

Coronavirus/COVID-19 Update

If you have any questions regarding the matters discussed in this memorandum, please contact the attorneys listed on the last pages or call your regular Skadden contact.

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The question is no longer whether the volatility created by the COVID-19 pandemic will deepen the difficulties businesses and other institutions face in the coming months, but by how much and in what ways. In the past few weeks, we have offered client mailings and webinars on COVID-19-related topics, and we will work to keep you informed of important developments as these issues evolve. Included below are updates to our recent commentary, with answers to questions we have been receiving.

Corporate

Impact of COVID-19 on M&A

By Paul T. Schnell

The COVID-19 crisis is continuing to have a dizzying impact on M&A, as it has on everything else. Since our [March 4, 2020 client alert](#) on the subject, the discussion has shifted from the “potential impact” to how the coronavirus is, in fact, significantly affecting every phase of the M&A process and every element of the acquisition agreement.

Buyers face a challenge in diligence trying to understand the myriad uncertain and far-reaching ways in which the virus is affecting the target company, with the target often not that far ahead of the buyer in figuring this out. Boards need advice on the special fiduciary issues raised by COVID-19 in approving transactions. Buyers are dealing with additional demands in obtaining acquisition financing. Targets are analyzing their sudden vulnerability to an unsolicited bid or shareholder activist campaign. Every page of the purchase agreement — from the extent to which the virus’ negative impact will be considered a MAC, to each representation and warranty, covenant on conducting business in the ordinary course, closing condition, termination right and indemnification provision — has to be analyzed using a COVID-19 lens.

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Still, deal parties are sometimes able to compromise on allocating the COVID-19 risk, and boards and management teams with greater risk tolerance are pursuing transactions: acquisitions by larger, financially strong companies of smaller companies; private equity firms deploying their large funds; intra-industry deals where the buyer is already living with the same COVID-19 risk; transactions in (the few) industries less affected by the virus or where the impact is not quite as difficult to assess; deals for financially troubled companies; spinoffs and split-offs where value can be unlocked without having to negotiate with a counterparty; and selected stock-for-stock combinations.

Vulnerability to Shareholder Activists

By Richard J. Grossman

With share prices declining precipitously over the last few weeks, many companies have expressed concern that they may become vulnerable to shareholder activists. Companies with existing activists already among their stockholders also should be alert. For example, Carl Icahn recently doubled down on his investment in Occidental Petroleum, increasing his position to nearly 10%. In response, the company adopted a shareholder rights plan, or so-called poison pill.

While the total number of activist campaigns may slow in light of the volatility (particularly if funds face redemptions), the significantly lower share prices likely will increase companies' vulnerabilities, and renewed efforts on activism preparedness are appropriate, including a vigilant stock watch program, a vulnerability self-assessment and creation of a preparedness manual. In addition, the increased vulnerability may call for additional board education/preparedness. These could include a review of fiduciary duties in the activism context, a simulation exercise on how to respond to an activist and placing a rights plan on the "shelf."

Considerations for Shareholder Meetings in Light of COVID-19

Stephen F. Arcano, Brian V. Breheny, Marc S. Gerber, Allison L. Land

The Centers for Disease Control and Prevention's recommendation to avoid large gatherings coincides with annual meeting season for many corporations. As a result, corporations are contemplating virtual annual meetings of stockholders, either in lieu of an in-person meeting or as a complement to an in-person meeting. This requires navigating public health concerns, the requirements of state corporate law, SEC proxy rules, and the policies and perspectives of investors and proxy advisory firms.

Authority To Hold Virtual (or Hybrid) Meetings

Many states, including Delaware, permit virtual meetings for annual and/or special meetings. Specifically, Delaware General Corporation Law (DGCL) Section 211 provides that Delaware corporations may hold shareholder meetings by means of "remote communication." If the bylaws of a Delaware corporation authorize the board of directors to determine the place of a meeting of stockholders, the board of directors may, in its sole discretion, determine that the meeting shall not be held at any place but may instead be held solely by means of remote communication.

Some other states restrict the ability to hold a virtual meeting. New York, for example, permits hybrid meetings but prohibits virtual-only meetings. A hybrid meeting occurs in a physical location but also allows participation via remote communication, giving shareholders the option to elect whether to attend in person or remotely.

Switching From Physical to Virtual (or Hybrid) Meetings

To put shareholders on notice that the corporation might switch from a physical to a virtual-only or hybrid meeting in light of the dynamic nature of COVID-19, the corporation should consider adding disclosure to its proxy statement alerting investors to the possibility that the meeting format may change. A corporation also may determine to hold a hybrid meeting but reserve the right to cancel the in-person portion of the meeting, effectively reserving the right to convert the meeting to a virtual-only format.

Notice and Proxy Statement Disclosure

In the event a corporation decides to hold a virtual-only or hybrid meeting, it should disclose in the proxy statement:

- The rationale for choosing to hold a virtual meeting (*i.e.*, due to COVID-19);
- How shareholders can access, participate and vote in the meeting;
- The availability of technical assistance to shareholders; and
- With respect to virtual-only meetings, whether a replay of the meeting will be available to shareholders after the meeting and whether answers to questions not addressed during the meeting will be posted online.

If the decision to switch from a physical to a virtual (or hybrid) meeting is made after the proxy statement is mailed, the corporation should issue a press release and file the release with the SEC as supplemental proxy materials. The change should be announced as early as possible ahead of the meeting in order to give shareholders time to adjust. Additionally, if converting

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to a virtual meeting after providing proxy materials that did not disclose such a possibility, the corporation should consider whether to distribute an updated notice of meeting to shareholders as of the record date, if time permits. The corporation also should ensure it takes all reasonable steps necessary to inform other intermediaries in the proxy process and other relevant market participants (such as the appropriate national securities exchanges) of the change.

Securities Laws and Exchange Considerations

Exchanges: Nasdaq and NYSE permit virtual meetings. Nasdaq also requires that shareholders are afforded the opportunity to discuss corporation affairs with management at each annual meeting.

Federal Securities Laws: The federal securities laws do not prohibit holding a virtual meeting.

