Navigating the COVID-19 Crisis – Q&A

Global Capital Markets Opportunities Guide

This Guide provides answers to common questions related to the effects of COVID-19 on global capital markets activity and on related considerations for issuers and underwriters. The Q&A in this Guide is based on the S&C Navigating the Covid-19 Crisis webinar series held on April 16, 2020.

Debt Capital Markets

1. What are the trends on the investment grade debt side?

Interestingly, the U.S. investment grade debt market has been very active this year throughout March and April. March saw some of the busiest days of the year and, although the investment grade debt markets usually experience a bit of a lull in early April before earnings season kicks into gear, that has not been the case this year. For example, on Tuesday, April 14th, eight issuers have each raised over $10 billion and over $350 billion of investment grade bonds have issued in the past four weeks. There are two complementary reasons for this. First, every issuer is thinking about liquidity as we face an uncertain future, so issuers are going to the market to add some liquidity even if it seems expensive relative to pre-COVID-19 debt costs. Second, investors, including those who are taking a break from the incredibly volatile equity markets, are drawn by attractive yields from well-known and well-capitalized issuers.

2. What trends have appeared on the high yield debt side?

In the primary market, there were a few weeks with close to no high yield activity. As the equity markets have improved, we have seen a gradual reopening of the high yield markets starting with the recent Yum! Brands bond offering. Still, the market has seen relatively few issuances. Nevertheless, we are seeing anecdotal evidence that more of the benchmark high yield issuers will have access to the market despite there being relatively few deals in the market. We have also seen quite a bit of activity on the liability management side for high yield issuers, focusing on maintaining liquidity on the one hand as well as covenant compliance and evaluation of the need for waivers. Covenant compliance is a developing issue.

3. What is the debt market like in Europe?

The developments in Europe on the debt capital markets have been very similar to what we have seen in the U.S. Large investment grade issuers used the first opportunity to secure further liquidity through bond issuances or drawings under Euro Medium Term Note programs and debtor-in-possession financings (DIPs). This was true across Europe. U.K., French, German, Dutch and other investment grade issuers went out and successfully executed these transactions. At the same time, there was a wave in other financing activity because in Europe, companies often finance themselves through bank financing rather than through the debt capital markets, especially in countries like Germany. In turn, the European high-yield market has come to a halt and has not yet really re-opened, even though some issuers and banks have begun thinking about re-opening. It is clear that high-yield issuers must expect the terms of such financing to be significantly more expensive than before the crisis, reflecting the change in risk assessment by investors.

4. Parts of Asia have been dealing with the COVID-19 situation since before the Lunar New Year holiday. What are the debt capital markets looking like in Mainland China and Hong Kong as restrictions on life and business begin to ease?

Mainland China and Hong Kong had to deal with the COVID-19 situation from an earlier time. In January, the debt capital markets were very busy, and at that time there was less clarity on COVID-19 as the situation was just beginning to unfold. As is common at the beginning of the year, many issuers were rushing to the market to raise capital before the Lunar New Year, which fell in the last week of January this year, and in part because Mainland Chinese businesses that wish to access the international debt capital markets would need to get regulatory approval from the National Development and Reform Commission, which allocates a quota to issuers so as to manage the country's overall foreign debt. So, those who received their approval for 2020 naturally took advantage of that window. February was very quiet as Mainland China was in lockdown mode. That created pent-up demand and from March we have seen investment grade issuers raising capital to strengthen their balance sheet and also take advantage of the reduction in interest rates. Although non-investment grade issuers also need capital, they are finding it more difficult to access the markets.

5. What are the debt capital markets looking like in Japan?

The Japanese debt capital markets have been slow since March. The market usually slows down in Japan from mid-March because many Japanese companies' fiscal year ends on March 31, and for pandemic-related funding needs, Japanese companies have relied more on banks than on the capital markets. Currently, some investment grade issuers with December fiscal year end are looking to access the markets and more investment grade issuers with March fiscal year ends are considering July. As in Hong Kong, non-investment grade issuers are having a hard time accessing the markets.

