COVID-19 and Public Companies: *This is a developing story*

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Topics

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The perfect storm of COVID-19 operational disruption, financial-market turmoil and business-model threat throws a complex mix of urgent questions at public company legal and governance officers.

We've summarized our thinking on several topics currently under discussion with public-company clients. Because the judgments involved in addressing these topics are often nuanced, we welcome the opportunity to discuss your concerns directly. Please reach out to any of the lawyers listed in sidebar or your regular Davis Polk contact.

Reviewing Your D&O Coverage *(✯ New)*

- In times of financial stress legal and governance officers frequently field questions from directors and executives about the quality of the company's D&O coverage.
- Our partner **Marshall Huebner** published an informative article in **Bloomberg Law** in September 2018 drawing on his extensive experience dealing with D&O policies in the insolvency context—when these policies are most needed, but when they may not be available because of policy language or business decisions made in sunnier times.
- Marshall's article walks through some of the key questions to ask when reviewing your current D&O coverage:
  - ✓ Do I have a single "ABC tower" that provides coverage for directors and officers (Side A), coverage for the company's indemnification obligations (Side B) and coverage for other claims against the company (typically securities class actions) (Side C)? If so, the bankruptcy court may decide that the proceeds from the policy are also property of the estate—potentially limiting coverage to directors and officers. And whether or not the company is in bankruptcy, the policy may be exhausted by the company's claims, leaving the directors and officers without coverage.
    - Consider purchasing additional standalone Side A coverage, or if that is too expensive, including well-drafted priority-of-payments clauses to ensure that Side A coverage must be paid before other coverages.
  - ✓ What happens if the company is bankrupt and unable or unwilling to pay its retention (i.e. deductible), which the insurer could use as grounds to deny coverage?

- This problem can be addressed by expressly making Side A coverage fully available in the event of "Financial Impairment," which should be defined to include a range of bankruptcy and insolvency scenarios.

✓ Does my "insured vs. insured" exclusion carve out suits by a bankruptcy trustee or similar entity on behalf of the company?

✓ Do my "prior knowledge" provisions impute knowledge of wrongdoing to innocent directors and officers?

✓ Are bankruptcy proceedings carved out of the change-in-control provisions?

Thinking Ahead to First Quarter Reporting *(☆ New)*

- As the quarter winds down, all public companies are considering what to say about the impact of COVID-19 in their earnings releases, on their earnings calls and in their 10-Q's.
- Our **March 30 memo** discusses these issues as well as such practical concerns as when to announce your earnings call.

Securities Offerings During a Closed Window or Blackout Period *(☆ New)*

- Yes, Virginia, you can offer securities during a company "closed window" or "blackout period," if you do so thoughtfully.
- Our **March 27 memo** explains the key things to think about.

Drawing on Your Revolver *(☆ New)*

- Many companies are considering whether to draw down all or a portion of their committed revolving credit facilities.
- Factors to consider when deciding whether to borrow under a revolver include:

✓ Is the company able to satisfy the conditions to borrowing?

- For most companies, these require that all reps and warranties are true and that there is no default at the time of borrowing.
- Reps will typically include a "no material adverse change" rep and, sometimes, a solvency rep, both of which will likely require extra scrutiny in today's environment.

✓ Is the borrowing permitted under the company's other debt instruments?

✓ What is the impact of the borrowing?

- Will the borrowing trip any leverage or coverage test in the future?
- If a financial covenant is tested on a "springing" basis, should the company exceed the springing threshold?
- Is the company subject to an "anti-cash hoarding" provision that limits the amount of cash the company can hold?
- Will the borrowing adversely affect pricing? Or adversely affect thresholds at which the company can take certain actions (e.g., restricted payments or investments)?
- Will the borrowing affect the company's ratings?
- Will the borrowing trigger a disclosure obligation? See 8-K Reporting Requirements—Revolver drawdowns below.

Being Alert to Who's in Your Stock—And Thinking About Defenses *(☆ New)*

- In normal times—which these are not—a company would typically have a takeover defense such as a rights plan ready and "on the shelf," but would not adopt the plan until an actual threat materializes.

