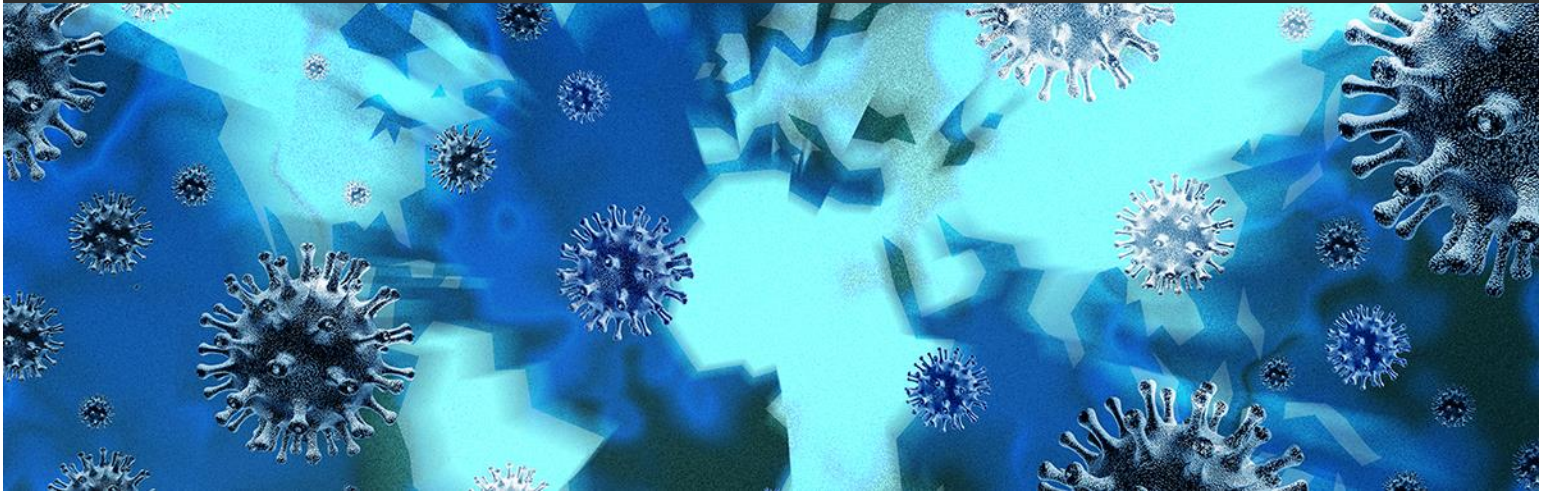


Alert | Health Emergency Preparedness Task Force: Coronavirus Disease 2019



2 April 2020

UK Suspends Wrongful Trading Rules for Company Directors Amid Coronavirus Disease 2019

On 28 March, UK Business Secretary Alok Sharma **announced** that the rules relating to ‘wrongful trading’ will be suspended on account of the issues that Coronavirus Disease 2019 (COVID-19) presents.

The suspension of wrongful trading provisions is retrospective from 1 March 2020 for three months, and according to the announcement, was done so directors of UK companies ‘can keep their businesses going without the threat of personal liability’.

The situation for many directors currently may well be serious due to business interruptions driven by COVID- 19. Additionally, and worryingly for business as well as on many other fronts, it is as yet uncertain how long the situation will carry on, such that projecting cash flow and earnings for many involves more estimate than static state forecasting – complicating liquidity planning and assessment of ability to meet debts ‘as they fall due’, the failure to do so being a possible trigger for insolvency.

Until this announcement, directors who concluded, or ought to have concluded, that their company had no reasonable prospect of avoiding insolvent liquidation would have faced clear risk, as soon as that likelihood became or should have become apparent, to the extent they had failed to take all steps they could to minimise loss to creditors. Of course, that never meant that businesses had to entirely avoid insolvent winding up. Nor did it mean that they would face certain liability if their actions meant that

losses were ultimately greater than they might have been. However, for directors of distressed companies, it was always a material and personal concern.

