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CORPORATE AND COMMERCIAL

Trading While Insolvent

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The existence of directors' and officers' insurance cover does not absolve directors of their responsibilities.

Many companies will encounter financial difficulties due to the COVID-19 emergency, with their officers facing the difficult decision of either continuing to trade or winding up the company.

While many company officers will take the decision to avail of new credit facilities from suppliers or financial institutions to trade their way out of financial difficulties, careful consideration needs to be given to whether the proposed course of action might breach the provisions of the Companies Acts.

Officers and members of limited liability companies do not normally have personal liability for corporate debts, but there are exceptions. For example, officers may be held liable for corporate debts where there has been:

1. reckless trading: described as the carrying on of any business of the company in a manner which the officer should have known would cause loss to the creditors of the company; or
2. fraudulent trading: described as the carrying on of any business of the company with intent to defraud creditors of the company.

Does a D&O insurance policy provide cover for personal liability arising from fraudulent trading?

While this is a complex area and the particular wording of the policy will ultimately determine whether cover is provided, it is normal for directors' and officers' (D&O) policies to exclude cover in respect of civil liability arising from "fraudulent or dishonest" acts or omissions. It follows that an officer would not be covered under a D&O insurance policy for liability arising from a finding that the officer had carried on the company's business in a fraudulent manner with the intent of defrauding creditors of the company.

What about in the case of reckless trading?

Some D&O insurance policies exclude cover for liability arising from "reckless" acts or omissions, while others exclude cover in respect of "fraudulent or dishonest" acts or omissions. It is therefore necessary to examine the precise policy wording and the conduct of the officer in question to determine whether his/her conduct falls within one of the policy exclusions.

In a case where reckless trading is alleged, a finding that an officer acted "honestly and responsibly" in relation to the conduct of the affairs of a company may relieve the officer of personal liability. Consequently, in a case where personal liability is imposed on an officer, the court is likely to have found that the officer's conduct was not "honest or responsible". Such a finding by a court would, in all likelihood, exclude cover under any available D&O policy.

As well as potential personal liability, an officer of an insolvent company may face restriction or disqualification from acting as a director or secretary of a company.

It is recommended that officers should obtain legal advice and should consider carefully their obligations when making decisions on whether a financially stressed company should continue to trade. The existence

of D&O cover should not be seen as a panacea to absolve officers of potential personal liability for the debts of their companies if they trade in a reckless or fraudulent manner.

For further information, please contact Shane Neville at sneville@lkshields.ie, Ian Lavelle at ilavelle@lkshields.ie or Jill Callanan at jcallanan@lkshields.ie.

The cross-disciplinary business crisis advisory team at LK Shields are available to provide practical advice and legal insights to employers, business owners, directors, insurance providers, compliance officers, HR professionals and decision-makers faced with a crisis.

If you would like to discuss this further, please contact crisis-advisory@lkshields.ie or any member of our business crisis advisory team. To subscribe to our crisis advisory news and insight please [click here](#).

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