COMPARATIVE ANALYSIS OF FIDUCIARY DUTY PAPERS

Holly Gregory, Carol Hansell, Laurence Hazell

This article and the papers referred to, which are available on the ABA website, are not intended to constitute legal advice. Expert local counsel should always be consulted when action is contemplated in relation to any of the laws, provisions and cases described herein.

Overview

The purpose of this project has been to develop our understanding of the role of corporate directors of limited liability corporations in a number of jurisdictions around the globe. We have approached this issue through an exploration of the concept of fiduciary duty - the duties of care and loyalty that are well understood as the predicates of director duties in the United States under State corporate law. This paper is the work product of members and friends of the American Bar Association, Section of Business Law, Corporate Governance Committee, International Developments Subcommittee.¹

Discussions of governance systems often appear to assume that directors have similar duties, without exploration of whether that is in fact the case. In common law jurisdictions the fiduciary duty is the cornerstone of the relationship between directors and the corporations they serve. However, the core concept of the fiduciary duty owed by a director to the corporation has in many ways evolved differently in these common law jurisdictions. Therefore what the concept of fiduciary duty actually means in terms of the duties, obligations and restrictions it imposes on directors is crucial to understanding corporate governance standards in those jurisdictions. Similarly, to understand the role of a board in the governance system in civil law jurisdictions² requires understanding what is required of a director, whether under a fiduciary duty concept or under another legal construct detailing parallel behavioural obligations and restrictions.

Approach Used in Comparing Project Papers in this Article

Members of the International Developments Subcommittee (and colleagues they co-opted across the globe) have contributed papers on the fiduciary duties of directors in twenty jurisdictions.³ Of these, eight are common law jurisdictions (United States, United Kingdom, Australia, Canada, Hong Kong, India, Malaysia and Singapore). We

¹ A list of all the contributors, their affiliations and the paper they contributed can be found at Appendix A
² For the purposes of this project we refer generally to “civil law” jurisdictions notwithstanding differences between Roman and Germanic legal traditions.
³ Argentina, Australia, Canada, China Croatia, France, Germany, Hong Kong, India, Indonesia, Macedonia, Malaysia, the Netherlands, Russia, Serbia, Singapore, Slovenia, Thailand, United Kingdom, United States.
have looked to the US and U.K. as the lead jurisdictions in the common law world for each issue. This has proven useful, because although U.S. and U.K. law have similar foundations, they have developed differently in many ways. Other Commonwealth jurisdictions like Australia, Canada, Malaysia and Singapore, together with jurisdictions strongly influenced by English law like Hong Kong, have developed generally in the same way as the U.K. law, although there too important differences are found.

In reviewing the non-common law jurisdictions, we look first to the issues raised in the French and German contributions along with the interesting points of comparison and contrast afforded by the contributions from Argentina, China, Indonesia, the Netherlands, Russia, Thailand and the countries of the former Yugoslavia (Croatia, Macedonia, Serbia and Slovenia). Transition economies that contributed to this project provided particular points of comparative interest, although in the case of China, Russia and India it is clear that the notion that they are developing countries must accommodate the significance these nations already have in the global economy.

All the contributions, whether from common or civil law countries, note that publicly listed corporations (and private limited liability companies) are deemed to be separate legal entities. That legal status facilitates flexible (and complex) patterns of ownership and makes possible the separation of those who own the corporation from those who manage it. Accordingly, there is perceived to be a need to impose standards of conduct and responsibility on the company's controllers to ensure that they manage the corporation's assets in the interests of the direct and indirect owners – that is the company and its shareholders.

To more readily capture some of the subtleties of the different legal traditions we have written this introduction for the papers; the papers themselves can be accessed online at www.placeholder.org/. The advantage of publishing the papers online is that it will allow the authors to amend their contributions to reflect changes in legislation and case law and online publication also allows the addition of jurisdictions not yet represented. The authors of the papers responded to a working outline ⁴ including some general propositions and illustrative questions to which they crafted their written response, as shaped by the legal architecture and relevance in the jurisdiction concerned. The different emphasis that authors placed on aspects of the working outline is itself illustrative of some of the subtleties of the different legal traditions and cultural mores that underlie a formal presentation of fiduciary duty concepts

**Dual Boards**

For the purposes of this paper we are concentrating on the top or supervisory board level - the equivalent of the board of directors in common law jurisdictions. Many civil law countries including Germany and the Netherlands have dual board systems comprised of a supervisory and management board. These contributions do emphasize the importance of the dual board structure to a proper understanding of director duties and they do appear to be distinct from the treatment of a company's officers in the

---

⁴ See Appendix B
governance system in common law countries, the closet equivalent to the management board.

In Germany the executive/management board (or "Vorstand") manages the business, while the supervisory board (the "Aufsichtsrat") controls and supervises the actions of the Vorstand. The German paper sets out some distinctions between the boards under current German corporate law in terms of an exception to "strict fiduciary rules" for the management board, because they are considered too restrictive for effective everyday management. However, it is clear that the extent of this exception is unclear in the cases that have come before Germany's Federal Civil Supreme Court.

The governance arrangements of the Netherlands company boards are unique in Europe and contrast markedly with board arrangements in France where the dual board structure can be adopted voluntarily. The updating of the Netherlands Civil Code by the more specific content of the Tabaksblat Committee recommendations, which came into force in 2004, reiterates the distinct duties of the Management and Supervisory boards.

**How did the concept of Fiduciary Duty Develop?**

Contributors were asked to explain how the concept of fiduciary duties developed in their jurisdiction. The US and the U.K. papers describe the emergence of common themes in response to similar challenges relating to capital formation. Both make the point that, as the corporate form grew in importance as a vehicle of commerce, there developed a need for a legally enforceable standard of conduct for those responsible for managing businesses which they did not themselves own.

The U.K. paper describes the connection between the limited liability corporation and the characterization of directors as fiduciaries in some detail. Limited liability joint stock companies were conceived during Britain's industrial revolution as investment vehicles that would promote capital formation. Investors were attracted to acquiring shares of the newly created corporations because of the opportunity to share in profits without needing to spend personal time and attention in managing the assets or operating the business and because their own liability was limited to the sum of their investment. The company was defined in law as being a separate legal person and it was the company (rather than the investor) who carried on the business, owned the assets and was exposed to any liabilities incurred in connection with running that business.

