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The Fiduciary Duties of Directors of Troubled Companies

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Directors and officers of financially distressed companies often face complicated, high-pressure decisions in fulfilling their fiduciary duties. For years, practitioners, legal scholars and even judges had struggled with whether (and when) directors and officers owed such duties to creditors as a company approached or entered insolvency. Courts in Delaware — the state of incorporation for many U.S. companies — have sought to clarify the issue in two seminal decisions of the past decade. The decisions in these cases, North American Catholic Educational Programming Foundation Inc. v. Gheewalla and Trenwick America Litigation Trust v. Ernst & Young, held that the duties owed to the corporation do not change as it nears insolvency or becomes insolvent. Rather, creditors simply become the principal residual beneficiaries of those duties.4 The Delaware judiciary has recently continued to interpret and apply these decisions.

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