COVID-19: Legal Considerations for Maintaining Business Continuity

The spread of the coronavirus (COVID-19) is having an impact on many businesses as they feel the effects of travel restrictions, market instability, labor shortages, factory closures and supply chain disruptions caused by the outbreak. While the full legal, regulatory and commercial implications of COVID-19 will continue to develop, the following information may prove valuable in assisting companies with a host of difficult questions on how to conduct business during this time of uncertainty. The main goal of this alert is to arm our clients and partners with information they can utilize in developing their plans and strategies.

Phillips Lytle’s multidisciplinary Coronavirus (COVID-19) Response Team is addressing the business and legal ramifications of this pandemic. With our deep experience in assisting clients with crisis management and emergency response in business, regulatory and litigated matters, we are poised and ready to help at a moment’s notice.

BUSINESS CONTRACTS & OBLIGATIONS

Force Majeure Clauses

A force majeure clause excuses the performance of a party where such performance has become impossible or impracticable due to circumstances outside that party’s control.

Thorough force majeure provisions enumerate specific instances, including floods, labor stoppages, and “acts of God” or natural disasters; allocate risk between parties; and provide for notice and mitigation of nonperformance.

In New York State, such clauses are narrowly construed. Ordinarily, only if the force majeure clause specifically includes the event that actually prevents a party’s performance will that party be excused.

Where no such clause exists, courts will likely perform a foreseeability analysis. If a party could have foreseen the event allegedly responsible for its nonperformance at the time the contract was made, a court could find such party liable for breach.

The Uniform Commercial Code (UCC) may apply to contracts governing the sale of goods. Section 2-615 provides that delay or nondelivery is not a breach where, among other things:

- Performance as agreed upon has been made impracticable by the occurrence of a contingency, the nonoccurrence of which was a basic assumption on which the contract was made; or
- Compliance in good faith with applicable foreign or domestic governmental regulation or order makes performance impracticable, whether or not it later proves to be invalid.

Rather than relying on traditional force majeure clauses or the UCC, drafters may want to incorporate into pending contracts specialized provisions that permit a modification of obligations or even termination in the case of pandemics, supply chain interruptions or adverse government mandates.

Anticipatory Repudiation and Adequate Assurances of Future Performance

Where circumstances indicate that a contract party may not perform, the party seeking performance might claim anticipatory repudiation of the agreement as a means of mitigating loss.

To be justified in terminating an agreement and claiming anticipatory repudiation, the adverse party must have, by a communication or action, substantially impaired the value
of the contract and clearly demonstrated an intent to not perform or not to continue to perform. Grounds for anticipatory repudiation may include an indication by the adverse party that it will not deliver the goods unless the party seeking performance pays an increased price.

It is important to note, however, that an erroneous claim for anticipatory repudiation will make the party seeking performance liable for breach. A simple delay in performance, for example, that does not impair the value of the contract, does not warrant anticipatory repudiation.

Where there are reasonable grounds for uncertainty, the party seeking performance has a right to demand adequate assurances. The demand should, among other things, be in writing; state the basis for the insecurity; indicate what assurances are being requested; and provide a timeline for the adverse party’s response. If the adverse party does not provide the requested assurances, it may be grounds for canceling the contract.

SEC Filings

On March 4, 2020, the Securities and Exchange Commission (SEC) issued an order to public companies subject to reporting requirements acknowledging that “[d]isruptions to transportation, and limited access to facilities, support staff, and professional advisors as a result of COVID-19, could hamper the efforts of public companies and other persons with filing obligations to meet their filing deadlines.”

Under certain circumstances, affected companies will receive an additional 45 days to file certain Securities Exchange Act of 1934 reports, including Form 10-K, Form 10-Q and Form 20-F, otherwise due between March 1, 2020 and April 30, 2020.

Regardless of when filed, companies may want to include mention of COVID-19 to the extent it may pose a risk to business operations.