However, corporations can only act through their human actors (the board of directors and managers who are charged with carriage of the company's business and affairs). As the U.K. paper notes, “[t]he central point of imposing fiduciary duties upon directors is prevent the utilization of the advantages of control at a cost to the company through a duty to act *bona fide* – as a fiduciary – in the interests of the company”. The Australian paper describes the development of the fiduciary duty in a similar way noting, that a fiduciary duty is typically established in law because the exercise by the fiduciary (the director) can adversely affect the interests of the person to whom the duty is owed (the corporation) and the corporation is at the mercy of its fiduciaries (the directors).
The US paper also describes the dichotomy created between the interests of officers and directors on the one hand and shareholders on the other as the size of corporations grew. In order to realign these interests, courts began to treat directors and officers as trustees, who had common law obligations to act in the best interests of the corporation's beneficiary's – the shareholders. As the law developed, the nature of the director's fiduciary relationship to the corporation became distinguished from the relationship between a trustee and the trust beneficiaries. However, the courts continued to insist on "undivided and unselfish loyalty to the corporation [which] demands that there shall be no conflict between duty and self interest."

The contributions from France and Germany both note the antiquity of the concept of a fiduciary, but in France the Code of Commerce of 1807 did not provide anything akin to a fiduciary duty concept and did not even countenance the regulation of companies for the different forms of incorporation available under the Code. In fact this first post Revolution code focused on the relationship between shareholders and the means for resolving their own differences. Corporations as such (societes anyonymes), only became the focus of legislation in 1867 in a law that provided that "corporations are managed by one of more revocable representatives chosen among the shareholders."

Even then, the French law did not provide for a board of directors as a collective body, although as a practical matter, shareholders often provided for the collective exercise of management of the company in company articles. In Germany fiduciary duty concepts as applied in the corporate context were directed at the company's shareholders - it being a later development to regard them as being owed to the company. But, according to the paper, by the beginning of the twentieth century concepts akin to fiduciary duty were embodied in German corporate law and since that time have been steadily developed by case law.

Two significant transition economies provide some interesting contrasts so far as the emergence and development of fiduciary duty concepts are concerned. In China, the concept only recently been adopted by the Chinese legal system. The adoption followed the introduction of Deng Xiaoping's "Four Modernizations" in 1978. These saw China embark on a program of regulatory reform to establish the legislative framework, institutions and practices required by a modern market economy.

Early in the Chinese reform process, emphasis was placed on the moral qualities of managers rather than their legal obligations. For example, the legislation governing stated owned enterprises provides that all managers hired must have "high morals, abide by the law, not commit corruption and be hardworking." The Company Law was first enacted in 1993, for a variety of purposes, including "to protect the lawful rights and interests of companies, shareholders and creditors".

---

5 The concept of a board of directors was first introduced to the 1867 Law through an amendment in 1917 and further expanded in 1940
The statute has since undergone revision, but originally required directors to "faithfully perform their duties and protection the interests of the company" and prohibited them from Using "their position, functions and powers in the company to seek personal gain". As an unnamed Chinese security regulator reportedly stated in 2001 "[u]ntil two years ago, no one here had heard of 'conflict of interest' or 'fiduciary duty'".

In Russia, as in China, ownership of private property was limited and corporations and share ownership were virtually unknown from 1917 to 1991. However, right before the collapse of the Soviet Union the government issued Decree 601 enacting the "Statute on Joint Stock Companies" One provision that bordered on an articulation of fiduciary duties was Article 10 of the legislation, which created damages liability for directors or management if malfeasant acts resulted in bankruptcy.

Within months of the Russian federation coming into being a 1992 law sought to accelerate the privatization process and a model charter included duties of loyalty and care and further legislative initiatives reinforced through a new Civil Code and Part II of that Code which introduces an agency relationship. So, while Russian law does not have a term that is the equivalent of "fiduciary" the Russian Law on Joint Stock Companies ("JSC Law") is patterned, in many respects, on US law which the author of the paper on Russia says can be thought of as effectively creating fiduciary type relationships.

While fiduciary duty governance practices have developed in response to the separation of ownership and control through the corporate form, this separation is at a far earlier stage in Thailand, which may explain the less well-developed legal responsibilities of directors in relation to the roles of managers and shareholders. Most Thai companies - both private and public - developed from family-owned businesses and often shareholding and management continue to be concentrated in family members. Investment decisions of "outside shareholders" (those not related to the controlling family) are understood to be based on their confidence in the controlling shareholders who are actively engaged in managing the firm. The directors owe duties of prudence and good faith to the shareholders under agency law and various statutes.

Putting aside the stage of development or recent transitions from other economic systems it does appear that the fiduciary duty concept did not develop in civil law countries in a way that is easily compared with common law jurisdictions. This appears to be mainly because of the absence of the distinction between legal and equitable title in civil law systems, despite their analogues to the concept of 'trust' or 'acting in trust'. Consequently some of the closest parallels in the civil law contributions come in the form of contemporary requirements that directors and officers have regard to transparency requirements or hew to guidelines promulgated by the OECD Principles of Corporate Governance. Reading the contributions invites some interesting parallels between capital formation and the governance systems as they developed in civil law countries and some features of contemporary transition or emerging market economies.
What does being a fiduciary mean?

The US paper describes a fiduciary as “one who must exercise a high standard of care in managing another’s money or property” and “one who owes to another the duties of good faith, trust, confidence, and candor.” Thus, the fiduciary duty of directors to the corporation they serve includes the duties of due care and loyalty. Good faith is a component of these duties.

In the US a preponderance of listed companies are incorporated in Delaware where several recent cases have addressed the concept of good faith. Good faith is particularly significant notion in the US context because corporate charters may exculpate directors for breaches of the duty of care (and such provisions have been adopted by most corporations) but are ineffective as regards acts or omissions that are not in good faith.

In U.K. law a fiduciary relationship carries an implication of vulnerability and dependency on the part of beneficiaries and a potential for fiduciaries to manipulate their powers for their own benefit or on behalf of others unconnected with the beneficiaries. The Latin root of the word fiduciary – fiduciarius – means one in whom trust reposes and the law developed ways to impose sanctions upon fiduciaries who failed to act in a trustworthy manner.

