



Focus on
COVID-19
Coronavirus

A&L Goodbody

Board Business: *Directors' duties, practical mitigation steps and assessment of financing arrangements*

The outbreak of COVID-19 continues to have a deep impact on businesses across all sectors. A growing number of companies are warning that they will fail to meet financial and commercial targets and global supply chains are being disrupted. The legal implications of this are far ranging, complex and evolving.

We take a look at directors' duties in the context of the current uncertain environment. In particular, we explore the position of directors of companies with solvency issues and the steps that should be taken by a board in order to best mitigate any solvency risks. We identify some practical steps directors can take to mitigate against potential risks.

Many companies are also considering how the pandemic will affect their existing and future financing arrangements. We identify some of the areas where financing and related agreements may be affected and look at some questions which should be considered at board level.

If there are any issues relating to the impact of COVID-19 which you would like to see dealt with in future editions, please do not hesitate to contact our [Corporate transactions team](#), [Finance team](#), and [Restructuring and Insolvency team](#).



You will find a full range of timely materials for businesses in our dedicated [COVID-19 HUB](#) on our website.

Directors' duties

It is important for directors to obtain all necessary information to assess and understand the business and legal risks posed by COVID-19 and to discuss and test management's strategies for mitigating these risks. In addition to looking at financing arrangements covered in Part 3 below, boards should also take steps to protect cashflow and ensure viability throughout this period.

Companies may be facing liquidity issues and/or default. In addition to engaging with funders, directors of affected companies also need to be aware of their legal duties, especially around decisions they may be considering making to get through current difficulties.

Directors have a range of fiduciary and other duties, chief among which is to act in the best interests of the company. Where a business is solvent and trading as normal, the company's directors owe their fiduciary duties to the company.

In circumstances where a breach of duty is proven, a director may be required to: (a) account to the company for any personal gain made from the breach; and (b) indemnify the company for any loss or damage resulting from the breach. The High Court of Ireland is empowered to relieve a director from personal liability if he or she has acted honestly and reasonably and where the court believes that, in the circumstances, the director ought to fairly be excused.

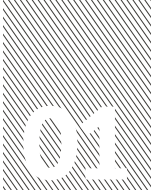
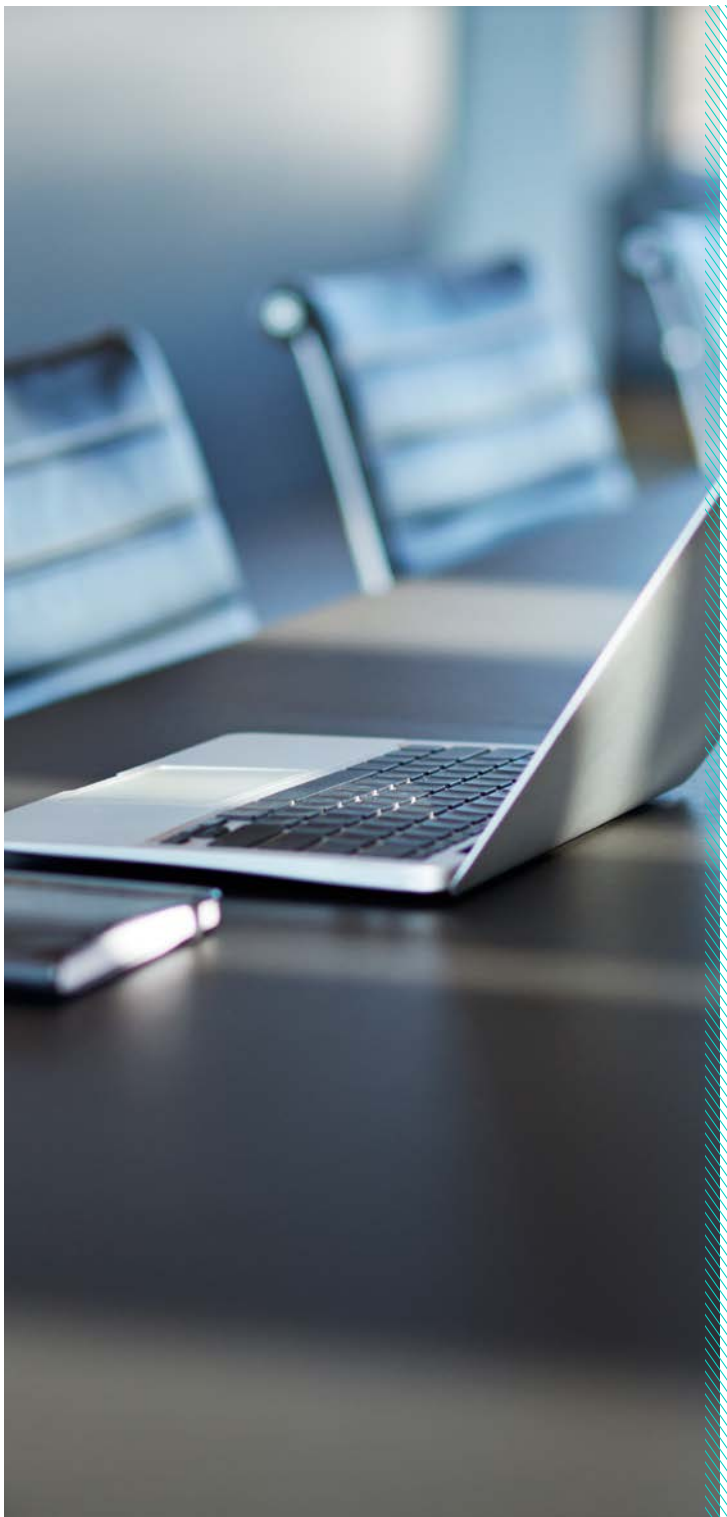
During times of uncertainty