6. In Australia, what issues should companies and underwriters be thinking about as they prepare to go to market on a bond offering?

We are working with several Australian companies considering Rule 144A investment grade and sub-investment grade debt offerings, as well as with a number of Australian and New Zealand financial institutions that are updating their U.S. debt programs for their December or March half-year results. Due to the volatility in the markets in recent weeks, the key consideration for companies is to have their documentation ready so they are prepared to launch an offering on short notice when market conditions permit. In addition to the challenge of ensuring their disclosure appropriately reflects the potential impact and risks posed by the COVID-19 pandemic, companies and their underwriting banks need to be mindful of the so-called "135-day period" for purposes of the auditors providing negative assurance in their comfort letter, which expires on or about May 14th for December year end or half-year end reporting companies. The ability of auditors to bring down stub period comfort after the latest management accounts is particularly challenging in the current environment as it is difficult, if not in certain cases impossible, for management to provide representations as to no change to selected financial line items post-February.

Another issue companies need to be mindful of is maintaining the consistency of disclosure in the domestic and U.S. and international markets to avoid potential allegations of differential disclosure. This becomes particularly challenging when undertaking an equity raising without a prospectus in reliance on the continuous disclosure regime of the Australian Stock Exchange where a Rule 144A debt offering will follow shortly thereafter utilizing a detailed "Rule 10b-5 compliant" offering document.

7. There are a number of government lending programs that are in the works under the CARES Act and other programs. Many of these programs are available only to investment grade issuers or so-called "fallen angels", who had investment grade ratings prior to March 22. What impact will these programs have on the bond markets in general – both investment grade and high yield?

We are still trying to figure that out. For example, the term sheet for the Primary Market Corporate Credit Facility, or that catchy name PMCCF, was released by the Fed last Thursday. It allows an investment grade issuer or "fallen angel" to issue bonds to an SPV capitalized by Treasury and the Fed. We have had conversations with issuers that are interested in learning more and we are working to coordinate those discussions. We believe that the Fed will want to see the program to be viewed as a success. It should help eligible issuers to have a market for their new issuances with predictable pricing and it should provide market liquidity to help us through some expected volatile times ahead.

Equity Capital Markets

1. What have public equity offering activity levels been looking like in the U.S?

Despite the emergence of COVID-19 in China in late 2019, U.S. equity capital markets were off to a strong start in the first two months of Q1, significantly ahead of the same period in 2019. Following increasing market volatility and the market fallout later in the quarter, equity deals significantly slowed in March. Deals in certain sectors, though, are getting done – principally in healthcare – and deals continue to get done in April. So far in April, we have seen about six deals go to market, raising approximately $1.2 billion.

The convert market has also continued to see strong activity levels despite COVID-19. In fact, the value of convert deals was about 40% higher in Q1 2020 than Q1 2019 and even March of this year was consistent with 2019. So far in April, nine deals have come to market, notably Carnival Cruise Lines raising approximately $2 billion in an offering on April 4, with more deals currently in the pipeline. Issuers tapping the convert market tend to be in the technology, healthcare and consumer sectors.

2. What trends do we see in Europe?

In Europe there have been a few weeks in March with basically no activity. Interestingly, some accelerated bookbuild offerings have already come back by the end of March and the beginning of April in the U.K., France, Germany and the Netherlands, including mainly primary deals with the issuance of new shares, often around 10% of the existing share capital.

Similar to what we see in the U.S., we have also seen convertible bond activity. Mostly, these transactions have not been rescue transactions by companies under pressure due to COVID-19, but rather capital raisings in industries that have not suffered but actually benefitted from the crisis, such as the recent offering by Dutch online pharmacy Shop Apotheke. Such transactions have been completed successfully, so investors are willing to engage. At the same time, it is fair to say that activity levels on the equity capital markets side are still very low compared with those of previous years. Of course, one category that has been missing almost entirely so far in Europe this year is IPOs. Despite the fact that we continue to work on several IPOs in Europe, these deals have been postponed to later in the year.

