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COVID-19: GOVERNANCE: DIRECTORS' DUTIES DURING THE COVID-19 CRISIS - PART 2 (AUSTRALIA)

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Legal Briefings – By **Andrew Eastwood and Tim Stutt**

In a series of articles, we explore issues and some practical matters that directors should be considering at this time.

The COVID-19 pandemic presents many issues for company directors. One question that arises is the extent to which directors owe a duty to consider the interests of creditors of the company and, if so, what such a duty requires. Further, the COVID-19 pandemic will shape the standard expected of directors in relation to their deliberations and decision-making, and directors should take steps to understand the risks and opportunities the COVID-19 pandemic presents to the company.

During the COVID-19 crisis, directors continue to owe their fundamental duties, namely to act with reasonable care and diligence, to act in good faith in the best interests of the company (which as we noted in our first article, may require the directors to take into account the interests of creditors in some circumstances) and for a proper purpose, and the duty not to use a director's position or information obtained as a director to gain an advantage or cause detriment to the company.

In relation to the directors' duty of care and diligence (both under statute and common law), authority supports the view that a director does not need to demonstrate greater skill in performing their duties than may reasonably be expected *in the relevant circumstances*.[1] The "circumstances" will be influenced by matters such as the state of the company's financial affairs, the size and nature of the company, and the urgency and magnitude of any problem.[2] Accordingly, it is clear that the COVID-19 pandemic will shape the standard expected of directors in relation to their deliberations and decision-making.

Each company will have its own needs and challenges, however in complying with their general duties, directors should take steps to understand the risks and opportunities the COVID-19 pandemic presents to the company. That will involve the Board satisfying itself that there is a robust system in place for overseeing the company's response to the pandemic, asking relevant questions of management, and ensuring that management is taking steps to address the identified risks and evaluate relevant opportunities.

In considering financial and non-financial risks to the company, some particular considerations include:

Supply chain disruption, and the potential flow on consequences for the company's ability to meet its contractual obligations. This may include considering what measures might potentially be available to mitigate such disruption, for example identifying alternative suppliers, seeking to amend supply agreements, and claiming on business interruption insurance. Companies should be aware that obtaining supply outside of their usual channels, or with lesser diligence processes, may also impact the company's risk profile, and could in some cases require mandatory disclosure in the company's modern slavery statement as an area of potential risk exposure.

Financial covenants and liquidity considerations. Directors should consider the liquidity position of the company, including possible headroom under current debt facilities and the potential availability of other sources of liquidity. This may also include rigorously testing updated cashflow forecasts covering a range of anticipated outcomes.

Compliance with employment, health and safety and other laws. Boards should discuss with senior management the employment, workplace health and safety issues posed by COVID-19. As part of these discussions, boards should seek to keep abreast of the changing regulatory environment, and review and test the company's risk management framework (including, where appropriate, seeking expert advice).

Any impact on the company’s material contractual arrangements, including implications under force majeure and material adverse change clauses.

Market disclosure, whether for listed companies under their continuous disclosure obligations, or (for example) the disclosure of risks for the purposes of capital raising documents.

Further, while the economic disruption caused by the COVID-19 pandemic creates risks, it also presents potential growth opportunities. As such, in addition to mitigating the risks identified, directors should ensure that they are positioning the company to take advantage of those opportunities.

Click here for COVID-19: Governance: Directors’ duties during the COVID-19 Crisis - Part 1 (Australia)

ENDNOTES

1. See, eg: *Australian Securities Commission v Gallagher* (1993) 10 ACSR 43 at 53; Trilogy Funds Management Ltd v Sullivan (No 2) 2015) 331 ALR 185 at [201].
2. *Australian Securities and Investments Commission v Cassimatis* (No 8) [2016] FCA 1023.

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

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