

PE SPONSORS AND PORTFOLIO COMPANIES COVID-19 WEBINAR

Legal Aspects of the Public Health Crisis
and What Companies Should be Doing Now

ROPES & GRAY

March 26, 2020

Questions?

**Please submit questions during this webinar
via the chat function on the webinar portal.**

AGENDA



- **Stimulus Package – CARES Act and Fed Actions**
- Navigating the Legal Landscape of the Public Health Crisis
- Practical Points for Managing your Employee Workforce
- Capital Planning and Credit Agreement Considerations
- Insurance Coverage Considerations
- Lessons Learned and Best Practices in Company Responses to COVID-19

Stimulus Package – CARES Act and Fed Actions

CARES Act

- Economic Stabilization and Assistance Program: **\$454B** for Treasury to invest in FRB lending programs
 - Treasury to endeavor to establish a program to assist US companies with 500-10,000 employees
- SBA-Backed Loans: **\$349B** for loans to small businesses (capped at **\$10M** per loan)
 - Affiliation rules likely disqualify most PE portfolio companies
 - Exceptions for targeted sectors – restaurants / lodging, SBA approved franchises and businesses that already receive financial assistance from SBIC funds
- Expanded unemployment benefits and tax relief

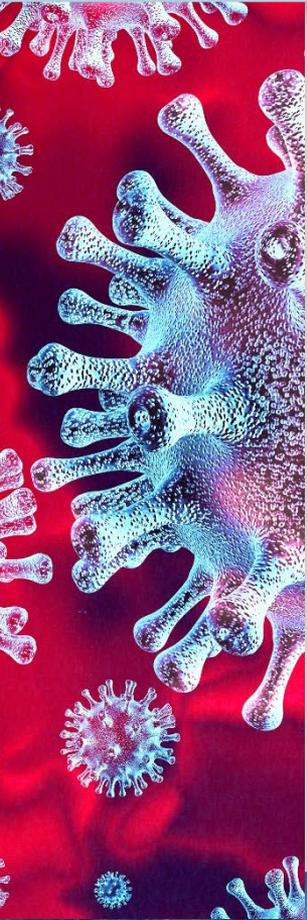
Main Street Lending Program

- To be established by FRB
- Targeted at small-medium sized businesses; details TBD

Primary Market Corporate Credit Facility and Secondary Market Corporate Credit Facility

- Targeted at investment grade borrowers

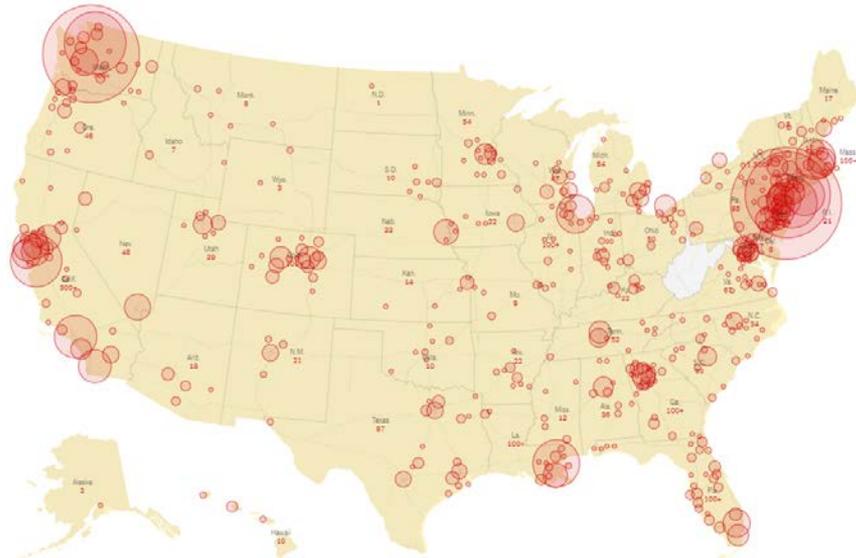
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U.S. Infection Statistics