Logistics

Required Measures. Corporations should consider the applicability of any state corporate law. For example, DGCL Section 211 requires that a corporation holding a virtual meeting:

- Implement reasonable measures to verify that each person deemed present and permitted to vote at the meeting by means of remote communication is a stockholder or proxyholder;
- Implement reasonable measures to provide such stockholders and proxyholders a reasonable opportunity to participate in the meeting and to vote on matters submitted to the stockholders, including an opportunity to read or hear the proceedings of the meeting substantially concurrently with such proceedings; and
- If any stockholder or proxyholder votes or takes other action at the meeting by means of remote communication, a record of such vote or other action must be maintained by the corporation.

Handling Questions: Q&As can be handled in three main ways in a virtual meeting, and prior to the meeting, the corporation should establish general rules of procedure (e.g., timelines/limits for questions and addressing the ordering of questions).

- Live Questions via Telephone: Similar to an earnings call, with an operator managing a queue of shareholders who will ask questions via telephone using a dial-in number.
- Live Questions via Text: Shareholders may submit questions in text during the meeting through the virtual platform. These questions typically are not seen by other shareholders.
- Presubmitted Questions: A corporation may require shareholders to submit all questions in advance.

In 2019, 96% of corporations allowed questions to be submitted online during the live meeting, about 16% allowed questions to be presubmitted online and about 3% allowed live phone line questions during the meeting, according to Broadridge, a leading provider of virtual meeting platforms.

Other Considerations

Recent SEC staff guidance encourages corporations, to the extent feasible under state law, to provide shareholder proponents or their representatives with the ability to present their proposals through alternative means (e.g., by phone or prerecorded audio/video). In 2019, 29 of the 326 virtual meetings hosted had shareholder proposals. Of these proposals, 27 were presented through operator-assisted phone lines, one was presented in person, and one was prerecorded and presented during the meeting, also per Broadridge.

Currently, ISS does not have a formal policy on virtual shareholder meetings in its U.S. guidelines. Glass Lewis adopted a policy on virtual shareholder meetings in 2019 providing for adverse voting recommendations against director nominees who serve on the governance committee of a corporation that holds virtual-only meetings without sufficient disclosure about shareholder participation rights. Such disclosure would include:

- Procedures for allowing shareholders to vote during the meeting;
- Location of posted questions and answers; and
- Instructions on how to access the virtual-meeting platform.

Historically, many investor groups have opposed virtual-only meetings of shareholders while acknowledging the potential benefits of supplementing in-person meetings with virtual meetings. For example, the New York City Comptroller's Office has said it will recommend that the New York City pension funds adopt a policy to vote against directors at corporations that continue to hold "virtual-only" meetings. While many institutional investors may not object to a virtual-only format for a routine annual meeting, they could object to this format when the meeting involves a vote on a contested matter, or at a special meeting. In addition, some providers of virtual-meeting platforms historically would not host contested shareholder meetings.

Nevertheless, investors and proxy advisory firms that are opposed to virtual-only meetings (including both Glass Lewis and the New York City Comptroller's Office) have expressed openness to virtual-only meetings for this year as a result of COVID-19. For example, the executive director of the Council of Institutional Investors said, "Given coronavirus concerns, it is reasonable that some corporations will go to virtual-only this

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spring, but we hope they will make it clear that this decision was one-off and that they follow best practices for making any virtual meeting participatory.”

We expect shareholders are likely to be generally understanding, particularly if an electronic live-question format is available, in light of the current situation.

For more information on these considerations, see our [March 4, 2020 client alert on this topic](#) and [“Matters To Consider for the 2020 Annual Meeting and Reporting Season.”](#)

Director Duties

By Edward B. Micheletti

Delaware law offers straightforward, basic principles that guide boards of directors through even the most complicated circumstances. These include the well-defined fiduciary duties of care and loyalty (which encompass disclosure and oversight responsibilities) and the business judgment rule, which prevents a court from second-guessing good faith, well-informed decisions by boards comprised of a majority of disinterested and independent directors. Focusing on these core Delaware corporate law principles, whether as part of normal business operations or during a time of crisis, should allow directors to avoid fiduciary breaches and protect against exposure to potential liability. For more information, see our February 19, 2020, client alert [“Directors’ Fiduciary Duties: Back to Delaware Law Basics.”](#)

Issues Surrounding Debt/Equity Repurchases

By Michael J. Zeidel

The extreme volatility in the capital markets has created opportunities for issuers to repurchase their debt and equity securities at attractive prices. The ability to consummate these transactions requires careful consideration of contractual, disclosure, securities law, corporate law, tax and accounting issues. For example, covenants in credit agreements and bond indentures, such as limitations on restricted payments, may restrict such activity or require the issuer to meet a financial ratio (such as a fixed-charge coverage ratio) in order to proceed with the transaction. The federal securities laws only permit purchases to be made when the issuer is not in possession of material nonpublic information, which will require an analysis of the impact of COVID-19 on the issuer’s results of operations, prior disclosure and previously announced guidance. Depending on the magnitude and manner of the repurchases, the tender offer rules may be unintentionally

implicated, which could require the issuer to make an offer to repurchase securities from other holders of the class. State corporate laws may only permit equity repurchases to be made out of “surplus” and thus limit the amount that can be repurchased. Finally, the repurchase of debt at a discount may result in cancellation of indebtedness income and impact the use of net operating losses.

Corporate Restructuring Challenges

By Michelle Gasaway, Paul Leake, George N. Panagakis

Companies dealing with liquidity or leverage issues also should consider liability management alternatives. In situations in which companies believe they have adequate liquidity but their outstanding bonds are trading at a discount to par, cash tender offers or privately negotiated repurchases can be utilized to buy back debt and capture the discount. If liquidity needs to be preserved, debt-for-debt transactions, whether by formal exchange offer or privately negotiated exchanges, can be structured to both extend debt maturities and capture discount opportunities. Companies with more complex capital structures also can consider “uptier” debt-for-debt exchanges, which may allow the company to extend debt maturities and/or capture discount in return for the new bonds being placed in a higher priority position than the original bonds, such as exchanging an unsecured bond for a secured bond. In connection with any such liability management transaction, restrictive covenants in the original debt instrument can be amended or eliminated if there is sufficient participation in the transaction (typically a majority of the outstanding principal amount) to further alleviate constraints on a company.