In addition to their ongoing statutory duties in "normal" times, directors should also be aware of their duties and to whom they are owed during times of financial uncertainty for the business. This will assist directors in actively managing their risk of personal exposure, where the company is insolvent or close to becoming so, and enable them to put in place prudent measures to protect themselves from liability.

If a company runs into financial difficulty and is unable to pay its debts in full as they fall due, directors continue to owe their duties to the company but must also act to protect the interests of company creditors. Typically, this means considering the impact of material decisions on creditors. Creditors do not have a direct right of action against a director for breach of fiduciary duties. Accordingly, only the relevant company (or its liquidator) may take an action for breach of duty against a director.

The purpose of directors taking these steps and acting in the interest of creditors is to:

- a. mitigate any claim made that they have acted inappropriately and should be held liable for the debts of the company; and
- b. ward off any attempt by an insolvency practitioner subsequently appointed seeking to restrict them in acting as directors.



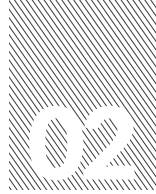
Directors duties

To ensure the directors are properly fulfilling their duties where they continue trading while in the zone of insolvency, the board should ensure that, at a minimum, the following occurs:

- Closely investigate the financial position and the future prospects for the company.
- Continuously monitor the company's financial position.
- Stress-test the financial information being relied on.
- Support the view that the company can continue to trade through its financial difficulties with documentary evidence and independent advice.
- Get an independent view on any proposed material transaction from an insolvency practitioner (e.g. disposals, acquisitions, group restructuring).
- Obtain legal advice on the implications of any proposed material action (e.g. disposals, acquisitions, group restructuring).
- Hold frequent board meetings.
- Prepare regular management accounts.
- Ensure that the company's books and records are current and accurate.
- Take material decisions only after considering the impact on creditors.
- Stress-test the rationale for making payments to creditors, especially ones within the same group, unless it can be justified as being in the ordinary course of business.
- Document key decisions and the reasons for them.

Where it is clear that a company cannot trade out of its difficulties, and it does not have a prospect of survival, the directors should take steps to put the company into liquidation. In such situation, it is important for the company and the directors to be aware of personal risks that can arise including **reckless and fraudulent trading, restriction and disqualification applications**.

At the time of publication, both the **UK and Australia** have announced changes to their insolvency laws including a temporary suspension on "**wrongful trading**" provisions to give company directors greater confidence to use their best endeavours to trade during the COVID-19 situation without the threat of personal liability should the company eventually fall into insolvency. Other existing laws in relation to fraudulent trading and director disqualification will continue in full force and effect. However, no similar changes have occurred in Ireland and it remains to be seen if the Irish legislature will look to follow suit.

