

## False statements

If a director makes a false statement in writing, in cases where such statement is required by the Companies Act as (i) a prerequisite for the effectiveness or enforcement of company's decisions, or as (ii) a precondition for certain proceedings, with the intention of initiating / conducting / concluding such proceedings, he shall be liable to a prison sentence of 6 months to 5 years and a fine.

If the above offence was committed with intent to cause damage to company's creditors or shareholders, and the amount of such damage exceeds 10 million RSD (ca. 83,000 EUR), the offender shall be liable to a prison sentence of one to ten years and a fine<sup>20</sup>.

## Legal Actions and Deadlines

The company and shareholders may bring action for damages against the director for any damage caused through the breach of duty of care, duty to disclose any personal interest, duty to avoid conflict of interest, duty of confidentiality and non-compete duty, within 6 months of becoming aware of such breach, however not later than 5 years of the actual date of such breach.

## How to strike a balance between the freedom to make effective business decisions and the limitations placed on the director by shareholders and/or the state?

- Become acquainted with the legal framework for director liability
- Anticipate events in doing business
- Identify legal risks and consult experts

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#### DISCLAIMER:

This text does not claim to cover a complete list of director liabilities as provided under the laws of the Republic of Serbia. Furthermore, this text may not serve as a substitute for legal advice in any given legal case.

1 Art. 33 of the Companies Act ("Off. Gazette RS", No. 36/2011, 99/2011), hereinafter: "CA"

2 Art. 41 CA

3 19 May 2014

4 Criminal Code of the RS ("Off. Gazette RS", No. 85/2005, 88/2005, 107/2005, 72/2009, 111/2009, 121/2012, 104/2013)

5 Art. 42 CA

6 Other than the director, persons owing special duties to the company are other representatives, members of the supervisory board, proxies, liquidator, partner, general partner, shareholders with material interest or controlling shareholders. The memorandum of association may identify other persons as owing special duties to the company.

7 Art. 63 CA

8 Persons affiliated with the director are:

- director's lineal kin, collateral kin within the third degree of kinship, spouse / de facto partner;
- director's spouse / de facto partner and their relatives within the first degree of kinship;
- director's adoptive parents or children, as well as descendants of adoptive children;
- all persons sharing the household with the director
- a legal entity in which the director holds a material interest or is a controlling shareholder;
- a legal entity in which the director is a member of a managing or supervisory body (hereinafter: "Affiliated Persons", Art. 62.1.2 CA)

9 Art. 582 CA

10 Art. 68 CA

11 Art. 69 CA

12 Art. 71 CA

13 Art. 583 CA

14 Art. 70 CA

15 Art. 72 CA

16 Art. 73 CA

17 Control represents a right or a possibility a certain person has, either independently or acting in concert with other persons, to exert controlling influence on the operations of a company through an equity interest in share capital, an agreement or a right to appoint the majority of directors or Supervisory Board members.

18 Material interest in share capital exists if a single person holds more than 25 % of the voting rights in the company, either independently or acting in concert with other persons.

19 Art. 76 CA

20 Art. 581 CA

# GUIDE

## to Director's Liability

LEGAL FRAMEWORK /SERBIA

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## Limitations of Director's Powers

The directors shall act within the limits of the powers conferred upon him by (i) company regulations or (ii) decisions of competent authorities.

Limitations of director's powers may not be enforced by the company against a third party, except in case of joint signatures<sup>1</sup>.

The director shall be held liable for **any damage** he may cause to the company by exceeding his powers, except in cases where he acted in accordance with a decision of a competent body or if his actions were subsequently approved by such body<sup>2</sup>.

If a director violates the duty to act within the limits of his powers, he shall be held **criminally liable** and face either a fine or a prison sentence of up to one (1) year. If the damage caused to the company exceeds 10 million RSD (ca. 83,000 EUR<sup>3</sup>), the offender shall be liable to a prison sentence of 6 months to 5 years, as well as a fine. Furthermore, the offender may be barred from holding an office or pursuing a vocation, in accordance with the Criminal Code<sup>4</sup>.

## Director as contract signatory on behalf of both parties

The director may not act as a counterparty to a contract and enter into a contract with the company in his name and for his account, or in his name and for the account of another person, or in the name and for the account of another person, without a special authorisation to that effect. Such authorisation is granted by the general assembly (Ltd. / inc.), unless otherwise provided for in the articles of association or the memorandum of association<sup>5</sup>.

## Duty of Care

The director<sup>6</sup> has the duty to carry out his tasks in good faith, with due care of a prudent businessman and in reasonable belief that his actions are in the best interest of the company.

The due care of a prudent businessman, that a director is required to exercise, is the level of care which a reasonably diligent person would use if they had the knowledge, skills and experience that might reasonably be expected of a person carrying out the functions of a director in a company.

Furthermore, if such person has specialist knowledge, skills or experience, such knowledge, skills or experience are also taken into account when evaluating the level of care. The director may also base his actions on the **expert opinion and information** which he reasonably believes to have been given in good faith.