As described in [“Issues Surrounding Debt/Equity Repurchases”](#) above, the ability to consummate these types of liability management transactions requires careful consideration of a number of contractual, disclosure, securities law, and tax and accounting issues. Additionally, an evaluation of the covenants and restrictions of all debt instruments is needed — both for determining whether the liability management transaction itself is permitted as well as for determining which restrictive covenants are imposing constraints on the company. Coordinating the amendment of credit facilities along with various debt exchanges also can enhance the prospect of extending liquidity and capturing discount.

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Liquidity Issues and Access to Funding

By Seth E. Jacobson, Michael J. Zeidel

As the coronavirus continues to disrupt the economy, the financial markets and our way of life in general, companies are focusing on liquidity and access to funding.

Revolver Availability

For companies with committed revolving credit facilities, drawing on such facilities is the most likely source of additional liquidity. Companies need to be aware of both (i) drawing conditions and (ii) the effect of drawings on any financial covenants as they determine whether and when to draw on their revolving credit facilities. The conditions to borrowing often include representations as to solvency and the absence of any event, change, condition or development that has had or could reasonably be expected to have a material adverse effect. Determination of the absence of a material adverse effect is highly fact-specific and also depends on the wording of the contract. However, case law has indicated that for a material adverse effect to occur, the adverse effect must be both significant and durational.

In the context of an asset-based loan (ABL), there are a few more considerations relating to the size of the drawing. ABL borrowers will want to leave enough cushion to account for potential imposition of reserves and declines in the borrowing base due to the current economic environment. Borrowers should be aware that several features of ABLs depend on the percentage of the line or the borrowing base that is drawn. For example, increased borrowings could trigger testing of the financial covenant, cash dominion and weekly borrowing base reporting and could eliminate certain investments, restricted payments and payments of other debt baskets.

In addition, publicly reporting companies electing to draw on their revolving credit facilities need to consider appropriate disclosure, including issuing press releases and filing a Form 8-K. A publicly traded company is required to file an 8-K when it enters into a material agreement, which often includes the entry into a debt agreement, such as a revolving credit facility. Typically, a draw-down on a revolving credit facility would not trigger an independent disclosure. However, a borrower may determine that the filing of an 8-K or other public disclosure is appropriate in connection with a draw-down based on the facts and circumstances of the specific situation. For example, disclosure may be required when the draw-down is material, either in the amount drawn or if the draw-down represents a material deviation from the company's historical practice or existing sources of liquidity. When determining whether an 8-K or other

public disclosure is appropriate, companies should consider, among other factors, the amount of the draw; the company's normal course of dealing; the company's current financial position; the intended use of proceeds of the draw; whether the draw would make a series of previously undisclosed individually immaterial obligations material in the aggregate; and whether the draw would make some existing public disclosure inaccurate, particularly disclosure included in the issuer's Management's Discussion and Analysis (MD&A).

Additional Sources of Capital

Companies seeking additional capital beyond drawings on existing lines of credit should consider other available sources of capital, including from direct or nonbank lenders. These other sources could include, among other things, financing secured by unencumbered assets, second or other junior lien debt, mezzanine or holdco debt, subordinated debt or preferred stock.

Impact on Energy and Infrastructure Projects

By Lance T. Brasher, Sean Shimamoto

Force Majeure Requirements

Whether an event constitutes "*force majeure*" under a contract involves a highly fact-specific analysis, and depends largely on the requirements of the contract. Typically, a *force majeure* event must be unforeseeable and beyond the reasonable control of the party making the claim. It may not be the result of any unreasonable acts of the party relying thereon, and it could not be avoided or mitigated by the exercise of reasonable precautions. Under some contracts, any event that satisfies the foregoing requirements, including an epidemic, constitutes *force majeure*; however, in many others, it must be specifically listed as an event that may qualify as *force majeure*.

In the project finance world, contracts often require an affected party to demonstrate that a *force majeure* event has specific impact, such as affecting a critical milestone in a project schedule, and often impose limitations on the timing of making *force majeure* claims. The remedies also may be prescribed: Does it excuse nonperformance? Does it allow for a change in the price or scope? Does it extend the time for performance? Projects often allow the non-affected party to terminate the contract if the affected party is unable to perform for an extended period of time, such as six months or a year. It is important for parties to these contracts to understand the requirements of the *force majeure* provisions. While loan and other project financing agreements do not contain *force majeure* provisions excusing the borrower for nonpayment, loan agreements may nevertheless

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contain many provisions relating to whether the borrower or its counterparties are affected by *force majeure* under a project contract. Lenders should carefully examine the effect of *force majeure* under financing documents, such as whether a borrower is obligated to give lenders a notice of *force majeure*, whether such *force majeure* constitutes a default under the loan agreement, or whether lenders must fund in the presence of this *force majeure* event. Understanding project documents and a project owner's rights under such documents vis-a-vis the project counterparty informs the analysis of what rights lenders have under financing documents.

Supply Delays May Affect Eligibility for Renewable Energy Tax Credits

Global supply chain disruptions are raising significant concerns among developers and investors in renewable energy projects that delivery of components (*e.g.*, turbines, modules, transformers, inverters, etc.) necessary to build such projects will be delayed, thereby negatively affecting eligibility for tax credits, which are dependent on when construction begins and is completed. One way to begin construction for tax credit purposes is to incur at least 5% of the project costs. Accordingly, many solar developers executed purchase orders at the end of 2019 for various components. Although the rules provide that taxpayers incur costs on the date of payment if, on the date of payment, they reasonably expect delivery of such components within three and a half months, it remains to be seen whether some investors will be uncomfortable asserting a begin-construction date in reliance on components that are not actually delivered within three and a half months due to supply chain disruptions caused by COVID-19. In addition, once construction begins, unless it is completed within a four-year safe harbor, the taxpayer must prove that it has been continuous since they began construction based on the facts and circumstances. Thus, wind projects that began construction in 2016 (the last year of eligibility for 100% of the tax credits), must complete construction in 2020 in order to avoid needing to prove continuity since 2016 based on the facts and circumstances. Although delivery delays caused by COVID-19-related disruptions should fall within the list of excusable disruptions set forth by the IRS, due to the uncertainty in the application of the facts-and-circumstances continuity requirement, many investors will be uncomfortable with projects that fall outside of the four-year safe harbor. It is unclear at this point whether Congress will grant extensions.