3. What have public offering activity levels been looking like in Australia?

In Australia, the COVID-19 pandemic has essentially put a halt to work on potential IPOs. However, we are assisting a number of our Australian publicly listed clients with preparing for equity offerings in the United States, particularly those seeking to take advantage of the emergency capital raising relief announced by the Australian Stock Exchange. For instance, there have been a number of equity raisings in recent weeks as the equity markets have bounced off their lows. Some of these have been by companies looking to fortify their balance sheets and obtain liquidity. We are also starting to see some companies exploring M&A opportunities and seeking to fund them through the issuance of equity. A number of further significant capital raisings are expected over the coming weeks and months, particularly if the economy remains weak or continues to deteriorate. Still, we are a long way from the US$70 billion in capital raisings that occurred during the global financial crisis in 2008 and 2009. Particular challenges raised by these equity offerings are structuring them to allow participation by institutional investors in the United States on a private placement or Rule 144A basis. This requires compliance with U.S. private placement requirements and publicity restrictions and sometimes creates a tension between a company's legitimate desire to fully inform the market and the U.S. private offering restrictions that limit the discussion of the offering in a public forum, such as on unrestricted teleconferences and webcasts.

4. What are the equity capital markets looking like in Hong Kong?

The Hong Kong equity capital market is certainly slower in Q1 of this year. We saw some issuers who had not committed to beginning the IPO process quite naturally defer making a decision to kick off the process. Those who have commenced the process had to deal with the question of due diligence and audit because the securities regulators expect that third party due diligence on customers, suppliers, etc. will be conducted in person at the third party's premises. Given the travel restrictions and social distancing requirements, many of such meetings cannot take place in person. The Hong Kong regulators were not willing to derogate from their normal expectation and so lawyers spent many hours trying to find a solution that could work for specific situations. While many companies were badly affected by COVID-19, a small segment benefitted. These include companies in the digital economy space, such as online food delivery, audio/video conferencing and entertainment, as well as in the broader healthcare sectors of pharmaceuticals, hospitals and medical equipment (even though not directly related to COVID-19). Some have seized the opportunity brought about by record-high stock price and buoyant demand to raise capital via accelerated bookbuild offerings (ABOs/ABBs), or private placements with institutional investors. On the other end of the spectrum, with stock prices of some companies at inexpensive valuations, some controlling shareholders who have access to financing are taking the opportunity to take their listed companies into private ownership.

5. The U.S. IPO market has essentially come to a standstill. Have there been any IPOs in the U.S. in the past few weeks?

The IPO market is always interesting to follow. After two IPOs came to market during the week of March 9th (which was the week when public gatherings started to be banned in the U.S.), one would have thought we would not see any IPOs for a few months. But that has not been the case. Three IPOs have priced in April, including two biotech companies that priced upsized offerings at the top of the range. And in both cases, after-market performance has been strong – one up by 50% and the other up by 70%. Although we should never give up on the IPO market, biotech and SPACs are a bit of their own animals. Nevertheless, given the market conditions, public gathering bans, closed venues and social distancing, it is fair to say that the IPO market is largely on hold.

6. In light of the markets, are issuers still preparing for IPOs?

IPOs have certainly not completely stopped, but the pace for IPOs is measured. Deals that are getting close to making their first public filing have been put on hold, but there is no reason for an issuer who is focused on a Q3 or Q4 IPO to go pencils down. Given the confidential filing process with the SEC, a number of issuers are deciding to continue to make progress and get themselves ready with preparing financial statements and prospectus drafting. Although the SEC staff has been working from home longer than most of us have, they have done so pretty seamlessly – in fact, it seems like many SEC staff members are as stir-crazy as we are, and therefore happy to pick up their phones and have a conversation.

