them in the performance of their function even if it is not explicitly or tacitly agreed.⁵²

5. THE DUTY OF CARE IN THE SYSTEM OF CONDUCT STANDARDS

What place does the duty of care have in the system of other standards of expected behaviour? The Civil Code distinguishes between, on the one hand, the ordinary care and caution that is expected of everyone acting (§ 4 CC)⁵³ and the professional care, on the other hand, that is expected of professionals (§ 5(1) CC).⁵⁴ The standard of ordinary care is the lowest standard of all, and the standard of professional care is the highest standard of all. Where does the duty of care fit in?

The doctrine concludes that exercising the functions of a director cannot be regarded as the exercise of a profession requiring professional-level competence.⁵⁵ The majority's approach is that the duty of care is the middle standard among ordinary care and professional care.⁵⁶

At the same time however, it recognises that a director cannot be incompetent because they are supposed to be able to conclude that they need professional assistance in solving a particular problem and because they must be able to supervise the provision of such professional assistance.⁵⁷ With these conclusions in mind, I do not think that we are precluded from concluding the case that, while a director need not be professionally competent in the way that is required of the company itself in legal dealings, they must be professionally competent in the way that is required of another director in a similar

⁵² Czech doctrine has therefore concluded the same rule that the British legislature expressed explicitly in sec. 174(2) UK Companies Act 2006. Under sec. 174(2) UK Companies Act 2006 [reasonable care, skill, and diligence] means the care, skill, and diligence that would be exercised by a reasonably diligent person with (a) the general knowledge, skill, and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company, and (b) the general knowledge, skill, and experience that the director has.

⁵³ Under 4 CC "[i]t is presumed that every person of full capacity has the mind of an average person and the ability to use it with ordinary care and caution, and that everyone may reasonably expect this of him or her in legal dealings. It's a rebuttable presumption."

⁵⁴ Under 5(1) CC "[w]hoever, in public or in dealings with another person, declares himself to be a member of a particular profession or class of persons, thereby shows that s/he is capable of acting with the knowledge and diligence associated with his or her profession or class of persons. If s/he acts without such professional care, s/he shall be held liable."

⁵⁵ HAVEL, *Obchodní korporace ve světle proměn*, p. 154 ff; ČECH – ŠUK, *c. d.*, p. 165; NOVOTNÁ KRTOUŠOVÁ, *Odpovědnost členů statutárních orgánů právnických osob*, p. 26; PATEK, *c. d.*, p. 183 ff; Judgment of the Supreme Court of 30 September 2019, case no. 27 Cdo 90/2019. Controversary Tomáš Dvořák concluded that if the law requires professional management of the company, the performance of the director's office must also be professional. (DVOŘÁK, T., *c. d.*).

⁵⁶ HAVEL – PIHERA, *c. d.*, p. 836 ff.

⁵⁷ NOVOTNÁ KRTOUŠOVÁ, *Odpovědnost členů statutárních orgánů právnických osob*, p. 52. In both horizontal and vertical delegation, the director is required to comply with the following rules if the required standard of care is to be achieved: (i) choosing the appropriate person, (iii) creating the appropriate conditions and providing adequate cooperation, and (iii) monitoring EICHLEROVÁ, K. in: ČERNÁ – ŠTENGLOVÁ – PELIKÁNOVÁ, *c. d.*, p. 391; Judgment of the Supreme Court of 30 September 2019, case no. 27 Cdo 90/2019.

position. In other words, I believe that the duty of care is a subset of professional care.⁵⁸ However, a director's professional care is lower level than the professional care which is required of the legal person whose a director is involved. The professional care of the legal person is more complex. In other words, the position of a director is a profession within the meaning of § 5 of the Civil Code.

6. NATURE OF THE DUTY OF CARE

The 2012, Civil Code abandoned the doctrine of the single tort and separated contractual and non-contractual liability for damages. It was the reason for opening the debate of the nature of the duty of care. The key question is whether the duty of care is a contractual or non-contractual obligation. Liability for a breach of a contractual duty consists of compensation for damages under § 2913 of the Civil Code. Damages for a breach of a non-contractual duty are dealt with in § 2910 of the Civil Code.