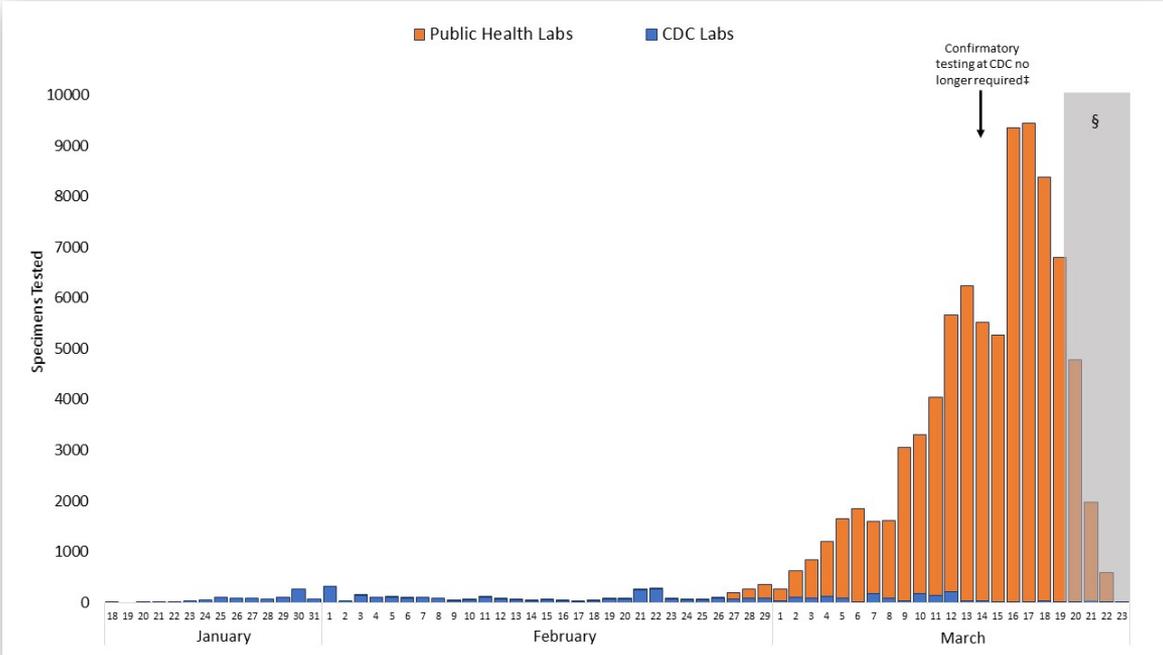
- Geographic hot spots: Washington, California, New York



Source: <https://www.nytimes.com/interactive/2020/us/coronavirus-us-cases.html>

Number of specimens tested for SARS CoV-2

Number of specimens tested for SARS CoV-2 by CDC labs (N=4,651) and U.S. public health laboratories* (N=83,391)



Source: CDC, 3/23/20

Legal Landscape

Federal Law

- Federal agencies' limited authority to prevent spread of infectious disease
 - Quarantine, Isolation, Surveillance and Contact Tracing
 - Containment at U.S. Borders;
 - **Centers for Disease Control (CDC); advisory to states**
- Grant/contract funding from **National Institutes of Health (NIH)/National Institute of Allergy and Infectious Diseases (NIAID), and Biomedical Advanced Research and Development Authority (BARDA)**
- Testing kits and drug or vaccine approval: **Food and Drug Administration (FDA)**
 - Approval to market, Emergency Use Authorization, Vaccine and drug development research