It will be interesting to see what happens to the IPO market after things start to open up again. Certainly, some companies will not have seen their businesses significantly affected, but they will no doubt be impacted by broader market conditions and investor sentiment. Others will have seen significant adverse effects that may take time to work through.

7. How can issuers adjust their transaction structures, especially for IPOs, to address the current situation?

Experience shows that investors may ask for a higher IPO discount shortly after a crisis, and we also expect that investors may be cautious regarding issuers with a high leverage post-IPO. Therefore, issuers may think about downsizing the IPO subject to free-float requirements and instead have larger secondary tranches post-lock-up. Issuers and banks may also consider increasing the primary tranche in the IPO to secure sufficient company proceeds and de-lever the issuer through the IPO.

PIPE Transactions

1. In prior market downturns, including the financial crisis, the market saw an increase in private investments in public equity, or PIPE, transactions. Based on recent activity, there is indication that the PIPE market will continue heating up. What has the PIPE market been seeing recently?

The playbook from prior market downturns has definitely been dusted off. We have already seen a few substantial PIPE transactions. The downturn was so fast that the issuers that need equity capital the most are having trouble getting their arms around selling equity at current prices, but over the next few months, we will see a very active PIPE market. We will see issuers whose valuations recover enough to make issuing equity attractive, and others that have no other alternative. In either case, a private process is very attractive given the overall market volatility.

2. What types of terms are expected to be the focus of significant PIPE transactions?

Beyond pricing, the key terms will focus on governance rights and protective security features. Governance rights will depend on the expected depth and duration of the relationship between the issuer and PIPE investors. The larger the equity stake, the more robust the governance rights. These rights include:

- board rights (meaning the right to appoint a specified number of directors to the board of directors/committees, which is often proportional to the investor’s as converted equity interest);
- voting and consent rights (which may include veto rights over key corporate actions taken by the issuer);
- registration rights (to provide for future liquidity of the common stock in public markets), among others.

Issuers may also seek to negotiate standstill provisions or lockup agreements. Finally, the protective features inherent in the instrument itself include dilution protection, conversion features and optional or mandatory redemption.

3. One issue that comes up in PIPE transactions is the question of whether shareholder approval is required for the transaction under stock exchange rules. The NYSE and NASDAQ rules are notoriously difficult to navigate and are key to focus on early in any transaction planning. There has been some recent relaxation of the rules, particularly with the NYSE. What kinds of changes have we seen?

On April 6, the NYSE filed an immediately effective rule change with the SEC that waives the application of certain shareholder approval requirements for new equity issuances through June 30, 2020. The relief is intended to provide NYSE-listed companies with flexibility to raise capital quickly during the COVID-19 crisis.

The relief expands two of the current exceptions to the stockholder approval requirements. First, under what's referred to as the "Related Party Transaction Rule", shareholder approval is required when a listed company issues equity securities to a director, officer or a "substantial security holder" that exceed 1% of outstanding securities/voting power prior to issuance. Where the related party status results from the person being a significant stockholder, the threshold is raised to 5% provided that the issuance meets specific minimum price requirements. The temporary waives significantly broadens the current exceptions and permits sales of securities to related parties, regardless of the percentages issued, provided: (1) the sale is for cash; (2) meets the minimum price requirements and (3) is approved by the company's audit committee (or a comparable committee of independent directors).

Second, under what is referred to as the "20% Rule", shareholder approval is required for equity issuances of more than 20% of the company's outstanding common stock or voting power. The rule is subject to several exceptions, including the "bona fide private financing" exception, which permits issuances of securities in excess of 20% for cash where the minimum price requirement is met so long as no one purchaser, or group of related purchasers, acquires more than 5% of the shares of the common stock prior to the sale. Recognizing that COVID-19 has created a liquidity crisis for many companies, NYSE noted that companies in distress often may obtain funding most easily by way of private transactions with a few key investors. The temporary relief waives the 5% ownership/voting threshold, permitting private placement of securities regardless of their size, the number of participating investors or the amount of securities purchased by any single investor provided that the minimum price requirement is met. These waivers put NYSE on equal footing with companies listed on NASDAQ, which does not require shareholders' approval in these circumstances.