Contractual liability for damages is a simple strict liability, whereas tort liability for damages is a subjective liability with presumed negligence. The difference between them is in fault, imputability in the possibility of awarding so-called net economic loss and the degree of liability for acting of helpers.⁵⁹

Supporters of contractual liability for a breach of the duty of care argue that the director's function is taken over voluntarily, and the relationship between the director and the company is contractual.⁶⁰

Those in favour of tort liability for a breach of the duty of care argue that it is a statutory duty which cannot be excluded by contract. Bohumil Havel and Vlastimil Pihera argue in favour of the conclusion of the director's tortious liability for the performance of their office that the office of the director is a "*private office*" which is "*endowed by law with certain rights and duties, irrespective of the title of the office*".⁶¹

Lucie Krtoušová Novotná argues that the director's liability is tortious because they act for the company as its legal and not contractual representative.⁶² Ivana Štenglová and Bohumil Havel add that "*the nature of the relationship and from it arising obligations (contractual v. statutory) and the nature of the representative authority arising from this relationship need not to be identical*".⁶³ I disagree with conclusion

⁵⁸ EICHLEROVÁ, K. in: ČERNÁ – ŠTENGLOVÁ – PELIKÁNOVÁ, c. d., p. 390.

⁵⁹ In detail see JANOŠKOVÁ, A. *Náhrada škody při porušení smluvní a mimosmluvní povinnosti v občanském právu* [Damages for breach of contractual and non-contractual obligations in civil law]. Praha: Wolters Kluwer ČR, 2021.

⁶⁰ ČECH – ŠUK, c. d., p. 174; LASÁK, J. Commentary to § 51 BCA. In: LASÁK, J. – DĚDIČ, J. – POKORNÁ, J. – ČÁP, Z. et al. *Zákon o obchodních korporacích: komentář* [Business Corporations Act: Commentary]. 2nd ed. Praha: Wolters Kluwer ČR, 2021, p. 360.

⁶¹ HAVEL – PIHERA, p. 836 ff.

⁶² NOVOTNÁ KRTOUŠOVÁ, L. Odpovědnost za jednání s péčí řádného hospodáře... z pohledu teorií právnických osob [Liability for acting with due care... from the point of view of legal entity theories]. *Časopis pro právní vědu a praxi*. 2020, Vol. 28, No. 2, p. 247.

⁶³ ŠTENGLOVÁ, I. – HAVEL, B. Commentary to § 51 BCA. In: ŠTENGLOVÁ, I. – HAVEL, B. – CILEČEK, F. – KUHN, P. – ŠUK, P. *Zákon o obchodních korporacích: komentář* [Business Corporations Act: Commentary]. 3rd ed. Praha: C. H. Beck, 2020, p. 165 (m. 4).

on tort liability based on the argument that they are a legal representative. A director is not a legal representative of the company like, for example, a parent of a minor child, because the company has the ability to influence who the director will be and has internal mechanisms to respond to the director's failure. Statutory representation is characterized by the fact that the represented party is not able to influence who their representative is and the mechanisms against their failure are external (e.g., court interference). This conclusion cannot be altered by the approach of case law and doctrine, which considers the director to be a representative *sui generis*, i.e., neither a contractual nor a statutory representative.⁶⁴ Personally, I am inclined to the view that we can consider a director as a *sui generis* representative. The reason for this conclusion is, in my opinion, the fact a director as representative of a legal person is regulated under the regulation of legal persons in the Civil Code and the regulation of representation applies to them only in the subsidiary. I do not agree with the conclusion that the fact the director is a *sui generis* representative means that only the general rules of representation can apply to them.⁶⁵ In my opinion the rules of contractual representation, which are consistent with a director's nature, can apply.⁶⁶ I regard the director as a *sui generis* representative because I do not consider the conclusion that they are a legal representative to be supportable also because in the exceptional situation where a director is appointed by the court as liquidator, so called against their will [§ 191(3) CC], we can also perceive that by accepting the position of director the person concerned was aware of this possibility if the company enters into liquidation and the court has decided to dissolve the company or no one has been called to act as liquidator in other cases.

Finally, there are views that, as a practical matter, it is irrelevant whether the liability is in contract or tort because the objective standard of the duty of care means that a breach of that standard occurs when a director is unknowingly negligent, which is close to contractual liability where the fault is not required.⁶⁷

7. DIFFERENCES BETWEEN DIRECTORS IN COMPANIES AND OTHER LEGAL PERSONS

What are the basic differences between the care of a duty of a director of a company and the care of a duty of a director of the other legal person? In the following, I mention only the basic ones, leaving aside especially those related to the bankruptcy of the company.

⁶⁴ LASÁK, J. Commentary to § 164 CC. In: LAVICKÝ, P. et al. *Občanský zákoník I: obecná část (§ 1–654): komentář* [Civil Code I: General Part (§ 1–654): Commentary]. 2nd ed. Praha: C. H. Beck, 2021, p. 612 (m. 1); ČECH – ŠUK, c. d., p. 21 ff; Judgment of the Supreme Court of 23 July 2019, case no. 27 Cdo 4593/2017.