A company may file a lawsuit against the director for any damage caused through a breach of the duty of care. In case that the **director proves** that he acted with due care of a prudent businessman, in accordance with the above rules, he shall not be held liable for any damage the company may have suffered as a result of his actions<sup>7</sup>.

**The burden of proof lies with the director.**

## Duty to disclose any personal interest

The concept of personal interest is fairly broadly defined. A personal interest is deemed to exist in case of:

1. transactions between the company and the director;
2. transactions between the company and persons affiliated with the director<sup>8</sup>;
3. legal actions taken by a company in judicial and other proceedings, waiver of rights, etc, in relation to the director and any persons affiliated with the director;
4. transactions / legal actions undertaken by a company:
  - which involve a third party that has a financial relationship with the director or an affiliated person, if it is likely that such relationship may affect the actions of the director, or
  - which would bring financial gain to a third party, if such third party has a financial relationship with the director or an affiliated person, and it is likely that such relationship may affect director's actions.

The director shall declare any personal interest to: (i) the board of directors or the general assembly (if there is only one director in the company) in a single-tier company, or (ii) the supervisory board in a two-tier company (hereinafter: "Competent Bodies") (Companies Act, Art. 65.1 & 65.2).

The declaration must include a detailed description of the transaction, as well as the nature and scope of the personal interest in question, and once it is made, the Competent Bodies shall decide whether or not to authorise the transaction / legal action (Companies Act, Art. 66.5).

If a transaction / legal action involving director's personal interest is not authorised, or if the authorisation is given based on false information, the company may file a lawsuit for annulment of such transaction and claim damages against the director (Companies Act, Art. 67).

If a director breaches the above rules related to personal interest with intent to cause damage to the company, he shall be held criminally liable and may face a fine or a prison sentence of up to one (1) year. If the damage caused to the company exceeds 10 million RSD (ca. 83.000 EUR), the offender shall be liable to a prison sentence of 6 months to 5 years, as well as a fine. Furthermore, the offender may be barred from holding an office or pursuing a vocation, in accordance with the Criminal Code<sup>9</sup>.

If the director proves (the burden of proof lies with the director) that the transaction / legal action was in the interest of the company, it shall be deemed that no breach of rules has occurred<sup>10</sup>.

## Duty to Avoid Conflict of Interest

The director shall not, for his own benefit or for the benefit of any affiliated persons:

- use any **assets** of the company;
- use any **information** he obtained in the capacity of a director, insofar as such information is publicly unavailable;
- abuse his **position** in the company;
- personally exploit **business opportunities** for entering into transactions that arise for the company<sup>11</sup>.

The director shall be held liable for **damages** if he breaches the duty to avoid conflict of interest, whilst the company may demand **transfer of benefits** gained by the director or an affiliated person<sup>12</sup>.

If a director breaches the duty to avoid conflict of interest with intent to obtain financial gain for himself or others, he shall be held criminally liable and may face a fine or a prison sentence of up to one (1) year. If the damage caused to the company exceeds 10 million RSD (ca. 83.000 EUR), the offender shall be liable to a prison sentence of 6 months to 5 years as well as a fine. Furthermore, the offender may be barred from holding an office or pursuing a vocation, in accordance with the Criminal Code<sup>13</sup>.

The director may be exempt from the liability, subject to obtaining prior or subsequent approval of the Competent Bodies<sup>14</sup>.

## Duty of Confidentiality

The director owes a duty to keep business secrets during his term as the director and two (2) years upon expiry of such term. The memorandum of association, articles of association, company decisions, or employment contract may provide for a longer period, however not longer than 5 years<sup>15</sup>.

A director shall be held liable for **damages** if he breaches the duty of confidentiality, and his employment contract may be terminated (Companies Act, Art. 74).

Please note – disclosure of privileged business information shall not be deemed as a breach of the duty of confidentiality if such disclosure is:

- obligatory under the law;
- necessary to perform business operations or protect company interests;
- made to the public or competent authorities with the sole purpose of calling attention to an offence punishable under the law.<sup>16</sup>

## Non-Compete Duty

The director may not, without the approval of the Competent Bodies:

- act as a partner, general partner, controlling shareholder<sup>17</sup> or shareholder with material interest<sup>18</sup> in another company with the same or similar scope of business activities (hereinafter: "Competitor")
- be an entrepreneur with the same or similar scope of business activities;
- be employed with or otherwise hired by a Competitor;
- be a shareholder or a founder of a Competitor.

The memorandum of association or articles of association may provide for an extension of non-compete duty even beyond the term in office as a director, however not longer than 2 years.

If a director breaches the non-compete duty, he shall be liable for damages, whilst the company may transfer benefits gained by the director or the Competitor. The director may be barred from pursuing his vocation and his employment contract, if any, may be terminated<sup>19</sup>.