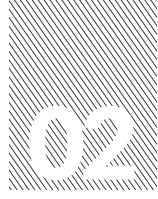
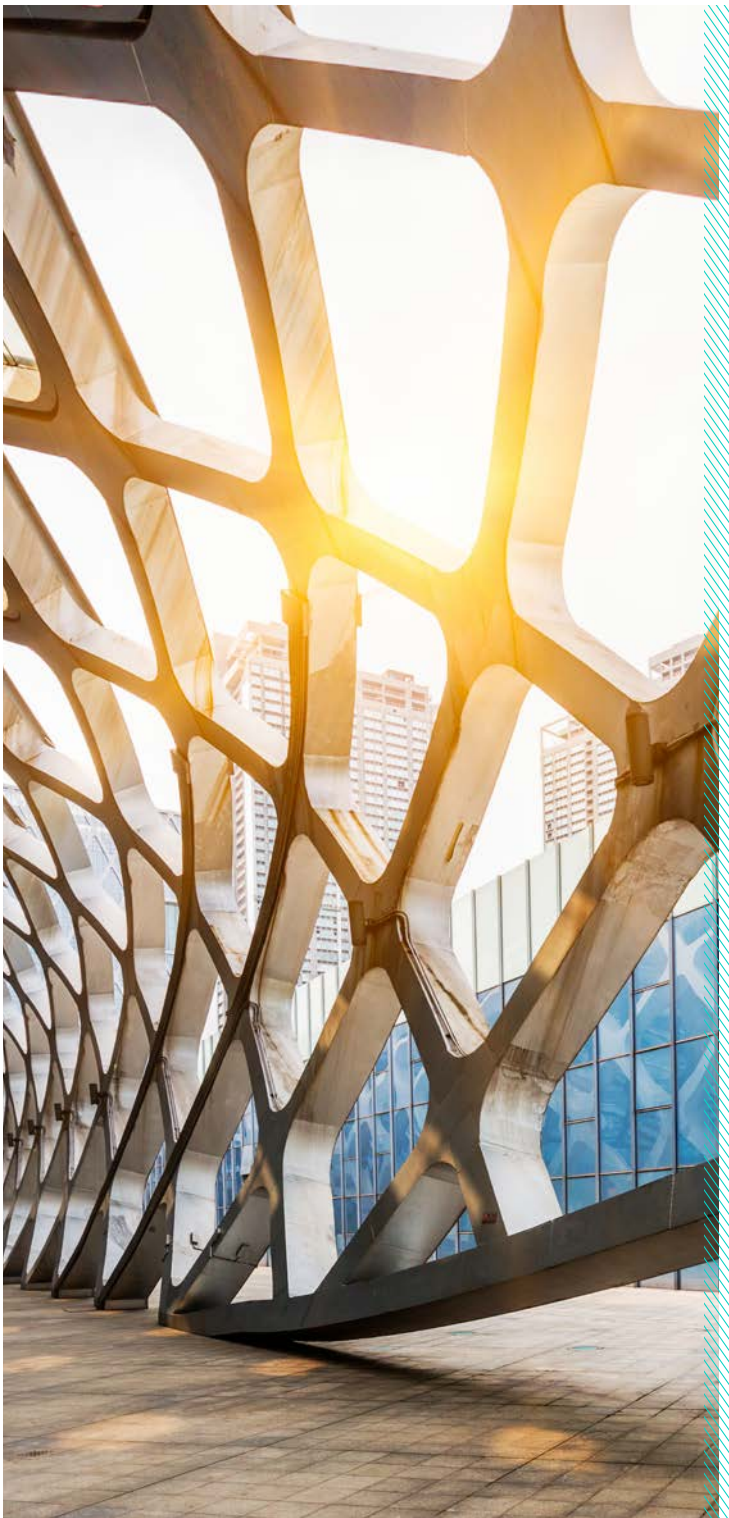


Practical steps for directors to mitigate against potential risk

Although COVID-19 is causing unprecedented challenges for many companies there are practical steps directors can take now to assess and manage risks the business may face from falling revenues, damaged liquidity, and turbulent market conditions.

Depending on the nature of the business, these may include the following.

