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The American Business Judgment Rule and Swedish Law

*A Comparative Analysis of the American Business Judgment
Rule and Its Eventual Counterpart in Swedish Law*

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Summary

The purpose of this thesis is to examine whether Swedish directors and CEOs can expect the Swedish courts to review business decisions in a similar way to how the American courts review business decisions. This examination enables a comparative analysis of whether something similar to the American business judgment rule exists in Swedish law, which some Swedish legal scholars claim.

The American courts are prohibited to review business decisions as long as the business judgment rule presumption is not rebutted. The American courts simply presume that in making a business decision, the directors of a corporation acted on an informed basis, in good faith, and in the honest belief that the action was taken in the best interests of the company.

There are conflicting statements about how the Swedish courts review business decisions according to the rules about liabilities of directors and CEOs in Swedish law. Lindskog, the Former Chief Justice of the Supreme Court of Sweden, states that the Supreme Court of Sweden has started to use the method liability when they accomplish the negligence assessment. According to the method liability, it is the considerations behind the decision that are reviewed and not the decision itself. Some legal scholars state that the fact that the business purpose in Chapter 3, Section 3 of the Swedish Companies Act is formulated in a vague way gives the directors and CEO a broad discretion to fulfill the business purpose and to make business decisions within the ordinary course of business. Other legal scholars state that Swedish courts do not review whether a business decision is unwise and that risky business decisions usually do not make the directors and CEO liable, at least as long as the business decisions are within the ordinary course of business. However, a Swedish court case demonstrates that there are no restrictions regarding what kind of business decisions the

Swedish courts can review and that they are unhindered to make an assessment of business decisions.

There does not seem to be a similarity between how American courts review business decisions according to the American business judgment rule and how Swedish courts review business decisions according to the rules about liabilities of directors and CEOs in Swedish law. There are tendencies that indicate that something similar to the American business judgment rule exists in Swedish law but it is unclear what the applicable prerequisites are in Swedish law. However, there are clear prerequisites in American law that clarify under what circumstances the American courts are allowed to review business decisions. The American business judgment rule presumption is a powerful shield against liability for the American directors. There is no such presumption in Swedish law that needs to be rebutted in order for the courts to review business decisions. This means that Swedish directors and CEOs do not seem to be able to make risky business decisions without fear of becoming liable. Therefore, it is misleading to state that there is something similar to the American business judgment rule in Swedish law.

Sammanfattning

Syftet med den här uppsatsen är att undersöka huruvida svenska styrelseledamöter och verkställande direktörer kan förvänta sig att de svenska domstolarna prövar affärsbeslut på ett liknande sätt som de amerikanska domstolarna prövar affärsbeslut. Undersökningen möjliggör en komparativrättslig analys av huruvida det finns något i svensk rätt som liknar den i amerikansk rätt existerande BJR, vilket några svenska rättsvetenskapliga forskare hävdar.

De amerikanska domstolarna är förhindrade att pröva affärsbeslut såvida BJR presumtionen inte är motbevisad. De amerikanska domstolarna presumerar att styrelseledamöterna fattade affärsbeslutet på ett tillfredsställande beslutsunderlag, i god tro och utifrån bolagets bästa intresse.

Det finns motstridiga uttalanden om hur svenska domstolar prövar affärsbeslut enligt skadeståndsreglerna för styrelseledamöter och verkställande direktörer i svensk lag. Lindskog, Högsta domstolens tidigare ordförande, uttalar att Högsta domstolen har börjat använda ett metodansvar vid aktsamhetsbedömningen. Enligt metodansvaret är det övervägandena som ligger bakom ett beslut och inte beslutet som sådant som ska prövas. Några rättsvetenskapliga forskare uttalar att det faktum att verksamhetssyftet i 3 kap. 3 § ABL är vagt utformat ger styrelseledamöterna och verkställande direktören ett stort handlingsutrymme att uppfylla verksamhetssyftet och att fatta beslut inom den ordinarie affärsverksamheten. Andra rättsvetenskapliga forskare uttalar att svenska domstolar inte prövar huruvida ett affärsbeslut är oklokt och att styrelseledamöterna och den verkställande direktören vanligtvis inte blir skadeståndsansvariga för riskfyllda beslut inom den ordinarie affärsverksamheten. Ett svenskt domstolsbeslut visar dock att det inte finns några begränsningar i svensk rätt beträffande vilka affärsbeslut svenska

domstolar kan pröva och att svenska domstolar oförhindrat kan göra en bedömning av affärsbeslut.

Det verkar inte finnas en likhet mellan hur amerikanska domstolar prövar affärsbeslut enligt BJR och hur svenska domstolar prövar affärsbeslut enligt skadeståndsreglerna för styrelseledamöter och verkställande direktörer i svensk lag. Det finns tendenser som indikerar att något som liknar BJR finns i svensk rätt men det är oklart vilka de tillämpliga rekvisiten är i svensk rätt. Det finns dock tydliga rekvisit i amerikansk rätt som klargör under vilka omständigheter amerikanska domstolar kan pröva affärsbeslut. Den amerikanska BJR presumptionen utgör ett starkt skydd för amerikanska styrelseledamöter mot skadeståndsansvar. Det finns i svensk rätt inte en presumptionsregel som måste motbevisas för att domstolarna ska kunna pröva ett affärsbeslut. Detta innebär att svenska styrelseledamöter och verkställande direktörer inte verkar kunna fatta riskfyllda affärsbeslut utan rädsla för att bli skadeståndsansvariga. Det är därför missvisande att uttala att det i svensk rätt finns något som liknar den amerikanska BJR.

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I am now eager to start my career in Stockholm.

Lund, Sweden on May 24, 2019

Erik Rosberg

Abbreviations

A.2d	Atlantic Reporter, Second Series
ABL	The Swedish Companies Act (<i>Swedish</i> : Aktiebolagslag (2005:551))
ALI	American Law Institute
BJR	Business Judgment Rule
CEO	Chief Executive Officer
Ch.	Law Reports, Chancery Division
Del.	Delaware
DGCL	Delaware General Corporation Law (As of March 28, 2019)
Directors	Board of Directors
EU	European Union
Ex rel.	On the relation of
In re	In the matter of
MBCA	Model Business Corporation Act (As of December 9, 2017)
NJA	Swedish Law Reports from the Supreme Court of Sweden (<i>Swedish</i> : Nytt Juridiskt Arkiv)
N.W.	North Western Reporter
prop.	Swedish Government Bill (<i>Swedish</i> : proposition)
SOU	Swedish Government Official Reports (<i>Swedish</i> : Statens offentliga utredningar)
SvJT	Swedish Law Journal (<i>Swedish</i> : Svensk Juristtidning)
U.S.	United States of America
WL	Westlaw

Terminology

Articles of Association. In this thesis, the term “Articles of Association” is used instead of one of the following terms: “Articles of Incorporation”, “Bylaws”, and “Corporate Charter”.

CEO. The terms “CEO”, “President”, “Managing Director”, and “General Manager” can all be used when reference is made to the highest-ranking manager of a corporation.¹ In this thesis, the term “CEO” is used.

Delaware Court. In order to simplify the presentation in this thesis, reference is made to the term “Delaware Court”, which includes all courts in Delaware. The courts of equity are also included in the term.

Director. In order to simplify the presentation in this thesis, the term “Director” is used synonymously with term “Officer” unless the distinction between the terms is important. This primarily applies to the chapters presenting American law.

Shareholder. The term “Shareholder” is used synonymously with the term “Stockholder”.²

Shareholders’ Meeting. This term refers to a meeting of all shareholders of a corporation. When the distinction is important, the term “Annual General Meeting” refers to a meeting that is held annually and the term “Special Shareholders’ Meeting” refers to an extraordinary meeting.

¹ Garner and Black (2009) p. 270, 1045 f., and 1304.

² Garner and Black (2009) p. 1500.

1 Introduction

1.1 Background

For more than a century, the American courts have used the American business judgment rule to shield the directors from liability.³ If the business judgment rule is applicable, the American courts do not review the directors' business decisions. Not even if the business decisions turn out to be poor.⁴ In Swedish law, it is not clear under what circumstances directors and CEOs can be held liable for business decisions that turn out to be poor. The issues related to the directors' and CEOs' liabilities in Swedish law are constantly discussed. The question is where the line for the directors' and CEOs' liabilities should be drawn in Swedish law.⁵ The Swedish legal scholars have started to discuss if there is something similar to the American business judgment rule in Swedish law.⁶

Below follows a short presentation of what legal scholars in Sweden have stated about the existence of something similar to the American business judgment rule in Swedish law.⁷ The statements in the list below present the development in the legal literature in a chronological order. Some legal scholars have repeated their statements, which is recognized in the footnotes.

³ Radin (2009) p. 53 ff.

⁴ Radin (2009) p. 13 f., 26, and 44 f.

⁵ Dotevall, "Liability of Members of the Board of Directors and the Managing Directors – A Scandinavian Perspective", *The International Lawyer*, Vol. 37, No. 1, (2003), p. 65; Eklund and Molin, "Ska man bli skadeståndsskyldig om man gör en dålig affär?", *Dagens Juridik*, September 29, 2010, <<http://www.dagensjuridik.se/2010/09/ska-man-bli-skadestandsskyldig-om-man-gor-en-dalig-affar>>, downloaded on January 25, 2019.

⁶ Andersson, "Business judgment rule och principen om efterkontrollbarhet", *Advokaten*, No. 9, (2017); Dotevall (2017) p. 89; Svernlöv (2012) p. 58; Östberg (2016) p. 449.

⁷ A more extensive presentation is provided in Chapter 5.4.

- Dotevall states: “A corresponding rule to the business judgment rule developed in American law exists in Swedish law.”⁸
- Johansson states: “Something similar [to the American business judgment rule]⁹ can be said to exist in Swedish law.”¹⁰
- Svernlöv states: “In Swedish law, there is not an explicit business judgment rule equivalent to the one in American law [...] at the same time, a similar principle can be considered to exist.”¹¹
- Östberg states: ”There is not a business judgment rule in Swedish law. At the same time, a similar principle exists.”¹²
- Lindskog states: “The Supreme Court of Sweden has started to approach the American business judgment rule.”¹³

There seems to be a consensus among the Swedish legal scholars. The hypothesis based on these statements is that something similar to the American business judgment rule exists in Swedish law. However, it is not clear what in fact is similar. That is the reason why the purpose of this thesis was chosen.

1.2 Purpose and Research Questions

The purpose of this thesis is to examine whether Swedish directors and CEOs can expect the Swedish courts to review business decisions in a similar way to how the American courts review business decisions. The way the courts review business decisions is crucial for the determination of liability. The purpose is also to scrutinize the statements made by the Swedish legal scholars and specifically the statements made by Lindskog,

⁸ Dotevall (2015) p. 375; Dotevall (2017) p. 89; See also Dotevall (1989) p. 169. The statement made by Dotevall is placed first in the list even if the quote was not explicitly expressed in 1989. However, a general statement can be found in Dotevall (1989).

⁹ Editor’s note.

¹⁰ Johansson (1990) p. 307; Johansson, “Interimistiska åtgärder vid aktiebolagsrättsliga processer – Något om tillämpningen av 15 kap. RB vid processer grundade på aktiebolagslagen”, in *SvJT* 1991 p. 604.

¹¹ Svernlöv (2012) p. 58.

¹² Östberg (2016) p. 449.

¹³ Andersson, “Business judgment rule och principen om efterkontrollbarhet”, *Advokaten*, No. 9, (2017); See also Lindskog (2018) p. 337 ff.

the Former Chief Justice of the Supreme Court of Sweden.¹⁴ This is done in order to enable a comparative analysis of whether something similar to the American business judgment rule exists in Swedish law.

The relevant research questions for the purpose of this thesis are formulated in the following way:

- Is there a similarity between how American courts review business decisions according to the American business judgment rule and how Swedish courts review business decisions according to the rules about liabilities of directors and CEOs in Swedish law?
- If there is not a similarity, how do American courts review business decisions according to the American business judgment rule and how do Swedish courts review business decisions according to the rules about liabilities of directors and CEOs in Swedish law, and what are the differences?

1.3 Method and Perspective

A comparative method is used in this thesis. Through the comparative method, comparisons are made in order to understand the similarities and differences between the different legal systems. The comparative method also aims at using the similarities and differences, which can be made through a comparative assessment of the different solutions in the legal systems or through an explanation of the reasons why there are similarities and differences.¹⁵ In order to make a good comparison, sufficient and updated knowledge about the law in the different legal systems is necessary.¹⁶ It is also obvious that there needs to be something to compare in order to make a valuable comparison.¹⁷

¹⁴ See Chapter 1.1.

