

FINANCIAL DISTRESS – TIP SHEET FOR BOARDS OF DIRECTORS

We live in uncertain times, where many companies face challenges brought about by the sudden and wide-ranging economic impact of COVID-19. Whilst the UK government are implementing measures to alleviate some of the financial consequences including the provision of emergency finance, government backed guarantees, and the deferment of tax, it is inevitable that many boards face unprecedented situations and challenges ahead. Your company's financial distress may be a challenging time in which critical, yet prudent decisions must be made. This tip sheet may focus your mind on best practice in these difficult circumstances.

WHAT ARE YOUR DUTIES DURING FINANCIAL DISTRESS/INSOLVENCY?

Outside of a distressed situation, you owe a duty to promote the success of the company for the benefit of your members as a whole. However, where your company is financially distressed and facing potential insolvency, as a director you must prioritise the interests of creditors as a whole (not just the interests of any individual creditor or class of creditors). Failure to recognise the interests of creditors and take steps to minimise potential losses to creditors at this time can give rise to personal liability.

WHAT ARE SOME THINGS YOU CAN DO TO PROTECT THE BOARD?

Here are our "top ten" practical steps where your company's financial position is deteriorating:

1. **Meet regularly and stay informed:** appropriate board minutes are a particularly important way of demonstrating you have complied with your duties. Remote meetings and telephone calls are widely accepted means of making board decisions and provisions for such are included in most articles of association.
2. **Seek professional advice:** obtaining expert advice relating to waivers, standstills, new finance, employee obligations, customer and supplier arrangements, compliance (including continuing disclosure obligations), and a restructuring or insolvency proceedings can help reduce the scale of any losses, minimise the risk of your liability, and avoid management being distracted by the consequences of non-compliance. In regulated industries,

you may consider obtaining advice in respect of your company's duties to the PRA/FCA (or any other appropriate regulators) and your own duties as a senior manager. Individual directors may also consider that they need separate advice.

3. **Consider whether to continue trading:** if you decide to continue to trade and do not take steps to minimise losses to creditors where there is no reasonable prospect of avoiding an insolvent liquidation or administration this may lead to personal liability for wrongful trading. Of course, there are many situations when continuing to trade will be in the best interests of creditors, so is a decision you must keep under constant review.
4. **Consider restructuring options:** in situations where your company's distress is not temporary, exploring the available restructuring options (having obtained professional advice) is a good way of demonstrating compliance with your duties.
5. **Consider individual companies within the group:** you need to consider the individual companies within a group context and the duties you owe to the creditors of each company when making a decision. If an entity in your group has a defined benefit pension scheme, for example, you may need to consult with the relevant trustees as well as the Pensions Regulator.
6. **Consider key contracts:** while monitoring key contracts (including finance arrangements) will be the company's obligation, you should review relevant provisions (like financial covenants and termination events) in order to develop the best course of action.
7. **Consider transactions:** consider your company's ability to meet its current and future obligations before entering into any new transactions (including new finance) and ensure these obligations are regularly reviewed. This includes any proposed payment of dividends.
8. **Consider intra-group arrangements:** review your group's existing arrangements, as the risk of insolvency may restrict your ability to borrow or make available intra-group funding or enter into intra-group transactions.
9. **Ensure proper records are kept and timely reporting:** ensure your company's books and records are being properly kept up to date, regular financial and operational reporting, and timely escalation of issues.
10. **Think carefully before resigning:** resignation will not discharge your responsibility for any previous conduct. Remaining on the board to drive a successful resolution may be the most effective means of mitigating risk.

FURTHER INFORMATION

You may find the following resources helpful:

[Financial difficulties triggered by the impact of Coronavirus: Issues for stakeholders](#)

[Coronavirus: Infrastructure finance - Immediate financing considerations for infrastructure investors and funders](#)

[Coronavirus: Leveraged Finance - Immediate financing considerations for financial sponsors, underwriters and debt investors](#)

[Cross Border Financing Guide](#) (CC Financial Markets Toolkit)

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