In the U.K. corporate context beneficiaries include the company and, derivatively, its shareholders while directors (and officers) fulfill the role of fiduciaries. Statutory injections into the case law on the fiduciary duties of directors and officers require them to take into account the interests of other stakeholders in certain circumstances, for example a company’s creditors in situations of pending or actual insolvency, and employee interests, although in the latter case statute law makes clear that the duty is owed to the company, not employees directly.

The paper on French law refers to the earlier noted that the jurisdiction does not have any term that is equivalent to the term fiduciary, because the French legal system does not have a concept similar to 'trust' or 'acting in trust.' Similarly, the fiduciary concept is not known in Dutch law, according to the Netherlands paper. Other civil law contributors’ note the absence of the distinction between legal and equitable title, another key ingredient of trusts in common law.

But both the French and the Netherlands papers note that statute (and in France the courts) have defined the duties and obligations of directors and officers of a corporation in ways that closely resemble their development in common law jurisdictions. In France, the principal obligation of the directors and executive officers is to act “in all circumstances in the interests of the corporation, even though its interests may differ from those of the shareholders.” This too, despite the conceptual differences,
is similar to the English common law, where, as we have already noted, the company itself, not its constituencies, remains the object of the directors’ duties.

The Thai paper emphasizes that as a practical matter the checks-and-balances provided through imposition of duties of care and loyalty on directors is less effective due to the dominance of controlling shareholders and the lack of enforcement mechanisms. However, the Thai paper also notes that pursuant to recent securities regulation, Thai publicly-listed companies are now required to have two independent directors whose role is to ensure that the interests of minority shareholders are protected against abuse by corporate insiders. While this development is significant, it may be that in practice, two independents can be an insufficient fraction to challenge management where all of the remaining board members are related to or affiliated with major shareholders and that the meaning of a fiduciary duty is still in an emergent state.

Similar issues arise in Malaysia, as illustrated through a comment from the former Chairman of the Securities Commission, Mr. Ali Abdul Kadir “the corporate governance issue in Malaysia is quite different from those in most industrialized nations. Unlike those countries, it is not the general separation of management of control that poses problems but the fact that there are many companies with large shareholders who exercise control rights where the risk of the minority shareholders being expropriated exists” and that, “there is a general perception that board of directors may not be as effective as required.”

Some jurisdictions deal with duties of good faith and loyalty as being part of the fiduciary duty while others consider the duty of care to be separate. In the U.K. the fiduciary duty of a director is distinct from the director’s duty to exercise ‘skill and care’, even though it is clear that a breach of fiduciary duty and a failure to exercise sufficient skill and care could arise on the same facts. This is because fiduciary duties evolved from equitable principles, which in turn are based upon a distinction between legal and beneficial titles to property as this developed in the common law. By contrast, the failure to exercise a required level of skill and care is part of the law of tort - specifically where a negligent action or inaction results in harm to the company, its shareholders, other stakeholders and third parties.

For ease of comparison the duty of loyalty and the duty of care are discussed under separate headings with respect to the distinctions between the US and U.K. jurisprudence and other countries referenced under both headings as seems most appropriate.

**The Duty of Loyalty**

In the US the duty of loyalty requires a fiduciary to put the best interests of the corporation ahead of the fiduciary's own interest quoting one case to the effect that: "the duty of loyalty mandates that the best interest of the corporation and its shareholders takes precedence over any interest possessed by a director, officer, or controlling
shareholder and not shared by the stockholders generally”. The paper describes some of the actions that could constitute a breach of the duty of loyalty including self-dealing, misappropriating corporate assets or opportunities, or engaging in a transaction with the corporation that is not substantively or "entirely fair" to the corporation.

Under Hong Kong law, the concepts of loyalty or “best interest of the corporation” find expression in the requirements “to act honestly, bona fide for the benefit of the company…and to avoid any conflict of interest”, while the Australian paper notes that being a fiduciary requires that directors do what they honestly believe to be in the company's best interests. Although the Australian courts have held that it is for the directors to determine what is in the company's best interests and the courts cannot substitute their own view, the courts will consider whether "an intelligent and honest man in the position of a director of the company concerned could, in the whole of the existing circumstances, have reasonably believed that the transactions were for the benefit of the company”.

The contribution from France says that there are many similarities with the concept of duty of loyalty in the United States and most of the country's law and jurisprudence on director duties centers on self-dealing transactions, trading by the directors in the shares of the corporation, competing with the corporation and actions that can result in criminal liability for directors. An interesting concept in French law concerns the misuse of corporate power or voting rights (abus de pouvoirs ou de voix), where a director utilizes corporate power or exercises voting rights (presumably on board decisions and with respect to voting shares of the corporation) in a manner contrary to the interests of the company, or for the benefit of another corporation in which the director directly or indirectly has an interest.

The contribution from Singapore discusses the role of nominee directors in relation to the duty of loyalty. The concept of a nominee director may be an unfamiliar one in the United States, although that is likely a result of a difference in nomenclature, rather than the circumstances covered by the idea. In the U.K and other common law countries influenced by its legal tradition the appointment of nominee directors is a common commercial phenomenon. The Singapore paper quotes the English judge Lord Denning to the effect that "It is done every day", most commonly where a company has a major stake in another and wants to keep an eye on the investment it has made by appointing someone trusted to the board of that company.

As a director of the investee company the nominee director owes it a fiduciary duty and that cannot be ignored even for the benefit of the investing company. This means that for the nominee director, the principal reason for his or her appointment, reporting back to the nominating company is an acute one. When the information s/he wishes to disclose to the investing company is confidential for the investee company it may well constitute a breach of the nominee director's duty to the investee company if the information is disclosed.

---

6 See *Cinerama, Inc. v. Technicolor, Inc.*, 663 A.2d 1156 (Del. 1995); *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993)
In Singapore, the issue was resolved statutorily to allow a director to disclose information so long as the nominee informs the investee board of the person(s) to whom the information will be disclosed. The nominee board must authorize the disclosure and to satisfy the statutory conditions the disclosure must not be likely the prejudice the company. In Thailand publicly listed companies, which as noted, are often family controlled entities are governed by a Public Companies Act that impose fiduciary-like duties on directors, embodying principles of due care and loyalty and preclusions on self-dealing by directors.