- However, the ongoing market dislocation may allow for rapid, undisclosed accumulations of positions at materially depressed prices.
  - ✓ Ideally you would already have a "stock watch" in place to try to detect accumulations in your stock, although often it's impossible to know all positions given that derivative holdings may need not be disclosed under current disclosure regimes such as Schedule 13D.
- In the current climate, an opportunistic party may be able to achieve a position of substantial influence or control without paying a control premium to other shareholders, with the result that the horse may be galloping out of the barn before a rights plan can be put in place.
- The board therefore may want to consider whether it makes sense, in these extreme conditions, to adopt a rights plan before an actual threat becomes apparent.
  - ✓ Interesting to note that at the end of 2019 there were 55 rights plans in place at U.S. companies, while at the end of 2009, as the country was exiting the financial crisis, there were 946 such plans in place.
- The board will want to consider the company's particular situation and the ways in which a rights plan may be customized to its circumstances, including as to term, trigger percentage, exempting passive investors and other elements.
- Any board adopting a rights plan before an actual threat appears will also want to be prepared to communicate its rationale to key shareholders and proxy advisers.

Board Activity

- Consider investing one committee, such as Audit, Executive or Risk, with authority to make decisions on behalf of the board in emergency situations relating to the pandemic (as determined by the committee), subject to statutory non-delegable matters.
  - ✓ Use this flexibility sparingly and only in emergencies.
- Courts may review board activity in a crisis more searchingly than actions taken "on a clear day."
- It may not always be possible, but when it is, try to follow customary corporate formalities such as notice (or waiver), preparation of minutes, and advance circulation of agendas and decks.
- Given the need to have remote meetings and increasing reliance on external board management software, review your ability to control the security of company-supported iPads provided to directors.

SEC Initiatives *(✰ Updated)*

- The SEC is admirably stepping up to help public companies impacted by the pandemic and its knock-on effects.
- For example, the SEC issued an **order** that provides public companies with an additional 45 days to file certain reports that would otherwise have been due by April 30. The relief is subject to conditions, and does not apply to conflict minerals filings due by May 31.
  - ✓ ✰ ***Update***: On March 25, the SEC issued a superseding **order** extending conditional filing relief through July 1. Our **March 26 memo** describes this relief in more detail.
- On our wish list is a public statement that the "wet signature" requirements of rule 302(b) of Regulation S-T be suspended for the duration of the crisis, or at least an assurance from the staff that no enforcement action will be taken against companies or individuals who are forced to make EDGAR filings without securing a manually signed signature page from the officers or directors authorizing the filing.
  - ✓ Until the agency does so, remember that manual signature and retention requirements continue to apply.

- ✓ ☆ ***Update***: On March 24, the SEC staff released a **statement** saying that while it continues to expect compliance with rule 302(b), it recognizes that some may experience difficulty complying under current circumstances. In light of this difficulty, the staff will not recommend enforcement action for non-compliance with rule 302(b) if:
  - the signatory (i) retains a manually signed signature page or other document authenticating, acknowledging, or otherwise adopting his or her signature that appears in typed form within the electronic filing and (ii) provides such document, as promptly as reasonably practicable, to the company for retention pursuant to rule 302(b);
  - such document indicates the date and time the signature was executed; and
  - the company establishes and maintains policies and procedures governing this process.
- ✓ See **Attachment A** to this memo for model policies and procedures.

- Similar relief from the notarization requirements of Form ID would be welcome.
  - ✓ ☆ ***Update***: On March 23, the SEC invited filers having difficulty meeting the Form ID notarization requirements to contact Filer Support at 202-551-8900, option 3.

8-K Reporting Requirements

CEO illness

- The illness of a CEO, CFO or other senior executive with the COVID-19 virus is not by itself reportable under 8-K item 5.02.
- However, if the executive's duties are temporarily transferred to another officer, that can trigger an item 5.02 reporting requirement, depending on the facts.
- Some companies have voluntarily reported executive officer illnesses as a way to address speculation or get ahead of the story. Companies should also consider whether the illness of a senior executive is material come the time of announcing earnings or filing of Form 10-K or 10-Q.
- Companies should review their emergency succession plans since the pandemic could render key executives unavailable at the same time.

Revolver drawdowns

- Even if you already filed your revolving credit agreement, a drawdown can itself trigger an 8-K item 2.03 reporting requirement if the draw is "material."
- Factors to consider when assessing materiality include:
  - ✓ Whether purpose of the draw is to keep your powder dry or to address a known liquidity problem
  - ✓ Size of draw compared to total assets
  - ✓ Size of draw compared to total debt outstanding as reported on your last balance sheet
  - ✓ Whether the company has a history of drawing on its revolver

Pre-releases and guidance changes

- An earnings pre-release or guidance change may create an 8-K obligation.
  - ✓ If the quarter is still in progress, any Reg FD-compliant manner of reporting is usually sufficient, although we expect most companies will use 8-K item 7.01 or 8.01 instead of relying only on a press release.
  - ✓ Report under item 2.02 if the quarter has ended, even if the pre-release isn't intended as a substitute for your quarterly earnings release.
  - ✓ Item 2.02 reporting also applies when a guidance change relates to the just-completed quarter.