Mergers and Acquisitions – Material Adverse Change

COVID-19 could have ramifications in merger and acquisition transactions. For example, a seller’s representations may include statements that various events have not occurred since a certain date and have not had a material adverse effect on the operations of the target company. In an attempt to limit the breadth of post-closing indemnification claims, sellers may attempt to include the effects of COVID-19 in the definition of “material adverse effect” and may add COVID-19-related impacts to the disclosure schedules.

Conversely, a seller may take the opposite position with respect to drafting closing conditions in transactions that have a gap period between signing and closing. In delayed sign/close transactions, the seller often accepts the buyer’s closing condition that there has not been a Material Adverse Change (MAC) between signing and closing. If the definition of MAC includes COVID-19 effects/events, then a buyer may have greater ability to refuse to close the transaction based on COVID-19 effects/events. Therefore, a seller should try to exclude COVID-19 effects from the definition of MAC. Even without a specific reference to COVID-19 in a MAC condition, the seller will need to monitor this definition closely to determine if it is impacted by COVID-19.

LABOR & EMPLOYMENT

Employers responding to COVID-19 in the workplace need to be aware of both their legal rights and responsibilities, as well as the practical considerations in doing so to minimize disruption to operations. While there are myriad labor and employment issues that may arise regarding the COVID-19 outbreak, we have highlighted below those that employers are most likely to face at this time.

Workplace Safety

The General Duty Clause of the Occupational and Safety Health Act requires that all covered employers provide their
employees with “employment and a place of employment which are free from recognized hazards that are causing or are likely to cause death or serious physical harm.” To meet this obligation, employers should follow the “Guidance on Preparing Workplaces for COVID-19” prepared by the Occupational Safety and Health Administration, which can be found here.

Medical Inquiries and Exams

Employers may ask employees who report being ill if they are experiencing flu-like symptoms. Employers may send sick employees home and require sick employees to remain out of work. Taking an employee’s temperature is considered a medical exam regulated by the Americans with Disabilities Act (ADA) and should not be done without consulting with counsel. All employee medical information must be kept confidential.

Wage and Hour Issues

Employees who are not working typically are not entitled to wages under the Fair Labor Standards Act (FLSA). However, with certain limited exceptions, salaried overtime-exempt employees must be paid their entire salary for any workweek in which they perform any work. Overtime nonexempt employees paid on a fluctuating-workweek basis under the FLSA must, with limited exceptions, also be paid their full salary in any workweek in which they perform any work.

Leave and Accommodation Issues

Currently, COVID-19 will not typically qualify as a disability under the ADA or a serious health condition under the Family and Medical Leave Act (FMLA), unless complications develop. COVID-19 may, though, qualify as a disability under state or local disability laws, such as the New York State Human Rights Law. Employers should be aware that the Families First Coronavirus Response Act (Act), which Congress is expected to pass and the President is expected to sign shortly, would amend the FMLA to provide job-protected leave for employees affected by COVID-19. The Act would also require employers with fewer than 500 employees to provide employees with paid sick leave for COVID-19-related absences.

Responding to COVID-19 in the Workplace

An employee with a confirmed or suspected case of COVID-19 should be sent home for a minimum of 14 days to reduce the chance of further infection. Employers should identify all employees who worked in close proximity (three to six feet) with the employee in the last 14 days and also send those employees home for 14 days for the same reason. Employees who are sent home should not be identified by name, as doing so could violate the ADA and applicable confidentiality laws. Employees remaining in the workplace should be informed of the confirmed or suspected case and about the steps that are being taken to reduce the risk of infection in the workplace. Employers should also consider having a cleaning company undertake a deep cleaning of the affected workspaces.

INSURANCE

Given the impact of COVID-19, many businesses are facing potential disruptions, downtime or decreased productivity and are concerned about the risk of loss to their business. Many companies may have insurance policies that potentially afford coverage for business interruption losses. Business Interruption (BI) Insurance is typically included within a property/casualty policy or in a comprehensive package policy as an add-on or rider. Such policies may cover some or all of the following:

- Lost profits;
- Fixed costs and expenses;
- Employee wages;
- Temporary location;
- Extra expenses incurred as a result of the interruption;
- Taxes; and
- Loan payments.
The availability and scope of insurance coverage will depend upon the language of the specific policies your company has in place and the details surrounding the business interruption. Businesses should also be mindful of the importance of providing notice and submitting claims to their insurance carriers in a timely manner.

