

BANKRUPTCY

Directors and officers of a corporation have a duty to protect both the insolvent corporation and the interests of its creditors. The question lies in which becomes more important where a company is failing financially.

There is disagreement about whether the Delaware Supreme Court decision essentially eliminated creditors rights to sue directors for breach of fiduciary duty for actions taken just before bankruptcy or while in the "zone of insolvency." There is no clear definition of zone of insolvency, nor is it clear whether directors have an obligation to reduce the company's liabilities to creditors when the company is failing. A Pennsylvania court held that only fraud would support a deepening insolvency case; whereas, the Delaware Supreme Court held that creditors have no right to sue directly those directors who were in a position to be held responsible for the company's shortcomings. Some attorney's disagree as well, while one Baltimore attorney claims that directors duties expand when the company is failing, other attorneys claims that directors would be torn between their fiduciary duty to the insolvent corporation if they had a direct duty to protect creditors.

The argument now turns on whether the creditors have a right to direct claims for breach of fiduciary duty or whether the claims must be brought in a derivative manner on behalf of the corporation and not the individuals.