4. The relaxation of listing standards is not just limited to the United States. There has been some relaxation in Australia as well, correct?

Yes, in recognition of the fact that that many Australian Stock Exchange-listed entities will need to urgently raise capital in the coming months to sustain their operations and protect themselves from a steep drop in revenue due to COVID-19, the ASX has introduced temporary relief by altering its listing rules to facilitate emergency capital raising by ASX-listed entities, which applies until July 31, 2020. Most significantly, ASX has increased the 15% limit on equity placements to 25%. The ASX also released a compliance update providing guidance and temporary relief to ASX-listed entities in respect of their continuous disclosure obligations, particularly in relation to updating the market on any earnings or operational guidance.

5. What are the current trends in Europe? Are particular industries accessing this market more than others, and will private equity play a big role?

There are a lot of discussions throughout Europe at the moment regarding PIPE transactions, for several reasons. ABOs/ABBs have largely been executed in industries that have not been affected or only minimally affected by the crisis. For capital raisings in more difficult industries, the risk premium and therefore discounts to share prices that institutional investors would request are still discouraging issuers from going out into the market, if at all possible. However, some investors, such as strategic buyers, large family offices or private equity funds may have a special insight into certain industries and may therefore be willing to move forward at acceptable prices. Further, companies may be concerned about their low share prices and seek protection against unsolicited takeover bids by issuing equity through a PIPE transaction to investors that they consider as stable, long-term oriented and somewhat immune against short-term takeover offers. We have also seen some investors opportunistically increasing their already existing stake in listed companies, for example, Italy-based Mediaset in German media group ProSiebenSat.1. As to private equity, we expect private equities to come more into this now. In the last few weeks, private equities were more focused on existing, already-signed transactions and on issues with existing portfolio companies.

This of course only offers opportunities for companies that are still attractive enough for new investors. In some industries that are hit most by the economic turmoil, rescue rights offerings may be needed. This is a lesson from 2002/2003 and 2008/2009, and we will see this throughout Europe again. The underlying concept – dilutive rights offerings with a significant discount to the Theoretical Ex-Rights Price (TERP) based on prospectuses to be approved by the national regulator – will be the same as the execution of such transactions, which often depend on the somewhat diverse corporate law concepts in the different countries in Europe. Some will require shareholder approval, others have significant authorized capital. Some can be executed after launch in a two-week process, others have rights offering periods of a minimum of four weeks.

Being Prepared for an Open Window

1. What should issuers be doing now to ensure that they are ready and are there any lessons that can be learned from companies that have gone through the capital raising process in the past few weeks?

Issuers need to be sure that they have in place the pieces necessary to complete an offering. Among the bigger issues at the moment are the accounting and disclosure issues that flow directly from the COVID-19 crisis. The SEC staff has provided some disclosure guidance that seeks to encourage more detailed disclosure about the individual impact and risks related to the pandemic. However, unfortunately many if not most issuers are finding it very difficult to provide any meaningful specific disclosures without knowing when social distancing guidelines are likely to be loosened. Not to mention, even if these issuers could make reasonable assumptions on that score, it would be difficult to predict how consumers will respond. Are people likely to immediately begin business or leisure travel again? Are they likely to buy consumer goods? Are they going to buy new homes or remodel older homes? Issuers need to address the challenges of simply preparing and vetting that disclosure in a remote working environment, possibly by rethinking how their disclosure controls and internal accounting controls work in a fully remote working environment. The difficulty in providing specific disclosures about the impact of COVID-19 will also flow into other aspects of the offering process. For example, accountants are dealing with their procedures on comfort letters, both with regards to the inquiries needed to confirm data, as well as the meaning of negative assurances in an environment in which financial metrics are surely being impacted, but in a manner that is difficult to quantify.

