

FINANCIAL DISTRESS TRIGGERED BY THE IMPACT OF THE CORONAVIRUS - TIP SHEET FOR SHAREHOLDER DIRECTORS IN THE UK

Many boards face unprecedented situations and challenges ahead. Directors representing shareholders (such as private equity investors), need to act with all directors to consider the economic challenges brought about by the sudden and wide-ranging economic impact of the novel coronavirus (COVID-19).

In addition, such representative directors must be acutely sensitive to managing conflicts and tensions relating to their appointing shareholder to ensure they fulfil their primary duty as a director, and take care not to expose their appointing shareholder and investment teams to liability.

PRACTICAL STEPS TO PROTECT THE BOARD

In distressed situations, all directors must consider the interests of the company's creditors as a whole. They must not favour any one shareholder over the creditors. This shift in focus requires special care and attention.

SHAREHOLDER DIRECTORS

The approach to the practical steps below will depend on the severity of the financial distress. Here are some practical considerations specific to shareholder directors where a company is in acute distress:

1. **Shareholder relationship:** establish an independent person within the shareholder organisation for making decisions as shareholder about its investment.
2. **Role clarification:** address the potential conflict as between the director and the appointing shareholder. Ensure that confidential information at the board level is not made available to shareholders except as required by law and contractually (e.g. by the shareholders' agreement), albeit such rights are customarily very broad.
3. **Deal team not to instruct the company:** if a company routinely complies with instructions from the deal team, there is a risk that the deal team can incur similar liabilities to directors.

ALL DIRECTORS

More generally, directors need to consider the following issues when dealing with distress:

1. **Keep proper records and stay informed:** detailed board minutes are invaluable to demonstrating that directors have complied with their duties. Remote meetings and telephone calls are widely accepted means of making board decisions.
2. **Seek professional advice:** obtaining expert advice (e.g. in respect of available restructuring options) greatly helps to reduce the scale of any losses, minimise the risk of directors' liability, and avoid management being distracted by the consequences of non-compliance. Where a company has listed debt, directors may also need to take advice to ensure that the company is complying with its obligations under market abuse legislation. Individual directors may need separate advice.
3. **Continuing to trade:** this is a decision which must be kept under constant review as it may be in creditors' best interests. Regular financial and operational reporting and timely escalation of issues are essential. Failure to take steps to minimise losses to creditors where there is no reasonable prospect of avoiding insolvency may lead to personal liability.
4. **Monitor key contracts:** including financing arrangements. Directors should regularly review financial covenants and termination events. Directors should also consider the ability of the company to meet its current and future obligations before entering into any new transactions.
5. **Intragroup arrangements:** directors need to consider companies within a group on an individual basis. Duties are owed to creditors of each individual company. The position may vary depending on the jurisdiction.
6. **Regulators:** directors should be mindful in certain regulated businesses of the need to involve regulators in decisions or to keep them informed and consulted.
7. **Be active:** resignation will not discharge a director's responsibility for any previous conduct. Remaining on the board to drive a successful resolution is often 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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