



PRIVATE COMPANY DIRECTOR LIABILITY AND PROTECTION

Being a corporate director can be a rewarding experience. Directors can use their business expertise to grow or improve a business. Corporate directors hire senior officers, oversee overall strategy and assess the potential need for change. Directors may receive cash compensation from or equity in the firms they serve allowing for financial benefits as well as professional and mental satisfaction.

However, in addition to the potential benefits, directors also face potential liabilities. While the risk is greater in the public company context, private company directors can face substantial personal liability. Potential claimants, include shareholders, creditors, unpaid employees and the government. The sources of liability for directors of private companies are numerous and include the following:

Breach of Fiduciary Duty. Just like their public company counterparts, private company directors owe shareholders the fiduciary duties of care and loyalty. While specifics vary by jurisdiction, the duty of care generally requires a director to perform duties with such care as an ordinarily prudent person would use. Directors thus have an obligation to inform themselves of all material information reasonably available to them before making a business decision. A breach of the duty of loyalty can occur when a director uses his or her position to promote a transaction or course of action that personally enriches such director but is not substantively fair to the company.

Creditors. When a financially distressed corporation enters the “zone of insolvency,” corporate directors are generally considered to owe fiduciary duties to creditors so as to maximize payouts. Once again, the scope of these duties may vary by jurisdiction.

Unpaid Wages and Payroll Taxes. Corporate agents such as directors may be liable for unpaid wages under the federal Fair Labor Standards Act of 1938 or unpaid payroll taxes under the Internal Revenue Code. In addition, certain states including Illinois, New York and New Jersey, can impose additional obligations on corporate directors for unpaid wages.

Regulatory. Private company directors may face liability for their companies’ violation of regulatory statutes such as the Foreign Corrupt Practices Act and antitrust statutes. The FCPA applies not only to public companies, but also to “domestic concerns” which includes any corporation with a principal place of business in the United States or organized under US law. Directors whose corporations do business overseas should be sure that their corporations have established FCPA compliance policies and procedures to which executives should strictly adhere.

Managers of limited liability companies face many of these same liability risks although the fiduciary duties of LLC managers may differ from those of corporate directors in certain jurisdictions.



To help navigate liability minefields, corporate directors should keep in mind the following:

Active Participation. Perhaps the best protection is to be an educated and active board participant. Board meetings should be held regularly. Directors should attend meetings, prepare in advance, participate in discussions, question officers and where appropriate, seek the opinions of lawyers, accountants, investment bankers and other professional advisors. In conflict-of-interest situations, directors with conflicts should recuse themselves from board deliberations.

Provisions in Organization Documents. Before accepting a directorship, an individual should review the company's articles of incorporation and bylaws to confirm that the company is empowered to indemnify its directors to the full extent permitted by applicable law.

Indemnity Agreements, Credit Support and Insurance. Directors can enter into indemnity agreements that provide additional financial support such as letters of credit. Such additional support can be crucial when companies are financially distressed and have difficulties meeting their obligations. Directors should also verify that there is insurance to cover them against applicable risks and that required premiums are being paid.

FisherBroyles attorneys can assist directors and corporations in devising cost-effective strategies that maximize board effectiveness, corporate flexibility and director protection.

If you would like additional information, please contact any of the following FisherBroyles partners:

Atlanta

Carl Johnston
(404) 636-2533
carl.johnston@fisherbroyles.com

Los Angeles

Steven Papkin
(310) 415-6254
steven.papkin@fisherbroyles.com

Chicago

Marty Robins
(847) 277-2580
martin.robins@fisherbroyles.com

Boston

Peter Cahill
(617) 475-0094
peter.cahill@fisherbroyles.com

Founded in 2002, FisherBroyles, LLP is a full-service, cloud-based national law firm with attorneys across the country. Conceived as the "Next Generation Law Firm®", FisherBroyles eliminates unnecessary overhead and instead offers a more cost-effective solution to clients across all industries. For more information visit our website at www.fisherbroyles.com.

This newsletter has been prepared for the general information of clients and friends of FisherBroyles. It is not intended to provide legal advice for a specific situation or create an attorney-client relationship. Under rules applicable to the professional conduct of attorneys in various jurisdictions, it may be considered advertising material.