¹⁵ Bogdan (2013) p. 18; Siems (2018) p. 2 f; Valguarnera (2013) p. 141 ff.

¹⁶ Bogdan (2013) p. 30 f.

¹⁷ Bogdan (2013) p. 46 f.

A functional approach characterizes the comparative analysis in this thesis but the cultural approach is not completely excluded.¹⁸ The functions of the objects that regulate a specific problem need to be the same in the compared jurisdictions. According to the functional approach, the basis is not the concepts in its own jurisdiction since it can have an impact on the comparative analysis. Instead, the basis is the function of the law.¹⁹ The functional approach is used in this thesis since the purpose of the thesis is to cover and analyze similarities and differences of how the American courts review business decisions and how the Swedish courts review business decisions.

The traditional legal dogmatic method can be said to be applicable in the Swedish descriptive Chapters 4 and 5. Through the traditional legal dogmatic method, the laws are interpreted through the traditional legal sources: legislation, case law, preparatory work, and legal literature.²⁰ Chapter 2 presents an overview of American corporate law and Chapter 3 presents the American business judgment rule. These chapters are more analytic than descriptive. In both Chapter 2 and 3, the comparative method is solely being used since the final goal is to enable a comparison. The application of the comparative method includes studies of the legal systems in foreign jurisdictions and these studies are not supposed to give rise to a detailed presentation of the foreign jurisdiction's current laws. The aim with Chapter 2–5 is to present sufficient material in order to enable a comparison of high quality in Chapter 6.

The comparison in this thesis is made between one civil law jurisdiction and one common law jurisdiction. Common law is based on court decisions while civil law is based on legislation.²¹ However, the difference between the legal systems is not an obstacle for the comparison in this thesis.

¹⁸ The concept “comparative method” is misleading since there are four dominating comparative methods. Two of them are the functional method and the comparative analysis of the legal culture. See Valguarnera (2013) p. 147.

¹⁹ Bogdan (2013) p. 48 ff; Siems (2018) p. 16 f; Valguarnera (2013) p. 152 ff.

²⁰ Kleineman (2013) p. 21 ff.

²¹ Balouziyeh (2013) p. 4; Siems (2018) p. 50 ff.

Comparisons between jurisdictions that are not too similar but at the same time not too different are encouraged. Therefore, many comparisons are made between a common law and a civil law jurisdiction in the Western world.²² It should also be noted that there are a lot of influences in Swedish corporate law from American corporate law. Therefore, studies of American corporate law can have much to add.²³

There is a vast amount of American cases that covers the American business judgment rule. The ones that have influenced the judicial development of the American business judgment rule the most are presented in this thesis. They are solely presented in the most relevant way for this thesis and they are not commentated to a great extent.

The statements made by the Swedish legal scholars are used in both the descriptive and the analytic parts. The reason is that their statements are what mainly establish the existence of a counterpart to the American business judgment rule in Swedish law. The Swedish case law that is relevant for the research questions is very thin and nothing can be deducted from the Swedish statutes. Consequently, the legal scholars' statements are necessary to study in order to understand if there is something similar to the American business judgment rule in either the Swedish statutes or the Swedish case law. The statements made by Lindskog are given a specific focus in both the descriptive and the analytic parts since Lindskog claims that the American business judgment rule's counterpart in Swedish law is the method liability.

An international perspective is applied throughout the thesis in order to place the research questions in a jurisdictional context. The aim with the international perspective is to enable a nuanced comparative analysis.

²² Siems (2018) p. 18.

²³ Svernlöv (2008) p. 26.

1.4 Material

Primary sources such as legislation and court cases are used to the greatest extent in this thesis. Secondary sources such as legal literature and legal articles are used in order to present a deeper understanding of both American and Swedish law. Regarding Swedish law, the use of secondary sources is necessary in order to enable an analysis of whether there is a counterpart of the American business judgment rule in Swedish law. The reason is that there is a lack of primary sources covering this.

Non-recent material is avoided to the greatest extent. However, it is inevitable to use some non-recent material since the collections of American legal literature in European law libraries are not completely updated. When non-recent legal literature is used, legal articles are used as a complement to the legal literature to the greatest extent in order to cover the updates that are important for the presentation in this thesis. The legal literature and articles are primarily selected based on how frequently they are cited.

There is a vast amount of literature presenting American corporate law. The overview of American corporate law in Chapter 2 includes work made by influential corporate law scholars. Literature by Backer, Bainbridge, Balouziyeh, Gevurtz, McAlinn, Rosen, and Stern is frequently cited. Comparative literature by Cahn, Donald, Kraakman, and Ventoruzzo is cited because the literature provides this thesis with comparative aspects that are valuable. The MBCA and the DGCL are also cited because they have an influence on American corporate law.²⁴ Material by Bruner, Radin, Sharfman, and Velasco is mainly cited in the part that deals with the duty of loyalty, duty of care, and good faith.

The main legal literature regarding the American business judgment rule in Chapter 3 is the sixth edition of the *Business Judgment Rule: Fiduciary*

²⁴ Gorris, Hamermesh, and Strine, "Delaware Corporate Law and the Model Business Corporation Act: A Study in Symbiosis", *Law and Contemporary Problems*, Vol. 74, (2011), p. 107 f.

Duties of Corporate Directors by Radin.²⁵ The book is one of the most comprehensive books covering the American business judgment rule. The book has also been cited in more than 50 American judicial decisions. Radin is in turn an experienced and respected practitioner.²⁶ American case law is also used in order to deepen the presentation about the American business judgment rule.

There is a vast amount of literature presenting Swedish corporate law. The traditional legal literature in the field of corporate law is used in Chapter 4 and 5. The literature by Dotevall and Svernlöv is frequently cited in the presentation of the duties and liabilities regarding directors and CEOs in Swedish law. The comparison between Swedish and American law in the literature by Dotevall has been helpful since it has provided general guidance. The literature by Östberg is frequently cited in the presentation of the duty of loyalty and the duty of care in Swedish law. In addition, literature by Samuelsson, Sandström, Skog, and Stattin is cited. Literature about general Swedish tort law by Hellner and Radetzki is of great use in the presentation of liabilities regarding directors and CEOs in Swedish law.

There is a lack of material that covers the method liability theory. Only preparatory work regarding financial advisors is possible to find. Therefore, the statements about the method liability made by Lindskog dominate the presentation of the method liability theory. The selection of the case law in Chapter 5.3.3 is based on Lindskog's statements.

Chapter 5.4 covers statements regarding the existence of something similar to the American business judgment rule in Swedish law. All the material that is possible to find is presented.

²⁵ Radin (2009) p. xxxix.

²⁶ Weil, Gotshal, and Manges LLP, "Stephen A. Radin", <<https://www.weil.com/people/stephen-radin>>, downloaded on April 26, 2019.

1.5 Previous Research

Much research has been conducted regarding duties and liabilities of directors and CEOs in Swedish corporate law and of directors and officers in American corporate law. However, there is a lack of research conducted regarding the existence of something similar to the American business judgment rule in Swedish law. It is only possible to find a few statements about this in the Swedish legal literature.

Dotevall, Johansson, Lindskog, Ohlson, Samuelsson²⁷, Stattin, Svernlöv, and Östberg have made statements in the legal literature about the existence of something similar to the American business judgment rule in Swedish law. Some legal scholars are more skeptical to the existence than others.²⁸ However, the majority of the statements are sparsely developed. Dotevall, Johansson, Lindskog, and Svernlöv are the ones who have developed their statements the most. Therefore, there is a focus on their statements in the analysis.

1.6 Delimitations

Certain delimitations have been made in order to achieve an in-depth analysis in relation to the purpose and research questions. Therefore, the presentation of American and Swedish corporate law includes only corporations and no unincorporated business entities.²⁹ No procedural questions or aspects related to alternative dispute resolution are presented in this thesis. There is a distinction between internal and external liability in Swedish law. The internal liability concerns damage that the company suffers while the external liability concerns damage that a shareholder or

²⁷ Together with Adestam and Nerep.

²⁸ See for example the statement made by Samuelsson, which is presented in Chapter 5.4.

²⁹ See Garner and Black (2009) p. 391 and MBCA § 1.40 (4) for a definition of a “corporation”.

someone else suffers.³⁰ The presentation in this thesis is focused on the internal liability.³¹

In Swedish law, an auditor has a similar position as a director when it comes to liability and an auditor's role is of importance.³² However, this thesis does not include the liability regarding auditors.

The corporate laws are different in every state in the U.S.³³ In the presentation of American law, statutory law and case law from primarily Delaware are used. However, references are made to sections in both the DGCL and MBCA. When reference is made to American law in this thesis, the assumption is that the laws in the U.S. are uniform unless anything else is stated. The reason why the laws of Delaware are used is that a substantial amount of the largest American companies are incorporated in Delaware.³⁴ Delaware is the legal home for more than half a million businesses. More than 50 percent of all the companies that are publically traded in the U.S. are incorporated in Delaware. The court system in Delaware can be seen as "the Mother Court of corporate law."³⁵ Additionally, the cases from Delaware often serve as a guide for the corporate doctrines in other states in the U.S.³⁶

The American business judgment rule's reach outside the U.S. in other jurisdictions except for Sweden would have been interesting to study. Parallels could have been drawn between Sweden and for example other countries in the EU with slightly similar legal systems. However, the comparison does only include Sweden and the U.S. Also, the American

³⁰ Bergström and Samuelsson (2015) p. 111.

³¹ It should be noted that the determination of culpability in Swedish law is conducted in a similar way both regarding internal and external liability. See Svernlöv (2012) p. 51 and 75.

³² Bergström and Samuelsson (2015) p. 107 ff. and 117 f; Chapter 29, Section 2, Paragraph 1 of the Swedish Companies Act; Sandström (2017) p. 286 f.

³³ Backer (2002) p. 176; Bainbridge (2015) p. 8 ff. McAlinn, Rosen, and Stern (2010) p. 327.

³⁴ Sharfman, "The Importance of the Business Judgment Rule", *New York University Journal of Law & Business*, Vol. 14, No. 1, (2017), p. 32.

³⁵ Radin (2009) p. 5 f.

³⁶ Radin (2009) p. 3.

business judgment rule in relation to mergers and acquisitions is not presented in this thesis.

1.7 Outline

In this thesis, the purpose and the research questions are approached in the following way. In Chapter 2, an overview of American corporate law is presented. The chapter includes a presentation of the corporate bodies and duties of the directors and officers. The duty of loyalty, the duty of care, and good faith are presented in the chapter. In Chapter 3, the American business judgment rule is presented. The chapter presents extensive information about the American business judgment rule. In Chapter 4, general information about the relationship between the corporate bodies in Swedish law is presented. Subsequently, the duties of the corporate bodies are covered. Lastly, the duty of loyalty, the duty of care, the business purpose, and the business object are presented. In Chapter 5, the liabilities of the directors and CEO in Swedish law are covered. The liability related to the used method, the so-called method liability is presented. Statements made by Lindskog, the former Chief Justice of the Supreme Court of Sweden, are covered. Court cases from the Supreme Court of Sweden that deal with the method liability are presented. Also, statements regarding the existence of something similar to the American business judgment rule in Swedish law are presented. In Chapter 6, the comparative analysis is conducted. The comparative analysis is focused on the research questions and mostly based on what is presented in Chapter 3 and Chapter 5. The reason is that the presentations in these chapters are the most relevant and interesting for the comparative analysis. Finally, the conclusions are presented.

2 Overview of American Corporate Law

2.1 Introduction

This chapter will present introductory and general information about American corporate law. First, the regulation of corporate law in the U.S. will be presented. Second, the relationship between the corporate bodies and the duties of the directors and officers will be presented. Third, the duty of loyalty, the duty of care, and good faith will be presented.

2.2 Regulation of Corporate Law in the U.S.

There are basically no federal laws that regulate corporations in the U.S. Since state law governs the corporations, the corporate laws are individual in every state in the U.S. The incorporators decide in which state they want to incorporate their companies.³⁷ Many companies choose to incorporate in Delaware, even if they do business in another state.³⁸ The reason is that the corporate laws in Delaware are both updated and modern, and offer flexibility. The corporate laws in Delaware are also well developed. The large number of companies in Delaware gives rise to a profuse amount of corporate litigation, which means that the respected courts in Delaware have already decided on many important routine questions.³⁹

Even if the corporate laws in the U.S. are different in every state, some harmonization is achieved through the MBCA and DGCL. Both the MBCA and DGCL influence the states when they update their corporate laws. The MBCA and DGCL also influence each other. The MBCA is used by most states in the U.S. while the DGCL, which is used in Delaware, is important

³⁷ Bainbridge (2015) p. 8 ff; Gevurtz (2010) p. 34 f; McAlinn, Rosen, and Stern (2010) p. 327.