State and Local Law

- States implement most surveillance and controls under police powers

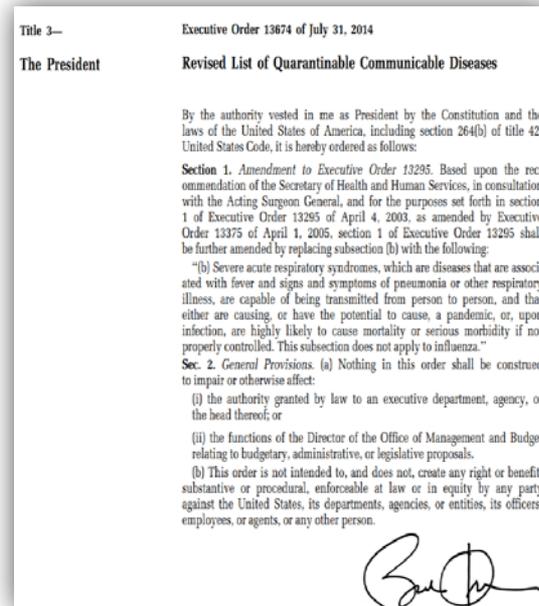
Legal Authority: Federal Law

- **Statutory: Public Health Service Act, § 361 (42 USC §§ 264-272), *CONTROL OF COMMUNICABLE DISEASES***
 - Long history and tradition of protecting against disease at national border and deferring to states to exercise police power.
 - **Strengthened in recent years** as part of wider strategy to limit the entry and spread of communicable diseases into the U.S. and among the states.
 - Pandemic and All-Hazards Preparedness Act (PAHPA) (2006)
 - Pandemic and All-Hazards Preparedness Reauthorization Act (PAHPRA) (2013)
 - Pandemic and All-Hazards Preparedness and Advancing Innovation Act (PAHPAIA) (2019)
 - Authority for carrying out these functions has been delegated to the **Centers for Disease Control and Prevention** (“CDC”).
 - Statute authorizes fines “of not more than \$1,000 or by imprisonment for not more than one year, or both” for violations.

See <https://www.phe.gov/Preparedness/legal/pahpa/Pages/default.aspx>

Legal Authority: Federal Law

- **Regulatory**: 42 CFR Parts 70 and 71
 - Implement federal quarantine authority across states (part 70) and into the states (part 71)
 - Authorized to detain, medically examine, and release persons arriving into the United States and traveling between states who are suspected of carrying these communicable diseases
- **Executive Order 13295** (last updated: July 31, 2014)
 - List of Quarantinable Communicable Diseases



Sources of Legal Authority: State and Local

States' authority derives from their police powers to protect the health, safety, and welfare of persons within their borders.

- States can enact laws to enforce the use of isolation and quarantine, or delegate authority to municipalities and counties.
- In most states, breaking a quarantine order is a criminal misdemeanor.
- State and local laws can vary greatly.
 - **For COVID-19, there have been a series of state and local/municipal public health orders for closure of businesses and “shelter-in-place”**
 - **Distinctions between “essential” and “non-essential businesses”**
 - **Federal CISA guidance on “essential critical infrastructure workforce,” but not binding on states and localities**

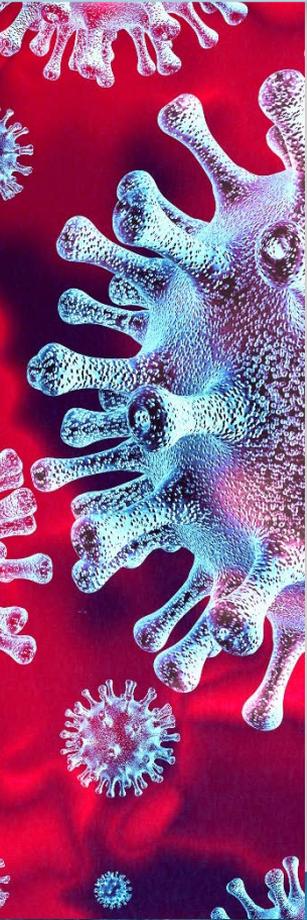
See <https://www.cdc.gov/quarantine/aboutlawsregulationsquarantineisolation.html>

Example of Local Quarantine & Isolation Law: NYC

Summary	Enumerated Police Powers (Examples)
<p>New York City empowers its Department of Health and Mental Hygiene to “take such action as may become necessary to assure the maintenance of public health, the prevention of disease, or the safety of the City and its residents.”¹</p>	<ul style="list-style-type: none">▪ Physicians, people in charge of health care providers, shelters or other group facilities, and educational settings have a duty to isolate any “case, carrier, suspect case or suspect carrier” of an enumerated list of contagious diseases.▪ Isolated or quarantined individuals may be ordered to remain at home “under such conditions and for such duration as the department may specify to prevent transmission of the disease to others.”▪ People are prohibited from engaging in acts that are likely to spread disease.

¹ *New York City Public Health Code § 11.17*

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Legal Issues for Employers

- **CARES Act – Unemployment Provisions**
 - Adds \$600 to existing state benefits
 - Broadens access – includes independent contractors
 - Extended time, eliminated waiting periods
 - Federal funding for state “short-time” compensation programs

Legal Issues for Employers

- **Families First Coronavirus Response Act**

- Signed by President Trump on March 18, 2020. Effective April 2.
- Expands protections under the Family and Medical Leave Act and provides for paid sick leave, to cover absences for certain COVID-19-related reasons.
 - Employers may opt out for health care providers and emergency responders.
 - Corresponding tax credit intended to reimburse for cost of paid leave.
- In place through December 31, 2020.