The countries of the former Yugoslavia (Croatia, Macedonia, Serbia, Slovenia) show some interesting variations when it comes to incorporating a duty of loyalty concept into their respective corporate laws. Serbia incorporated duties of loyalty and care statutorily, which has been broadened considerably in an all-new law on Business Companies in 2004, while by contrast the new Macedonian law does not have a general duty of loyalty, but rather has a detailed set of prohibitions and requirements about competing with the company and interested-party transactions involving it.

The Duty of Care

The US paper describes the directors' duty in its most basic sense, as "a duty to act carefully in fulfilling the important tasks of monitoring and directing the activities of corporate management. It requires that directors act in good faith, with the care an ordinarily prudent person in a like position would exercise under similar circumstances and in a manner the director reasonably believes to be in the best interests of the corporation." The duty of care includes both care and loyalty elements but the concept of care focuses upon board processes and the availability and timeliness of information delivered to the board's members, so that they can properly discharge their duties.

Prudent decisions are based upon knowledge of the company's business and its significant business plans. Directors need to use reasonable diligence in gathering and considering credible information, adequately deliberate on the relevant issues and manifest understanding of the likely consequences that flow from each decision before making it. Often, this will require relying on management or competent legal or financial experts to assist them but the decision remains theirs, management and experts can help, but they must not supplant the directors' decision making.

Likewise many of the jurisdictions in our sample note directors may reasonably rely upon and delegate board functions to board committees, corporate officers and independent advisors, provided that the choice to delegate is an informed decision, that ultimate responsibility is retained by the directors and that the delegation was reasonable. The delegating director remains under a duty to monitor their actions.

As already noted, in the United Kingdom (and in many of the other commonwealth jurisdictions) the duty to exercise "skill and care" is considered to be distinct from the fiduciary duty, even though it is clear that a breach of fiduciary duty and failure to exercise the required level of skill and care could arise on the same facts.
However, commonwealth jurisdictions are hardly on the same page when it comes to this issue. In Australia, the distinction between them does not amount to a real difference when examining their exercise in practical day-to-day contexts.

Conversely, in Canada the distinction is an important one, particularly with reference to creditors. In considering whether directors owe a duty to creditors when the corporation becomes or nears insolvency, the Canadian courts have looked to the fiduciary duty as codified in the corporate statute, which provides that, in discharging their duties, directors must act "honestly and in good faith, with a view to the best interests of the corporation."

The reference to the interests of the corporation, among other things, led the Canadian Supreme Court to conclude that directors did not owe a fiduciary duty to creditors. The statutory duty of care requires directors to "exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances". Because there is no reference here to the corporation, the Supreme Court held that it was possible for directors to owe a duty of care to creditors, at least when the matter at issue was subject to the Quebec Civil Code. The significance of this aspect of the decision for other Canadian provinces (which are common law jurisdictions) has yet to be tested.

The concept of the duty of care in India is particularly interesting with respect to directors' attendance at board meetings. Indian corporate law presumes negligence when a director absents himself from three consecutive meetings of the board or for a continuous period of three months, whichever is longer, without obtaining leave or absence from the board and provides that in such case that director's office stands vacated. And when fraud against a company is apparent on mere superficial examination of the company’s affairs, directors who fail to prevent the commission of such fraud are liable for dereliction of duty notwithstanding that they have not committed any dishonest act themselves.

Controversy exists in India as to whether an independent director can be held liable for the actions of the company if it is shown that in spite of exercise of due skill and diligence, the director did not detect the legal violations committed by the company. Whilst the country's Companies Act, 1956 does not specifically refer to non-executive directors; a distinction is made in the Act between a 'whole time' director and other directors. While the latter non-executive directors have a duty to keep abreast of the businesses activities and financial status of the company, and as noted, regularly attend board meetings, it appears that conscientious fulfilment of these duties may mean that the court will be inclined to apply a different standard from that which would be applied to a 'whole time' director.

In Argentina – the Argentine Companies Law (ACL) requires directors to posses a certain specific professional ability, common to people who manage businesses of the same or similar nature. In general, this qualification requires from the director a much higher degree of intellectual capability than that which would be expected from an ordinary person. In this sense, the ACL requires a specific aptitude in regards to the industry or business within which the company operates. It is on the grounds of this legal
standard that the “improper performance of their office” mentioned in Section 274 of the ACL is judged and comprises all breaches of statute, regulations, articles and by-laws of the company the director belongs to. However, the Argentine paper also makes clear that case law has many times confirmed that a specific lack of business ability in and of itself is not sufficient to disqualify a director if that does not entail an inability to meet duties inherent to his or her conduct as a director of a company.

The applicable standard of care applies to both boards in Germany – they must employ the care of a diligent and conscientious manager in discharging their duty to run the business. A member of the Vorstand or the Supervisory Board who breaches this duty is personally liable (if several acted jointly, then they are jointly and severally liable) to the company, unless s/he acted (a) on the basis of a lawful resolution of the shareholders or (b) the business decision in question manifests the required duty of care under the German business judgment rule. The German Company Integrity and Modernization Act (UMAG) inserted a new section into the country's Stock Corporation Act, which under certain circumstances permits members of both boards to be sued directly by a shareholder for breach of this duty.

In Serbia the concept of “dobar privrednik,” translated as “good businessman”, is long established in Yugoslav law as meaning a person with business knowledge and experience who acts with due and appropriate care. It resembles the similar concept in German and other continental European law and it is found in all four of the current laws covered in the paper on the countries of the former Yugoslavia.

**The Business Judgment Rule**

Many of the jurisdictions we have reviewed have adopted some form of a "business judgement rule" in evaluating the conduct and decisions made by corporate directors. Essentially, the courts in these jurisdictions hesitate to intervene in decisions made by a board if the only issue is the quality of the business judgement. In the US, the courts presume the directors engaged in appropriate conduct with due care and in the best interests of the company and will only review that conduct if the plaintiff can overcome this presumption for example, by evidence of a conflict of interest or indication of self-dealing.