³⁸ Sharfman, "The Importance of the Business Judgment Rule", *New York University Journal of Law & Business*, Vol. 14, No. 1, (2017), p. 32 f.

³⁹ Gevurtz (2010) p. 40 f; McAlinn, Rosen, and Stern (2010) p. 327; Radin (2009) p. 7.

due to the fact that a very large number of companies are incorporated in Delaware. There are several sections in the MBCA that can be seen as codifications of the common law in Delaware.⁴⁰ Therefore, there are similarities between the states both regarding corporate law statutes and case law. However, there are still important differences among the states.⁴¹

The ALI Principles of Corporate Governance also influence the state laws. The ALI Principles assemble the laws in various states and also reflect the current laws in the various states. The ALI Principles are updated on a continuous basis, as new cases are decided.⁴²

A company can be organized after either a one-tier or a two-tier system. The one-tier system only includes one corporate body that can both manage the company and monitor the management of the company. The two-tier system, on the other hand, includes two corporate bodies. One of them has a monitoring function while the other is responsible for the management of the company. American corporate law is organized in accordance with the one-tier system.⁴³

2.3 The Duties of the Directors and Officers

The shareholders' meeting sometimes needs to vote on a business decision that is fundamental for the company.⁴⁴ Such a business decision could for example involve a sale of all the assets belonging to the company.⁴⁵ An annual general meeting is normally held each year.⁴⁶ A corporation can also hold a so-called special shareholders' meeting under certain

⁴⁰ Dooley and Goldman, "Some Comparisons Between the Model Business Corporation Act and the Delaware General Corporation Law", *The Business Lawyer*, Vol. 56, (2001), p. 737 ff. and 764; Gorris, Hamermesh, and Strine, "Delaware Corporate Law and the Model Business Corporation Act: A Study in Symbiosis", *Law and Contemporary Problems*, Vol. 74, (2011), p. 107 f.

⁴¹ Ventrizzo (2015) p. 35.

⁴² Bainbridge (2015) p. 10.

⁴³ Kraakman (2017) p. 50; Ventrizzo (2015) p. 249 ff.

⁴⁴ Balouziyeh (2013) p. 49; Gevurtz (2010) p. 11.

⁴⁵ Ventrizzo (2015) p. 276.

⁴⁶ DGCL § 211 (b); MBCA § 7.01.

circumstances.⁴⁷ The shareholders' meeting elects the directors of a company.⁴⁸

The directors are responsible for the management of the company's business and affairs.⁴⁹ This is expressed in the following way in the DGCL: "The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors."⁵⁰

The directors have a broad discretion to manage the company's business and to maximize the profit of the shareholders. It does not matter what the directors do in order to maximize the profit of the shareholders. What is important is that they simply do it.⁵¹ *Dodge v. Ford Motor Co.*⁵² is an American landmark case stating that a "business corporation is organized and carried on primarily for the profit of the stockholders."⁵³

The directors appoint the officers.⁵⁴ The officers are responsible for the day-to-day business operations and can take all actions that the directors have delegated to them.⁵⁵ The officers get their authority from the directors.⁵⁶ The directors need to delegate authority to the officers in order for the officers to perform certain functions.⁵⁷ It is not possible for the officers to perform a major transaction if the directors have not already approved it.⁵⁸ The directors are responsible to monitor the officers and make sure that they fulfill their duties.⁵⁹ In a broad sense, the directors make decisions while the officers usually carry them out.⁶⁰

⁴⁷ DGCL § 211 (d); MBCA § 7.02.

⁴⁸ DGCL §§ 211 (b) and 216 (3); Gevurtz (2010) p. 179 and 186; MBCA §§ 7.28 (a) and 8.03 (c).

⁴⁹ Gevurtz (2010) p. 190.

⁵⁰ DGCL § 141 (a). See also MBCA § 8.01 (b).

⁵¹ Backer (2002) p. 180. Balouziyeh (2013) p. 50.

⁵² 170 N.W. 668 (1919).

⁵³ *Dodge v. Ford Motor Co.*, 170 N.W. 668, 684 (1919).

⁵⁴ DGCL § 142 (b); MBCA § 8.40 (a) and (b); McAlinn, Rosen, and Stern (2010) p. 327.

⁵⁵ Gevurtz (2010) p. 11; McAlinn, Rosen, and Stern (2010) p. 327.

⁵⁶ Backer (2002) p. 183; Gevurtz (2010) p. 11.

⁵⁷ MBCA § 8.41.

⁵⁸ Backer (2002) p. 183; Gevurtz (2010) p. 11.

⁵⁹ Backer (2002) p. 177.

⁶⁰ Gevurtz (2010) p. 179.

The directors can either manage the company themselves or let the officers do it. The growing conception is that the directors monitor, instead of manage, the company's affairs.⁶¹ However, the directors are ultimately responsible for the management of the company and for major business decisions.⁶² For example, the directors are responsible to approve extraordinary investments and other operational business decisions that are not included in the officers' day-to-day business operations.⁶³ The directors also have the power to make decisions regarding the payment of dividends and the compensation to the CEO.⁶⁴ In addition, the directors are also responsible for the overall policies and strategies of the company.⁶⁵ The directors act collectively which means that an individual director has no own authority.⁶⁶

2.4 Duty of Loyalty, Duty of Care, and Good Faith

The directors and officers are so-called fiduciaries of their companies. The directors of a company owe fiduciary duties both to the company and to the company's shareholders. The officers also owe the same fiduciary duties to the company and the company's shareholders. The fiduciary duties include the duty of loyalty, the duty of care, and good faith.⁶⁷ The duty of loyalty and the duty of care that an agent owes to the principal are in essence the same as the duty of loyalty and duty of care that the directors owe to the shareholders.⁶⁸

The fiduciary duties were historically comprised of the duty of care and the duty of loyalty. The business judgment rule, which will be presented in the

⁶¹ Backer (2002) p. 179; Cahn and Donald (2018) p. 356; Gevurtz (2010) p. 190.

⁶² Gevurtz (2010) p. 11 and 190; McAlinn, Rosen, and Stern (2010) p. 327.

⁶³ Backer (2002) p. 179; McAlinn, Rosen, and Stern (2010) p. 327.

⁶⁴ Backer (2002) p. 179; Ventoruzzo (2015) p. 277.

⁶⁵ McAlinn, Rosen, and Stern (2010) p. 327.

⁶⁶ Gevurtz (2002) p. 190.

⁶⁷ Radin (2009) p. 1 f; Velasco, "How Many Fiduciary Duties Are There In Corporate Law?", *Southern California Law Review*, Vol. 83, No. 6, (2010), p. 1232 f.

⁶⁸ Backer (2002) p. 179 f.

next chapter, protected alleged breaches of the duty of care. The fairness test was on the other hand used to review breaches of the duty of loyalty. Primarily the courts in Delaware have developed the fiduciary duties and they are more complex today. In *Smith v. Van Gorkom*⁶⁹, directors were held liable for breaching the duty of care since they were not sufficiently informed before making the business decision.⁷⁰ This was a shock for both the corporate and the legal communities since the gross negligence standard almost seemed unreachable.⁷¹ Many people did not consider the directors' conduct inappropriate or in line with what amounted to gross negligence.⁷² In *Cede & Co. v. Technicolor, Inc.*⁷³, the court explained that the fiduciary duties consist of not only the duty of care and the duty of loyalty but also good faith.⁷⁴ In *In re The Walt Disney Co. Derivative Litigation*⁷⁵, the duty of good faith was confirmed as a fiduciary duty.⁷⁶

However, *Stone v. Ritter*⁷⁷ later clarified that good faith cannot be seen as an independent fiduciary duty.⁷⁸ Good faith is instead included in the duty of loyalty.⁷⁹ Consequently, if the director acts in bad faith, the director will breach the duty of loyalty owed to the company. The directors need to make a good faith effort to carry out their assignment as directors.⁸⁰

⁶⁹ 488 A.2d 858 (Del. 1985).

⁷⁰ Sharfman, "Being Informed Does Matter: Fine Tuning Gross Negligence Twenty Plus Years After Van Gorkom", *The Business Lawyer*, Vol. 62, No. 1, (2006), p. 136.

⁷¹ Sharfman, "Being Informed Does Matter: Fine Tuning Gross Negligence Twenty Plus Years After Van Gorkom", *The Business Lawyer*, Vol. 62, No. 1, (2006), p. 136; Sharfman "The Importance of the Business Judgment Rule", *New York University Journal of Law & Business*, Vol. 14, No. 1, (2017), p. 48 f; Velasco, "How Many Fiduciary Duties Are There In Corporate Law?", *Southern California Law Review*, Vol. 83, No. 6, (2010), p. 1232 f.

⁷² Velasco, "A Defense of the Corporate Law Duty of Care", *The Journal of Corporation Law*, Vol. 40, (2015), p. 658; Velasco, "How Many Fiduciary Duties Are There In Corporate Law?", *Southern California Law Review*, Vol. 83, No. 6, (2010), p. 1232 f.

⁷³ 634 A.2d 345 (Del. 1993).

⁷⁴ Velasco, "How Many Fiduciary Duties Are There In Corporate Law?", *Southern California Law Review*, Vol. 83, No. 6, (2010), p. 1232 f.

⁷⁵ 906 A.2d 27 (Del. 2006).

⁷⁶ Velasco, "How Many Fiduciary Duties Are There In Corporate Law?", *Southern California Law Review*, Vol. 83, No. 6, (2010), p. 1232 f.

⁷⁷ 911 A.2d 362 (Del. 2006).

⁷⁸ Hill and McDonnell, "Stone v. Ritter and the Expanding Duty of Loyalty", *Fordham Law Review*, Vol. 76, Issue 3, (2007), p. 1769; Radin (2009) p. 3.

⁷⁹ Radin (2009) p. 788 f.

⁸⁰ Radin (2009) p. 789.

The duty of loyalty requires the directors to act in good faith and preserve the best interests of both the company and the shareholders.⁸¹ Through the duty of loyalty, the company is guaranteed that the business decisions are made with the corporation's and the shareholders' best interests in mind and not with the directors' interests in mind.⁸²

The duty of care on the other hand requires the directors to act on an informed basis when they make business decisions.⁸³ The duty of care means that if there is a risk of harm connected to a specific conduct, the responsible person has a duty to act as a reasonable person would have acted under the same circumstances in order to avoid harm.⁸⁴ Generally, the duty of care is seen as less rigorous, less strict and weaker than the duty of loyalty in American law.⁸⁵ The duty of care is essentially never enforced. A claim solely based on the duty of care will normally not lead to liability for the directors. Usually, only violations of the duty of loyalty will lead to liability⁸⁶

The courts use the standard of review in order to evaluate if someone has acted within the duty of care. The normal standard of review in tort law is ordinary negligence while there are different standards of review in corporate law.⁸⁷ The gross negligence standard, superior to ordinary negligence, is applied in order to determine if a director acted within the duty of care.⁸⁸ The gross negligence standard is what most commentators suggest should be the standard of culpability that will impose liability on

⁸¹ Radin (2009) p. 2. See DGCL § 144.

⁸² Radin (2009) p. 789 f.

⁸³ Radin (2009) p. 2.

⁸⁴ Gevurtz (2010) p. 278.

⁸⁵ Bruner, "Is the Corporate Director's Duty of Care a 'Fiduciary' Duty? Does It Matter?", *Wake Forest Law Review*, Vol. 48, (2013), p. 1037 f; Velasco, "The Diminishing Duty of Loyalty", *Washington and Lee Law Review*, Vol. 75, Issue 2, (2018), p. 1037 f.

⁸⁶ Sharfman, "Being Informed Does Matter: Fine Tuning Gross Negligence Twenty Plus Years After Van Gorkom", *The Business Lawyer*, Vol. 62, No. 1, (2006), p. 136 and 160; Velasco, "A Defense of the Corporate Law Duty of Care", *The Journal of Corporation Law*, Vol. 40, (2015), p. 650.

⁸⁷ Velasco, "A Defense of the Corporate Law Duty of Care", *The Journal of Corporation Law*, Vol. 40, (2015), p. 651.