Given the need to act quickly and the possible limited market windows, it is also important that boards of directors are kept apprised of financing needs and plans so they are able to act quickly. Most companies have been very good about providing frequent updates to their boards about the impact of COVD-19, but maintaining that discipline and in particular including updates on financing needs and the state of the market will be important.

2. What are other steps issuers should be taking to be ready to access the market?

Maintaining an effective shelf will be important for companies to be in a position to access the markets quickly and opportunistically. For less active issuers, that means making sure your shelf is current or not going to expire in the near term. And if it is expiring, issuers should consider putting up a new one. Some companies may need to reassess their S-3 eligibility or status as a well-known seasoned issuer (WKSI). In particular, given the significant decline in equities in recent weeks as a result of COVID-19, many companies have seen their market capitalization take a big hit, which could result in a company being at risk of losing their WKSI status. WKSI status requires an issuer to have a worldwide market capitalization of $700 million or more, measured as of a date within 60 days of the "determination date" – which is the later of the filing date of the most recent registration statement or the time the most recent amendment to the issuer's shelf was filed or updated pursuant to 10(a)(3) by means of filing its Form 10-K. Although there is a well-established process for converting a WKSI shelf to a non-WKSI shelf without interrupting an issuer's ability to go to market, this would pose a problem for a company filing a registration statement for the first time or after expiration of its prior registration statement, as it would require SEC review of the shelf, rather than automatic effectiveness.

3. Are there any special considerations for foreign private issuers?

Yes, the issues that foreign private issuers need to be mindful of in terms of disclosure and preparedness are similar to those described earlier. In particular, when preparing for an offering, issuers should expect enhanced or heightened due diligence by underwriters, counsel and the auditors related to their comfort letter procedures, particularly in respect of the potential impacts of COVID-19 on the company's business and financial performance. With everyone working remotely, and with the U.S. desks of the accounting firms many times in a difficult time zone for the issuer, the timing to complete the preparatory work should not be underestimated. In addition, since most foreign private issuers do not report results on a quarterly basis, but rather six-monthly and annually, as mentioned earlier, the "blackout" period for the auditors to provide negative assurance in their comfort letter expires on or about May 14th for December year end or half-year end reporting companies. Also, since almost all foreign private issuers maintain their principal listing in their domestic market, those issuers face the additional challenge of maintaining the consistency of their disclosure in their home market with what they will be disclosing in U.S. offering documents or filings.

4. What other issues should foreign private issuers be thinking about given that mandatory reporting is on a much less frequent basis?

Since most foreign private issuers do not report quarterly, it raises some of the practical issues discussed earlier, such as the 135-day rule for negative assurance in auditors' comfort letters. It also means that they sometimes may have more flexibility to access international debt or equity markets, particularly the United States, compared to their U.S. peer companies who blackout of new issuance until their 10-Qs are filed with the SEC. In fact, we advised an Australian global company recently that was able to take advantage of relatively favorable market conditions to launch an equity offering while U.S. companies in the sector were out of the market pending release of their 10-Qs.

5. What changes, if any, should be expected with regard to blackout periods or insider trading policies in response to COVID-19 and the extreme volatility in the markets?

It's probably too early to make this assessment. Although China is relaxing some measures, other countries in Asia are tightening and there is fear that China may tighten again if the situation takes a turn for the worse.

Disclosure Considerations

1. The SEC has been putting out a lot of guidance recently and it can be hard for all of us to keep up, but one statement stood out: the recent statement by Chairman Jay Clayton and Director of the Division of Corporation Finance Bill Hinman. What are the key takeaways of that statement?

