

focus on legalities

Obligations and liabilities of a board member in Estonia – **Part 2**



Introduction

Since many SCCE member company board members are non-Estonians, I thought it would be a good idea to write a bit about the obligations and liabilities that follows once you have become a board member in an Estonian company. (If you want to learn more about the difference between a Swedish board and the Estonian supervisory and management boards, please refer to issue nr 1/2007 of **focus**.)

In **focus** issue nr 3/2007 I wrote about the rights, obligations and liabilities of supervisory board members. In this issue I will focus on management board members.

I will start again by stating that there are two boards in an Estonian limited company, according to the main rule. In an Aktsiaselts there is always both a supervisory board and a management board. In an Osühing, there may be only a management board. The main rule is that if the share capital of Osühing exceeds 400 000 EEK the company should either have a supervisory board or at least three members in the management board.

The tasks and the election of the management board members

The management board (Est: juhatus) is the body that represents and directs the company and organises its accounting. This is the body that runs the day-to-day business. In case there is only one management board member, this one is in Estonian called juhataja.

An employed managing director (Est: tegev direktor), which you can find in some Estonian companies, should not be mixed up with a management board member. The difference between a management board member and an employed managing director is foremost that the rights and obligations of a management board member is set in the Commercial Code (Est: Äriseadustik) while a managing director is an employee of the company and his/her tasks are set forth in an employment agreement.

The management board is elected by the supervisory board for a maximum term of three years.¹ If the articles of association stipulates a longer term that is ok for up to five years. Please note that this means that all management board members must be re-elected after each maximum term. This is something that many companies tend to forget about.

The management board members possess the right to represent the company so even though the management board is inferior to the supervisory board, the signatory powers lie with them alone.

The management board shall, in directing the company, adhere to all lawful orders of the supervisory board. Transactions that are beyond the scope of everyday economic activities may only be concluded with a consent of the supervisory board.

One very important issue among the tasks of a management board member is to call for a special shareholders' meeting if the net assets of the company are less than one-half of its registered share capital. Also worth mentioning is that it is the task of the management board to prepare the annual report of the company.

Pay, vacation, agreements between a board member and the company

The supervisory board decides about the remuneration of the board member and the size of such.² There is no general obligation to pay remuneration to a management board member, but only in cases where the board member is also a shareholder, can one claim that this may be acceptable.

As a management board member is not employed, this means that issues like vacation, providing of working equipment, how and when either party can terminate the legal relationship, all this needs to be agreed upon separately. This is usually made in a so called service agreement.

¹ In case the company does not have a supervisory board, the management board is elected by the shareholders.

As the management board member cannot represent the company in agreement/s with him/herself, the supervisory board/shareholders must make a formal decision to appoint somebody to sign any agreement concluded with a management board member.

Unless these requirements are fulfilled, the company cannot enter into any valid agreement with its management board member/s. I would strongly advise all management board members to check if such a decision was made prior to concluding your service agreement (if you have any).

Management board meetings – are these necessary?

In case there are three or more management board members, the board must elect a chairman. But even if there are only two management board members, it could still be wise to have board meetings and to take minutes of these. This is important if it later turns out that a board member would like to claim that he/she was not aware of a certain decision or how different board members voted in a certain issue.

As no-one is interested in more administration than necessary; only when making important decisions, and especially if the board members have different opinions, formal meetings with signed minutes would be advisable.

Competition and secrecy restrictions

All board members are restricted under law to compete with the company. In case of breach of the competition restrictions,

² In case the company does not have a supervisory board, this decision is made by the shareholders.

the company may demand from such board member to stop the prohibited activity, transfer any income received through the prohibited activity as well as be obliged to compensate the company for any damages suffered.

All management board members are obliged to preserve the business secrets of the company under law.

Liability of a management board member

A member of the board shall fulfil his or her obligations with the due care of a diligent entrepreneur.

Management board members who cause damage to the company by violation of their obligations shall be liable joint and several for compensation for the damage caused. This means that the company can turn against either board member and claim compensation. But if a certain member is able to demonstrate that he or she has fulfilled its obligations (for example through minutes from board meetings), liability will not occur for that person.

Based on practice from the Estonian Supreme Court it may be concluded that a member of the management board should fulfil at least the following minimum criteria to avoid liability: be careful, sufficiently informed to make decisions and not to take unnecessary risks for the company.

A claim for payment of compensation to a company may also be submitted by an creditor of the company if the assets of the company are not sufficient to satisfy its claims. The general limitation period for submitting claims against a management board member is five years.

Some advise for a management board member

In addition to the above, the articles of association may grant the management board more or less rights and obligations. If you are a management board member of an Estonian company, I strongly advise you to study the articles of association of that company with care. If you do not understand Estonian, you should make sure that a professional translator translates them and if you have questions, you should turn to a professional advisor.

Karolina Ullman

Partner MAQS Law Firm

Member of the Swedish and Estonian Bar Associations

Karolina Ullman

Karolina holds a Master of Laws from Stockholm University from 1998. She did her Swedish court practise 1999-2001 in Bollnäs District Court.

In 2001 she joined MAQS Law Firm's Stockholm office as an associate, assisting MAQS Law Firm's clients with an interest in Estonia.

Since 2002 she has worked part time in Estonia and as from 2004 full time. In October 2005, MAQS Law Firm opened its full service law firm in Estonia where Karolina is one of five partners.

Karolina speaks Swedish, Estonian and English. She is a member of the Swedish Bar Association and an associated member of the Estonian Bar Association.

MAQS Law Firm is a dynamic full service law firm within business law with offices in Stockholm, Gothenburg, Malmö, Copenhagen, Warsaw and Tallinn.

Karolina Ullman



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