⁸⁸ Radin (2009) p. 457 f.

directors. Simply bad judgment will usually not make the directors liable.⁸⁹ The Delaware Court has stated this in *Aronson v. Lewis*⁹⁰ and *Smith v. Van Gorkom*⁹¹. This has also been reaffirmed several times.⁹²

2.5 Summary

The corporate laws are different in every state in the U.S. The MBCA and DGCL contribute to some harmonization. The shareholders' meeting elects the directors of a company and in turn, the directors appoint the officers. The directors are responsible for the overall management of the company's business. The officers are responsible for the company's day-to-day business operations. The directors monitor the officers and make sure that they fulfill their duties. The directors and officers are so-called fiduciaries of their companies. This means that the directors and officers owe fiduciary duties both to the company and the company's shareholders. The duty of loyalty, the duty of care, and good faith are included in the fiduciary duties. The duty of loyalty requires the directors to act in good faith and preserve the best interests of the company and the shareholders. The duty of care requires the directors to act on an informed basis when they make business decisions for the company. The duty of care is weaker than the duty of loyalty in American law.

⁸⁹ Radin (2009) p. 457 f; Sharfman, "The Importance of the Business Judgment Rule", *New York University Journal of Law & Business*, Vol. 14, No. 1, (2017), p 48 f.

⁹⁰ 473 A.2d 805 (Del. 1984).

⁹¹ 488 A.2d 858 (Del. 1985).

⁹² Radin (2009) p. 465 f.

3 The American Business Judgment Rule

3.1 Introduction

This chapter will present information about the American business judgment rule. General information about the business judgment rule and the rationales of the business judgment rule will initially be presented. Subsequently, this chapter will present detailed information about the business judgment rule presumption and its components.

3.2 Overview of the Business Judgment Rule

The business judgment rule is considered to be the most prominent and important standard of judicial review in the area of corporate law.⁹³ U.S. courts have used the business judgment rule for more than 175 years.⁹⁴ The business judgment rule is a so-called “standard of judicial review of director conduct, not a standard of conduct.”⁹⁵ The general conception among the courts in the U.S. is that the business judgment rule applies equally to both directors and officers.⁹⁶

Black’s Law Dictionary defines the business judgment rule as “the presumption that in making business decisions not involving direct self-interest or self-dealing, corporate directors act on an informed basis, in good faith, and in the honest belief that their actions are in the corporation’s best interest.”⁹⁷

⁹³ Bainbridge, “The Business Judgment Rule as Abstention Doctrine”, *UCLA, School of Law, Law and Economics Research Paper Series*, No. 03-18, (2003), p. 1; Sharfman, “The Importance of the Business Judgment Rule”, *New York University Journal of Law & Business*, Vol. 14, No. 1, (2017), p. 29.

⁹⁴ Radin (2009) p. 26.

⁹⁵ Radin (2009) p. 11.

⁹⁶ Radin (2009) p. 398.

⁹⁷ Garner and Black (2009) p. 226.

The drafters of the MBCA stated that the business judgment rule is to be seen as a broad common law concept according to which the directors' business decisions will not be overturned if there are rational business reasons behind the decision.⁹⁸ The MBCA is not codifying the business judgment rule and the elements of the rule are continuously to be developed by courts.⁹⁹

The business judgment rule presumes that the directors acted in a faithful way when they carried out their fiduciary duties.¹⁰⁰ In *Aronson v. Lewis*¹⁰¹, a landmark case, the Delaware Court ruled that the business judgment rule is “a presumption that in making a business decision, the directors of a company acted on an informed basis, in good faith, and in the honest belief that the action was taken in the best interests of the company.”¹⁰² Following *Aronson v. Lewis*¹⁰³, the Delaware Court has continued to state the presumption regarding the business judgment rule. *In re Walt Disney Co. Derivative Litigation*¹⁰⁴ is a later and prominent case in which the Delaware Court quotes *Aronson v. Lewis*¹⁰⁵.¹⁰⁶

If the directors get sued, the American courts are only going to review the business decision in order to ascertain that the plaintiff has put forward enough evidence that will overcome the business judgment rule presumption. If it is not possible for the plaintiff to overcome the business judgment rule presumption, the court will be prohibited to review the business decision further.¹⁰⁷

⁹⁸ Radin (2009) p. 53.

⁹⁹ Radin (2009) p. 403 f; See MBCA § 8.31.

¹⁰⁰ *Beam ex rel. Martha Stewart Living Omnimedia, Inc. v. Stewart*, 845 A.2d 1040, 1048 (Del. 2004); Radin (2009) p. 11.

¹⁰¹ 473 A.2d 805 (Del. 1984).

¹⁰² *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984); Radin (2009) p. 42.

¹⁰³ 473 A.2d 805 (Del. 1984).

¹⁰⁴ 906 A.2d 27 (Del. 2006).

¹⁰⁵ 473 A.2d 805 (Del. 1984).

¹⁰⁶ Radin (2009) p. 11.

¹⁰⁷ Radin (2009) p. 13.

The courts are normally unwilling to erase a business decision made by the directors and replace it with another decision made by a judge. It would not serve as a protection for the shareholders to do so. Instead, the courts want to ensure that the business decisions are made independently and without any self-interest. Generally, directors are not only appointed to the board because of their business mindset but also because they have the right qualifications and skills to make evaluations and determine what is the best business decision for the company.¹⁰⁸

The business judgment rule gives the directors “broad discretion in making corporate decisions [...] without judicial second-guessing in hindsight.”¹⁰⁹ This means that the courts will not second-guess the merits of a business decision. The business judgment rule does recognize the fact that a director might have to make important business decisions without knowing what the future will look like. Sometimes, the director might also have to make the business decision rapidly without further evaluations and thoughts.¹¹⁰

The business judgment rule protects the directors from honest mistakes and even from poor business decisions causing the company a considerable economic loss.¹¹¹ This was expressed in the following way by an American court: “Although defendants’ investment scheme may have turned out to be unwise, the business judgment rule shields them from liability in the absence of bad faith, a conflict of interest or personal bias.”¹¹² Also, even if the business outcome might seem wrong, irrational, and stupid afterwards, it is of no legal importance since it will not be subject of a judicial review.¹¹³ The business judgment rule is “the only formulation which attends the interests of vigorous entrepreneurship while, at the same time, protecting

¹⁰⁸ Radin (2009) p. 13 f.

¹⁰⁹ Radin (2009) p. 14.

¹¹⁰ Radin (2009) p. 15.

¹¹¹ Radin (2009) p. 18 f.

¹¹² Radin (2009) p. 18 f.

¹¹³ Radin (2009) p. 19 f.

shareholders and their companies from the predations of those who would pick off and plunder.”¹¹⁴

It can be said that the shareholders through their investments in the company accept the risk that a monetary loss might occur due to unwise business decisions.¹¹⁵ “The value of a shareholder’s investment, over time, rises or falls chiefly because of the skill, judgment and perhaps luck – for it is present in all human affairs – of the management and directors of the enterprise. When they exercise sound or brilliant judgment, shareholders are likely to profit; when they fail to do so, share values likely will fail to appreciate. In either event, the financial vitality of the corporation and the value of the company’s shares is in the hands of the directors and managers of the firm. The corporation law does not operate on the theory that directors, in exercising their powers to manage the firm, are obligated to follow the wishes of a majority of shares. In fact, directors, not shareholders, are charged with the duty to manage the firm.”¹¹⁶

3.3 The Rationales of the Business Judgment Rule

One of the reasons why the business judgment rule exists is that corporations would otherwise not function properly. It would be difficult to recruit directors if the directors were to be held liable for business decisions that were made in good faith but turned out to be unwise.¹¹⁷ There are both uncertainties and risks associated with business decisions that can prove to be good and give rise to a large profit. It is considered positive for the economy to protect the directors’ reasonable risks. Corporate directors often need to take risks in order for the business to thrive. In addition, a company’s business would stagnate if the shareholders unconditionally

¹¹⁴ Radin (2009) p. 19 ff.

¹¹⁵ Radin (2009) p. 21.

¹¹⁶ *Paramount Communications Inc. v. Time Inc.*, 1989 WL 79880, 749–750 (Del. Ch. 1989).

¹¹⁷ Radin (2009) p. 30.

would have the possibility to challenge all business decisions and if the courts could intervene easily and change the directors' business decisions.¹¹⁸

Directors need to make business decisions without the fear of becoming liable. In widely dispersed companies, there will always be some shareholders who do not support the business decisions made by the directors.¹¹⁹ Also, the shareholders vote the directors to office and delegate to them the responsibility to manage the company's business. This means that the shareholders that are unpleasant with their work can make sure not to reappoint them.¹²⁰ From a business point of view, directors should be encouraged to take business risks by entering new product markets, innovate, and develop new products.¹²¹

Also, the courts are ill equipped to decide on cases that involve complex corporate business decisions. The judges are simply not trained to do it. Since the judges are not as qualified as the directors, it will not make sense to let them, instead of the directors, manage the business affairs and make business decisions.¹²²

3.4 The Presumption

The Delaware courts presume that “in making a business decision the directors of a corporation acted on an informed basis, in good faith, and in the honest belief that the action taken was in the best interest of the company.”¹²³ More than 35 jurisdictions in the U.S. other than Delaware apply the business judgment rule presumption.¹²⁴

¹¹⁸ Radin (2009) p. 30 f.

¹¹⁹ Taylor, “Tender Offers and the Business Judgment Rule”, *University of Miami Business Law Review*, 171, (1999), p. 185.

¹²⁰ Radin (2009) p. 40.

¹²¹ Radin (2009) p. 31.

¹²² Radin (2009) p. 35.

¹²³ *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984); *In re Walt Disney Co. Derivative Litigation*, 906 A.2d 27, 52 (Del. 2006); Radin (2009) p. 42.

¹²⁴ Radin (2009) p. 45.

If “the board act[s] with due care, good faith, and in the honest belief that they are acting in the best interests of the stockholders”¹²⁵, the courts will not review their business decision. Instead, they will defend it. The directors will not become liable if they make a business decision that turns out to be irrational if the business judgment rule is applicable.¹²⁶ The business judgment rule presumption means that a court will not do an objective reasonableness test in order to review the business decision. Instead, the court will defend the directors’ business decision if it was based on proper grounds.¹²⁷

As long as the business judgment rule presumption is not overturned, the directors will not be held liable for their business decisions, not even for unwise business decisions. When the business judgment rule is not overturned, the business decisions will not be substituted by court judgments.¹²⁸

The implication of the business judgment rule is that the plaintiff needs to overcome the business judgment rule presumption in order to state a claim. The primary burden of proof is consequently placed on the plaintiff. In order for the plaintiff to overcome the business judgment rule presumption, enough evidence must be put forward to demonstrate that the directors breached their fiduciary duties or that they acted in bad faith when they made the business decision.¹²⁹

If the plaintiff cannot put forward enough evidence, the business judgment rule protects the directors from liability. It is considered to be a very tough task for the plaintiff to overcome the business judgment presumption.¹³⁰ However, if the plaintiff does overcome the presumption, the defendant needs to put forward enough evidence that demonstrate that the business

¹²⁵ Radin (2009) p. 44.

¹²⁶ Radin (2009) p. 44.

¹²⁷ Radin (2009) p. 45.

¹²⁸ Radin (2009) p. 13 f. and 44 f.

¹²⁹ Radin (2009) p. 53 ff.

¹³⁰ Radin (2009) p. 53 f.

decision was fair to both the company and to all shareholders of the company. The court will then make a detailed fairness determination of all aspects of the business decision. This includes detailed reviews of the decision-making process.¹³¹

In this context, it is important to clarify that business decisions that constitute fraud or illegality are not protected by the business judgment rule.¹³²

3.5 The Components of the Presumption

The business judgment rule presumption consists of four components, namely a business decision, disinterestedness and independence, duty of care, and good faith. The business judgment rule presumption is only rebutted if the plaintiff can demonstrate that any of the four components was not fulfilled.¹³³

(1) First of all, there needs to be a business decision made by a director. Failure to take an action is not considered as a business decision.¹³⁴ (2) It is important to note that the business judgment rule does not protect directors who have had an interest in a specific business decision since the directors might not have made the business decision without the personal benefits in mind. The business decision simply needs to be in the best interest of the company. If the directors have breached their duty of loyalty, the business judgment rule is not applicable.¹³⁵ (3) The duty of care element of the business judgment rule is comprised of the directors' duty to act on an informed basis. When making the determination of whether a director was informed or not, the court determines if the directors informed themselves with all material reasonably available before making the business decision. The directors only need to be informed about the material facts that are

¹³¹ Radin (2009) p. 62 f.