Regulatory

Antitrust-Related Considerations

By Clifford H. Aronson, Karen M. Lent, Giorgio Motta, Tara L. Reinhart, Steven C. Sunshine, David P. Wales

Collaborations With Competitors

Companies seeking to collaborate with competitors in response to the COVID-19 crisis must keep in mind, as the Department of Justice has recently cautioned, that the antitrust laws remain in effect, and agreements among competitors that set commercial terms may be illegal. Nevertheless, companies may collaborate in order to promote important public and commercial interests under certain circumstances. For example, information sharing and collaborations between companies to improve virus response, minimize supply chain disruption, or promote health and safety benefit the public and are thus unlikely to violate the antitrust laws, provided the companies continue to otherwise compete and do not also agree to set commercial terms. Companies also have the right, under the *Noerr-Pennington* doctrine, to collectively petition the government, including in connection with lawmaking and policy changes contemplated in response to the crisis. Finally, as federal agencies have stated following previous natural disasters, collaborations to combine critical resources or services to meet consumer needs or to combine distribution networks to bring goods to consumers in a more efficient or speedy fashion can be procompetitive as long as they are narrowly focused and limited in scope. Companies that are considering collaborations with competitors in response to the COVID-19 crisis should consult with legal counsel before proceeding.

Anti-Price-Gouging Statutes

Companies considering even small price increases in response to changes in supply and demand in the wake of the COVID-19 outbreak should be aware of anti-price-gouging (APG) statutes. While no U.S. federal statute is specifically designed to combat price gouging, at least 34 states and the District of Columbia have explicitly enacted APG statutes or regulations that generally prohibit excessive price increases on certain categories of goods and services upon the occurrence of a triggering event, typically a declared state of emergency. COVID-19 has raised significant concerns among state attorneys general about the practice of price gouging. For example, New York Attorney General Letitia James recently issued numerous cease-and-desist letters to merchants charging exorbitant prices for hand sanitizer and disinfectant spray and emphasized her office would continue to investigate reports of price gouging throughout the state. In some states (*e.g.*, California) price increases on essential goods

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of as little as 10% can and will trigger enforcement, punishable by significant per-violation civil or criminal monetary penalties or even imprisonment. Companies that operate marketplaces on which third parties sell their goods also should ensure that price gouging is not occurring on their platforms. In Europe, antitrust agencies are closely monitoring potential price changes in the context of COVID-19. For example, some companies are under investigation by Italian antitrust regulators after prices for products such as hand sanitizer and disinfectant skyrocketed as the coronavirus outbreak intensified.

US Merger Control

Both the Department of Justice and the Federal Trade Commission have instituted temporary procedures for the electronic filing of Hart-Scott-Rodino forms, with the FTC prohibiting hard-copy filings altogether. The FTC also has announced that it will cease granting early termination of the HSR waiting period for all transactions. Both agencies also announced other changes to merger processes. The DOJ will temporarily: (i) request that merging parties subject to in-depth investigations agree to certain timing agreement revisions, including adding an additional 30 days to complete the DOJ's review; (ii) conduct all meetings by phone or video conference, absent extenuating circumstances; and (iii) postpone depositions and reschedule using secure videoconferencing capabilities. The FTC likely will implement similar changes and has announced that most personnel will be working remotely and prohibited from traveling, and that almost all internal and external meetings will be done via telephone or videoconference.

EU Merger Control and State Aid

The European Commission is encouraging companies to delay merger notifications until further notice, where possible. The Commission is adopting every measure to ensure business continuity but, at this stage, is likely to prioritize its resources on the open, ongoing merger investigations. Other antitrust authorities have issued similar statements, imposing or recommending a delay in merger notifications, and review periods are impacted as a result of constraints in remote working capabilities by a number of agencies. In parallel, the Commission has pledged to fast-track the state aid review of support measures by EU national governments to help companies affected by the COVID-19 crisis access vital liquidity and ensure their commercial viability. The first COVID-19-related state aid package, presented by Denmark, was approved on March 12, 2020, in just 24 hours, and many more are expected to follow. Dedicated guidelines for COVID-19-related state aid are expected to be released in the coming days to cover direct subsidies and tax cuts to companies up to a certain amount. Such guidelines are also expected to cover state guarantees for loans taken by companies

from banks, subsidized public loans to companies and specific rules allowing banks to channel state aid directly to companies in need. For additional information, see our March 16, 2020, client alert "[European Commission Delays Merger Notifications Until Further Notice, Develops Emergency State Aid Response to COVID-19 Outbreak.](#)"

Families First Coronavirus Response Act

By David E. Schwartz, Risa M. Salins, Brittany Ellenberg

On March 14, 2020, the United States House of Representatives passed H.R. 6201, the Families First Coronavirus Response Act. On March 16, 2020, the House introduced H. Res. 904 directing the clerk of the House to make certain corrections to H.R. 6201. The Senate passed and the President signed the bill on March 18, 2020.

Emergency Leaves for Employees

Both the Emergency Family and Medical Leave Expansion Act and Emergency Paid Sick Leave Act will be effective not later than 15 days following the enactment of the legislation and will expire on December 31, 2020. Both acts apply to employers with fewer than 500 employees and also grant the secretary of labor authority to issue regulations to exclude health care professionals and emergency responders from the acts and to exempt small businesses with 50 employees or less, if the requirements of the acts would jeopardize the viability of the business. Potential overlap between the acts may be subject to clarification by the legislature. Under both acts, an employer of an individual who is a health care provider or emergency responder may choose to exclude such employee from coverage.

Emergency Family and Medical Leave Expansion Act

H.R. 6201 covers those who have been employed by the employer for at least 30 days. Eligible employees will be provided with up to 12 weeks of job-protected leave under the Family and Medical Leave Act (FMLA) if the employee is unable to work (or telework) due to a need for leave to care for the employee's child if the child's school or place of care has been closed, or the child care provider is unavailable, due to an emergency with respect to COVID-19 declared by a federal, state or local authority. During the first 10-day period, the FMLA leave may be unpaid; however, employees may choose to use accrued vacation, personal leave or sick leave during this period. Following the first 10 days, employers must then provide eligible employees with pay at a rate of at least two-thirds of the worker's regular rate of pay at the number of hours the employee would normally be scheduled to work. The paid leave may not exceed \$200 per day and \$10,000 in aggregate.