- Review all material contracts, including insurance policies and key customer/supplier arrangements, to determine whether they are impacted by the current situation. Review how both the company's and the counterparties' rights might be affected.
- In particular, focus on financial covenants, events of default, termination provisions, frustrating events, force majeure, indemnities and guarantees. Force majeure clauses are particularly relevant during a crisis and detailed analysis may be required. [Here](#) you can find our briefing on force majeure.
- To retain stakeholder confidence, open up an honest and regular dialogue with your key investors, suppliers, lenders, material creditors, and debtors (where applicable).
 - » **Lenders:** Where fundamental to your ongoing trading, you may have to consider having a commercial discussion with lenders or other counterparties about revising credit or contractual terms, or seeking payment deferrals, repayment holidays, rent moratoria, etc.
 - » **Debtors:** Renew efforts to collect any payment arrears where applicable to your business.
 - » **Investors:** Consider whether the company needs new capital or investment to continue in business in the immediate term.
 - » **Suppliers:** consider finding alternative supplies or tightening credit terms including retention of title clauses until payment has been made.
- The Irish Government has introduced a number of supports to impacted businesses. Additional supports are also being provided from financial institutions and others. A further discussion of these supports are available [here](#). Consider the measures being introduced by the Irish Government or indeed from a wider EU perspective to see what impact such measures may have on your company.
- Consider what comfort can be taken from governmental support or lender engagement in decisions being made about the future of the business or the ability to continue to trade. Among such considerations could be to cease trading for a short period of time in order to preserve the value of the business, so as to avoid worsening the position of creditors until economic factors improve.
- Ensure the board is comfortable with the company's viability and continues to monitor the appropriateness of its current business plan. Consider whether CapEx and other discretionary expenditure are a priority, and whether there is a strategy to preserve value at this time.
- Where there is a real concern about liquidity or solvency, be proactive and involve your legal and financial advisors from an early stage, so they can take you through your options and possible solutions, and help you manage risk.
- One particular point to note at this time - be alive to health and safety risks posed by COVID-19. In light of the health and safety risks posed by COVID-19, businesses should review risk assessments to address the impact on



Practical steps for directors to mitigate against potential risk

work practices of the ongoing public health crisis. Aside from the obvious health risks to employees, a failure to do so may put the business at risk of potential prosecution by the Health and Safety Authority or the Director of Public Prosecutions if a company suffers an outbreak, with resulting fatalities. Those businesses who continue to operate as “essential services” must also ensure they have appropriate policies and procedures in place to comply with statutory requirements in this respect. If failings are attributable to directors, officers or managers, they too could face personal risk for health and safety matters in certain circumstances and in particular where they are involved in day to day operational control and that control (or lack of) led directly to an incident. [Here](#) you can find our COVID-19 health & safety briefings.



Financing arrangements

Debt funding is typically an important part of the capital structure for companies and following what has been an extremely challenging period for many company's liquidity is now key. Management teams and boards are actively considering their current and anticipated funding requirements, including assessing the terms of their existing finance arrangements.

In order to assist with the formulation and implementation of an appropriate strategy, we have considered the key aspects of some common financing arrangements entered into by Irish companies. This note is focussed primarily on bilateral or syndicated credit agreements but a number of the principles will apply also to those companies that have accessed the debt capital markets.

