

FINANCIAL DISTRESS - TIP SHEET FOR BOARDS OF DIRECTORS OF COMPANIES (HONG KONG)

We live in uncertain times, where many companies face challenges brought about by the sudden and wide-ranging economic impact of Coronavirus. Whilst governments globally are implementing measures to alleviate some of the financial consequences, it is inevitable that many boards face unprecedented situations and challenges ahead. Your company's financial distress may be a challenging time in which critical, yet prudent decisions must be made. This tip sheet may focus your mind on best practice in these difficult circumstances.

WHAT ARE YOUR DUTIES DURING FINANCIAL DISTRESS/INSOLVENCY?

Outside of a distressed situation, you owe a duty to act for the benefit your company's members as a whole. However, where your company is financially distressed and facing potential insolvency, as a director you must also have regard to the interests of creditors as a whole (not just the interests of any individual creditor or class of creditors). Failure to recognise the interests of creditors and take steps to minimise potential losses to creditors at this time can give rise to personal liability.

WHAT ARE SOME THINGS YOU CAN DO TO PROTECT THE BOARD?

Here are our "top ten" practical steps where your company's financial position is deteriorating:

1. **Meet regularly and stay informed:** appropriate board minutes are a particularly important way of demonstrating you have complied with your duties. Remote meetings and telephone calls are widely accepted means of making board decisions and provisions for such are included in most articles of association.
2. **Seek professional advice:** obtaining expert advice relating to waivers, standstills, new finance, employee obligations, customer and supplier arrangements, compliance (including continuing disclosure obligations), asset valuation and a restructuring or insolvency proceedings can help reduce the scale of any losses, minimise the risk of your liability, and avoid management

being distracted by the consequences of non-compliance. Individual directors may also consider that they need separate advice.

3. **Consider whether to continue trading:** Hong Kong does not yet have an 'insolvent' or 'wrongful' trading regime, but a director may be personally liable for all or any of the debts of the company where he is found to have carried on the business for the purpose of defrauding creditors. There are many situations when continuing to trade will be in the best interests of creditors, so it is a decision you must keep under constant review.
4. **Consider restructuring options:** in situations where your company's distress is not temporary, exploring restructuring options (having obtained professional advice) is a good way of demonstrating compliance with your duties.
5. **Consider individual companies within the group:** you need to consider the individual companies within a group context and the duties you owe to the stakeholders of each company when making a decision. The risk of cross-default or insolvency may also restrict your ability to borrow or make available intra-group funding or enter into intra-group transactions.
6. **Consider key contracts:** while monitoring key contracts (including finance arrangements) will be the company's obligation, you should review relevant provisions (like financial covenants and termination events) in order to develop the best course of action.
7. **Consider transactions:** consider your company's ability to meet its current and future obligations before entering into any new transactions (including new finance) and ensure these obligations are regularly reviewed. This includes any proposed payment of dividends.
8. **Ensure proper delegation of authority:** ensure key personnel have properly allocated responsibilities and carefully consider the flow of information to members and employees.
9. **Ensure proper records are kept and timely reporting:** ensure your company's books and records are being properly kept up to date, regular financial and operational reporting, and timely escalation of issues.
10. **Think carefully before resigning:** resignation will not discharge your responsibility for any previous conduct. Remaining on the board to drive a successful resolution may be 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 \(COVID-19\): Challenges for Employers](#)

[Coronavirus Issues relating to Capital Markets in APAC](#)

[Coronavirus \(COVID-19\) Issues relating to Loan Financings in APAC](#)

[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)

CONTACTS

Scott Bache

Partner, Restructuring
and Insolvency

T +852 2826 3493

E scott.bache

@cliffordchance.com

Joanna Charter

Consultant,
Restructuring and
Insolvency

T +852 2826 2458

E joanna.charter

@cliffordchance.com

Phoebe Lo

Senior Associate,
Restructuring and
Insolvency

T +852 2826 3465

E phoebe.lo

@cliffordchance.com

Anthony Wang

Partner, Banking and
Finance

T +852 2826 3434

E anthony.wang

@cliffordchance.com

Matthew Truman

Partner, Banking and
Finance

T +852 2826 2488

E matthew.truman

@cliffordchance.com

Dauwood Malik

Partner, Banking and
Finance

T +852 2826 3485

E dauwood.malik

@cliffordchance.com

Andrew Whan

Partner, Corporate

T +852 2825 8903

E andrew.whan

@cliffordchance.com

Neeraj Budhwani

Partner, Corporate

T +852 2826 2428

E neeraj.budhwani

@cliffordchance.com

Bryan Koo

Partner, Corporate

T +852 2826 2478

E bryan.koo

@cliffordchance.com

Donna Wacker

Partner, L&DR

T +852 2826 3478

E donna.wacker

@cliffordchance.com

Thomas Walsh

Partner, L&DR

T +852 2826 8052

E thomas.walsh

@cliffordchance.com

Edward Johnson

Partner, L&DR

T +852 2826 3427

E edward.johnson

@cliffordchance.com

Matt Fairclough

Partner, Capital Markets

T +852 2825 8954

E matt.fairclough

@cliffordchance.com

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Clifford Chance, 27th Floor, Jardine House,
One Connaught Place, Hong Kong

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