**RESTRUCTURING & FINANCE**

Earlier this month, the Office of the Controller of Currency (OCC), Federal Deposit Insurance Corporation (FDIC), and state regulators advised banks they regulate to take care of customers affected by COVID-19, recommending that they allow for short-term flexibility in loan repayment. Despite this general recommendation, the OCC cautioned banks that any loan modifications “should be based on the facts and circumstances of each borrower and terms of the loan.” The FDIC advised banks to evaluate whether or not certain loans experiencing pandemic-related stress qualify for restructuring. In summary, although COVID-19 is negatively impacting business as usual, whether or not a specific business will be considered for flexibility in its loan repayments will be evaluated on the specific challenges facing each business.

Parties to loan documents impacted by the COVID-19 outbreak should promptly analyze their rights and obligations. This includes the following:

- Understand and evaluate your business’s facts and circumstances;
- Prepare a 13-week cash flow forecasting the impact of recent events on cash flow;
- Identify key provisions of the loan documents that may be affected by recent events (e.g., representations, warranties, debt service and other covenants, events of default, requirements to comply with all laws, etc.);
- Identify notice requirements that may have been triggered;
- Analyze the potential consequences of a breach and/or default on the business or any guarantor under the loan documents or other agreements and legal obligations;
- Identify potential alternatives to cure or mitigate the default or breach;
- Keep detailed records that include the scope of the interruption to your business, and detail the factors the business may use to seek forbearance and/or restructuring with its lender;
- Develop a plan of what relief would be required to bridge the business through the pandemic-related stress; and
- Absent developing a workable internal solution, be proactive and commence a dialogue with the lender to negotiate the terms of a restructuring or forbearance of unachievable obligations under the loan documents.

In addition, the Small Business Administration is working with states to provide up to $2 million in low-interest disaster recovery loans to small businesses and not-for-profit businesses severely impacted by COVID-19. The interest rates are 3.75% for for-profit businesses and 2.75% for not-for-profits, with up to a 30-year repayment term.

**ENVIRONMENTAL**

There are a number of environmental compliance issues linked to the COVID-19 pandemic, which will need to be considered by businesses both near- and long-term. These include:

- Certain exemptions to National Environmental Policy Act and State Environmental Quality Review Act compliance;
- Identification and use of United States Environmental Protection Agency registered antimicrobial products that are determined to be effective as to COVID-19. The updated list of these products is available at https://www.epa.gov/sites/production/files/2020-03/documents/sars-cov-2-list_03-03-2020.pdf;
- Proper labeling of new or modified cleaning and antimicrobial products under both Federal and applicable state laws;
- Potential heightened disposal requirements for medical and infectious wastes;
Emergency compliance orders related to noncompliance due to supply chain and other disruptions; and
Availability of adequate and timely compliance and waste disposal testing resources.

As the response to the pandemic evolves, many new and novel compliance issues are likely to arise.

**DATA SECURITY & PRIVACY**

As organizations increasingly move online for day-to-day business activities during this pandemic, it is important not to sacrifice data security for the sake of business expediency. Existing policies should be consulted and followed, and an organization should employ a multidisciplinary team to develop what may be an evolving strategy. The team, at a minimum, should be comprised of personnel from human resources, finance, IT, corporate security and the Board. Specifically, organizations should:

- Consult policies, particularly policies concerning data management and security, personal devices, business continuity, data backup and recovery, and incident response to guide strategic decision-making;
- Use an efficient and secure messaging system for all employees, even those who do not have regular access to their work e-mails remotely;
- Use an efficient and secure messaging system for clients and business partners, and timely advise them on how they may communicate with their employees and how you plan to conduct transactions;
- Communicate strategy clearly and in a timely manner to employees, especially if the employees work from home and/or use their own personal devices to do so;
- Carefully vet online platforms and applications before endorsing mass use by employees;
- Consider strategies to reduce network traffic (such as staggered working hours);
- Obtain sufficient licenses for necessary software and prohibit employees from sharing passwords/accounts;
- Provide a list of FAQs regarding anticipated technical issues to reduce calls to the IT help desk regarding common questions (such as checking internet speed and how to increase internet bandwidth);
- Consider providing a tip sheet to employees on how to maintain confidentiality and avoid security threats, taking into account that an employee may be sharing space with their children who are home from school and spouses who are also working from home, or working from public places that provide unsecured WiFi;
- Remind employees of restrictions regarding minimum device and browser security requirements (software versions should be updated and patched), particularly if connecting to the organization’s network;
- Remind employees not to share the devices that they use for work purposes, which may be tempting as their family members are forced to also work or attend classes from home;
- Consider implementing increased security measures, such as two- or multi-factor authentication and access limitation (in scope and duration) to what is necessary;
- Employ Mobile Device Management or Mobile Application Management tools to control data on employees’ devices and train employees to notify the organization swiftly if their device is compromised or lost; and
- Remind employees not to use unapproved methods of communication, devices or access to data. For instance, employees should be wary of downloading documents to their personal device, or using personal e-mail or chat applications, particularly where the data may be automatically saved on a personal cloud. Employees should also use the organization-provided Virtual Private Network exclusively to access the organization’s information system.

The foregoing are just examples of issues to consider when moving an organization’s workforce from physical offices to an online environment. Data privacy and security...
obligations continue to apply and should not be ignored during this time.

**REAL ESTATE**

While our primary concern is health and safety, we also need to look at our contractual obligations, such as purchase and sale agreements and leases.

The following are key terms that need to be considered:
- **Force majeure**;
- **Time is of the essence**;
- **Material Adverse Change (MAC) or Material Adverse Effect (MAE)**; and
- **Best efforts**.

These concepts are often specifically covered in agreements, but not always.

**Force majeure** is typically a matter of the specific definition within an agreement. **Force majeure** is discussed in greater detail above. Keep in mind that **force majeure** generally involves when, not if. **Force majeure** events typically will delay an obligation to perform, but not forgive it. This contrasts with “time is of the essence” which, in simple terms, means that a deadline is strictly enforced. A MAC or MAE clause may, depending on the terms and conditions of the agreement, excuse performance entirely. Lastly, the phrase “best efforts” is a subjective concept, which is not easily defined.

In the context of a commercial lease, additional concepts to consider are “interruption of access and/or services,” and “BI Insurance.”

Leases often address circumstances where access to space and/or services are interrupted. These provisions are often aggressively negotiated and typically provide for a certain period of time before the clause takes effect. The specific lease provisions need to be reviewed to determine whether rent is abated.

BI Insurance becomes critical in this context. Some leases specifically require a landlord or a tenant to maintain BI Insurance. It is not necessarily true that if a landlord has BI Insurance, the tenant is not obligated to pay rent. Nor is it true that if a tenant has BI Insurance, it will cover the payment of the rent to the landlord.

This is merely an introduction to general concepts. The specific terms and conditions of the applicable agreements must be reviewed carefully. We recognize that there is much to consider in interpreting your obligations under agreements affecting real estate. Many of these provisions are governed by legislation and case law. Only time will tell whether there will be additional legislation enacted with respect to the COVID-19 pandemic.

In the meantime, everyone is well advised to:
- **Stay informed**;
- **Be vigilant and flexible**;
- **Maintain standards of care at least equal to your prior practices and the current practices of peers (such as other employees and other building owners)**;
- **Adhere to and enforce governmental mandates; and**
- **Consider various possible future scenarios and do what you can to prepare contingency plans for such scenarios, including, without limitation, working with your IT departments and supply vendors to ensure that necessary services and supplies are available.**

In addition, you need to continue to adhere to the other requirements of law, such as labor and employment, health and privacy requirements.

**Additional Assistance**

*For further assistance with the specific business impacts of COVID-19, please contact a member of the Coronavirus (COVID-19) Response Team or the Phillips Lytle attorney with whom you have a relationship.*
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