That was a very interesting statement that Jay Clayton and Bill Hinman put out last week. It is worth a read. Many times SEC statements can be quite technical, but you could tell this one came from two former disclosure practitioners. We would cite two takeaways. First, after stressing the importance of business continuity information, it asked issuers to put out forward-looking information, noting that at this point in this crisis, historical information has relatively less significance. In their words, issuers will not be second-guessed by the SEC for good faith efforts to provide appropriate forward-looking information. Secondly, it cited the need for that information to aid the overall economic recovery, noting that not only shareholders but also stakeholders, such as customers and suppliers, rely on that information to make their own business decisions.

2. Are issuers taking heed of the guidance and altering some of their disclosure?

To a certain extent, yes. We are not seeing a trend toward quantitative guidance, but issuers are putting out fulsome business continuity information and looking forward qualitatively with properly framed assumptions that are also set forth.

3. There remains so much uncertainty about COVID-19 and when the economy will open. Take for example some industries, such as travel, that are entirely dependent on the timing of lifting of restrictions in the first instance, but then add on top of that the timing of when people will really begin to travel again in full force. How should companies be approaching any forward-looking guidance and how can they best protect themselves from legal exposure down the line?

The SEC has encouraged companies to provide disclosure that would help investors evaluate the current and expected impact of COVID-19 through the eyes of management and to proactively revise and update disclosure as facts and circumstances change. Companies should be providing as much information and guidance as possible, but also emphasizing the forward-looking nature of any guidance, with as much detail regarding risk factors as possible. It will be important for companies to avoid boilerplate where possible, and inform investors about the various factors relevant to their business that could cause any guidance or other statements regarding future performance not to be met.

If we look at the developments in Europe in light of the COVID-19 pandemic, the European Securities and Markets Authority, the French Financial Market Authority, the U.K. Financial Conduct Authority (UK FCA) and Financial Reporting Council as well as the German Federal Financial Supervisory Authority recently reminded market participants of their disclosure and other transparency obligations under applicable European and national laws. They all emphasized certain aspects of dealing with "material non-public information" or "inside information" as defined under European law that are particularly relevant in these times inter alia for earnings releases and interim or full-year guidance statements. The details of these public statements partially differ, but all regulators acknowledge the difficulties that issuers may have in assessing the effects of the current crisis on their companies and in predicting future results, while of course still reminding issuers to comply with the applicable regime of adequately informing the market. In this context, the UK FCA has granted issuers a temporary two-month extension, to the four months from the end of their financial year they normally have, to publish their audited annual financial reports.

4. What kinds of issues and concerns should Mainland Chinese and Hong Kong issuers keep in mind?

Most Chinese businesses have a financial year end of December 31 and under the Hong Kong Stock Exchange rules, such companies must report their financials by end of March. A failure to report their earnings would lead to a suspension in the trading of their shares. So, after the Lunar New Year, Hong Kong regulators were really concerned that a significant number of companies could not have their audit work done in time for their earnings release, which could lead to many suspensions and negatively impact the market. Hong Kong regulators were willing to show some flexibility in this respect, but fortunately most companies reported their earnings before the end of March deadline and so this potential crisis was averted. Another issue was the need for listed issuers to update the markets on any inside information from the time such information arose. In the beginning when there was so much uncertainty, there was some hesitancy to be the first to make statements but soon thereafter many companies gave an update on the impact of the shutdown on their businesses, which then became the norm. Some also took the opportunity to disclose the efforts they made to provide assistance to those in need as part of their corporate social responsibility.

5. Issuers and their counsel will certainly be focused on the content of the earnings release and should be prepared to host the earnings call remotely and deal with any technology issues. But there is another aspect of earnings season, and that is the post-call discussions with investors and analysts. Are there considerations that issuers should keep in mind?

Yes. This quarter, management and the IR function should be keenly aware of potential issues that could arise with respect to compliance with Regulation FD. The Regulation FD risk arises from the dynamic nature of and uncertainty surrounding COVID-19 and the possibility of inadvertently communicating material non-public information selectively. In this environment, facts may change quickly and any new information or “color” provided in the supplemental private conversations may be viewed as material, particularly as it may relate to the company’s response to COVID-19’s changing circumstances. The recent SEC guidance has been clear on the importance of issuers taking necessary steps to avoid selective disclosure when discussing material information related to the impacts of COVID-19. Management and IR should be coordinating internally to avoid potential foot faults in these post-earnings discussions. For some companies, this may involve limiting how far past earnings private discussions may occur. For others, it may involve updating the market more frequently to permit management to engage in discussions with investors/analysts later in the quarter.