⁶⁵ Judgment of the Supreme Court of 23 July 2019, case no. 27 Cdo 4593/2017.

⁶⁶ EICHLEROVÁ, K. *Zastoupení podnikatele* [Representation of Entrepreneur]. Praha: Wolters Kluwer ČR, 2022, p. 22.

⁶⁷ LASÁK, *Commentary to § 51 BCA*, p. 360; ŠTENGLOVÁ – ŠUK, c. d., p. 153 ff.

The business judgment rule is expressly articulated only for business corporations in the Business Corporations Act.⁶⁸

We can divide the consequences of a breach of due care into private and public law. The private law consequences of a breach of due care by a director in a company include the possibility of removal from office, the obligation to compensate for damages, the obligation to hand over benefits of a breach, the reversal of the burden of proof, and the creation of legal liability for the debts of the legal entity towards its creditors.⁶⁹

The directors can be removed without cause. The breach of a duty is legally relevant in the case of the removal of the director who is a shareholder. In this case, the shareholder shall not vote on the issue of their removal.⁷⁰

While a director of another legal person than business corporations is obliged to compensate for damage in case of a breach of due care, the liability of a director in a company is broader, as they are obliged to compensate not only for pecuniary damage but also for non-pecuniary damage.⁷¹ The obligation to hand over the benefit and the reversal of the burden of proof only applies to a company's director, not to directors of other legal entities.

It is impossible to limit the extent of a company's director's indemnification *ex ante*; it is possible based on a settlement agreement approved by a two-thirds majority of the general meeting *ex post*.

Under 52(2) of the Business Corporations Act, if the issue before the court is whether a director has acted with due care, the burden of proof is on that director unless the court decides that the director cannot fairly be required to do so. This means that the plaintiff has the burden of alleging and proving the director's conduct, the injury, and the causal connection between the director's conduct and the injury.⁷² It is for the director, as the defendant, to allege and prove that they did not breach their duty of care in the conduct in question. Under this doctrine, the burden of proof is on the plaintiff in the case that the defendant is the heir of the director.

The public law consequences of a breach of the duty of care include a disqualification order and the incurrance of criminal liability. While any director of any legal person may commit a criminal offence due to a breach of due care, the court's decision to disqualify a director from office (disqualification) applies only to company directors.

⁶⁸ It is widely debated in doctrine whether the business judgment rule applies only to companies or also to other legal persons. In detail see JOSKOVÁ, L. Business Judgment Rule in the Czech Republic. *Acta Universitatis Carolinae Iuridica*. 2022, Vol. LXVIII, No. 3, pp. 37–47.

⁶⁹ ŠTENGLOVÁ – ŠUK, *c. d.*, p. 153 ff.

⁷⁰ §§ 173(1) para c) and 426(1) para c) BCA.

⁷¹ This conclusion is implied from § 3(2) of the BCA. According to it, if this law imposes an obligation to compensate for damages, it also imposes an obligation to compensate for non-pecuniary damage. The Business Corporations Act does not expressly impose a duty to compensate directors for damages; the Civil Code provides for that. However, the doctrine implies that a director is also liable for non-pecuniary damage caused by the breach of their duties. LASÁK, J. Commentary to § 3 BCA. In: LASÁK, J. – DĚDIČ, J. – POKORNÁ, J. – ČÁP, Z. et al. *Zákon o obchodních korporacích: komentář* [Business Corporations Act: Commentary]. 2nd ed. Praha: Wolters Kluwer ČR, 2021, p. 31 ff. Conversely HAVEL, B. Commentary to § 3 BCA. In: ŠTENGLOVÁ, I. – HAVEL, B. – CILEČEK, F. – KUHN, P. – ŠUK, P. *Zákon o obchodních korporacích: komentář* [Business Corporations Act: Commentary]. 3rd ed. Praha: C. H. Beck, 2020, p. 11 (m. 4).

⁷² Judgment of the Supreme Court of 4th September 2018, case no. 27 Cdo 4163/2017.

Disqualification applies only to directors of the managing board, *de facto* director, shadow director, and liquidator, not to directors of the supervisory board.⁷³

8. CONCLUSIONS

During the recodification of private law, the legislature tried to clarify many issues related to the duty of care by detailed regulation. However, some issues have remained unresolved, and new ones have arisen.

This article deals with some key points of the duty of care in Czech company law. Its aim is to describe selected key aspects so that the Czech approach can be compared with approaches in other countries (see other national reports).

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⁷³ § 63 ff BCA.