Planning and communication with your lenders

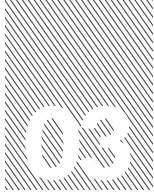
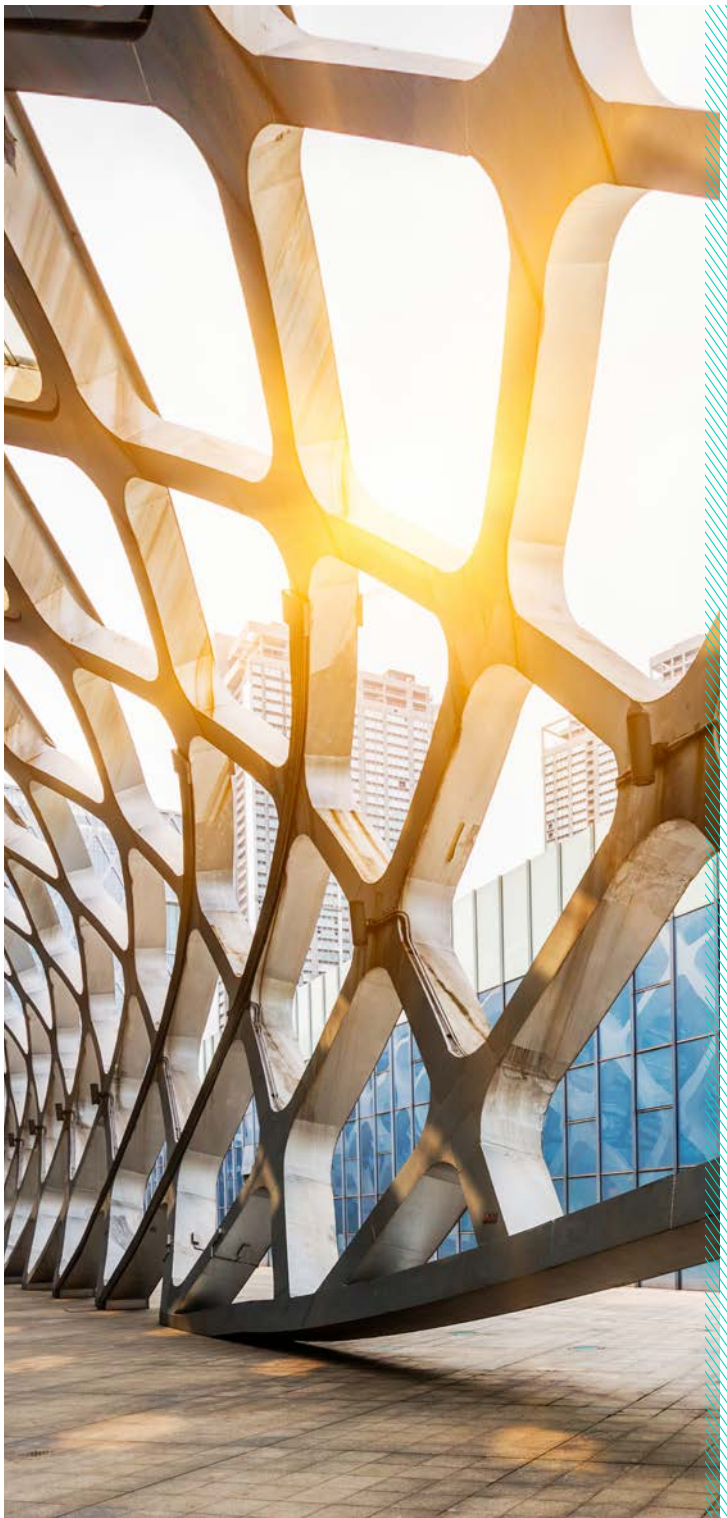
Preparing as detailed an analysis as is possible, in the current uncertain climate, of the company's immediate and medium term funding needs is naturally a key plank on which to plan. So too is having a clear understanding of the company's contractual rights, and obligations, under its existing credit arrangements.

It is important that a company revises its financial plans to present as clear a picture as possible of what those needs are and where difficulties may arise in the context of its existing credit arrangements (with respect, in particular, to financial and other covenants and repayment obligations). That will allow the company to formulate what its 'ask' may be of its funders. Companies facing liquidity issues and / or default should consider engaging with their funders as soon as possible following that analysis.

The company has revolving credit facilities – will these be affected?

Companies anticipating financial difficulties may wish to take proactive steps to draw down any undrawn commitments in the short term to maximise financial resources, notwithstanding the additional interest costs of doing so. Companies with revolving credit facilities should review the terms of those facilities as soon as possible. Generally, the drawing of additional funds will be conditional on there being no default or event of default outstanding and the continued accuracy of the repeating representations referenced in the credit agreement.

Boards should carefully consider the timing of any borrowing and the impact that COVID-19 may have on the covenants and representations contained in the credit agreement into the future. Before drawing additional facilities, company directors should also familiarise themselves with any 'clean-down' requirements in their finance documents (being requirements to pay down fully a facility for a short period of time rather than just rollover outstanding loans).



Financing arrangements

Should we look to amend, or have waived, certain terms of our financing arrangements?

This will depend on the factual position and the specific terms of your financing agreements. If an amendment or waiver is advisable, two practical elements to consider are:

- the procedures which may need to be followed in the finance documents; and
- what percentage of consenting lenders may be required for the waiver/amendment.