In all of the jurisdictions in our sample the courts are prepared (at least in theory) to review the independence and diligence of the directors decision making processes and similarly to the United States are prepared to presume that a business decision has been made in good faith by directors in a disinterested non self-serving way, based upon an informed view of the relevant facts with a view to serving the best interests of the corporation. But it is a presumption that can be rebutted by evidence to the contrary.

In some jurisdictions, the rule is framed by statute, and in others, like the United Kingdom, it is not referred to as a rule as such at all. Nevertheless the case law shows a marked reluctance to second guess the decisions of directors, even if the court, with the benefit of hindsight, finds that the exercise of the director's discretion in deciding company policy did not in fact result in actions that were in its best interests.
So, under the business judgement rule or equivalent case law, directors need not fear judicial sanction for making decisions that ultimately turn out to be wrong. The purpose, as described in the US paper, is to allow directors to take risks in the decision-making process without fear that a court, with 20/20 hindsight, will later second-guess the substance of the directors' business decision. However, directors whose decisions are coloured by self interest or lacking in the required level of diligence may find themselves liable to the corporation for any damage caused as a result of their tainted actions.

More specifically, the US paper describes the business judgement rule as a judicial presumption that business decisions are made by: (i) disinterested, independent directors; (ii) with informed due care; (iii) with a good faith belief that the decision will serve the corporation's best interests. If the party challenging the director’s actions cannot overcome the presumption by alleging facts challenging the process, good faith or independence of the board, or by alleging facts suggesting that the directors' decision cannot be attributed to any rational business purpose, then the courts will not second guess the substance of director decisions.

The Canadian business judgment rule is not a presumption, as it is in the United States. Rather, the court will examine the process followed by the directors, specifically, whether informed judgement was exercised by disinterested directors. The court looks to see that the directors made a reasonable decision not a perfect one. Provided the decision taken is within a range of reasonableness, the court will not substitute its opinion for that of the board, even though subsequent events may cast doubt on the board's determinations about facts, circumstances and inferences at the time the decision was made.

Australia has introduced a statutory business judgment rule. Under the applicable provisions of the corporate statute, a director will be taken to have met the prescribed requirements of the duty of care and diligence and the equivalent duty at common law or in equity in respect of a business judgment made by them if they fulfill the following requirements:

- the business judgment was made in good faith for a proper purpose;
- the director did not have a material personal interest in the subject matter of the business judgment;
- the director(s) informed themselves about the subject matter of the business judgment to the extent they reasonably believed to be appropriate; and
- the director rationally believed that the business judgment was in the best interests of the corporation.

The relevant section of the Australian statute presumes that a director's belief that the judgment is in the best interests of the corporation is a rational one unless no reasonable person in the position of the director could hold that belief.
French courts have accepted that the management of a corporation involves the taking of risks and that the occurrence of damages resulting from them does not automatically lead to the liability of the “managers” (i.e., the directors or the general manager, or both). In fact, French courts have only found directors liable when their actions were not those of a conscientious and honest director. The French paper describes the application of the "business judgment rule" (in quotation marks in the paper) in order to avoid the application of hindsight when examining a board of directors decision.

Germany, like Australia, has a statutorily based business judgment rule and the two tier board system introduces some distinctions that would not be evident in a unitary board system with regard to responsibilities that cannot be delegated to or conferred upon the other. However a revision of the rule in 2005 appears to apply to both boards, at least to the extant that the supervisory board approves the business decisions of the management board.

The amended statutory language comes after the words: "In managing the business the members of the management board shall employ the care of a diligent and conscientious manager"; and then continues "A breach of duty does not exist, if the member of the management board in a business decision could reasonably assume on the basis of adequate information, to act in the interest of the company." While this particular translation of the statute from the German original makes it appear that the judgment is an intra-mural affair among the two boards own members, it is nonetheless a standard which outsiders, including the judiciary, would be capable of applying.

The Singapore High Court puts an interesting gloss on the discussion of the business judgment rule in a decision that makes clear that the court will be slow to interfere with the commercial decisions taken by directors in good faith, explaining that it is for the marketplace rather than the court to punish and censure those decisions. While that may be a sentiment that is tacitly shared by other jurisdictions with developed securities markets it offers an interesting contrast with Indonesia. There the legal system, based on Roman-Dutch law with Islamic law components, has a corporate statute specifying key elements of fiduciary duties. However, it remains unclear whether a director acting in good faith and with the requisite skill and care can avail him/herself of some form of business judgment defense.

Interestingly, Thailand which is a Civil Law jurisdiction within a Buddhist culture also appears to be equivocal when it comes to specific law or precedent regarding the availability of a business judgment rule presumption in favor of the defendant director. Putting the state of development of fiduciary duty law aside, it may be that notions of personal responsibility for actions taken inhibit the development of the business judgment rule in these two countries.

Russia's Joint Stock Companies Law calls for a recognition by the courts of the realities of the corporate world. The relevant article reads:
“When determining the grounds and extent of liability of members of the board of directors (supervisory council) of a company, of the one-person executive body of a company (director, general director) and (or) members of the collective executive body of a company (governing board, directorate) and of the managing organization or manager, account must be taken of the usual conditions of business dealings and other circumstances which are of significance for the case in question.”

And, anticipating the next section of this article, the Russian Code of Corporate Governance also reflects the rationale of the business judgment rule:

“At the same time, it should be born in mind that managing the affairs of the company is a complex process with the risk that decisions made by the board of directors acting reasonably and in good faith will ultimately prove wrong and entail adverse consequences for the company.”

The role of Corporate Governance Codes

The establishment, purpose and use of corporate governance Codes provide an interesting point of comparison and contrast in the studied jurisdictions. Although prevalent in both common and civil law countries the United States is most notable for not having anything like the U.K. Combined Code or the Australian Principles of Good Corporate Governance and Best Practice Recommendations.

While the various States (principally Delaware) govern US incorporation the role of the stock exchanges listing rules and a host of reports and commentary provide a wealth of information and guidance on the promotion of good governance best practices for corporations. Also US corporations themselves have inaugurated their own specific codes of conduct that applies to the board, management and employees, emphasizing ethical standards, compliance with applicable law and behavioral maxims that are intended to exemplify the corporation's commitment to high standards of conduct in competitive settings.