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Emergency Paid Sick Leave Act

H.R. 6201 also will require covered employers to provide full-time employees with two weeks (80 hours) of immediate paid sick leave and part-time employees with immediate paid sick leave based on the number of hours the part-time employee works, on average, in a two-week period. Qualifying reasons for the use of emergency paid sick leave include if the employee:

- i. is subject to a federal, state or local quarantine or isolation order related to COVID-19;
- ii. has been advised by a health care provider to self-quarantine due to concerns related to COVID-19;
- iii. is experiencing symptoms of COVID-19 and seeking a medical diagnosis;
- iv. is caring for an individual who is subject to an order as described in (i) or has been advised as described in (ii);
- v. is caring for a son or daughter if their school or place of care has been closed, or their child care provider is unavailable due to COVID-19 precautions; or
- vi. is experiencing any other substantially similar condition specified by the Secretary of Health and Human Services in consultation with the Secretary of the Treasury and the Secretary of Labor.

An employee who meets the qualifications in (i), (ii) or (iii) should be paid at their regular rate for the two-week period. If the employee is caring for a family member who meets one of the qualifying conditions in (iv), (v) or (vi), the employee should be paid for two weeks (80 hours) of paid sick leave at two-thirds of the employee's regular rate of pay. An employer may not require an employee to use other paid leave prior to using the emergency paid sick leave provided under this act. Paid sick leave pay shall not exceed \$511 per day if used for the qualifying reasons described in (i), (ii) or (iii), or \$200 per day for reasons described in (iv), (v) or (vi).

Emergency Unemployment Insurance Stabilization and Access Act

The bill also introduces the Emergency Unemployment Insurance Stabilization and Access Act, which provides \$1 billion in funds for emergency grants to states for activities related to processing and paying unemployment insurance benefits. Of those funds, \$500 million is allocated to all states that (i) require employers to provide notification of unemployment compensation to eligible employees; (ii) ensure that employees have at least two methods to apply for unemployment compensation (e.g., in-person, by phone or online); and (iii) notify applicants

when an application is received and being processed. The other \$500 million is allocated to emergency grants to states that experience a 10% or more increase in unemployment over the same quarter in the previous calendar year.

Tax Credits for Emergency Paid Sick Leave and Family and Medical Leave

The bill also provides tax credits for employers providing emergency FMLA leave and emergency paid sick leave as a credit against the tax imposed by Section 3111(a) of the Internal Revenue Code. Employers will receive a tax credit equivalent to 100% of the qualified emergency FMLA and paid sick leave wages required to be paid by the Emergency Family and Medical Leave Expansion Act and the Emergency Paid Sick Leave Act.

Political Law Considerations

By Ki P. Hong

Disclosing Issues Under Lobby Registration and Reporting

As federal, state and local governments are making unprecedented decisions to address the COVID-19 crisis, it is as important as ever for businesses to ensure that their interests are being protected. When communicating with public officials regarding these decisions, one has to comply with the various registration and reporting rules regarding lobbying activity. These rules require disclosure of, among other items, the government decision being lobbied. Depending on the business, publicly describing such decisions may raise shareholder or public relations concerns. Many of the lobbying laws allow a filer to exercise a certain level of discretion in describing the issues lobbied.

Assisting Governments in Addressing COVID-19

Governments at the federal, state and local levels are seeking help from private industry to address the COVID-19 crisis. This may range from in-kind donations for direct use by the government or constituents (such as parking lots, facilities and free services) to writing a check to a charity. Different restrictions and prohibitions exist depending on how such assistance is structured, particularly regarding the entity or person on whose behalf the assistance is provided. For example, if a business provides free services at the personal request of an official, it may qualify as an illegal gift to him or her, whereas a gift to a governmental entity is generally permitted. The permissibility of a gift to a private charity at the request of an official may, depending on the jurisdiction, be prohibited under certain government ethics rules.

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COVID-19: US Tax Considerations

By Nathaniel Carden, Nickolas Gianou, Alec J. Jarvis, B. Chase Wink

As the COVID-19 pandemic continues to generate unprecedented volatility and uncertainty in the global capital markets, taxpayers should begin planning for a downturn. Although no one is yet able to predict the potential length of such a downturn, we have described below a number of tax planning ideas and related considerations that may be relevant to taxpayers going forward.

Tax Reform Limitations on Deductions

A little over two years ago, Congress enacted the most significant U.S. tax reform legislation since 1986, the Tax Cuts and Jobs Act (the TCJA), which included a number of limitations on the use of certain tax losses and deductions. The market disruption caused by the coronavirus is likely to exacerbate the effects of these provisions.

For example, under the TCJA, net operating losses (NOLs) arising after 2017 generally cannot be carried back and, when carried forward, can offset no more than 80% of taxable income. Thus, a taxpayer that recognizes a \$100x NOL in 2020 and \$100x of positive taxable income in 2021 will have to pay tax on \$20x of the 2021 income, even though over the two-year period it broke even. As a result of these new limitations, losses and other deductions are in general more valuable from a cash-tax perspective when they are used to offset current-year income rather than carried forward to offset future-year income. The effect of these limitations will be particularly acute if a coronavirus-driven downturn causes taxpayers to incur significant NOLs.

Similarly, Section 163(j) of the TCJA sharply limits the ability of businesses to deduct interest payments when calculating their taxable income. Under this new limitation, a taxpayer's allowable deduction for interest expense in a particular tax year is generally limited to the sum of its business interest income plus 30% of "adjusted taxable income" (taxable income with certain adjustments), with any excess carried forward to future years. As a result, a distressed taxpayer can easily find itself owing cash taxes even when it has suffered an overall economic loss — for example, where its adjusted taxable income is \$100x and its interest expense exceeds \$100x, in which case its interest deduction would be limited to \$30x and it would owe cash taxes on \$70x. Many taxpayers that targeted debt levels in order to keep their interest expense within the Section 163(j) limits may find that the coronavirus has unexpectedly put them in this position.

Taxpayers that expect to face the foregoing limitations might consider structuring and planning techniques to mitigate the effects of those limitations. For example, taxpayers expecting to run a current-year loss that would otherwise become an NOL should consider whether it is an appropriate time to engage in taxable transactions with built-in gain assets, including cash sales of unwanted assets, sale/leaseback transactions, taxable spin-offs of unwanted business lines and other income-acceleration transactions. Such transactions would increase the use of current-year losses, thus reducing the amount of NOLs that will become carryforwards subject to the 80% limitation, and may permit the taxpayer to do a transaction that would be tax-prohibitive in a more profitable year. In addition, for a taxpayer running into the Section 163(j) limitation, a sale/leaseback transaction of leveraged property may have the additional benefit of converting 163(j)-limited interest expense into economically similar but unlimited rent expense.

