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Comparison of Directors' Duties Across England and Wales, Germany, Italy, the Czech Republic and the Slovak Republic

November 2024

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With the current focus in England on directors' duties given the recent decision in *BHS*,[1] we thought it would be an opportune time to examine the duties of directors across several European jurisdictions. Directors' duties can vary between different jurisdictions in terms of the descriptions of the role of directors, general duties and obligations applying to such individuals in going concern scenarios versus distress and subsequently insolvency scenarios. However, many have a common feature – the obligation not to continue trading if a company is insolvent.

This article explores directors' duties across England and Wales, Germany, Italy, the Czech Republic and the Slovak Republic. It is not intended to be a comprehensive guide and is only a high-level summary of the general position as at the date of this article.

England and Wales

Directors of solvent English companies have statutory duties that they owe to the company. Each director owes these duties individually. In the exercise of those duties, generally and while the company trades solvently, directors must act in good faith and in a manner that would most likely promote the success of the company for the benefit of its members as a whole. Directors' statutory duties require them to also take into account wider factors, such as the environment, employees, the standard of their business conduct, business relationships with suppliers and customers, and any other relevant circumstances. Additionally, English law does not distinguish between executive, nonexecutive or shadow directors.

However, the statutory duty to promote the success of the company is modified where a company is bordering on insolvency, such that the directors must also then balance the interests of creditors alongside their duty to consider the interests of shareholders (i.e. the so-called "creditor duty"). The judgment handed down in *Sequana*[2] clarified that the creditor duty is engaged when a director knows, or ought to have known, that a company is insolvent or bordering on insolvency, or that an insolvent liquidation or administration of the company is probable. Accordingly, a mere "real risk" of insolvency at some future date is not in itself sufficient to trigger the creditor duty, and directors may, in the appropriate circumstances, attempt to trade through financial difficulties

The modified duty was recently considered and developed in the case of BHS, where the court found the former directors of BHS liable for "misfeasance trading" in breach of their duties (including the so called "creditor duty). This new type of claim appears to have heightened the risk of personal liability for directors where a company is facing insolvency, given that liability under this head of claim can arise much earlier than it can for wrongful trading, which requires the directors to have known – or that they ought to have known – that insolvency was inevitable. The directors were penalised in BHS for breaches of their directors' duties where their actions effectively caused losses for the company that had an "insolvency-deepening" effect.

Directors of English companies can also be personally liable for transactions that they have entered into prior to a company entering insolvency if such transactions have caused a loss to the company or its creditors – for example, if they have disposed of company assets at an undervalue, intentionally paid creditors to place them in a better position in the event of an insolvency, continued to trade the company knowing that insolvency was inevitable or made unlawful dividend payments. They may also become liable for certain unpaid company tax debts. In addition, directors can also be disqualified as a consequence of their actions (or inactions).

Germany

In Germany, directors of solvent companies are required to act with the diligence of a prudent businessperson and exercise their duties in accordance with applicable laws, the company's constitutional documents, instructions from shareholders, and any obligations set out under their respective employment agreements. They must also continuously monitor any developments that could endanger the company's existence and take appropriate countermeasures.

When a German company is either insolvent or at the brink of insolvency, German insolvency laws mandate directors to protect creditors' interests by filing for insolvency promptly and, in any event, within three weeks of the company being unable to pay its debts as and when they fall due (save where the liquidity issues are either minor or temporary), or within six weeks of the company becoming over-indebted. In assessing whether a company is overindebted, the directors have to consider whether it is more likely than not that the company will remain liquid for the next 12 months ("positive going concern prognosis").

1 *Wright and others v. Chappell and others; Re BHS Group Limited* [2024] EWHC 2166 (Ch)

2 *BTI 2014 LLC v. Sequana SA*

If the prognosis is negative, the obligation to file will arise. If the company is insolvent, directors can only make payments provided that they align with prudent business practices, and when a company initiates insolvency proceedings, the directors must also consider the interests of creditors.

Under German insolvency laws, a failure to file for insolvency in a timely manner may constitute a criminal offence carrying imprisonment of up to three years or a fine. Directors may also be disqualified from holding directorships for a period of up to five years.