The board should also be aware that the costs and expenses of the lenders/agent/trustee in connection with amendments/waivers will typically be for the borrower and there may be amendment or waiver fees charged. In addition, lenders may apply other conditions to the giving of an amendment or waiver, which could include additional capital being obtained, the provision of (additional) collateral or other requirements.

In this regard, the board should consider on a pro-active basis what “gives” or concessions that it can offer to lenders to secure the necessary waivers and amendments (if needed). Examples might include additional collateral, further oversight or reporting structures, additional margin (arising at a later date) or further covenant restrictions.

From a practical perspective the logistics of executing amendments to existing financing agreements in the current environment, ie electronic signatures, requirements for witnesses etc, will need to be considered and factored in from a timing perspective. This is likely to be particularly relevant in the context of syndicated facilities where you have multiple lenders a majority or all of whom may have to consent to any such amendments, depending on the terms of the financing agreement.

Events of default

Financing agreements typically contain events of default. Borrowers and lenders will need to re-assess these events of default in light of the material impact that COVID-19 is having on businesses and the economy more generally.

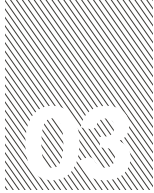
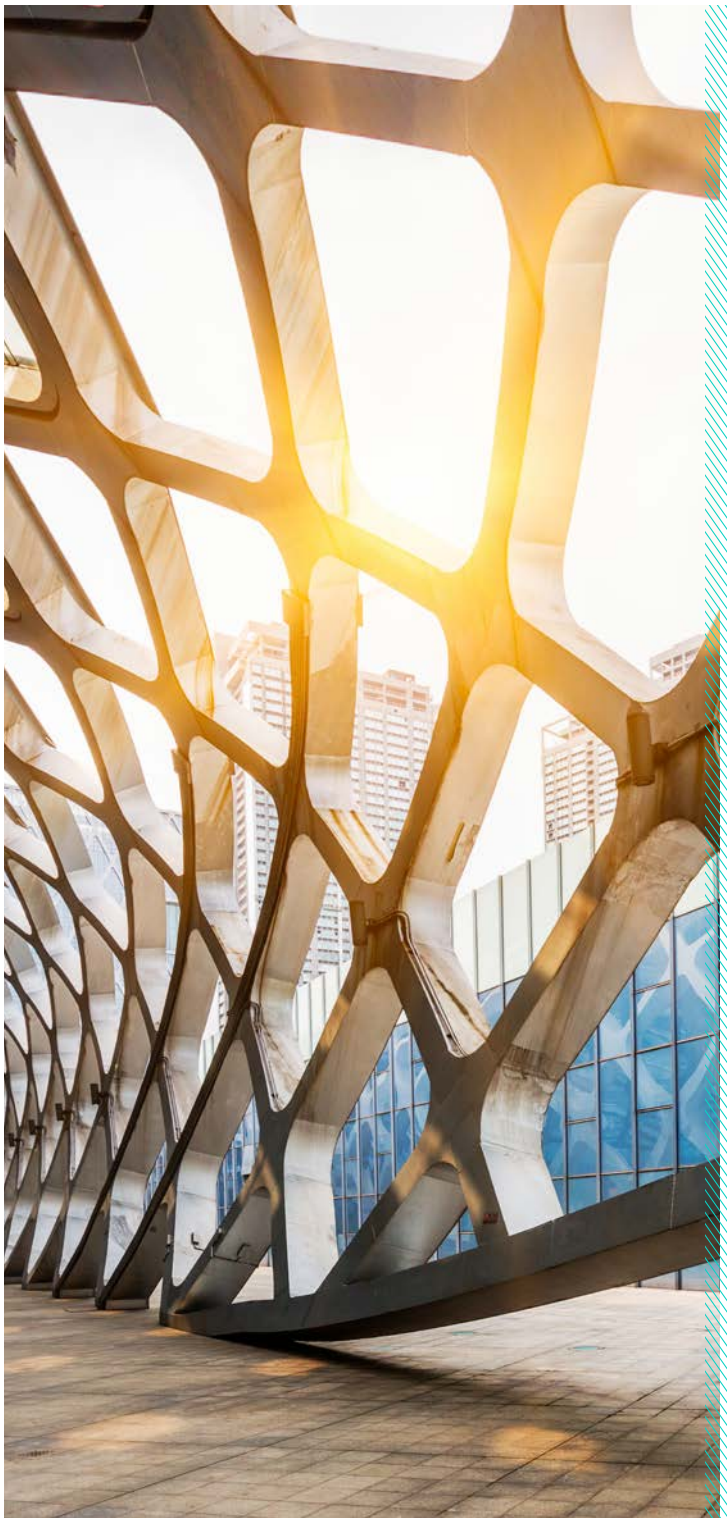
The range of potential breaches contained in finance documents is wide, complex and also evolving; however, some examples are set out below. It should be noted that whether or not there is a breach will depend on the drafting of the documents and the facts of the case. Borrowers may seek to avoid triggering an event of default by anticipating at an early stage what defaults are likely to arise and (i) taking steps to avoid this (including exercising any cure rights) and/or (ii) applying ahead of time for a waiver or amendment to the finance documents.