Debt Restructuring Issues

Many taxpayers will need to modify or otherwise restructure their debt in the event of a prolonged downturn. This can raise a host of tax issues. For example, a debtor that retires debt for less than its principal amount or modifies debt at a time when it is trading at a discount may recognize cancellation-of-indebtedness income (CODI) that results in an immediate cash tax owed, even though the debtor is in financial distress. Similarly, modified debt that trades at a discount may become subject to the applicable high-yield discount obligation (AHYDO) provisions, a punitive set of rules that defer and even wholly disallow a significant portion of the debtor's interest deductions.

In the aftermath of the 2008 financial crisis, Congress provided important relief on these issues, temporarily suspending the AHYDO rules in certain circumstances and creating an election for taxpayers to defer CODI for up to five years (with the income to be recognized ratably beginning at the end of the initial five-year deferral period). It remains to be seen what measures Congress may adopt in response to a coronavirus-triggered downturn.

International Tax Issues — Offshore Cash as a Potential Source of Liquidity

The TCJA included a dividend exemption system that generally exempts from U.S. federal income tax dividends received by U.S. corporate parent companies from their 10%-or-more-owned foreign subsidiaries, provided that a one-year holding period and certain other requirements are met. This could provide a source of liquidity in a downturn as the new system theoretically allows U.S. corporations to access foreign subsidiaries' cash at a significantly reduced U.S. tax cost as compared with the pre-TCJA system.

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However, the dividend-exemption system has a number of limitations that could materially reduce its ability to provide a much-needed liquidity valve in a downturn. First, the dividend-exemption system only applies to earnings that have not already been subject to tax under the Subpart F and GILTI regimes. For many taxpayers, a substantial portion (if not all) of their earnings are taxed under Subpart F or GILTI and are then able to be distributed to their U.S. parent as previously taxed earnings and profits (PTEP). While distributions of PTEP are generally tax free for U.S. federal income tax purposes, such distributions may result in taxable gain if the amount of the distribution exceeds the U.S. shareholder's basis in the first-tier foreign subsidiary's stock. The relevant stock basis rules, including the timing of basis increases resulting from Subpart F or GILTI inclusions and basis decreases resulting from distributions of PTEP, are complex and should be considered carefully in connection with any material distributions of PTEP.

In addition, the dividend exemption system does not apply to all non-PTEP earnings. For instance, "hybrid dividends" (*i.e.*, dividends for which the foreign corporation receives a deduction or other income-tax benefit) are ineligible, and the IRS has promulgated temporary regulations that would exempt only 50% of dividends to the extent attributable to earnings generated during the so-called "gap year" for noncalendar-year corporations (*i.e.*, between January 1, 2018, and the foreign corporation's year-end for the year that included but did not end on December 31, 2017 — *e.g.*, November 30, 2018, for a November 30 taxpayer).

Finally, the dividend exemption system does not apply to sales of stock of foreign corporations, except to the extent the gain on such sales is treated as a dividend under Section 1248. Accordingly, such sales are unlikely to be a U.S.-tax-efficient means of seeking liquidity in a downturn scenario. Other structures (such as a check-and-sell involving a deemed liquidation by way of a U.S. check-the-box election followed by a sale of the disregarded entity), however, may be worth exploring.

Other International Tax Considerations

Other elements of the TCJA's overhaul of the U.S. international tax system may require careful attention from taxpayers in the event of a downturn. First, earnings subject to GILTI (which applies to a controlled foreign corporation's total net income, less a 10% "routine" return on such corporation's aggregate tax basis in its tangible, depreciable property), are generally thought of as being taxed at a 10.5% rate, which represents the current U.S. federal corporate income tax rate of 21% and a 50% deduction under Section 250 of the Internal Revenue Code, which serves to cut the general corporate rate in half. A similar

deduction applies to "foreign-derived intangible income" (FDII) to arrive at its baseline rate of 13.125%. These deductions are reduced, however, to the extent a domestic corporation's FDII and GILTI exceeds its overall taxable income in a taxable year (*i.e.*, if the corporation is in a loss position aside from FDII and GILTI). The IRS has released proposed regulations that would, when finalized, provide that the domestic corporation's overall taxable income for purposes of this limitation is computed taking into account any deduction for carried-forward NOLs, as well as any allowed interest deduction. In effect, purely domestic losses (*i.e.*, losses aside from FDII and GILTI) or carried-forward NOLs first reduce purely domestic income (*i.e.*, non-FDII and non-GILTI income) taxable at a 21% rate, but any excess then reduces the lower-rate FDII and GILTI pro rata. Accordingly, taxpayers that want the full benefit of the Section 250 deduction for GILTI and FDII in a taxable year and would otherwise be in a loss position domestically should consider engaging in transactions that accelerate taxable income to free up a portion of the GILTI or FDII deduction.

In addition, the foreign tax credit system applicable to GILTI no longer employs a "pooling" system, which had the effect of smoothing year-by-year variations in income and taxes paid. Instead, taxes attributable to GILTI must be used, if at all, in the year incurred. This "use it or lose it" system means that a taxpayer whose foreign subsidiaries incur income taxes attributable to GILTI is likely to bear double tax if it is unable to credit such tax in the relevant year (because of insufficient income in the relevant basket or otherwise). For example, taxes incurred by a controlled foreign corporation that has a "tested loss" (*i.e.*, a loss for GILTI purposes) in a tax year are per se noncreditable. In anticipation of a potential downturn, taxpayers should consider whether there are foreign restructuring steps that could maximize the ability to utilize foreign tax credits to mitigate the effects of this "use it or lose it" system. If the tested loss entity were held directly by an entity that reliably generates "tested income," for instance, a step as simple as "checking the box" on the tested loss entity could, depending on the facts, result in the tax credits becoming utilizable.

Multinational Enterprise Supply Chains

The COVID-19 pandemic has created significant disruptions to many multinational enterprise (MNE) supply chains and limited the ability of MNE personnel to travel on business, raising a number of important international tax considerations.