¹³² Radin (2009) p. 378.

¹³³ Radin (2009) p. 86 f.

¹³⁴ Radin (2009) p. 87 f.

¹³⁵ Radin (2009) p. 92 f.

considered to be within the directors' reasonable reach. Therefore, they do not have to be informed of every single fact.¹³⁶ (4) Good faith is not an independent duty like the duty of loyalty and the duty of care. Therefore, a failure to act in good faith may only lead to liability indirectly, while a breach of the duty of loyalty or the duty of care may give rise to liability directly. A failure to act in good faith will indirectly lead to liability through the duty of loyalty.¹³⁷

3.6 Summary

In *Aronson v. Lewis*, the Delaware Court ruled that the business judgment rule is a presumption that in making a business decision, the directors of a company acted on an informed basis, in good faith, and in the honest belief that the action was taken in the best interests of the company. The business judgment rule presumes that the directors acted in a faithful way when they carried out their fiduciary duties. If the directors are sued, the courts only review the business decision in order to ascertain that the plaintiff has put forward enough evidence that will overcome the business judgment rule presumption. The business judgment rule presumption consists of four components, namely a business decision, disinterestedness and independence, duty of care, and good faith. The business judgment rule presumption is only rebutted in those unusual cases when the plaintiff can demonstrate that any of the four components was not fulfilled. If the plaintiff cannot overcome the business judgment rule presumption, the court is prohibited to review the business decision further. Then, the business judgment rule protects the directors from liability and they will not become liable for their business decisions, not even for unwise business decisions. Directors need to make business decisions without the fear of becoming liable. Courts are also not equipped to decide on complex corporate business decisions.

¹³⁶ Radin (2009) p. 308.

¹³⁷ Radin (2009) p. 329 and 787 f.

4 Duties of the Corporate Bodies in Swedish Law

4.1 Introduction

This chapter will present introductory and general information about the duties that apply to the different corporate bodies in Swedish law. First, the relationship between the corporate bodies will be presented. Second, the duties of the corporate bodies will be presented. Third, the duty of loyalty, the duty of care, and general information about the business purpose and the business object will be presented.

4.2 The Relationship Between the Corporate Bodies

There are four corporate bodies in Swedish law, namely the shareholders' meeting, the directors, the CEO, and the auditor. The first one is the superior decision-making body, the second and third one are the management bodies and the last one is the controlling body.¹³⁸ It should be noted that it is not mandatory for private companies to have a CEO.¹³⁹

The shareholders' meeting is the superior body of a company. The directors are subordinate to the shareholders' meeting.¹⁴⁰ In turn, the CEO is subordinate to the directors, which is made clear by Chapter 8, Section 29 of the Swedish Companies Act. The hierarchy means that the CEO must first turn to the directors and then to the shareholders' meeting.¹⁴¹

¹³⁸ Sandström (2017) p. 283; Svernlöv (2008) p. 36.

¹³⁹ Rodhe and Skog (2018) p. 176; Svernlöv (2008) p. 36.

¹⁴⁰ Dotevall (2015) p. 204 f.

¹⁴¹ Dotevall (2015) p. 228 and 269.

Companies can be organized after either a one-tier or a two-tier system. Swedish law is influenced by the two-tier system but is closer organized to the one-tier system.¹⁴²

The directives submitted by the shareholders' meeting should be followed as long as they are not in conflict with the articles of association according to Chapter 8, Section 34 of the Swedish Companies Act. Chapter 8, Section 41 of the Swedish Companies Act states that directors and CEOs have a duty to determine whether a decision made by a superior corporate body is made in accordance with the Swedish Companies Act, any other laws, the annual financial report, or the articles of association.¹⁴³

4.3 The Corporate Bodies and Their Duties

4.3.1 Shareholders' Meeting

In Swedish law, the shareholders' meeting is the highest decision-making body of a company.¹⁴⁴ At the shareholders' meeting, the shareholders have the possibility to make decisions regarding the company's affairs according to Chapter 7, Section 1 of the Swedish Companies Act. The shareholders' meeting can leave directives that the directors will be bound by and also make certain decisions on an exclusive basis.¹⁴⁵ In order to be able to vote at a shareholders' meeting, a shareholder needs to be a legitimate shareholder, which means that the shareholder needs to be registered in the share register.¹⁴⁶ Since the shareholders have economic interests in the company, it is rational that the shareholders can make decisions that affect the economy of the company. Also, the shareholders have an interest to make

¹⁴² Dotevall (2015) p. 229; Östberg (2016) p. 107.

¹⁴³ Dotevall (2015) p. 271.

¹⁴⁴ Dotevall (2015) p. 205; Svernlöv (2008) p. 37.

¹⁴⁵ Dotevall (2015) p. 205.

¹⁴⁶ Samuelsson, [the Swedish Companies Act (ABL), the comment of Chapter 7, Section 1, note 310], Karnov on February 2, 2019.

sure that the directors and CEO as well as the majority shareholders of the company do not abuse their power.¹⁴⁷

An additional shareholders' meeting, a so-called special shareholders' meeting, can take place if the directors find it necessary. This is in accordance with Chapter 7, Section 13 of the Swedish Companies Act.

4.3.2 Directors

Chapter 8, Section 8 of the Swedish Companies Act states that the shareholders' meeting appoints the directors. Only a physical person can be appointed as a director.¹⁴⁸ According to Chapter 8, Section 13 of the Swedish Companies Act, the period during which a director is in office lasts until the close of the first annual general meeting held after the year in which the director was appointed.

The directors are responsible for the organization and management of the company's business according to Chapter 8, Section 4 of the Swedish Companies Act. The directors have the most far-reaching duty to manage the company.¹⁴⁹ However, the directors have the possibility to delegate tasks to the CEO or someone else. When they do, they get a supervisory function.¹⁵⁰ Anyhow, it is not possible for the directors to delegate all their duties related to the management of the company since they have the superior responsibility for the management of the company.¹⁵¹

The directors need to follow decisions made by the shareholders' meeting even if the directors' opinion is that the decision is inappropriate from a business perspective.¹⁵² When it comes to managerial decisions of extraordinary nature, the directors need to let the shareholders' meeting

¹⁴⁷ Östberg (2016) p. 91.

¹⁴⁸ Samuelsson, [the Swedish Companies Act (ABL), the comment of Chapter 8, Section 8, note 519], Karnov on February 2, 2019.

¹⁴⁹ Dotevall (2015) p. 267; Svernlöv (2008) p. 37.

¹⁵⁰ Dotevall (2015) p. 267.

¹⁵¹ Dotevall (2015) p. 277.

¹⁵² Dotevall (2015) p. 272.

make a decision.¹⁵³ Nevertheless, it is important that efficiency and discretion is maintained. This means that sometimes it might be both practically inappropriate and potentially hostile towards to company to let the shareholders' meeting make a decision.¹⁵⁴

4.3.3 CEO

The CEO is responsible for the day-to-day business operations according to Chapter 8, Section 29 of the Swedish Companies Act. The CEO has to act based on the instructions from the directors since it is the directors who decide the content of the day-to-day business operations. What is included in the day-to-day business operations is dependent on the company's specific business as well as on the size of the company. The day-to-day business operations do not include decision that are unusual or of great importance.¹⁵⁵

4.4 Duty of Loyalty and Duty of Care

There is a duty of loyalty in Swedish law that applies to the directors and CEO.¹⁵⁶ The duty of loyalty that applies to the directors and CEO is not expressly regulated in the Swedish Companies Act but can be deducted through the rules regarding conflict of interests in Chapter 8, Section 23 and 27, and through the general clause in Chapter 8, Section 41.¹⁵⁷ The legal discussion regarding the duty of loyalty within corporate law is both incomplete and limited. Therefore, it is not possible to find a clarifying description of the meaning of the duty of loyalty.¹⁵⁸

The general rules that are applicable within a contractual relationship between a principal and an agent are also applicable between the company and the directors and CEO.¹⁵⁹ The relationship between the principal and the

¹⁵³ Dotevall (2015) p. 269.

¹⁵⁴ Dotevall (2015) p. 270.

¹⁵⁵ Dotevall (2015) p. 267 ff; Svernlöv (2008) p. 37; Svernlöv (2014) p. 95 f.

¹⁵⁶ Dotevall (2017) p. 142 ff; Östberg (2016) p. 151.

¹⁵⁷ Dotevall (2015) p. 292.

¹⁵⁸ Bergström and Samuelsson (2015) p. 95.

¹⁵⁹ Dotevall (2017) p. 147; Prop. 1975:103 p. 376 f; Stattin (2008) p. 362.

agent can give rise to a conflict of interest. In the corporate sphere, this conflict of interest usually arises when the director or CEO has a personal interest, which is in conflict with the interest of the company.¹⁶⁰ In Swedish law, the duty of loyalty simply means that the directors and CEO cannot directly or indirectly use their positions in order to benefit their own interests.¹⁶¹ The directors and CEO need to act loyally towards the company and the company's shareholders, and put the company's interests first.¹⁶²

The directors and CEO have a more independent role compared to agents in general. For example, the directors do not have to call a special shareholders' meeting in order to determine if a decision is in the best interest of the company or not.¹⁶³ It can also be noted that there is a slight difference between the duty of loyalty that applies to the directors and the duty of loyalty that applies to the CEO.¹⁶⁴

The duty of care has not been extensively addressed in case law and the legal scholars' opinions about the duty of care are not consistent. However, the most consistent view among the legal scholars is that the directors and CEO need to follow the ordinary care required by agents in general.¹⁶⁵ This means that the directors and CEO need to act with the ordinary care when they manage the company's business.¹⁶⁶ The duty of care is in Swedish law sometimes used as synonym to the duty of loyalty.¹⁶⁷ The duty of loyalty can also be considered part of the duty of care.¹⁶⁸

In order to fulfill their duty of care, the directors and CEO need to prepare and carry out their assignments in a satisfying way and also make sure that

¹⁶⁰ Dotevall (2015) p. 281.

¹⁶¹ Dotevall (2015) p. 293 and 308.

¹⁶² Dotevall (2015) p. 228; Dotevall, "Liability of Members of the Board of Directors and the Managing Directors – A Scandinavian Perspective", *The International Lawyer*, Vol. 37, No. 1, (2003), p. 81.

¹⁶³ Dotevall (2015) p. 293.

¹⁶⁴ Dotevall (2017) p. 147.

¹⁶⁵ Stattin (2008) p. 362; Östberg (2016) p. 321.

¹⁶⁶ Östberg (2016) p. 319 ff.

¹⁶⁷ Munukka, "Lojalitetsprincipen som rättsprincip", *SvJT* 2010, p. 839; Östberg (2016) p. 62.

¹⁶⁸ Östberg (2016) p. 62.

business decisions are made on an acceptable basis. The riskier the business decision is, the more preparations and examinations of the underlying material need to be done before the directors or CEO make the business decision.¹⁶⁹

4.5 Business Purpose and Business Object

Unless there is something else stated in the articles of association, the business purpose of a company is to generate profit according to Chapter 3, Section 3 of the Swedish Companies Act. Both directors and CEOs have a duty to fulfill the purpose of the company and they need to make sure that the company generates profit.¹⁷⁰ A definite scope of the business purpose is hard to define. Therefore, the directors and CEO get a broad discretion to fulfill the business purpose.¹⁷¹

There is a duty for both the directors and CEO to be active and make sure that the company fulfills the business purpose.¹⁷² The duty to be active is most likely included in the duty of care.¹⁷³ The CEO usually needs to be active on a more frequent basis than the directors since the CEO is responsible for the day-to-day business operations.¹⁷⁴ However, the duty to be active does not mean that the directors and CEO are not allowed to make risky business decisions that might not lead to a profit.¹⁷⁵

The business reasons behind a business decision will usually not be challenged as long as the business decision made by the directors or CEO has been decided in a satisfying way. This means that, as long as the duty of loyalty is observed, the directors and CEO have a broad discretion to manage the company's business. However, this cannot be the case when a

¹⁶⁹ Östberg (2016) p. 322.

¹⁷⁰ Dotevall (2015) p. 228.

¹⁷¹ Dotevall (2015) p. 194.

¹⁷² Dotevall (2015) p. 375; Sandström (2017) p. 263; Östberg (2016) p. 322.

¹⁷³ Östberg (2016) p. 322.

¹⁷⁴ Sandström (2017) p. 263.

