

GUIDANCE TO UK DIRECTORS

The guidance set out in this document is provided for the benefit of UK directors in order to address certain potential insolvency-related risks which may arise as a result of the challenging circumstances affecting many companies presently.

LOOKING TO THE FUTURE

To date, beyond furloughing measures, all of the Government's actions to preserve businesses have been to postpone liabilities (rather than cancel them). Therefore, as we navigate the effect of the pandemic, a key focus for boards and their advisors will be on reaching compromises where there is not enough money to satisfy all creditors.

COVID19 – TEMPORARY SUSPENSION OF WRONGFUL TRADING LIABILITY

The wrongful trading provisions set out in the Insolvency Act 1986 provide that a director of a company can be personally liable if found to have continued to trade (and did not minimise losses to creditors) at a time when there was no reasonable prospect of the company avoiding insolvent liquidation or administration.

The Government introduced a suspension of directors' personal liability for wrongful trading with retrospective effect from 1 March 2020 to 30 June 2020 (which can be extended). The aim of the suspension is to deter directors (concerned about potential wrongful trading liability) from commencing insolvency procedures and to encourage businesses to continue to trade (or simply exist) through the COVID-19 crisis.

However, despite the suspension of wrongful trading liability, other directors' duties and potential liabilities continue and, therefore, the risk of liability as a result of a breach of such duties or other provisions continues to exist.

DIRECTORS' DUTIES

The Companies Act 2006 sets out seven specific duties of directors:

1. To act within powers.
2. To promote the success of the company for the benefit of its members as a whole (this duty is displaced in favour of the company's creditors where there is a real risk of insolvency).
3. To exercise independent judgment.
4. To exercise reasonable care, skill and diligence.
5. To avoid conflicts of interest.
6. Not to accept benefits from third parties.
7. To declare interests in proposed transactions or arrangements with the company.

MISFEASANCE

Section 212 of the Insolvency Act 1986 enables the official receiver, a liquidator, a creditor or a shareholder to apply to court for the recovery of money or payment in respect of damages from officers of an insolvent company (or those concerned in its management) who have misapplied or retained or become liable or accountable for any money or property of the company, or have been guilty of misfeasance or breach of fiduciary or other duties in relation to the company.

ANTECEDENT TRANSACTIONS

These are certain transactions which occur within specified periods prior to a company's insolvency (principally, transactions at undervalue and preferences).

A transaction at an undervalue is a transaction pursuant to which the company receives no consideration, or consideration which is worth significantly less than the value of the consideration provided by the company. This provision only applies where, at the time of or as a result of the transaction, the company was unable to pay its debts. Note that this is presumed in the case of transactions with connected parties.

A company grants a preference if it does anything which has the effect of putting one of the company's creditors (or a surety or guarantor for any of the company's liabilities) into a position which, in the event of the company going into insolvent liquidation or administration, will be better than the position they would be in if that thing had not been done.

DIRECTORS' DISQUALIFICATION AND COMPENSATION

Following the liquidation or administration of a company, the appointed insolvency practitioner is required to file a report on the conduct of the directors of the company with the Secretary of State for Business, Energy and Industrial Strategy. If, based on the findings in the report, the Secretary of State considers that the director's conduct was unsatisfactory he or she may bring proceedings to prohibit them from acting as a director of another company. The Secretary of State has three years in which to apply for a disqualification. In addition, the Secretary of State may apply to court for a compensation order, or agree a compensation undertaking, in respect of a disqualified director whose actions have caused loss to the company's creditors.

PROACTIVE MANAGEMENT

- Maintain a proactive approach to debt collection and conserving cashflow.
- Consider requesting payment holidays from key stakeholders including lenders, landlords and suppliers to ease cashflow.
- Consider applying for Government relief: CBILS, CLBILS, CCFF, Future Fund, BBLs, JRS, business rates holiday, grant funding.
- Continually monitor the Company's financial position and future cash flows in order to review the position of each creditor and to consider how the resources available to the Company should be deployed (in the interests of the creditors as a whole), in particular in relation to making any critical payments.
- Continually liaise with the Company's secured creditor(s) and ensure that they/it are supportive of the Company.
- Continue to take professional advice aimed at reviewing whether insolvent liquidation or administration is inevitable.
- Regularly schedule and hold quorate board meetings to discuss the financial status of the Company and all relevant transactions. These meetings should be minuted.
- Consider availability and terms of any D&O insurance cover.

For further information concerning potential insolvency-related risks and issues, please contact:



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