Legal Issues for Employers

- **New York Paid Leave Law** (by way of example – watch state-by-state responses)
 - On March 18, 2020, Governor Cuomo signed into law new legislation in response to COVID-19.
 - The COVID-19 provisions provide:
 - Unpaid sick leave to all employees subject to quarantine or isolation.
 - Paid sick leave to all employees subject to quarantine or isolation at companies with more than 10 employees and over \$1 million in net income during the previous tax year.
 - After the employee has exhausted the paid sick leave, eligible to receive paid family leave and disability benefits under New York's Workers' Compensation law for the period of quarantine or isolation.

Legal Issues for Employers

- **Testing Employees and the Americans with Disabilities Act**
 - Employers may ask employees if they are experiencing symptoms of COVID-19.
 - Employee medical exams, including temperature checks, allowed under current circumstances.
 - May require fitness-for-duty notes.
 - Note resulting demand on health care provider time and attention.
 - ADA does not prevent requiring sick employees to stay away.

Legal Issues for Employers

- **COVID-19 Exposure in the Workplace**
 - Responding to employee who falls ill at work
 - Employee tested for COVID-19
 - Test pending versus confirmed positive
 - Contact assessment
 - “Contacts of Contacts”
 - Confirmed positive in adjoining suite or facility
 - Important: if an employee tests positive for COVID-19 infection, if possible, coordinate with local and/or state public department of health to perform contact assessment

Legal Issues for Employers

- **Working From Home**

- Consider allowing employees to work from home if at all possible
 - Trend toward “shelter in place” orders
 - Future ramifications for ADA reasonable accommodation obligations?
- Legal issues:
 - OSHA
 - Minimum wage
 - Recording hours worked
 - Discrimination laws
 - ADA
 - Who pays for necessary work from home equipment



Steps All Employers Should Be Taking

- For those businesses with active workplaces (either because no local shutdown recommendation or order is in place or because the business is essential):
 - Educate employees on developments in WHO, CDC, and U.S. State Department guidance.
 - Instruct symptomatic employees to stay away from the workplace.
 - Provide sanitizing / hand-washing stations and regularly clean facilities.
 - Appoint a Human Resources representative as a central resource.
 - Cancel non-essential meetings and/or company gatherings.
 - Prepare an internal workplace response plan.
 - Offer telecommuting for employees whose job duties can be performed remotely.
 - Prepare for temporary workplace closures and/or large-scale telecommuting arrangements.



Workforce Cost-Saving Measures

- Layoffs
- Furloughs
- Salary/wage reductions
- Hours reductions
- Voluntary leave programs
- Voluntary exit programs

Webinar: COVID-19 in the Workplace and Workforce Cost-Saving Measures

March 30, 2:30 PM Eastern

Discussion of Real-World Examples

- Ropes & Gray has been advising employers from all over the country and across industries about responding to COVID-19 exposure and related workplace issues.

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Leveraged Financing Markets

- Scarce liquidity in the institutional lender market
 - General investor flight from risk, outflows from loan mutual funds and ETFs
 - Difficulty pricing risk amidst extreme uncertainty
 - Potential loan liquidations to comply with margin calls, loan to value and other requirements for certain lender vehicles
- Primary institutional markets for new syndicated loans and bonds closed for all but very select credits and loan types
 - Severely limits banks' ability and willingness to underwrite new debt
 - But many direct lenders actively looking for opportunities to make loans
- Steep secondary market declines with pricing and volume varying by industry
 - Combination of risk assessment and market dislocation
 - Price quotes or averages may not be indicative if wide bid / ask spreads
 - Expected wave of ratings downgrades may further impact both volume and pricing

Financing Related Legal Developments

- Federal guidance on loan modifications and reporting for financial institutions states financial institutions should work constructively with borrowers unable to meet obligations because of the effects of COVID-19
 - Focus on payments (deferrals, fee waivers and similar actions) not financial covenants
 - FASB confirmed COVID-19 related short-term payment modifications to borrowers who were current prior to any relief will not be troubled debt restructurings
- NY Executive Order cannot refuse to grant 90 day forbearance based on financial hardship as a result of the COVID-19 pandemic
 - Limited, if any, practical benefit to corporate borrowers
 - Intended focus appears to be residential mortgages and consumer banking services
- Some governmental restrictions on collection of consumer receivables, but currently no expected governmental intervention on corporate receivables

