

Directors' duties amidst the coronavirus outbreak

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The COVID-19 pandemic has affected businesses all over the world. Whilst directors will actually consider that their primary responsibility is to keep the business running during difficult times, it is equally important to bear in mind that this should be done in accordance with the law and via appropriate means. A director should always have regard to the company's financial status and avoid entering into transactions that are in breach of his/her fiduciary duties as director, especially when the company's solvency is open to question. If losses are incurred from such transactions the director may be held personally liable. This article sets out some advice for Hong Kong company directors amidst the current climate.

Directors must always act in the best interests of the company. This generally means that they must act in a way which benefits the shareholders as a whole. However, when a company is insolvent or on the verge of becoming insolvent, directors should be aware of the following:

- Duty to consider the interests of the company's creditors

In the context of potential insolvency, directors must take into account the interests of creditors when making decisions on behalf of the company. This duty requires directors to ensure that the company's assets are not exploited or dissipated for their own benefit to the prejudice of the creditors' interests. Breach of such duty may result in personal liability.

In the case of *Tradepower (Holdings) Ltd (in liq) v. Tradepower (Hong Kong) Ltd and Ors*¹, the directors implemented a scheme shortly before the company was wound up, stripping the company of a valuable asset in favour of their own company. The court found no justification for the scheme and drew an inference that the directors had acted with an intent to defraud the company's creditors. In the end, the court set aside the scheme and held the directors personally liable for the loss occasioned by the company.

- Preferential payment to creditors should be avoided

When a company is insolvent, directors should avoid paying debts to one creditor in preference to another, as such payments may be set aside and recovered as a preference from the recipient². The directors in question may also be held personally liable for a breach of duty in having effected that preference³.

- Courts' power to disqualify a person from acting as a director

Where a company becomes insolvent and the court is satisfied that a person's conduct as director makes him/her unfit to be concerned in the management of a company, the Hong Kong courts have power to disqualify him/her from acting as a director of any company for up to 15 years⁴. Such disqualification can arise when a director is convicted of an indictable offence, persistently breaches specified provisions of Hong Kong company law, or is guilty of

committing fraud or any other breach of duty in the winding-up of a company.

- Strict requirement to pay employees' wages on time

It is an offence if an employer wilfully, and without reasonable excuse, fails to pay wages within the statutory time limit⁵. Insolvency is no defence. Any director, manager, secretary or other similar officer of the company is guilty of the same offence if he consents to, connives in or is negligent as to the non-payment of wages⁶.

In the case of *HKSAR v. Li Fung Ching Catherine*⁷, a director was held personally liable for the company's failure to pay wages. The court was of the view that the financial difficulty of the company and the director's desire to restore the company's financial situation by allocating funds to the daily operation of the company did not constitute a "reasonable excuse".

- Continuous disclosure obligations for listed companies remain

Under prevailing rules, events (including those related to the COVID-19 pandemic) which could have a material impact on share prices will need to be disclosed by way of announcement. Directors should continue to monitor the company's financial position and maintain close contact with the board and key members of the audit team. Directors who are prevented from travelling to a meeting, possibly because of a travel ban or quarantine, should assess whether they are thereby prevented from properly appraising the company's operations in order to form an opinion on the subject matter. If so, alternative modes of communication (e.g. virtual meetings) should be considered to ensure the director has met the requisite standard of care.

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1. [2008] HKCU 1715↔
 2. Section 266B of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32)↔
 3. Section 276 of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32)↔
 4. Section 168H of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32)↔
 5. Section 63C of the Employment Ordinance (Cap. 57)↔
 6. Section 64B of the Employment Ordinance (Cap. 57)↔
 7. [2012] HKEC 807↔

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