As an initial matter, in many MNEs, the directors of many subsidiaries are corporate executives who have significant relevant experience (*e.g.*, as commercial directors or legal or finance professionals) and often are residents of other countries. As a

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result of recent international travel bans and the closure of many borders to nonresidents, many of these executives may not be able to convene in each jurisdiction containing a subsidiary for which they act as a director. In certain tax systems, and subject always to any treaty override, this may call into question the tax residency of the subsidiary, because the location of meetings that differ from where they have historically been held may lead a tax authority to eventually conclude that the subsidiary is now managed elsewhere. Similarly, countries could potentially assert that directors or managers who are employed by one subsidiary but who may live in another country (e.g., a neighboring European jurisdiction) create a permanent establishment for their employer subsidiaries. We are hopeful that tax authorities will take a flexible approach to the application of these tests in light of the restrictions on movement created by COVID-19. Although some limited precedent exists for discretion being operated by authorities favorably in prior situations of constraint on movement, this remains an area of uncertainty. Equally, the new substance rules recently imposed on certain financial centers by OECD and the EU also have become more challenging to follow in certain cases. Tax authorities in some jurisdictions have been approached for guidance, in a similar vein to approaches to statutory organs regarding regulatory relief.

Second, the inability to travel may impede the ability of the employees of MNE subsidiaries to undertake their day-to-day activities that support the development, enhancement, maintenance, protection or exploitation (e.g., so-called DEMPE functions in OECD Transfer Pricing Guidelines parlance) of the MNE's intangibles. In many countries, particularly in Europe, the performance of these functions is a key part of the allocation of income between jurisdictions. Likewise, while the U.S. regulations do not follow the DEMPE-based approach as closely as some other countries' rules do, U.S. MNEs also must manage the U.S.'s Subpart F rules, which result in current (and full-rate) taxation of the income of foreign subsidiaries unless certain requirements are met. One frequently relevant requirement is that the subsidiary manufacture the products it sells. In modern global supply chains involving significant outsourcing, this is often done through managers who oversee critical manufacturing functions, rather than employees who actually perform the physical manufacturing (often referred to as "substantial contribution"). These managers may now be unable to perform their typical duties due to governmental travel restrictions or generally applicable corporate repatriation policies for expatriates, creating doubt as to whether the functions normally relied upon to satisfy these tests can be performed by anyone within the MNE organization.

Finally, the economic disruptions created by COVID-19 will create new and additional business decisions, as companies reevaluate investments and change their operations, as well as their sources for materials or know-how, in order to adapt to changing circumstances. These decisions also are likely to be important in any evaluation of either DEMPE functions or substantial contribution, so MNEs should ensure that, to the extent feasible given other COVID-19-related restrictions, they are performed in a manner consistent with existing tax positions or taken into account in assessing new positions.

Litigation

Judicial Response to COVID-19 Crisis

By John H. Beisner

To date, federal and state courts nationwide have responded to the COVID-19 crisis by issuing highly individualized temporary rules and directives. Generally, the courts remain open for business, attempting to address civil litigation motions and case management issues as normally as possible. However, many have curtailed live appearances, canceling hearings or opting to conduct them telephonically. Many appellate courts, including the U.S. Supreme Court, are postponing oral arguments, and some state appellate courts have simply canceled arguments, indicating that pending matters will be decided on the paper record unless the parties are granted leave to present oral argument at a later date.

Consistent with government directives to limit group activities, most courts have postponed all trials to avoid exposing potential jurors to the coronavirus. Some are beginning to cope with a growing wave of extension requests in civil cases, as counsel encounter difficulties meeting existing deadlines, particularly those implicating discovery. Many depositions are being postponed, as witnesses and counsel become unwilling to travel. Other discovery is lagging, as many businesses are now working remotely, resulting in limited ability to make corporate personnel available for interviews or to gather documents/data. In response, courts have begun to issue orders declaring omnibus 21- to 30-day extensions of all deadlines. Of note, such orders specifically exempt deadlines (particularly those regarding the initiation of appeals) that trial courts lack authority to adjust.

Although most courts are attempting to maintain a business-as-usual atmosphere, civil litigation activity likely will be curtailed to an increasing degree as "stay-at-home" policies are imposed by local officials, resulting in substantial, widespread delays in litigation matters nationwide.

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Reduced IRS Audits and Litigation

By Christopher P. Murphy

IRS audit activity is likely to decrease significantly or may cease altogether as steps are taken to slow the transmission of COVID-19. As of March 16, 2020, the U.S. Office of Personnel Management has decided to keep open federal offices in Washington, D.C., with “maximum telework flexibilities to all current telework eligible employees, pursuant to direction from agency heads.” Considering the rapidly evolving landscape, it is highly likely that federal offices will close or mandate teleworking. Moreover, because so many audits of large companies take place onsite, and because many of the country’s largest employers (such as Google) have temporarily closed their offices, it seems inevitable that audit activity will slow considerably in the coming weeks and maybe even months, as taxpayers and the IRS will be unable to meet in person. Finally, as of March 16, 2020, certain areas of the country have enacted “shelter-in-place” requirements that prohibit individuals from leaving their homes other than for essential reasons. This delay in audit activity likely will lead to increased requests from the IRS to extend statutes and other deadlines, such as the estimated completion date for certain audit cycles.

Taxpayers should continue to meet current audit deadlines when possible. To the extent that is not possible, taxpayers should request extensions from their exam teams with a brief explanation as to why an extension is needed (*e.g.*, employees are unable to gather information due to office closures). Open-ended extensions should be requested as the situation remains very fluid, and it is uncertain when employees will be able to return to their offices.

It seems almost inevitable that courts will close or significantly decrease services. The Tax Court already has taken such steps. As of March 13, 2020, the Tax Court closed its buildings to visitors and canceled scheduled trial sessions through the end of April 2020. Unresolved cases will be rescheduled for trial. As of March 16, 2020, certain federal district courts and appellate courts remain operational. However, this situation is constantly changing, and closures are almost certain at this stage. For example, in March 2020, the U.S. Court of Appeals for the Ninth Circuit canceled oral argument hearings scheduled for the remainder of the month. On March 12, 2020, the U.S. Supreme Court closed its building to the public and on March 16, 2020, postponed oral arguments at least through April 1, 2020. The “shelter-in-place” requirements in place in certain parts of the country also will require federal courts in those areas to suspend normal operations.