However, the 'comply or explain' approach characterized by the U.K. Combined Code and some other European code-based approaches provide not only instructive embellishment to statutory or case law duties for directors as in Russia (see above), but also act as guideposts for directors in the exercise of their fiduciary duties. In particular, 'comply or explain' principles provide directors with the opportunity to consider the good faith exercise of their fiduciary duties in ways that do not necessarily have to 'comply' with stated best practice if, in their judgment, it would be in the best interests of the company to depart from that practice.
Other advantages apart, such as the ability to change and modify these codes more easily than primary legislation, they can act to empower directors own decision making in contrast to the significant reliance placed on legal and other kinds of advice. Some of the background thinking and rationale for the U.K.'s codification of director duties is discussed more fully in the next section.

**To Whom are Fiduciary Duties Owed?**

In the United States (Delaware and certain other jurisdictions), directors owe their fiduciary duties to the corporation and its common shareholders. In the United Kingdom the courts have interpreted statute and case law to the effect that the fiduciary duties of a director are owed the company alone. The U.K. paper says this excludes a holding company or a subsidiary or someone to whom the company itself has obligations. In particular director duties are not construed as owing to individual shareholders, but rather collectively to the company's members as its shareholders. While the U.S and U.K. papers formulate their response to the question with a differing emphasis on what 'the company' as the object of the duty in fact means, the two papers appear close in terms of fundamentals.

The Australian contribution cites U.K. authority as a starting point, but emphasizes that particular circumstances may give rise to a duty owed by a director to a shareholder where that is necessary to negate the effect of an unconscionable use of director power against the interests of that shareholder. In essence, this is another way of formulating the requirement, widespread among commonwealth jurisdictions, that the director shall act *bona fide* in the interests of the company, always acting for a *proper* rather than any *collateral* purpose (see the contribution from India and the discussion of duties to shareholders as another example).

The Canadian contribution highlights the already discussed issue of nominee directors (in Canada the vast majority of the corporations listed on the Toronto Stock Exchange have controlling shareholders) and the stress the Canadian courts have laid on such nominee directors ensuring that the director places the interests of the company before that of the nominator.

The U.S. paper offers a very clear example of how fiduciary duties are utilized in such a situation. Where there is a controlling shareholder that shareholder takes on the status of a fiduciary notwithstanding their ability to act and vote their own economic interests so long as their actions are not to the detriment of the corporation of the minority holders. The role of blockholders in Malaysia and family ownership in Thailand raise the same kind of concern, although each of the papers details the difficulties encountered in adhering to fiduciary duty standards as centered on the corporation as a result.

In Croatia, by contrast, the law does not explicitly impose fiduciary duties on a controlling shareholder but the law contains the concept of "Using influence in the
company" which produces similar results. Likewise, in the Netherlands, where a director is a controlling shareholder (or nominee thereof) his or her duties toward other minority shareholders (and other third parties generally) is heavier.

Although all of the contributions discussed so far appear to agree that directors' fiduciary duties are owed to the corporation that appears to invite differing interpretations of what 'the corporation' means. The problem is made manifest in the contribution from Argentina where the duty to act with loyalty was construed as the duty to act in favor of the "interests of the company", an apparently uncontroversial proposition on its face. However, that construction prompted a debate among Argentine legal scholars and in the case law about how the interests of the company should be defined.

The Argentinean situation appears to have been further complicated by later decreed corporate governance rules that initially define the corporate interest as the interests of all shareholders, but then subsequently elaborates directors (and officers) duties and responsibilities by stating that they should give "priority to the common interest of all the shareholders over any other interest, including the interest of the controlling shareholder(s)' And once that proposition was enunciated some Argentine scholars took the view that the corporate interest also included employee and other kinds of stakeholder interests, depending on the circumstances in which the directors acted.

Directors of a French corporation are potentially liable, not only to the corporation and its shareholders, but also to employees, creditors or other third parties who have suffered damage as a result of the board of directors 'wrongful acts'. However, before concluding that France is wholly unlike the other jurisdictions discussed in this section, it is important to remind ourselves of the fact that French law only recently introduced a "fiducie" (fiduciary) concept into its law. Consequently, the apparent differences in potential liability that French directors are exposed to really reflect the wider ways that directors in all jurisdictions, through statute and regulation, tortious acts or breach of contract may be held liable for their actions or inaction by a variety of claimants.

One of the most recent innovations on director duties and those to whom the duties are owed emanates from the U.K. in the Companies Act 2006. For the first time in U.K. law the common law rules and equitable principles relating to director duties have been codified in a way that sets out how directors are expected to behave and to whom and what they should have regard in discharging their duties as directors. The aim of the Act is to provide clarity and guidance to directors and to address they key question 'in whose interests should companies be run'.

The official commentary on the Act emphasizes that codification is not merely a matter of transposing wording taken from judgments into legislative propositions, but rather to illuminate the general principles and do so in a way that continues to allow the courts to develop the law on the basis of the statutory statement of director duties while permitting directors to have a clear idea of their duties without having to resort to extensive and expensive legal advice.
Earlier drafts of the legislation raised concern that the scope of directors duties was being expanded to include communities in which the company operates and the impact of company operations on the environment, thus vastly expanding those to whom the duties would be owed. But the framework of the legislation shows that, for example, the duty to promote the success of the company now requires directors to have regard to facts like the interests of the company's operations on the community and environment in order to reflect the wider contemporary expectations of responsible business behavior.

While case law will answer what the courts regard as legitimate expectations in terms of responsible business behavior, it is evident that the codification of the duties is meant to also provide behavioral maxims and a reference guide for directors as they discharge their duties. It is too soon to say what the impact of U.K. statute on the country's case law and director behavior will in fact be, but the fact that the legislation has been nearly ten years in the making, illustrates the depth of the changes that a codification of director duties entailed in a country with case law on the subject spanning more than two centuries.

**Enforcement of Director Fiduciary Duties**

The ability of the company, most often derivatively through its shareholders, to use the courts to enforce director duties was specifically referred to in the working outline sent to contributors of the papers. However, the specifics of enforcement actions are complex and for the purposes of this overview we have come to the conclusion that reference to them is best made by examining the original materials. In addition, discussion of how director duties can be enforced through the legal process gets close to offering legal advice - something we explicitly seek avoid at the outset of this article.