Ratings downgrades and other triggering events

- 8-K item 2.04 reporting may be required if a ratings downgrade or other event results in the acceleration or increase of a debt obligation.

Reductions-in-force

- Material charges resulting from a RIF may trigger an 8-K item 2.05 report.

Termination of a material agreement

- Termination of a material agreement under a *force majeure* or similar clause may trigger an 8-K item 1.02 reporting requirement.

Material impairments

- A definitive decision to take a material impairment charge triggers reporting under 8-K item 2.06.

Failure to meet a continuing listing standard

- If you receive a delisting notice, or notify a stock exchange that you are not in compliance with its continuing listing standards, an 8-K item 3.01 report is triggered.
  - ✓ For example, a NYSE-listed company faces delisting if the average closing price of its common stock is less than $1 over a consecutive 30 trading-day period.

Annual Shareholder Meeting Logistics *(☆ Updated)*

Changing meeting location, date or time

- If you need to change the location, date or time of your meeting after mailing the proxy, SEC rules are satisfied by issuing a press release, filing it as definitive additional soliciting materials, and notifying your stock exchange and key service providers (e.g. Broadridge).
- State corporate law may require notification to shareholders. For Delaware companies, absent special circumstances such as a contentious agenda item, we believe that notice of the change as described above should be sufficient if the meeting is held within 60 days of the record date.

Switching to a virtual-only meeting

- Switching to a virtual-only meeting after mailing the proxy is an option for Delaware companies and companies organized in some other states.
  - ✓ Executive orders, court orders or emergency legislation may be forthcoming to permit virtual-only meetings in states where they are currently prohibited.
- Remember to review, and if necessary amend, the by-laws to ensure they do not prohibit virtual-only meetings.
- Although some proxy advisory firms and institutional shareholders disfavor virtual-only meetings, in light of the pandemic some influential institutions have publicly stated their support for virtual meetings that ensure shareholder voices are heard.
- It's not just a conference call however, since the ability to cast votes at the meeting is needed. The logistics are complex and a specialized service provider is generally necessary.
  - ✓ These providers suggest contacting them at least 2 to 3 weeks in advance of the meeting.
  - ✓ Capacity constraints at the service providers may render this option unavailable for some companies as the season progresses, so we suggest at least exploring the option now, perhaps even in those states where it is currently prohibited.
  - ✓ ☆ ***Update***: See **Attachment B** to this memo for model rules of conduct for a virtual meeting.

Barring attendance by shareholders reporting or exhibiting symptoms of infection

- A company should have the ability on public and workplace-safety grounds to bar attendance by any shareholder reporting or exhibiting symptoms of COVID-19 infection.

Stock Buybacks, Dividends and 10b5-1 Plans

Buybacks

- Companies with available cash and depressed stock prices may consider instituting or ramping up stock buybacks.
- The company would have to conclude it has no material non-public information (MNPI).
- Management should be aware that buyback activity is politically disfavored and may disqualify, limit or impact the company's future participation in government relief programs.

Dividends

- Companies that are considering suspending dividend payments need to be mindful of SEC disclosure implications. Those that have to date have issued press releases, with one company having filed an 8-K describing this with other 8-K triggering events.
- Suspending a dividend on preferred stock impacts the availability of Form S-3.

Cancelling a 10b5-1 plan

- A company may consider whether to cancel an existing company stock purchase 10b5-1 plan, or whether to permit or direct the CEO or other executive officer to cancel a selling plan.
- Although 10b5-1 plans can be cancelled even at a time when the company or the executive is in possession of MNPI, we generally recommend against doing so because cancellation can create a suspicion that the plan (and potentially other plans) was not entered into in good faith, and thereby weaken the effectiveness of the 10b5-1 affirmative defense to insider trading if it were ever needed.
- Still, unexpected significant developments should provide a legitimate basis for cancelling a 10b5-1 plan for a company or executive without a problematic history of cancellations. Note, however, that a plan cannot be simply amended while the company or executive has MNPI.
- The cancellation of one plan should not dictate the cancellation of another plan. Each cancellation should be analyzed on its own merits.
- Company purchase plan cancellation considerations:
  - ✓ Is the plan being cancelled to preserve cash better used to support near-term liquidity?
  - ✓ Was the plan entered into before the severity of current conditions was broadly recognized?
  - ✓ A new plan can be put in place only once the company no longer has MNPI.
- Executive selling plan cancellation considerations
  - ✓ Is the plan being cancelled because of the optics of reporting insider sales in a time of crisis? If so consider limiting cancellations to the CEO and CFO only, and not to a broader group of executives whose sales do not draw as much market scrutiny.