Taxpayers should be aware that despite these closures, courts have not yet started implementing any uniform deadline extensions (the Supreme Court has clearly stated that the building remains open for official business and that filing deadlines are not being extended). If extensions are needed, taxpayers and their counsel should file requests. Considering the circumstances, the IRS and/or Department of Justice likely will agree to any such extensions, and thus motions could be filed jointly.

Potential Securities Litigation Issues

By Jay B. Kasner, Scott D. Musoff, Susan L. Saltzstein

The uncertainties created by the outbreak of the coronavirus and its impact on companies across all industries, from travel and leisure to technology, have already given rise to securities litigation. On March 12, 2020, two putative securities class actions arising from coronavirus allegations were filed, one against Norwegian Cruise Lines in the U.S. District Court for the Southern District of Florida and another against Inovio Pharmaceuticals Inc. in the U.S. District Court for the Eastern District of Pennsylvania. While each of these cases has unique allegations, they exemplify the risks that public companies face when making coronavirus-related disclosures in the face of uncertainties and volatile stock markets, which tend to lead to increased securities litigation.

Corporate disclosures relating to the potential impact of the virus on performance and projections will be viewed in hindsight. Thus, the context of such disclosures, what they specify and the factual circumstances underlying each case can significantly affect potential liability. Careful attention to the timing and drafting of disclosures is essential. In particular, companies should pay close attention to continually updating risk factors and cautionary language, especially those surrounding forward-looking statements in order to maximize the protections of the PSLRA’s safe harbor. Management’s keen focus on projections and guidance in this rapidly changing environment is imperative and may include updating or disavowing prior guidance depending on the situation. (See “Company Earnings Guidance and Market Outreach During the Coronavirus Pandemic”). It is also important to signal clearly when an issuer expresses an opinion or belief about the virus’ potential impact (*e.g.*, say “we believe”), because opinion statements often are afforded greater protection against securities claims than pure statements of fact. In this fluid situation, where events continue to unfold each day, it is vital to anchor disclosure decisions to specific facts or changes in facts as support when such disclosures will be judged in hindsight. (See “Impact on Public Company Disclosures and Other Considerations.”)

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Company Earnings Guidance and Market Outreach During the Coronavirus Pandemic

By Jay B. Kasner, Scott D. Musoff, Susan L. Saltzstein, Michael J. Zeidel

The worldwide disruption and uncertainty caused by the COVID-19 pandemic has resulted in many publicly traded companies forewarning investors that they will miss their earnings. As SEC Chairman Jay Clayton recognized, the effects of the coronavirus are not easy to assess or predict and depend on many factors beyond an issuer's control and knowledge. Chairman Clayton also stated that how issuers plan for the uncertainty created by the coronavirus and how they respond to events as they take place may be material to investors' decisions. Thus, companies should evaluate carefully during this time (i) whether to update or withdraw their existing guidance and (ii) the appropriate timing and manner for doing so.

The same principles that apply to issuers in less chaotic times provide direction for companies considering whether to update their guidance now. Issuers likely will be judged — in hindsight — against whether they had a reasonable basis to believe in their guidance, a standard which plaintiffs may argue should be viewed objectively and in comparison to their peers. As such, companies should remain cognizant of, and regularly monitor, how other market participants treat their guidance, particularly that of their relevant competitors.

Although the federal securities laws do not generally impose an explicit duty to update forward-looking statements, some courts have found that a “duty to correct” and “duty to update” may exist under certain circumstances. For instance, a duty to correct may arise if the issuer's disclosure was materially false when made, and a duty to update may apply if the issuer's disclosure became materially false in light of new developments. In 2019, the U.S. Supreme Court refused to hear an appeal from the U.S. Court of Appeals for the Ninth Circuit, in which the Ninth Circuit held that an issuer must update a prior statement of fact when the “value” or “weight” of the statement is “diminished” by subsequent events. In that case, *Khoja v. Orexigen Therapeutics, Inc.*, the Ninth Circuit determined that a drug company became obligated to disclose later clinical trial results for an obesity drug because they represented, in the court's view, a complete reversal of the previously disclosed results, which had “clearly suggested a promising venture.”

In approaching disclosures generally, an opinion — such as a projection of future earnings — should not be considered misleading just because some fact or event, like disruption

caused by a pandemic, causes the projection not be realized as expected. The question, ultimately, will concern whether the issuer's belief reasonably or fairly aligned with information known by management and analyzed at the time it formed its opinion. Even if an issuer reaches an incorrect conclusion, a court should consider whether the issuer reached its view based on a reasonable basis and with the information then at hand. In the end, this inquiry is fact-intensive and often is hotly contested in the securities litigation context.

Not all industries are impacted equally and using a facts-and-circumstances approach ought to serve issuers well in making difficult decisions concerning the timing of disclosures. Lastly, all issuers should review and consider whether updates to their industry and market projections disclosures, pursuant to Items 303 and 305 of Regulation S-K, as well as their risk factors, will be necessary in connection with future SEC disclosures, such as first quarter earnings releases and Form 10-Q filings.

Commercial and Financial Agreements

By Julie Bédard, Amanda Raymond Kalantirsky

The coronavirus outbreak may significantly impact many companies' commercial and financial agreements. The magnitude of the event cannot detract from the legal analysis that needs to be performed for each particular set of circumstances. Under any given contract, the application of the different clauses that may come into play will need to be reconciled. Those clauses may include representations/warranties, *force majeure* or “material adverse event” clauses, notice requirements, termination rights or dispute resolution provisions.

Despite the outbreak, parties may not be in breach of their agreements, and contract terms should be reviewed closely in order to ascertain whether a party is, in fact, prevented from complying with its contractual obligations. Parties facing questions over whether performance under a particular contract may be suspended or excused will need to analyze the language of any *force majeure* clause. Legal doctrines such as impossibility, frustration of purpose or others may also be relevant.

A contract review and any actions undertaken may require multijurisdictional coordination in order to ensure a consistent approach, and a company's response may be fluid depending upon the changing regulatory and health/safety circumstances. For additional details on these types of issues, see our February 26, 2020, mailing, “[Coronavirus/COVID-19: Implications for Commercial and Financial Contracts](#).”

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