We encourage readers interested in this particular area to examine the papers themselves, bearing in mind that in some, particularly transition or developing economies there may be enforcement provisions in recently developed corporate statutes, but little appetite or the means for bringing an action. Consequently, there is a dearth of cases applying or interpreting these provisions. There are also key differences regarding the burden of proof in some jurisdictions (e.g. Germany) and also the role of precedent (e.g. Indonesia).

**Director Fiduciary Duties: Common Themes and Key Differences**

A way to begin illustrating the common themes and key differences in director fiduciary duties in the twenty jurisdictions is to consider the concept of director independence. Ideas about director independence appear to have their center of gravity very much within developed market economies, in part reflecting the significant separation between ownership and control that typifies these countries. For example, director independence requirements in the U.S. and the U.K are well established in listing rules and best practice codes respectively and require a preponderance of, or a significant fraction of the board to be comprised of individuals without ties to management.
Contributions from India, Malaysia and Thailand (among others) detail requirements that boards have at least some independent board members, where the intended role of these independents is to safeguard the interest of minority shareholders against abuses by management or controlling shareholders. While the effectiveness of these independent board members is questioned in many of the papers it is clear that they are meant to provide a resource and a reminder that the board, as a whole, should discharge its duties with attention to fiduciary responsibilities.

However, utilizing economic modes of development as a way to provide comparative analytical insights about director fiduciary duties is questionable, because ownership structures in developing markets can have significant similarities with countries like Canada, where, as we have noted, the vast majority of corporations listed on the Toronto Stock Exchange have controlling shareholders. Also, the development of fiduciary duties were born out of a concern about the separation between ownership and control at a time when capital markets were in their infancy. In other words, while developed and emerging economies can be used to draw interesting points of comparison and contrast they do not appear to provide a satisfactory way for distinguishing commonalities and differences among the contributions.

All of the jurisdictions, irrespective of their place on a scale of developed or developing economies, and whether they fall within the civil or common law tradition, place emphasis on articulating the skills required for the effective discharge of directors' fiduciary duties, together with the board practices and processes that will manifest their use. In fact, this is particularly true with regard to papers from some of the transition or emerging market economies, where the emphasis is particularly evident. No doubt this is partly due to the advice sought in crafting new corporate laws. Our contributions from Russia and Yugoslavia are particularly significant in this regard because they were authored by individuals who had a significant role in crafting the laws and appear to have been drafted to showcase the proficiencies required and duties expected of directors, which in turn serve a role in attracting capital as well as talent.

What the papers show, as a collection, irrespective of legal tradition (or stage of economic development) is that the role of independence is not reducible to, much less guaranteed by, simplistic tests of a lack of connectedness with either the corporation itself or the company's management. Rather, there appears to be recognition that construing independence merely as an absence of connection with the corporation or its management, could remove candidates from consideration as board members who have just the kind of talents the company needs.

That is why, as the U.S. paper makes clear, allegations of mere personal friendship or even an outside business relationship are alone insufficient to render an individual non-independent. What needs to be looked for is whether such friendship or relationship confers a benefit to the director that is not made available to the company s/he serves. That exercise of judgment, by the director or nominee for director, or for other board members, is a manifestation of fiduciary duties.
Are Contemporary Fiduciary Duty Standards Evolving?

(For discussion by subcommittee on 12 August 2007, San Francisco)
### Appendix A  List of Contributors their affiliations and the paper they contributed

<table>
<thead>
<tr>
<th>Name</th>
<th>Affiliation</th>
<th>Country</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ashley R. Altschuler</td>
<td>Weil, Gotshal &amp; Manges LLP</td>
<td>United States</td>
</tr>
<tr>
<td>Kala Anandarajah</td>
<td>Rajah &amp; Tann</td>
<td>Singapore</td>
</tr>
<tr>
<td>Raman Bet-Mansour</td>
<td>Debevoise &amp; Plimpton LLP</td>
<td>France</td>
</tr>
<tr>
<td>Severine Canarelli</td>
<td>Debevoise &amp; Plimpton LLP</td>
<td>France</td>
</tr>
<tr>
<td>Holly J Gregory</td>
<td>Weil, Gotshal &amp; Manges LLP</td>
<td>United States</td>
</tr>
<tr>
<td>Carol Hansell</td>
<td>Davies Ward Phillips and Vineberg LLP</td>
<td>Canada</td>
</tr>
<tr>
<td>Laurence Hazell</td>
<td>Standard and Poor's</td>
<td>United Kingdom</td>
</tr>
<tr>
<td>Lexa Hilliard</td>
<td>3/4 South Square</td>
<td>United Kingdom</td>
</tr>
<tr>
<td>Tan Kait Jane</td>
<td>Air Asia, Berhad</td>
<td>Malaysia</td>
</tr>
<tr>
<td>Tom Jersild</td>
<td>Mayer, Brown, Rowe &amp; Maw LLP</td>
<td>Yugoslavia (countries)</td>
</tr>
<tr>
<td>Elizabeth Johnstone</td>
<td>Blake Dawson Waldron</td>
<td>Australia</td>
</tr>
<tr>
<td>Douglas Mancill</td>
<td>Deacons</td>
<td>Thailand</td>
</tr>
<tr>
<td>Ira M. Millstein</td>
<td>Weil, Gotshal &amp; Manges LLP</td>
<td>United States</td>
</tr>
<tr>
<td>Philip Payne</td>
<td>Blake Dawson Waldron</td>
<td>Indonesia</td>
</tr>
<tr>
<td>Roswell Perkins</td>
<td>Debevoise &amp; Plimpton LLP</td>
<td>Russia</td>
</tr>
<tr>
<td>Alfredo Rovira</td>
<td>Brons &amp; Salas</td>
<td>Argentina</td>
</tr>
<tr>
<td>Leo Seewald</td>
<td>Goodmans</td>
<td>Hong Kong</td>
</tr>
<tr>
<td>Justin Shmith</td>
<td>Blake Dawson Waldron</td>
<td>China</td>
</tr>
<tr>
<td>Cyril Shroff</td>
<td>Amarchand &amp; Mangaldas</td>
<td>India</td>
</tr>
<tr>
<td>Richard Smerdon</td>
<td>Osborne Clark</td>
<td>United Kingdom</td>
</tr>
<tr>
<td>Paul Storm</td>
<td>NautaDutilh</td>
<td>the Netherlands</td>
</tr>
<tr>
<td>Lim Wee Teck</td>
<td>Rajah &amp; Tann</td>
<td>Singapore</td>
</tr>
<tr>
<td>Parveen Thakral</td>
<td>Deacons</td>
<td>Thailand</td>
</tr>
<tr>
<td>Prof. Mirko Vasiljeric</td>
<td>University of Belgrade</td>
<td>Yugoslavia (countries)</td>
</tr>
</tbody>
</table>
Appendix B Work Outline for the Project

The following are the general propositions on which this project is based.

