Article

Coronavirus: Directors in Crisis Mode

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As the financial and social impact of COVID-19 is felt across the globe, decision makers are facing and will continue to face serious challenges. In light of the rapidly evolving business environment, driven by factors largely outside of their control, it is more important than ever that directors make rational and well-reasoned decisions.

In this article, we consider some of the issues Cayman directors are likely to be faced with and how they might discharge their duties and obligations in these exceptionally difficult times.

Who is a director?

Due to the nature of the Cayman financial services industry, many directors of Cayman companies are independent non-executive directors. A non-executive director is neither an employee nor part of the executive management team. Non-executive directors often perform a high-level supervisory role, monitoring the activities of the executive team and participating in the development of corporate strategy. From a Cayman law standpoint, there is no substantial difference between the core duties of an executive director and non-executive director.

It is also important to consider whether the same duties and obligations apply to other members of the management structure. In Cayman, the courts have held that shadow directors (i.e. those who direct the directors but are not called directors), *de facto* directors (i.e. those who claim to be directors but are not validly appointed), nominee directors (i.e. those directors nominated by a particular shareholder), and, in some cases, senior managers may all have the same duties that apply to formally appointed directors.

What duties do directors have?

Cayman directors are subject to both fiduciary and non-fiduciary duties. Directors should bear in mind that satisfying fiduciary responsibilities involves honesty, loyalty and good faith (not necessarily competence). In broad terms, directors must act in good faith, in accordance with the company's governing documents and in a way that is likely to promote the company's success.

When exercising their powers, directors must exercise independent judgment. In these trying circumstances, unless full disclosure is made and all necessary waivers are obtained, directors must not place themselves in a position where an actual or potential conflict of interest exists. Directors must not use company assets, information or opportunities for their own profit.

Many directors will be concerned by the fact that external factors are limiting their ability to maintain control and make fully informed decisions. However, provided that decisions are made honestly with the intention of protecting the company, fiduciary duties are not infringed. Courts are always reluctant to over-analyse the commercial judgment of directors with the benefit of hindsight. That is especially true at such a unique and difficult time. Therefore, while the situation changes on a daily basis, provided that directors continue to act in good faith with the company's best interests in mind and take independent advice where appropriate, the Courts are unlikely to criticise their conduct.

Unlike in the US, Cayman law does not regard the duty to exercise reasonable care as a fiduciary duty. As opposed to being focused on honesty and loyalty, the duty of care and skill is focused on competency. As made clear in recent judgments in Cayman, directors have a continuing duty to acquire and maintain sufficient knowledge and understanding of the company's business to enable them to properly discharge their duties as directors. Importantly, for present purposes, this does not mean that a director must "get it right" every single time, but s/he must act reasonably in all the relevant circumstances.

Doubtful solvency

The uncertainty and restrictions in place due to the novel coronavirus are making it extremely difficult for companies to plan ahead and are placing huge pressure on cash flow. Even the most successful and profitable companies are likely to find themselves in uncharted territory and under unprecedented financial pressure.

If directors are concerned about the financial health of their business in either the short-term or long-term, the focus of their duties may need to shift from promotion of the company for the benefit of all shareholders to acting in the best interests of all creditors of the company. If a company is entering the realm of doubtful solvency, directors should take independent professional advice as early as possible and consider the appointment of provisional liquidators to provide the company with a period of breathing space. This is to help mitigate the risk of potential personal liability under Cayman legislation.

There are various practical steps directors might consider in the present circumstances, such as dealing openly and regularly with creditors and adopting cost-cutting measures where possible. These are commercial, rather than legal, considerations but may assist with protecting directors from a legal perspective at a later date. If directors ultimately form the view that the company cannot avoid insolvency, they must convene a meeting and pass a resolution to wind up the company or seek an order of the Cayman court.

Comment

Many companies incorporated in the Cayman Islands include an indemnity in their governing documents for the benefit of directors and officers. Directors then typically insure against their own liability should that indemnity be engaged at any point. In high-profile judgments in *Weavering* and *Primeo*, the Cayman courts provided guidance on the enforceability of indemnity and exculpatory provisions. Directors may wish to review their respective individual positions and take advice in light of the novel coronavirus and the high pressure situations many are faced with.

As difficult as this may be in the present circumstances, it is important that directors hold regular meetings (by telephone or video-conference) and record in the minutes any commercial decisions they make based on reputable independent advice. At or outside of any such meetings, directors should ensure that they have reliable financial information to hand and maintain regular contact with service providers, such as auditors and actuaries, to assist them in their decision-making.

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