¹⁷⁵ Dotevall (2015) p. 375.

business decision is considered obviously unmotivated from a business point of perspective.¹⁷⁶

A general principle in Swedish law is that a business decision only violates the business object and the company's interests if the business decision obviously deviates from the business object in the articles of association.¹⁷⁷ Through this principle, the directors get the necessary discretion they need in order to make business decisions.¹⁷⁸

4.6 Summary

The directors have the most far-reaching duty to manage the company's business. The CEO is responsible for the day-to-day business operations, which do not include business decisions that are unusual or of great importance. The general rules that are applicable within a contractual relationship between a principal and an agent are also applicable between the company and the directors and CEO. The duty of loyalty requires the directors and CEO to not directly or indirectly benefit their own interests and in this way cause harm to the company. The directors and CEO need to make sure that they act loyally towards the company and the company's shareholders, and that they put the company's interests first. The duty of care requires the directors and CEO to prepare and carry out their assignments in a satisfying way and to make business decisions on an acceptable basis. The directors and CEO need to act with the ordinary care when they manage the company's business. The directors and CEO have a duty to fulfill the purpose of the company, which means that they need to make sure that the company makes a profit. The directors and CEO have a broad discretion to fulfill the business purpose. According to a general principle, a business decision violates the business object and the interests of the company if the business decision obviously deviates from the

¹⁷⁶ Östberg (2016) p. 322.

¹⁷⁷ Dotevall (2015) p. 378; Nerep, Adestam, Samuelsson, [the Swedish Companies Act (ABL), the comment of Chapter 29, Section 1 at 3.11.4], Lexino on January 25, 2019; NJA 1987 s. 394 at 404 f; Östberg (2016) p. 255.

¹⁷⁸ Nerep, Adestam, Samuelsson, [the Swedish Companies Act (ABL), the comment of Chapter 29, Section 1 at 3.11.4], Lexino on January 25, 2019

business object in the articles of association. This principle gives the directors the necessary discretion they need in order to make business decisions for the company.

5 Liabilities of Directors and CEOs in Swedish Law

5.1 Introduction

This chapter will present information about the liabilities of directors and CEOs in Swedish law. The tools that the Swedish courts use when they decide on a case dealing with liabilities of directors and CEOs will be presented. This chapter will also present information about the liability related to the used method, the so-called method liability theory. Also, statements about the American business judgment rule and the existence of something similar in Swedish law will be presented.

5.2 Determination of Culpability

5.2.1 Overview

In Swedish law, the determination of culpability is based on Chapter 29, Section 1, Paragraph 1, Sentence 1¹⁷⁹ of the Swedish Companies Act. According to Chapter 29, Section 1 of the Swedish Companies Act, a director or CEO who intentionally or through negligence causes damage to the company has to indemnify the company. The liability is individual for each director.¹⁸⁰ These rules about liabilities regarding directors and CEOs are more far-reaching than general Swedish tort law.¹⁸¹ The purpose with the rules is to make sure that directors and CEOs act in a way that does not cause harm to the company.¹⁸² General Swedish tort law is applicable along with Chapter 29, Section 1 of the Swedish Companies Act.¹⁸³

According to general Swedish tort law, it is the injured plaintiff who has the burden of proof and needs to present enough evidence that the alleged

¹⁷⁹ In order to simplify the presentation, this reference will subsequently be referred to as Chapter 29, Section 1.

¹⁸⁰ Dotevall (2017) p. 65.

¹⁸¹ Svernlöv (2008) p. 38.

¹⁸² Svernlöv (2008) p. 42.

¹⁸³ Svernlöv (2012) p. 57.

tortfeasor was negligent. The same principle is applicable regarding the application of Chapter 29, Section 1 of the Swedish Companies Act.¹⁸⁴

There are four prerequisites that must be fulfilled in order for a director or CEO to become liable. First, damage must have occurred. Second, the damage must have been caused within the tortfeasor's assignment. Third, the tortfeasor must have been negligent. Fourth, there must be an adequate causal connection.¹⁸⁵

5.2.2 Loss

A loss needs to have occurred in order for liability to arise. In this context, a loss means an economic measurable loss that the injured plaintiff has suffered grudgingly.¹⁸⁶ A loss that occurs in the corporate world is normally a so-called pure economic loss. A pure economic loss does not have any connections to property damages or personal injuries. The loss can arise from both an act and a failure to act.¹⁸⁷

5.2.3 Loss Within the Assignment

A director or CEO needs to have been appointed as a director or CEO in order to become liable for a loss. The directors' and CEOs' assignments are based on a contract with the company. The act or the omission needs to have been caused within their assignments. Their liability can only be extended to the day they commenced their assignments.¹⁸⁸

¹⁸⁴ Dotevall (2017) p. 57.

¹⁸⁵ Båvestam, "Något om den skadeståndsrättsliga betydelsen av försäkransmeningar i börsbolagen årsredovisningar", *SvJT* 2006, p. 5 f; Dotevall (2015) p. 348; SOU 1995:44 p. 241.

¹⁸⁶ Dotevall (2015) p. 360 f; Dotevall, "Liability of Members of the Board of Directors and the Managing Directors – A Scandinavian Perspective", *The International Lawyer*, Vol. 37, No. 1, (2003), p. 72.

¹⁸⁷ Svernlöv (2012) p. 52 f; Svernlöv (2014) p. 203.

¹⁸⁸ Dotevall (2015) p. 349.

5.2.4 Negligence Assessment

The determination of whether a director or CEO has been negligent or not begins with a comparison between how the director or CEO should act and how the director or CEO has acted in the particular case.¹⁸⁹ This comparison creates an understanding of the necessary degree of carefulness and if the tortfeasor should have acted in another way. It might be necessary to adjust the degree of carefulness in each individual situation.¹⁹⁰ For example, Chapter 29, Section 1 of the Swedish Companies Act is applicable to both directors and CEOs but the standard of care does not have to be the same. Therefore, the negligence assessment should reflect the different assignments and duties that the directors and CEOs have.¹⁹¹

The Swedish Companies Act, the applicable Annual Accounts Act, the articles of association, and the instructions from the shareholders' meeting are assessed in order to determine if a director or CEO has been negligent or not.¹⁹² It is possible for the courts to make an independent negligence assessment if there has not been a violation of the Swedish Companies Act, the applicable Annual Accounts Act, articles of association, or instructions from the shareholders' meeting. The independent negligence assessment is based on an assessment of the risk of damage, the size of the likely damage, and the possibilities to avoid the damage. The greater risk of damage, the greater carefulness is expected in order to avoid damage.¹⁹³

The duty of care and the duty of loyalty are placed under the general culpability rule in Chapter 29, Section 1 of the Swedish Companies Act. The incorporators, directors, and CEOs need to follow the same degree of prudence as would be required from an agent in general.¹⁹⁴

¹⁸⁹ Hellner and Radetzki (2018) p. 33.

¹⁹⁰ Hellner and Radetzki (2018) p. 33.

¹⁹¹ Dotevall (2015) p. 357.

¹⁹² Svernlöv (2012) p. 61; Stattin (2008) p. 359.

¹⁹³ Svernlöv (2012) p. 67 f.

¹⁹⁴ Prop. 1975:103 p. 504; Svernlöv (2012) p. 59.

5.2.5 Adequate Causal Connection

There needs to be causality between the negligent act or omission and the negative effect, i.e. the damage.¹⁹⁵ The causality is analyzed through the necessary and sufficient conditions. If an act or omission is a necessary condition for the resulting damage, the damage would simply not have occurred if the act or omission did not take place. If an act or omission is a sufficient condition for the resulting damage, the act or omission simply leads to the damage.¹⁹⁶

It does not matter if the act or omission was the most important reason why the damage occurred. It only needs to be a contributing reason.¹⁹⁷ A director or CEO will not be held liable if the damage would have occurred even if the negligent act or omission never took place.¹⁹⁸

The causal connection between the negligent act or omission and the damage also needs to be adequate in order for liability to arise.¹⁹⁹ This means that too remote consequences and too unexpected effects are sorted out.²⁰⁰ It needs to be possible to expect the resulting damage to occur.²⁰¹

5.3 The Method Liability

5.3.1 The Method Liability Theory

According to the method liability theory, it is not the result itself that is important for the liability question. Instead, what matters and what might lead to liability is how the assessment, i.e. the used method, that led to the result was performed. It is important that the assessment was carried out in a

¹⁹⁵ Nerep, Adestam, Samuelsson, [the Swedish Companies Act (ABL), the comment of Chapter 29, Section 1 at 3.1.2], Lexino on January 25, 2019.

¹⁹⁶ Hellner and Radetzki (2018) p. 188 ff.

¹⁹⁷ Hellner and Radetzki (2018) p. 190.

¹⁹⁸ Dotevall, "Liability of Members of the Board of Directors and the Managing Directors – A Scandinavian Perspective", *The International Lawyer*, Vol. 37, No. 1, (2003), p. 74.

¹⁹⁹ Hellner and Radetzki (2018) p. 195 ff.

²⁰⁰ Dotevall, "Liability of Members of the Board of Directors and the Managing Directors – A Scandinavian Perspective", *The International Lawyer*, Vol. 37, No. 1, (2003), p. 74; Hellner and Radetzki (2018) p. 195 ff.

²⁰¹ Hellner and Radetzki (2018) p. 195 ff.

professional way or in a way that was in line with good practice. The method liability is applicable regarding various professions.²⁰²

5.3.2 Statements Made by Lindskog

Lindskog states that it may be difficult to make a retrospective assessment of whether an act was negligent or not. This is especially the case when an act is based on a person's own judgment. The conclusions that a judge draws when reviewing another person's acts are usually criticized since they are based on backward reasoning and because they lack connection with the reality. If the judge is aware of the fact that damage has occurred, that knowledge may have an impact on the negligence assessment.²⁰³

Lindskog states that the Supreme Court of Sweden in its application of Swedish law has started to approach the American business judgment rule through the method liability. In some court cases, which will be presented in Chapter 5.3.3 below, the Supreme Court of Sweden implies that it is the method behind the act and not the result that is important for the negligence assessment. In other words, the considerations behind the decision and not the decision itself shall be reviewed. Lindskog means that the American business judgment rule's counterpart in Swedish law is the method liability. This method liability is used when the courts review whether an act was cautious or not. Lindskog emphasizes that the courts need to focus on the situation when the act was taken and not on the subsequent chain of events.²⁰⁴

Further on, Lindskog means that the people who make decisions need to do it in writing if they have enough time to do it. The reason is that it is possible to review a decision if it is made in writing. In some court cases, the Supreme Court of Sweden has presumed that decision makers have been negligent when they have not been able to present anything in writing. In

²⁰² SOU 2002:41 p. 33.

²⁰³ Lindskog (2018) p. 337 f.

²⁰⁴ Andersson, "Business judgement rule och principen om efterkontrollbarhet", *Advokaten*, No. 9, (2017).

addition, if a decision is made in writing, it works as a quality assurance.²⁰⁵ The directors can review themselves in order to make sure that they have the necessary skills to perform their assignment. This can be seen as the first step in the assessment of the method liability.²⁰⁶

Lindskog states that the following sentence in a court case from the Supreme Court of Sweden, which will be presented in detail in Chapter 5.3.3.2 below, can be seen as an expression of the American business judgment rule's existence in Swedish law:²⁰⁷ "There are no reasons to challenge the directors' standpoint as long as the directors have kept themselves updated about the requirements in a reasonable way and as long as they make a serious evaluation of the current situation."²⁰⁸ According to Lindskog, a serious evaluation ought to mean that the directors need to document their standpoints in a way that enables scrutiny.²⁰⁹

Lindskog states that it is usually not possible to challenge the assessments behind decisions. It simply needs to be accepted that assessments may give rise to different decisions. This means that a decision needs to be accepted even if it turns out to be irrational. Anyhow, a decision needs to be based on necessary and adequate assessments due to the existing method liability. Therefore, the decision makers will be held liable if a decision is not based on an adequate assessment.²¹⁰

5.3.3 Swedish Case Law

5.3.3.1 Introduction

Below follows a presentation of some court cases that, according to Lindskog, demonstrate that the Supreme Court of Sweden has started to approach the American business judgment rule through the so-called

²⁰⁵ Andersson, "Business judgement rule och principen om efterkontrollbarhet", *Advokaten*, No. 9, (2017).

²⁰⁶ Lindskog (2018) p. 337 f.

²⁰⁷ Lindskog (2015) at 9.2.4.

²⁰⁸ NJA 2012 s. 858 at note 22.

²⁰⁹ Lindskog (2015) at 9.2.4.