1.1 In common law jurisdictions fiduciary duties of loyalty and good faith are the cornerstone of the relationship between directors, officers and the corporations they serve. Fiduciary duties also require directors and officers to employ the care, skill and diligence that a reasonably prudent person would exercise in performing his or her functions for the company, utilizing objective and subjective tests of reasonableness.

1.2 The obligations and restrictions fiduciary duties impose on directors and officers together with the standards of care they are meant to exercise are crucial to understanding corporate governance norms and practice in a particular jurisdiction.

1.3 To appreciate how corporate governance in non-common law jurisdictions may differ we need to investigate whether similar fiduciary duties and duties of care exist - or if other concepts are utilized in their place - and what obligations, restrictions and standards they impose upon the conduct of directors and officers.

How did the concept of directors' fiduciary duties develop?

The central aim of this part of the project is to provide an account of the historical development of the concept of fiduciary duties in the jurisdiction concerned particularly as these bear upon the director’s relationship to the company. Understanding the historical antecedents of directors' fiduciary duties and the standards of care they should employ aids understanding the role played by these concepts in modern corporate governance. For example, common law antecedents of the legal nature of the office of director include “agent”, “trustee” and “managing partner”. Although fiduciary institutions existed in Roman law (Fiducia) and in Germanic customary law (Treuhand), neither tradition gave rise to a distinction between legal and equitable title to property as developed in the common law. Consequently the fiduciary duties developed in trust law are essentially unknown in civil law jurisdictions. But there are parallels, particularly in terms of the relation of confidence between the fiduciary and those who placed their trust in that person. Indeed, the Latin root of the word fiduciary – fiduciarius – means one in whom trust reposes.

What does being a fiduciary mean?

The corporate model separates ownership from control. Fiduciary duties deal with the delegation of control to non or fractional owner directors and officers, giving them significant discretionary powers over the corporation that cannot be constrained by other legal devices (for example the requirements of trusteeship) without undermining key objectives of the corporation such as accepting levels of risk necessary to achieve desired levels of return on the investments made by the non-controlling ‘outside’ shareholders and creditors.

A fiduciary relationship implies vulnerability and dependency on the part of the ‘beneficiaries’ (the corporation and its shareholders and creditors) and the potential for the fiduciaries (the directors and officers) to manipulate the powers of the corporation for their own benefit. So the fiduciary has the power to control the corporation and its assets but the exercise of that power is conditioned by a duty to Use it in the best interests of the corporation and its constituents.

Contributors might consider completing this section with a contemporary description of the fiduciary duties of directors in their jurisdiction. Such descriptions could include landmark case law as well as any statutory or regulatory innovations that have elucidated current understandings of the fiduciary duties of directors and to whom, and in what circumstances these duties are owed.
Illustrative Questions:

- What is the legal role of the board (or boards) of directors? Does the board collectively have responsibilities that are distinct from those of the directors individually?

- Can the directors and/or the board (or boards) delegate any of their duties and if so, which ones and to whom, and are there any conditions attached to this delegation in terms of retaining overall responsibility for the action (or inaction) by the delegate?

- What are the legal standards governing the conduct of directors in the performance of their fiduciary duties and do those standards incorporate a care/prudence element or equivalent (civil law) concepts?

- Do these standards include good faith, ‘honesty of purpose’ elements and/or strictures against self-dealing or self-enrichment at a cost to the corporation and/or prohibitions on utilizing corporate opportunities for directors?

How are these duties made manifest in the jurisdiction?

Matters for discussion in this section could include the avoidance of conflicts of interest by prohibiting directors utilizing corporate opportunities for their own benefit, or the necessity of evidencing the requisite level of care, skill and diligence by a paper trail showing how a decision was arrived at after sufficient, collective consideration by the board. Rules of confidentiality, and conversely, the duty to disclose various kinds of information, could also be discussed, in particular, the complexities that can arise if directors also hold office at another company or institution where they may find their fiduciary duties to one compromised by similar duties at another. How such ‘conflicts’ are reconciled, whether by forethought and disclosure about them and/or by resignation from one or both offices where such conflicts have occurred will provide a key point for comparative analysis when the contributions are collated.

Illustrative Questions

- Is there jurisprudence that avoids “second-guessing” director conduct with the benefit of hindsight designed to limit judicial (or regulatory intervention that might chill legitimate business activity (e.g. the business judgment rule)? In other words, are decisions of the directors protected, provided that they have exercised their fiduciary duty and duty of care?

- Are there any initiatives to codify (and/or simplify) the duties of a director? Is there any jurisprudence on how the courts have interpreted these codes or statutory provisions and, if so, have these led to contemporary governance best practice ideas being imported into court decisions?

To whom are these duties owed?

Many jurisdictions formulate these obligations as owing to the corporation itself. Thus, although shareholders elect directors, the directors owe a fiduciary duty to the company rather than the generality of shareholders or those who supported the directors’ candidacy for office.

Other legal traditions, statutory interventions and developments in case law modify that position. For example, statutes may require an exclusive focus on creditors if certain financial conditions occur and case law in various jurisdictions recognize the role of derivative and minority actions under the rubric of “oppression remedies” in certain circumstances. Any special treatment of substantial or majority shareholders (blockholders) in companies could be detailed in this section.
Illustrative Questions:

- Who can bring an enforcement action for a breach of duties by a director? Does the law entertain the concept of a derivative suit (an action brought by shareholders on behalf of the company) or is some form of private action available?

- Can directors be held liable personally for a breach of their duties and, if so, can the company indemnify them and may the company, in turn, obtain insurance and are there limits imposed by statute or otherwise on the indemnity or insurance coverage (e.g. in cases of misrepresentation or fraud)?