Issues for directors to consider in light of coronavirus COVID-19

Following the outbreak of the coronavirus COVID-19 pandemic, directors are taking steps to ensure that companies can continue to operate. While it is natural to focus on the immediate practical implications of operating in this challenging environment, directors should also ensure they keep in mind their broader duties and disclosure obligations.

Directors' duties

In many jurisdictions, directors of a company are subject to statutory or fiduciary duties which require them to consider carefully the long term impact of their actions on the company's stakeholders. These stakeholders often extend to employees, suppliers and customers as well as the shareholders of the company. Directors need to be aware of these stakeholder interests when deciding how best to direct the actions of their company and will need to balance carefully the short-term needs of the company against the long term impact of their decisions.

Given the uncertainties surrounding the pandemic, particularly in relation to its duration, it may be difficult for directors to ascertain how their immediate actions may impact on the long-term success of the company and/or its various stakeholders. However, directors can mitigate their risks by ensuring that they act in good faith and in a prudent and reasonable manner based on the information available at the time of making each decision, recording the fact that they have taken a broad range of interest and factors into account.

Financial condition and potential insolvency

Many companies are likely to experience a decline in their financial condition as a result of coronavirus COVID-19, perhaps as a result of cash flow issues, falling income or deterioration in asset values. This could result in companies being unable to meet their scheduled loan repayments or in the breach of financial covenants in loan agreements. It is imperative that directors closely monitor these matters and engage with lenders in a timely manner.

While directors ordinarily owe their duties to a wide range of stakeholders, in the event that the company experiences financial difficulties which could result in insolvency, the directors should begin giving greater weight to the interests of the creditors of the company. It is often challenging for directors to determine precisely when they must switch their focus to the interests of creditors, and the weight that must be given to such interests at a particular point in time. This task will be made more difficult given the rapidly evolving nature of the coronavirus COVID-19 crisis. Failure to protect creditors, and in some jurisdictions failure to file for insolvency proceedings at the appropriate time, could result in directors facing personal liability, so it is important that the directors seek professional advice as soon as there is any concern regarding the solvency of the company.

Financial reporting

Companies may face practical difficulties in relation to the preparation and audit of annual accounts. Travel and movement restrictions are likely to mean that staff and external auditors will have much reduced access to company sites and records. Regulators in some jurisdictions are extending deadlines for the filing of accounts. Directors should seek advice from their auditors as to the position in their jurisdiction and, to the extent necessary to benefit from an extended filing deadline, make any necessary applications in a timely manner.

Companies should also discuss with their auditors whether balance sheet adjustments or post balance sheet disclosures should be made in relation to the impact of coronavirus COVID-19. Given the uncertainties surrounding the longevity of coronavirus COVID-19, auditors may have concerns regarding the ability of companies to continue as going concerns and they may wish to make qualifications to the audit. Directors need to consider whether any qualifications to audit (or any material delay in finalising the audit) will trigger an event of default under loan agreements.

Company disclosures

In addition to routine financial disclosures, directors need to consider their responsibilities to disclose information in the annual report regarding the principal risks associated with, and the impact of, coronavirus COVID-19. Directors should endeavour to identify and articulate the precise risks that their company is facing and ensure risk reporting is not generic.

If the company is listed, it must continue to discharge its continuing obligations under its regulatory regime, including ensuring that regulatory announcements regarding the impact of coronavirus COVID-19 are made in a timely manner. Given the situation is changing rapidly the directors must keep this under regular review and ensure that the company is in a position to make disclosures to the market promptly as required.

Duty of care to employees

In most countries, companies have specific legal obligations relating to the care of their employees and should safeguard employees' health and safety and provide a safe place to work. Please refer to our publication 10 practical steps for global employers, right now for more details on steps that directors can take to satisfy these obligations.

Insurance

In conjunction with their brokers, directors should consider whether their existing corporate insurance policies cover the company's business interruption caused by coronavirus COVID-19 and how such pandemic-related exposure can be effectively mitigated going forwards. That consideration should include an appraisal of existing D&O policies purchased for the directors as individuals as well as any indemnities provided by the company for their benefit, in order to understand the extent to which their own position is protected

Operational matters

In this uncertain time, business decisions will be subject to increased scrutiny and directors need to ensure that all key operational matters are reassessed in light of coronavirus COVID-19. This includes retesting contingency plans and refining them as the situation progresses. Operational matters that should be included in this review include:

- *employee matters*: the impact of reduced staffing levels, redeployment of staff and working remotely; effective communication with, and between, employees; and fulfilling the duty of care to employees;

- *cash preservation*: managing operations, expenditure and finance facilities to ensure that sufficient cash is available to meet ongoing requirements;

- *stakeholder and other third party communications*: maintaining regular dialogue with employees, customers, suppliers and shareholders (please refer to Coronavirus COVID-19: implications for AGMs for further detail on shareholder engagement at AGMs); revising communication procedures to reflect altered ways of working; and, if listed, ensuring regular contact with brokers, analysts and advisers and ensuring regulatory disclosures are maintained even with alterations to the number or location of employees;

- *IT*: the impact of remote working on systems and assessing whether any enhancements are required to IT capabilities; and ensuring continued maintenance and updating of IT security;

- *continuing education requirements*: ensuring directors and other senior employees are briefed on the rapidly changing requirements in each of the jurisdictions in which the business operates; and hold regular board and senior management calls;

- *impact on corporate and commercial activity*: reviewing existing contracts to understand the potential impact of coronavirus COVID-19; assessing whether companies (and their trading partners) can meet existing contractual obligations; understanding the effects on the company's supply chain; and considering the impact on corporate transactions and whether altered terms are required as a result of coronavirus COVID-19;

- *accounting*: considering whether more regular management accounting and internal reporting is required; regularly updating forecasts to reflect changes to the company's risks and contingency planning; and monitoring compliance with banking facilities.;

Liabilities

In the event that companies are considered to have been inadequately prepared for coronavirus COVID-19, or failed to effectively implement their contingency plans, directors could be exposed to claims from employees or shareholders. Likewise, failure to disclose adequately the risks and impact of coronavirus COVID-19 could result in directors being subject to both civil and, in the case of listed companies, criminal sanctions.

Should you wish to discuss the issues raised in this alert, please contact your usual DLA Piper Corporate contact.

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Article originally appeared here.