In addition, defaults, and the notification of them, may have effects on other agreements, or licenses if applicable, that the company has entered into. It should also be noted that upon the occurrence of an event of default the lender often has a relatively unrestricted right to transfer the debt during the period where an event of default continues to exist. This again emphasises the need to engage with lenders as soon as possible.

Material Adverse Change provisions

It is relatively common for financing agreements to contain an event of default on the occurrence of a ‘material adverse change’ (MAC). The purpose of a MAC clause is to capture certain risks that cannot be anticipated at the time the loan agreement is signed.

The ability of a lender to invoke a MAC clause will depend on the wording of the clause and the specific facts (as it is ultimately a question of fact as to whether it has occurred). MAC can be difficult to prove in practice and therefore has (traditionally) seldom been used by lenders. The practise with respect to COVID-19 may well evolve over time.



Financing arrangements

Cessation of business

It should be considered whether the 'cessation of business' event of default could be triggered by mandatory or voluntary closure of a business or activities as a result of the pandemic.

Non-compliance with financial covenants

The majority of business sectors are already seeing a slowdown in business activity as a result of the pandemic. If this results in a material deterioration of the financial position of a company, it may not be able to meet its financial covenants. How immediate an issue this is will depend on how frequently the covenants are tested and when the next test date is (in addition to the materiality of the impact of the pandemic on business).

Failure to comply with information undertakings

Borrowers will likely have obligations to notify their lenders of the occurrence of certain events under their financing agreements (including the occurrence of a default). A failure to do so will amount (subject to any remedy period) to an event of default. Defaults, and the notification of them, may have effects (such as a cross default) on other agreements or licenses of a borrower.

Default

A default or an event of default will typically be a drawstop (i.e. prevent the drawing of further loans), which can be particularly relevant on revolving facilities as noted above. It will also (subject to any grace periods and cures) permit a lender to accelerate and enforce. While such a drawstop may well have negative consequences for a borrower regardless of

the industry they are engaged in it is likely to be particularly relevant for borrowers engaged in the construction sector. In these circumstances any such drawstop is likely to have knock on consequences such as an inability of the borrower to make required payments to contractors etc which may lead to claims against the borrower as a direct result of the drawstop.

Our statutory financial statements will be delayed – will this have an impact on our financing arrangements?

Financing agreements may contain deadlines by which the audited financial statements must be provided. This is typically 120/150/180 days after the end of the relevant fiscal period.

Where a company expects to experience a delay in the finalisation of its audited financial statements, and if relevant, intends to avail of the COVID-19 extensions for publishing of audited financial statements which have now been provided for by a number of regulators, it may need to also seek a waiver from its lenders for any such delay.

Directors should be prepared, proactive and engaged

We are experiencing an unprecedented crisis and it is understandable that many directors may feel a strain on their judgement and their ability to perform their duties. A prudent director, however, is unlikely to go far wrong where he or she is conscious in their daily business activities of adhering to their fiduciary duties. Overall, directors should be prepared, proactive and remain fully engaged on all aspects of the business to navigate the road ahead.

Please do not hesitate to contact A&L Goodbody if you should wish to discuss any of the matters raised in this publication.

In our next edition we will continue to look at the impact of COVID-19 on company boards as the disruptive effect of the pandemic intensifies.

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