²¹⁰ Lindskog, "Aktieägaravtal – kommentarer med anledning av en avhandling", in *SvJT* 2011 p. 273 and note 30.

method liability.²¹¹ Lindskog states that the court cases have not added any new substantial law. Instead, the tools to conduct an assessment have been developed.²¹²

5.3.3.2 NJA 2012 s. 858

In this court case, a director did not present the necessary financial reports and the question was if the director had been negligent.²¹³ The Supreme Court of Sweden meant that the negligence assessment should focus on whether the director acts in a way that on the whole is defensible with regard to the company's current situation. The Supreme Court of Sweden meant that they should review the director's business decision in a more generous way if a company is struggling with economic difficulties. Companies with economic difficulties usually need the kind of business decisions that may not be easy to make. There are usually no grounds to question the business decisions and acts by the directors as long as they have made a serious assessment and kept themselves updated about the current situation.²¹⁴

5.3.3.3 NJA 2013 s. 145

In this court case, an underage pyromaniac burned down a shopping mall when she was momentarily placed at her mother's home. This took place while the municipality cared for her under the Care of Young Persons Act.²¹⁵ The Supreme Court of Sweden meant that it could be motivated to focus on how the decision was made instead of focus on the content of the decision. If a decision is based on what the Supreme Court of Sweden refers to as a "good methodological order", the decision should be considered acceptable.²¹⁶ What is meant by a "good methodological order" depends on the situation when the decision was made. It is necessary to consider who makes the decision, what the decision concerns and how fast the decision needs to be decided. Also, the evaluation of the present situation on which

²¹¹ Andersson, "Business judgement rule och principen om efterkontrollbarhet", *Advokaten*, No. 9, (2017).

²¹² Lindskog (2018) p. 339.

²¹³ NJA 2012 s. 858 at note 1.

²¹⁴ NJA 2012 s. 858 at note 22.

²¹⁵ NJA 2013 s. 145 at note 1–8.

²¹⁶ NJA 2013 s. 145 at note 56.

the decision is based should in most cases be made in writing. This does not only allow for a review but does also compel a more thorough consideration by the decision makers before they make the decision.²¹⁷

5.3.3.4 NJA 2013 s. 842

In this court case, the Swedish Environmental Court wrongly imposed an environmental sanction fee on a company.²¹⁸ The Supreme Court of Sweden stated that a court needs to demonstrate its considerations in an open and explanatory manner in their reasoning. This mainly concerns such considerations that directly affect the outcome of the court case. A court should primarily strive to present such information that is necessary in order to understand the court's reasoning.²¹⁹ If the court presents an adequate analysis of the legal situation, this is not an incorrect application of the law, although the analysis leads to a conclusion that deviates from the law. Not even if the conclusion deviates significantly from the law.²²⁰ However, if the court's conclusions are incompatible with the law and if the court does not present a sufficient analysis with regard to the circumstances, this may be enough to trigger liability.²²¹

5.3.3.5 NJA 2014 s. 798

In this court case, a trustee in bankruptcy waited five years to sell shares and a promissory note. The purpose was to get a higher purchase price but this did not happen. The court case dealt with the examination of the trustee in bankruptcy's fees.²²² The Supreme Court of Sweden stated that a trustee's acts should normally be accepted if the trustee has made careful considerations on an adequate decision basis that can enable an investigation. As long as careful considerations are made, it does not matter if it later turns out that the acts were unfavorable. However, the trustee's

²¹⁷ NJA 2013 s. 145 at note 57.

²¹⁸ NJA 2013 s. 842 at note 1–11.

²¹⁹ NJA 2013 s. 842 at note 35.

²²⁰ NJA 2013 s. 842 at note 37.

²²¹ NJA 2013 s. 842 at note 38.

²²² NJA 2014 s. 798 at note 1–3.

acts can generally not be considered taken with the necessary care if the trustee cannot present an adequate decision basis.²²³

5.3.3.6 NJA 2015 s. 1040

In this court case, a contractor relied on the fact that others were using a specific construction and that the construction was generally prevalent in the industry. Later, a substantial fault in the construction appeared.²²⁴ The Supreme Court of Sweden observed that it is not sufficient to rely on what others do. Therefore, it was unimportant for the negligence assessment that the used construction was prevalent in the industry. The contractor should have ascertained the durability of the construction with suitable acts before using this method.²²⁵ The company was deemed negligent since the contractor was not able to show that the company had carried out any actual investigations before the act was taken.²²⁶

5.4 Statements About the American BJR and Swedish Law

Dotevall states that Chapter 3, Section 3 of the Swedish Companies Act is formulated in a vague way. Therefore, the directors and CEO get a broad discretion to fulfill the business purpose and make business decisions within the ordinary course of business in a way that is comparable with the American business judgment rule.²²⁷ Dotevall means that there is a rule in Swedish law that corresponds with the American business judgment rule. However, the business decision needs to be in line with the other sections in the Swedish Companies Act and the business object in the articles of association.²²⁸

Johansson claims that there is something similar to the American business judgment rule in Swedish law since the Swedish courts do not review

²²³ NJA 2014 s. 798 at note 9.

²²⁴ NJA 2015 s. 1040 at note 1–9.

²²⁵ NJA 2015 s. 1040 at note 25.

²²⁶ NJA 2015 s. 1040 at note 26.

²²⁷ Dotevall (2015) p. 194 and 374 ff; Dotevall (2017) p. 82.

²²⁸ Dotevall (2015) p. 374 ff.

whether a business decision is unwise or not. Usually, risky or speculative business decisions will not make the directors liable, at least as long as the business decisions are within the ordinary course of business. According to Johansson, it is obvious that the directors can use their broad discretion when they conduct the company's business.²²⁹ Johansson bases the statements on a court case from the Supreme Court of Sweden²³⁰, in which it was explicitly stated that the review of a decision does not involve whether the decision is suitable. The court case involved a non-profit association.²³¹

Svernlöv states that an explicit business judgment rule that is equivalent to the American business judgment rule does not exist in Swedish law. Nevertheless, Svernlöv states that a similar principle to the American business judgment rule can be said to exist in Swedish law since the Swedish courts will not review a business decision in order to determine if the business decision was unwise or not. This means that directors and CEOs normally do not face liability claims even if the company has suffered a loss because of their risky and speculative business decisions. However, the business decisions need to be within the ordinary course of business and need to be based on sufficient preparations. It is not easy to separate negligent acts from unwise business decisions but it is obvious that the directors and CEO have a significant amount of discretion to manage the company's business.²³²

Östberg states that there is not a business judgment rule in Swedish law. On the other hand, Östberg claims that there is a similar principle to the American business judgment rule in Swedish law since the directors have a broad discretion to manage the company's business. This means that risky or unwise business decisions will only lead to liability under obvious and

²²⁹ Johansson (1990) p. 307; Johansson, "Interimistiska åtgärder vid aktiebolagsrättsliga processer – Något om tillämpningen av 15 kap. RB vid processer grundade på aktiebolagslagen", in *SvJT* 1991 p. 604.

²³⁰ NJA 1987 s. 394.

²³¹ NJA 1987 s. 394 at p. 403.

²³² Svernlöv (2012) p. 58.

special circumstances. Nevertheless, the directors might need to be more diligent and careful in the decision-making process before they make a risky business decision.²³³

Samuelsson²³⁴ states that the directors, through the principle that a business decision only violates the business object and the company's interests if the business decision obviously deviates from the business object in the articles of association, get the necessary discretion they need in order to make business decisions. In order to review a violation of this principle, it may be possible to use an analysis influenced by the American business judgment rule.²³⁵

Stattin is in an article backing up the arguments made by Ohlson that the American business judgment rule has not had an impact on Swedish law but that it is possible to argue in a similar way in Swedish law.²³⁶ Ohlson states that the directors and CEO have a broad discretion to decide how the business purpose is achieved in the best way.²³⁷

In a court case from the Stockholm District Court²³⁸, the respondents argued, similar to how the American business judgment rule works, that the court cannot review the business decisions made by the directors unless certain conditions are not fulfilled. The respondents based their arguments on the components of the American business judgment rule presumption. The court observed that there are no restrictions regarding what kind of business decisions the courts can review according to Swedish law.

²³³ Östberg (2016) p. 449.

²³⁴ Together with Adestam and Nerep.

²³⁵ Nerep, Adestam, Samuelsson, [the Swedish Companies Act (ABL), the comment of Chapter 29, Section 1 at 3.11.4], Lexino on January 25, 2019.

²³⁶ Stattin, [Book Review] "Göran Ohlson, Vikten av vinst – en studie om syftets betydelse i bolagsstyrning, akademisk avhandling, Iustus förlag, 2012" in *SvJT* 2012 p. 639. See also Stattin (2008) p. 370 ff.

²³⁷ Ohlson (2012) p. 116.

²³⁸ T 18024-04.

Therefore, the court was able to make an assessment of the directors' business decisions and determine whether they had been negligent or not.²³⁹

5.5 Summary

It is the used method that led to the result instead of the result itself that is important according to the method liability theory. Lindskog states that the Supreme Court of Sweden in its application of Swedish law has started to approach the American business judgment rule through the method liability. The reason is that the Supreme Court of Sweden implies that the acts behind a decision are important for the negligence assessment and not the decision itself. Lindskog states that the decision makers need to document their standpoints in a way that enables scrutiny. The reason is that the Supreme Court of Sweden has presumed that people have been negligent when they have not made their decisions in writing. Many Swedish legal scholars state that something similar to the American business judgment rule exists in Swedish law. Some Swedish legal scholars argue that the directors and CEO have a broad discretion to manage the company's business in a way that is similar to the American business judgment rule. Other Swedish legal scholars argue that Swedish courts do not review a business decision in order to determine if it was unwise or not and that directors and CEOs are normally not held liable for risky business decisions. Therefore, there is something similar to the American business judgment rule in Swedish law. However, a Swedish court states that there are no restrictions regarding what kind of business decisions the Swedish courts can review.

²³⁹ T 18024-04 p. 20.

6 Comparative Analysis

6.1 Introduction

This chapter will present a comparative analysis. The focus will be on the following research questions that were presented in Chapter 1.2:

- Is there a similarity between how American courts review business decisions according to the American business judgment rule and how Swedish courts review business decisions according to the rules about liabilities of directors and CEOs in Swedish law?
- If there is not a similarity, how do American courts review business decisions according to the American business judgment rule and how do Swedish courts review business decisions according to the rules about liabilities of directors and CEOs in Swedish law, and what are the differences?

6.2 The Review of Business Decisions in American and Swedish Law

Lindskog states that the Supreme Court of Sweden through its use of the method liability in some court cases has started to approach the American business judgment rule.²⁴⁰ The question is if the way the Swedish courts review business decisions according to the method liability can be considered similar to how the American courts review business decisions according to the American business judgment rule.

The Supreme Court of Sweden implies through some court cases that the considerations behind the business decision are important for the negligence assessment and not the business decision itself. This is similar to the effect that the American business judgment rule has. Instead of reviewing a business decision, the American courts presume that in making a business decision, the directors of a company acted on an informed basis, in good

²⁴⁰ See Chapter 5.3.2.

faith, and in the honest belief that the action was taken in the best interests of the company. The presumption's effect is simply that American courts do not review the business decision itself.

It is possible to discern tendencies of something similar to the American business judgment rule in the court cases that Lindskog refers to. However, it is important to note that they are only tendencies and that they are vague. The court cases do not explicitly state that the Swedish courts always shall review the considerations behind the business decision instead of the business decision itself. For example, the Supreme Court of Sweden states that there are usually no grounds to question the business decisions and acts by directors and CEOs as long as they have made a serious assessment and kept themselves updated about the current situation.²⁴¹ The question is when business decisions can be questioned even if directors and CEOs have made a serious assessment and kept themselves updated about the current situation. This is not clear and it is an uncertainty for Swedish directors and CEOs. In addition, the Supreme Court of Sweden states that it could be motivated to focus on how the business decision was made instead of focusing on the content of the business decision.²⁴² The Supreme Court of Sweden does not further develop when it is not motivated to focus on how the business decision was made. It is not completely clear that the Swedish courts always will review the considerations behind the business decision instead of the business decision itself. In comparison to the U.S., there are clear prerequisites that state when an American court can review a business decision.

The method liability does not include a presumption that prevents the Swedish courts from reviewing a business decision. The presumption is a fundamental part of the American business judgment rule. The presumption is rarely rebutted and the American directors and officers can make risky business decisions without the fear of becoming liable.

²⁴¹ See Chapter 5.3.3.2.

²⁴² See Chapter 5.3.3.3.