Regulation FD and Insider Trading

Communications with investors and analysts

- Recognize that most CEOs, CFOs and IR professionals are not accustomed to discussing the impacts of a global pandemic on their business.
- Information provided to an investor or analyst about the impacts could unwittingly reveal MNPI—positive or negative—about current or future operational or financial performance, and create a Reg FD issue.
- Consider whether to remind executives of the need to be circumspect when talking about the impacts of the pandemic in any non-Reg FD-compliant setting.

Communications with suppliers and customers

- Communications with suppliers and customers in their capacities as such should generally not be covered by Reg FD. However, because these communications may well involve MNPI (or the inadvertent disclosure of MNPI), it is a good idea to remind suppliers and customers that your communications are confidential and, if applicable, covered under NDAs.

Communications with employees

- Similarly, while communications with employees are generally not covered by Reg FD, you should take care not to include MNPI in employee communications unless the receiving employees understand that they may not trade before it is made public or is no longer relevant.

Executive Compensation

- Just like stock buybacks, no one will be surprised to hear that executive compensation is likely to be affected by future participation in government relief programs.
- Companies that have not yet mailed the proxy may want to consider recognizing the COVID-19 crisis and the need to support public health and safety in any Chairman, CEO or Lead Director letter.
- You may also consider adding a headnote to the CD&A acknowledging the potential impact of the pandemic on the company's 2020 performance and reminding shareholders that the impact was not factored into 2019 compensation, but will likely be a factor in 2020 compensation decisions.

Policy and Procedures for Manually Signing and Retaining SEC Filings in Light of COVID-19 Outbreak
[Date], 2020

Policy

It is the policy of the Company to comply with the rules of the Securities and Exchange Commission (the "SEC") governing the manual signing by officers and directors of each document that is to be electronically filed by the Company with the SEC (a "Filing") and the retention of such manually signed Filings. In the event the COVID-19 outbreak makes it impracticable to comply with such rules under current circumstances, it is the policy of the Company to comply with the procedures outlined in paragraph 2.

Procedures

1. Subject to paragraph 2, an officer or director signing any Filing should manually sign such Filing at or before the time the Filing is electronically submitted to the SEC and concurrently provide the manually signed Filing to the Company. The Company will retain the manually signed Filing for 5 years and will provide the manually signed Filing to the SEC on request.

2. Where it is impracticable to comply with the procedures described in paragraph 1 due to circumstances arising from the COVID-19 outbreak, the officer or director should:

    a. Manually execute the signature page of the Filing at or before the Company electronically submits the Filing to the SEC (if a printer is not available, the officer or director may manually sign his or her name to a substitute page of paper);

    b. Indicate the date and time the manual signature was executed on the Filing signature page (or substitute page); and

    c. Deliver the manually signed Filing signature page (or substitute page) to the Company as soon as reasonably practicable in light of the circumstances. The Company will retain the manually signed Filing (or substitute page) for 5 years and will provide the manually signed Filing (or substitute page) to the SEC on request.

ANNUAL MEETING OF SHAREHOLDERS
[Date]
RULES OF CONDUCT

Welcome to our 2020 Annual Meeting. In fairness to all shareholders in attendance, please observe the following Rules of Conduct.

1. The Chairman of the Annual Meeting will conduct the meeting in accordance with the Agenda.

2. Because this is a meeting of shareholders, only shareholders as of the record date of [date], 2020 are permitted to vote or ask questions during the Annual Meeting. If you have already voted your shares, your vote has been received by the Company's inspector of elections and there is no need to vote again, unless you wish to revoke or change your vote.

3. If a shareholder has a question about one of the matters on the Agenda, please submit the question in the field provided in the web portal for consideration. [Alternatively, you may ask a question by calling the telephone number that is included on the virtual meeting platform.]

4. To allow us to answer questions from as many shareholders as possible, we will limit each shareholder to [two] questions. We ask that questions be succinct and cover only one topic per question. [In the interest of having sufficient time to give all shareholders an opportunity to ask questions, we may summarize the questions received on the portal.]

5. Questions from multiple shareholders on the same topic or that are otherwise related may be grouped and answered together.

6. Shareholder questions are welcome, but we do not intend to address questions that are irrelevant to the business of the Annual Meeting or relate to a personal matter. The Chairman of the meeting will determine whether questions are out of order.

7. The Chairman may answer the question directly or invite another company representative to respond.

8. We will do our best to answer as many questions as we can on any matters listed on the Agenda before the end of the meeting.

9. Recording of the Annual Meeting is prohibited. [A webcast playback will be available at [website] [__] days after completion of the meeting.]