Directors can also be held personally liable under civil heads of claims where they have violated their duties, causing the company to suffer loss (e.g. transactions at an undervalue, or transactions that are detrimental to creditors of the company). Additional liabilities can also arise from a failure to pay certain taxes, declaring and paying dividends to shareholders that result in the company being unable to pay its debts as and when they fall due.

Italy

Directors of solvent Italian companies are required to act diligently to fulfil their duties in accordance with the law and the company's constitution. This includes a duty to continuously monitor events that could potentially trigger the insolvency of the company. Where directors detect distress, they are required to address this (e.g. by considering appropriate restructuring and reorganisation measures and processes).

Once a company is insolvent, directors of Italian companies must focus on company asset preservation and avoid making any preferential payments, and not continue to trade if it would be detrimental to the financial position of the company. Where the statutory minimum share capital is not met, directors must also refrain from entering into any new transactions.

To avoid further worsening the position of the company, the directors are also required to file an insolvency petition without delay.

Although, under Italian laws, encountering corporate distress does not require directors to consider the interests of creditors of the company, they can be liable to them if, as a result of their actions, there are insufficient assets to satisfy creditor claims.

There is scope under Italian laws for both civil and criminal penalties to attach to directors. A director can face criminal sanctions for, among other reasons, concealing the company's distress and insolvency or continuing to obtain loans, or either attributing nonexistent assets to themselves or simulating claims that are wholly or partly nonexistent, in each case, to influence or obtain the requisite approval for a restructuring agreement.

Under Italian laws, directors can be held liable to the company and the company's creditors, as well as to third parties, in each case, under civil heads of claims. Broadly, these liabilities may arise where the director's actions are prejudicial to, and cause losses to, any of these parties in the context of corporate distress.

Czech Republic

Directors of solvent Czech companies are required to act in the best interests of the company, exercising due managerial care, while maintaining loyalty and confidentiality. Once the company begins to experience financial distress, or insolvency is impending, the directors must convene a general meeting of the company without delay, and the directors are also obliged to file for insolvency without delay.

There is scope under Czech laws for both civil and criminal penalties to attach to directors. Czech law recognises a special category of "insolvency criminal offences" under which directors may receive custodial sentences of up to eight years and be banned from certain activities. The insolvency criminal offences under Czech laws include, but are not limited to, causing damage/loss to creditors, preferential treatment of creditors, causing insolvency of the company, participating in collusion during insolvency proceedings, and breach of duties during insolvency proceedings.

Civil penalties may also arise for directors where they have breached their director duties, and damage or harm is caused to the company as a result of such breach. Directors may also be held liable for damage caused to creditors of the company if they continue to trade in circumstances where they ought to have filed for insolvency, and the foregoing causes loss to the creditors. Czech courts have the power to order directors to make up any shortfall in company assets if the director contributed to the insolvency of the company as a result of breaching their duties. There are also a number of financial penalties that may be incurred by directors in such circumstances – from being ordered to surrender their remuneration, or profits, received in the performance of their functions in relation to the company in the two years prior to the insolvency proceedings being commenced, to fines, financial penalties and director disqualification.

Slovak Republic

Directors of solvent Slovak companies are subject to fiduciary duties and are required to act with the diligence of a prudent businessperson. They must discharge their duties with regard to the applicable laws, the company's constitutional documents, shareholder instructions and any obligations set out in their employment contracts.

Where a Slovak company is in crisis or distress, the directors are obliged to act with due diligence and take all action to overcome this. A company will be in crisis where the ratio of the company's equity to its liabilities is less than 8-to-100.

If a Slovak company is either insolvent or overindebted (i.e. under a balance sheet test, the company's liabilities – actual, contingent and prospective – exceed its assets, and it has at least one creditor), it is deemed to be bankrupt under Slovak law. The foregoing triggers a 30-day period in which directors must file for bankruptcy.

Under Slovak laws, directors can face criminal sanctions, personal liabilities and other ramifications (such as disqualification proceedings). Directors who fail to file a petition for the bankruptcy of the company on time may be required to compensate creditors if they are prejudiced by the delay in filing. Further, directors may also be liable to pay a contractual penalty to the company's bankruptcy estate of €12,500.

Failing to file for bankruptcy proceedings in time is also a criminal offence under Slovak law, as is entering into any transaction once the company is in financial difficulties that may be deemed a preference.

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