Some of the court cases that Lindskog refers to express that the decision makers need to present an adequate decision basis.²⁴³ In American law, the directors do not have to demonstrate anything as long as the plaintiff does not rebut the presumption. The review by the Swedish courts seems to be based on what the directors and CEO can demonstrate while the review by the American courts is initially only based on what the plaintiff demonstrates.

Lindskog's statements about the documentation requirement are not in line with the American business judgment rule. The documentation requirement appears to be a substantial part of the method liability. The American business judgment rule does not contain a documentation requirement. American law has apparently not influenced the course that Lindskog obviously has embarked upon. Instead, it seems that Swedish law deviates from the legislative development in the U.S. This in fact reduces the veracity of the legal scholars' statements that there is something similar to the American business judgment rule in Swedish law. It would have been more rational to follow the legislative development in the U.S. and, for example, use a presumption with similar prerequisites as the American business judgment rule.

The Supreme Court of Sweden has presumed that decision makers have been negligent when they have not been able to present anything in writing.²⁴⁴ This clearly shows that there is a difference between how the American courts review business decisions according to the American business judgment rule and how Swedish courts review business decisions according to the rules about liabilities of directors and CEOs in Swedish law.

²⁴³ See Chapter 5.3.3.4, Chapter 5.3.3.5, and Chapter 5.3.3.6.

²⁴⁴ See Chapter 5.3.2.

It should be noted that some of the Swedish court cases that Lindskog refers to are not pure corporate law cases. The method liability is found in different legal environments. All the American cases that are presented in this thesis are pure corporate law cases.

The method liability and the American business judgment rule cannot be considered similar. There are underlying similarities between the effect that the American business judgment rule has and how reviews are made according to the method liability. However, business decisions are not reviewed similarly according to the method liability and the American business judgment rule. It may be possible that Swedish and American courts draw similar conclusions regarding the liability question. Nevertheless, one cannot be sure that a Swedish court and an American court will come to the same conclusion as long as the courts have different approaches.

Currently, it does not seem justified to make a comparison between the method liability and the American business judgment rule. The way that the Swedish courts review business decisions according to the method liability and the way that the American courts review business decisions according to the American business judgment rule cannot be considered similar. Lindskog's statements about how the Swedish courts review business decisions must be seen as primitive in relation to how American courts review business decisions according to the American business judgment rule. There are similarities but the differences are too obvious. The statements made by Lindskog simply seem to be visions of how Lindskog would like Swedish law to be applied. The case law that Lindskog refers to is insufficient for the statements that Lindskog makes. Even if the statements seem to lack substantial evidence, Lindskog can be said to have created a vision of a future application of Swedish law.

Some other legal scholars state that something similar to the American business judgment rule exists in Swedish law. From a legal perspective,

these statements do not seem to be clear enough in order to achieve a greater legal certainty for the directors and CEO since it is unclear what is similar.

Dotevall states that the business purpose in Chapter 3, Section 3 of the Swedish Companies Act is formulated in a vague way. This gives the directors and CEO a broad discretion to fulfill the business purpose and make business decisions within the ordinary course of business in a way that is comparable with the American business judgment rule.²⁴⁵ It is hard to think that the broad discretion by itself would establish a business judgment rule in Swedish law. The American business judgment rule has evolved through case law and is associated with clear prerequisites. It is unclear what the applicable prerequisites are in Swedish law. However, the broad discretion does allow for a business judgment rule to be created in Swedish law, which can be done by either the legislator or the courts.

Johansson states that Swedish courts do not review whether a business decision is unwise. Usually, risky or speculative business decisions will not make the directors liable, at least as long as the business decisions are within the ordinary course of business. Similarly, Svernlöv states that the Swedish courts do not review a business decision in order to determine if the business decision is unwise. This means that directors and CEOs normally do not face liability claims even if the company has suffered a loss because of their risky business decisions.²⁴⁶ It should be noted that the statements by Johansson and Svernlöv are based on a court case that deals with a non-profit association. Also, it is not persuasive to state that risky or speculative business decisions usually or normally do not make the directors and CEO liable. Clear prerequisites should state under what circumstances the courts can review business decisions. It should be clear for the directors and CEO when they can be held liable for their business decisions. There are clear prerequisites in the U.S. that state when the American courts can

²⁴⁵ See Chapter 5.4.

²⁴⁶ See Chapter 5.4.

review business decisions and it is clear for the American directors when they can be held liable for their business decisions.

The statements that Swedish courts do not review whether a business decision is unwise should be seen in contrast to the court case from the Stockholm District Court. The Stockholm District Court stated that there are no restrictions regarding what kind of business decisions the Swedish courts can review and the court also made an assessment of the directors' business decisions.²⁴⁷ The court case demonstrates that Swedish courts can review whatever business decision they want and that they are unhindered to make an assessment of the business decision. In the court case, which is a pure corporate law case, the respondents base their arguments on how American courts review business decisions according to the American business judgment rule. The court case makes it clear that there is not a presumption in Swedish law that prohibits the Swedish courts from reviewing business decisions. The court rejects the existence of something similar to the American business judgment rule in Swedish law. Therefore, Swedish courts are able to review business decisions in a way that is not possible in the U.S. In American law, the courts are not allowed to review a business decision as long as the American business judgment rule presumption is not rebutted. No such presumption that needs to be rebutted by the plaintiff can be seen in Swedish law. Instead, the business decisions can be reviewed when the Swedish courts assess whether a director or CEO should be held liable. Consequently, there is a risk that a Swedish court's assessment of a business decision leads to liability for the Swedish directors and CEO.

The court case can be seen as an illustration of how Swedish courts can review and make an assessment of business decisions according to the rules about liabilities of directors and CEOs in Swedish law. There is obviously an uncertainty since the Stockholm District Court states something that is different from what some legal scholars state. Until something else is

²⁴⁷ See Chapter 5.4.

indicated by another court, the Swedish courts do not seem to be restricted and can review whatever business decision they want and make an assessment of the business decision.

Perhaps Swedish courts have started to approach the American business judgment rule but it seems to be too early to state that there is something similar to the American business judgment rule in Swedish law. The Swedish law appears to be too thin. Clearer prerequisites need to evolve in Swedish law in order to justify a righteous comparison. There seems to be tendencies in Swedish law that indicates that there is something similar but not anything more than that. It is possible to agree on the fact that there are tendencies in Swedish law, but one would simply go too far by stating that there is something similar to the American business judgment rule in Swedish law. It also seems unclear what actually exists in Swedish law. Consequently, it seems to be misleading and an overstatement to state that something similar to the American business judgment rule exists in Swedish law.

Simply accepting conceptualizations can lead to fallacies. Words and labels are important in law and deficiencies can have impacts on society. It is likely that Swedish lawyers, because of the statements made by the Swedish legal scholars, believe that there is something similar to the American business judgment rule in Swedish law while that is probably not the case. At least it is not certain if there is something similar. Swedish lawyers might have advised their American clients in a somewhat misleading way because of the statements made by the legal scholars. There are similarities in Swedish and American law regarding directors' duties and liabilities. However, the comparison clearly shows that the way the American courts review business decisions according to the American business judgment rule differs from the way Swedish courts review business decisions according to the rules about liabilities of directors and CEOs in Swedish law. There are obviously differences regarding the conceptualization in American and Swedish law. Based on the Swedish legal scholars' statements, the concept

of the “business judgment rule” does not seem to have the same meaning in American and Swedish law. The Swedish legal scholars seem to refer to something that cannot be considered concrete.

Similar rules facilitate for companies when they want to expand globally. Certainty is crucial and companies need to foresee what they can expect from the jurisdictions in which they want to expand their businesses. Sweden could attract American companies by stating that there is a proper and clear business judgment rule in Swedish law that is applied in the same way as the American counterpart. Currently, American companies might refrain from expanding their businesses to Sweden if they are aware of the fact that it is not clear under what circumstances directors and CEOs can be held liable for risky business decisions.

The problem with risky business decisions is that they can prove to be either good or poor. However, risky business decisions are essential for a company’s success. Therefore, risk-taking needs to be accepted to a large extent. The question is under what circumstances a business decision can be challenged according to Swedish law. For directors and CEOs, it is crucial that these circumstances are clear.

There are obviously uncertainties in Swedish law. The uncertainties need to be addressed. Therefore, the Supreme Court of Sweden should make clear what directors and CEOs can expect from their assignments. Some companies might find it difficult to recruit and retain the most qualified directors and CEOs because of the uncertainties that exist. These uncertainties can have a negative impact on the overall economy.

The American business judgment rule offers a powerful protection for the American directors against liability suits. The same cannot be said about the rules about liabilities of directors and CEOs in Swedish law since it is not obvious how the Swedish courts apply them in order to review business decisions. The comparison is based on the hypothesis that something similar

to the American business judgment rule exists in Swedish law. However, the hypothesis does not seem to correspond with how business decisions are reviewed in Swedish law. Therefore, it is not really certain what the American business judgment rule should be compared with in Swedish law. This of course complicates the comparison. The tendencies have been gathered and analyzed in the best way possible in this thesis. The material that covers whether there is something similar to the American business judgment rule in Swedish law is in all ways insufficient. This is the reason why it is not possible to present a completely clear analysis. The American business judgment rule can basically only be compared with the statements made by the Swedish legal scholars. What some legal scholars mean by “similar” is not clear. The problem with the legal scholars’ analyses is that they lead to the conclusion that there is something similar to the American business judgment rule in Swedish law. The statements by the legal scholars are not developed enough for such a conclusion. The legal scholars’ statements that there is something similar to the American business judgment rule in Swedish law seem to be misleading. The details are important and need to be considered before someone states that there is a similarity.

6.3 Summarizing Conclusions

In American law, the business judgment rule prohibits American courts to review business decisions as long as the presumption is not rebutted. The business judgment rule presumption consists of four components, namely a business decision, disinterestedness and independence, duty of care, and good faith. The business judgment rule presumption will only be rebutted in those rare cases when the plaintiff can demonstrate that any of the four components was not fulfilled. As long as the American business judgment rule presumption is not rebutted, the American courts are not allowed to review a business decision. Instead of reviewing a business decision, the American courts simply presume that in making a business decision, the directors of a company acted on an informed basis, in good faith, and in the honest belief that the action was taken in the best interests of the company.

There are conflicting statements about how the Swedish courts review business decisions according to the rules about liabilities of directors and CEOs in Swedish law. Lindskog states that the Supreme Court of Sweden has started to review business decisions according to the method liability. The method liability means that the considerations behind the business decision shall be reviewed and not the business decision itself. A documentation requirement appears to be a substantial part of the method liability. Some legal scholars state that the fact that the business purpose in Chapter 3, Section 3 of the Swedish Companies Act is formulated in a vague way gives the directors and CEO a broad discretion to fulfill the business purpose and make business decisions within the ordinary course of business. Other legal scholars state that Swedish courts do not review whether a business decision is unwise or not and that risky or speculative business decisions usually do not make the directors and CEO liable, at least as long as the business decisions are within the ordinary course of business. However, a Swedish court case demonstrates that there are no restrictions regarding what kind of business decisions the Swedish courts can review and that Swedish courts are unhindered to make an assessment of business decisions.

There are some apparent differences between how the American courts review business decisions according to the American business judgment rule and how the Swedish courts review business decisions according to the rules about liabilities of directors and CEOs in Swedish law. The major difference is that the American courts apply a presumption that prohibits them to review business decisions as long as the business judgment rule presumption is not rebutted. In Swedish law, there is no presumption that needs to be rebutted in order for the Swedish courts to review a business decision. There are no restrictions regarding what kind of business decisions the Swedish courts can review. There is also a documentation requirement in Swedish law that does not exist in American law. However, it must be noted that it is not completely clear how the Swedish courts review business

decisions and this complicates the comparison. There are tendencies that Swedish courts review the considerations behind the business decision and not the business decision itself but it is unclear what the applicable prerequisites are in Swedish law. In contrast, there are clear prerequisites in the U.S. that state when the American courts can review business decisions.

There does not seem to be a similarity between how American courts review business decisions according to the American business judgment rule and how Swedish courts review business decisions according to the rules about liabilities of directors and CEOs in Swedish law. How the Swedish courts review business decisions according to the rules about liabilities of directors and CEOs in Swedish law must under all circumstances be seen as primitive in relation to how American courts review business decisions according to the American business judgment rule. The American business judgment rule works as a powerful shield against liability claims for the American directors and officers. Swedish directors and CEOs do not seem to be able to make risky business decisions without the fear of becoming liable. Therefore, it is misleading to state that there is something similar to the American business judgment rule in Swedish law. Also, it is evident that one should be cautious to state that there is an identity because it can be misleading.

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