Financing Related Action Items

- Assess (and continually re-assess) liquidity and financial covenant compliance
 - Update forecasts for new information and developments
 - Include COVID-19 sensitivities for extreme downside and optimistic cases
- Review credit agreements and indentures for potential “foot” fault defaults
- Confirm timely audit processes and if “going concern” qualification potential, proactively consider impact on customers, vendors, lessors, etc.
- Review lender group and scrutinize and exercise consent rights for lender assignments to avoid opportunistic lenders with short-term investment horizon
- Assess opportunistic transactions, such as debt and stock repurchases, but also consider liquidity, solvency, fiduciary duties and corporate governance
- Develop communication strategy for addressing agents, lenders, rating agencies, etc.

Liquidity – Sources

- Cash is king – maintain prudent cushion over customary cash balances
- Liquidity Sources
 - Cash – assess (and reassess) delays in receivables and evaluate (and reevaluate) creditworthiness of account debtors
 - Evaluate availability and accessibility of revolving credit facilities and consequences of full draw
 - Evaluate continuing viability of other liquidity sources, e.g. receivables factoring
- Uncertainty and constant new developments complicate forecasting and require continual updating
 - If liquidity tight, prepare 13-week cash flow/liquidity projections and update bi-weekly
- Proactively develop contingency options for supplemental liquidity
 - For additional debt, also consider impact on financial covenants

Liquidity – Uses

- Cash outflows
 - Review payment terms with suppliers, vendors, landlords, etc.
 - Anticipate potential incremental costs
 - Operational measures to address internal COVID-19 considerations
 - Temporary cost increases, e.g., increased costs for shipping, freight, raw materials
 - Needs to replace or supplement supply chain, including sources and distributors
 - Consider options to address inefficiencies for full fixed costs, e.g. paying full rent and wages despite temporary facility closures or limited productivity due to alternating daily shifts
- Debt service costs, if severe liquidity constraints, consider lender relief
 - PIK interest options
 - Defer amortization
 - Waive or defer fees

Revolving Credit Borrowings

- Assess current and prospective ability to satisfy relevant revolver borrowing conditions - absence of defaults and bring-down of representations and warranties, including as to absence of MAE
- “MAE” considerations
- Consider consequences of drawing revolver
 - Potential to trigger “springing” financial covenant compliance and whether proceeds can be counted in cash netting for leverage calculations
 - For ABL facilities, “cash dominion”
 - Messaging to banks and for public filers, potential disclosure requirements
- Currently, “banks” are believed to be healthy and well capitalized with little concern over systemic risk
 - Governmental and banking authorities are taking actions to ensure liquidity
 - Greater fund risk for non-bank lenders, which may be facing their own liquidity issues

Financial Covenants

- Forecasting EBITDA and covenant compliance is challenging at best
- Work with counsel to review and maximize addbacks and adjustments to EBITDA as defined in credit documents before you need them
 - Incremental costs associated with COVID-19 measures should generally qualify for non-recurring / unusual item addbacks
 - Pro forma “run rate” adjustments for cost savings measures
 - Loss of anticipated revenues generally not eligible for addback unless specifically addressed
- Proactively review with the sponsor, counsel and other advisors to assess strategies
 - Potential covenant relief in the form of holidays, waivers or resetting levels
 - Modifications to EBITDA definitions to address specific issues
 - For potentially difficult situations, tool chest of negotiating sticks and carrots

Capital Structure – Sponsor Capital Infusion

- General Considerations
 - If may need relief from lenders, consider deferring as negotiating tactic
 - Lenders may require anyway or can be used as a “carrot”
 - Consider whether single “equity cure” would be sufficient
 - Balance versus immediate cash needs
 - Ability to recover investments (whether in the form of debt or equity)
 - Restrictions in financing documents
 - Corporate governance if solvency is questionable
 - If in the form of debt, challenges by other creditors (equitable characterization)
 - If structured properly, risk can be minimized
 - Larger issue may be cost and time defending creditor challenge
 - Depending on the type of investment, there may be other accounting and tax implications so allow time for planning and structuring