However, there are still risks for directors. Following are key points to consider:

1. Whilst the details have not been published, the statements may imply that other duties remain intact. The ‘wrongful trading’ risk arose from legislation contained within the Insolvency Act 1986. Directors, of course, have other more general duties. What is not clear is the extent to which directors may still be exposed to legal risks arising from those other duties, some of which overlap with the insolvency-specific legislation. Those other duties derive from both the Companies Act and case law.
2. At some stage, the situation will improve and return to (a new) normal. But there are difficulties in predicting when that will happen, especially when trying to determine what the longer-term implication will be, should, for example, the after-tremors be significant in terms of seasonal reactivation and the timing of development of effective vaccines. But, the suspension of the wrongful trading duties is termed as temporary.
3. Whilst the legislation to be introduced may protect the interim liability of the directors, when the relaxations are withdrawn, the effects, already felt by businesses, will have to be considered in assessing business viability going forward. As such, when the health risk abates, the protections fall away, and some businesses face the prospect of insolvent winding up, or fall into insolvency, the risk position of the directors may be considerably heightened.
4. The relaxation of directors’ duties in this regard may not affect the perspective of other stakeholders in the businesses in question. To be viable, companies will have to ensure that they do not actually become insolvent during the relevant timeframe. In achieving that, there are significant challenges. First, those businesses will require liquidity. Whilst many governmental programs have been announced, there is the question of speed to market. Whatever processes need to be gone through to ensure that that liquidity arrives in a timely fashion have yet to be implemented. And, it remains to be tested whether government support will be sufficiently broad-reaching, sufficient in quantum and timely to meet those needs. Government departments, like all other sectors, will experience significant human resource and efficiency pressures given the need for home-working. At the same time, private sector financiers also have duties, and cannot simply ignore them when considering what credit they should make available and what they should deny.
5. There are some businesses which may not have been viable regardless of the issues presented by COVID-19. The statements so far made by government officials target issues presented by that development as being the linchpin of the relaxation. In some if not many cases, difficulties may arise in determining which issues relate to the virus and which do not. However, the disassociation may be necessary.

Of course, directors need to consider these points whilst continuing to protect the health and well-being of their employees and staff, on both a legal and human basis.

In the meantime, though, the development may be viewed a positive one for directors. It gives them some leeway to continue in business without the immediate risk of personal liability. However, given the points raised above, they may wish to consider carrying on, in many respects, as if the relaxation had not been introduced. To that end, the following are considerations for directors during this time of uncertainty:

1. Take steps to ensure that losses to creditors are minimised;
2. Hold board meetings on a more regular basis to review the position (i.e., at least weekly);
3. Properly minute all decisions reached and the basis upon which such decisions are reached to ensure proper consideration is given to relevant factors;
4. Attempt, so far as is possible, to develop projections of business performance, which may be premised on differing assumption bases as to the anticipated duration of the issue;
5. Look for earnings generating and loss minimisation exercises that may not be possible to pursue now but which may be as soon as circumstances improve, including plans to generate liquidity in the short term: and
6. Take advantage of any financial assistance offered by government and its agencies.

Whilst a temporary reprieve from ‘wrongful trading’ rules is beneficial, the UK government may recognize that some recuperation period and relaxation of rules and regulation may be warranted in the immediate aftermath of COVID-19, as it may take time for business finances and prospects, earnings and balance sheet repair, to return to something approaching normality. The government may also recognize that the concession now afforded to directors in terms of liability may have to be extended to provide them time to put otherwise viable businesses back on sure footing. In the meantime, although payment holidays have been introduced in some areas, for example mortgage payments by individuals and rental payments, the ‘moratorium’ is not universal, and other creditors may seek to take enforcement action or petition for insolvency. In that event, the directors might be protected from liability, but the businesses themselves would be imperilled.

** This GT Alert is limited to non-U.S. matters and law.*

For more information and updates on the developing COVID-19 situation, visit [GT’s Health Emergency Preparedness Task Force: Coronavirus Disease 2019](#).

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