Capital Structure – Debt Repurchases

- Repurchasing debt may become attractive if pricing reflects market dislocation but not long-term value
- Review financing agreements with counsel for mechanics, options and considerations
 - Conditions, limitations on funding sources and other restrictions
 - MNPI issues, trading windows, “big boy” language, creeping tenders from open market purchases
 - Indentures typically provide mechanics for redemptions, but not open market purchases and tender offers
- Consult with counsel on credit agreement and indenture requirements and other considerations
 - Tax consequences, including cancellation of debt income
 - Securities law requirements, including disclosures
 - Corporate governance considerations, including scope of fiduciary duties, liquidity and solvency

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Business Interruption (“BI”) Insurance

- Traditionally part of commercial property insurance
 - Requires direct physical loss as a trigger for coverage for lost business income
 - Civil authority coverage also generally requires physical property damage
 - Insurers likely to deny coverage because no physical damage to property
 - Insureds may argue that virus contamination is “direct physical loss,” but coverage dispute is likely
 - Policies also often exclude virus-related loss (pollution or contamination exclusions)
- For product manufacturers, potential for coverage if an infected employee contaminates product or equipment leading to a recall and/or shutdown
 - May be covered under product recall and/or traditional BI policies
- Specialty insurance products (if already in place) may cover BI without physical damage, but such policies are rare and expensive

BI Insurance

- Legislative efforts underway to force BI coverage for COVID-19 losses
 - Bills introduced in at least three states (OH, NJ, MA) would compel insurers to cover BI losses due to COVID-19 despite lack of physical damage and virus exclusions
 - Insurers would likely be reimbursed with public funds
 - Important to submit claims for all potential BI losses while legislative efforts play out
- Cyber insurance
 - Claims (e.g., data breach, privacy breach, ransomware attacks) are likely to increase as employees work remotely for sustained periods and computer networks are tested

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Be Proactive Rather Than Reactive

- Businesses should have a dedicated COVID-19 Response Team to:
 - monitor developments
 - serve as a centralized source for decision-making
 - coordinate communications
 - anticipate, adapt to and reduce COVID-19 related risks
- Consult the experts (e.g., Chief Medical Officer, Public Health Officials)
- Focus on tech capabilities for telework and practical strategies for social distancing. Consider impact on morale and teamwork.
- Reassess short and long-term business plans and strategy to preserve and drive long-term value
- Reach out to our public health order response team, a dedicated team knowledgeable about all PHOs that have been adopted at the state and local level at PHOrdersTeam@ropesgray.com

Focus on the Health and Safety of your Workforce

- Remote work and technology support
- Staggered teams and start times
- Limit travel
- Limit meetings and visitors
- Separate work locations
- Enhanced cleaning / disinfection procedures

Communicate Strategically

- Communication is key and should be continuous
 - Board of Directors
 - Employees
 - Customers / Clients
 - Governments and regulatory agencies
 - Other companies within your industry
 - Lenders, Equityholders and other key stakeholders

Continue Business as Usual (to the extent possible)

- As applicable, let customers / clients know you are open for business
- Set expectations with your workforce that customers/clients may rely on your business more than ever during the public health crisis
 - But, remember that workforce is dealing with new and different issues.
- Addressing Public Health Orders is not an “old” issue
 - Vary by jurisdiction
 - Subject to lobbying
 - Ropes & Gray’s task force: PHOrdersTeam@ropesgray.com

Consider Compensation Structures

- The public health crisis has upended life in America in a few weeks and companies should reconsider compensation programs in light of this new reality to motivate leadership and performance
- Responses will need to balance effective incentives with sensitivity in certain cases to public and political perception
- Targets for annual incentive bonus programs may be outdated even if set in January or February
- Focus will need to be given to the valuation at which equity awards are set in light of fluctuating equity values in the public markets

The End-Game: Planning for Business Resumption

- Conflicting Guidance
- Enhanced building security protocols and screening of visitors
 - Landlords may impose these even if specific businesses do not
- Surveillance of employee health conditions to prevent recurrence and protect co-workers and customers / clients
- Cleaning and sanitation emphasis is not going away after this initial turbulent period
- Phased ramp-up in offices and retail locations; gradual staffing increases
- Social distancing will continue on mass transit, causing delays
- Need for staggered work schedules

We can help you

- Ropes & Gray has launched a **COVID-19** online hub at www.ropesgray.com/en/coronavirus for resources related to the outbreak. Please visit this site frequently for up-to-date insights on legal considerations in connection to the coronavirus, business continuity best practices, and maintaining the health and safety of your people.
- Please email your questions to: PEWebinarQuestions@Ropesgray.com

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