There will be a need to focus on Regulation FD and the content of discussions more than ever before.

6. The SEC has a lot of proposed amendments on deck that we have been tracking in-house. What will happen to all of that proposed rulemaking?

While the SEC remains fully operational, it’s fair to say COVID-19 has been in the forefront of their agenda. Proposed rulemaking certainly will be delayed; the question will be for how long. The staff has recognized that COVID-19 may have delayed the completion and submission of comments in response to certain proposed actions for which the comment period expired in March. The SEC said it won’t take action on these matters before May 1 to allow commentators additional time if needed to submit comments. This extension applies to proposals related to amendments to the qualifications of accountants, amendments to the definition of accredited investor and disclosure of payments by resource extraction issuers, among others. The deadline for comments on other proposed rulemaking remains unchanged at the moment, although the SEC’s website notes that Chairman Clayton will consult with other Commissions and expand the list as appropriate. Notable proposed amendments for which comments remain on schedule include amendments to MD&A (comments due April 28) and amendments related to improving access to capital in private markets (comments due June 1).

7. We are in the middle of preparing our 10-Q right now and are wondering whether we should repeat all of our risk factors or just update for COVID-19 and any other updates. What are the best practices in this case?

The form provides for disclosure of material changes from the risk factors in the Form 10-K. So the form requirement goes to updates. Furthermore, although we have discussions with issuers from time to time about repeating the whole set of risk factors so the new information does not stand out, your COVID-19 risk disclosure is not bury-able. The best practice, and the recommended practice here, is to just update for COVID-19 – no one is going to miss it.

8. I have a registration statement in process with the SEC. Are they still reviewing registration statements?

Yes, the SEC continues to review registration statements. And in our experience, this is true for all major regulators world-wide. We have, for example, two prospectuses currently under review by the German regulator BaFin, and neither the review periods nor the process itself has changed. So, regulators are fully functioning globally.

Share Repurchases

1. What have we seen with regard to share repurchase activity in the past several months?

Some companies may have a fair amount of liquidity but nevertheless are seeing their stock price severely depressed. Rewinding a few weeks, as the COVID-19 situation began to unfold and some of the government funding legislation was making its way through Congress, it looked like there might be a complete ban on share repurchases. The total ban on share repurchases was not implemented, instead, companies looking for government funding under certain of the plans would be restricted in repurchasing their shares. Nevertheless, we saw a lot of companies terminate their share repurchase programs, for a wide range of reasons – some likely to preserve cash and others for optics reasons. However, there are some companies that may look to opportunistically repurchase their shares.

2. What are some of the considerations for companies that may be looking to start a share repurchase program at this point?

Certainly, issuers that are considering accessing government funding will want to take those plans into consideration. Other issuers that do not expect to access government funding may want to preserve their ability to do so if circumstances change significantly. For those issuers entering into new repurchase programs, they need to be comfortable that they do not have material nonpublic information. With circumstances around COVID-19 changing as quickly as they are, a determination that an issuer is not in possession of material nonpublic information may be more difficult than under normal circumstances. Depending on a company's particular circumstances, it should consider whether it may need to revisit, refresh or update previous disclosure before repurchasing shares. It is important to keep in mind that, in the context of repurchases, undisclosed "good news", or an overstated description of risks or negative impacts, could, when viewed in hindsight, be problematic. Lastly, some companies may want to consider the optics of entering a share repurchase program at this time.

The government funding point is key. Governments around the world are providing funding at extraordinary levels, some in the form of grants and many in the form of loans. Those come with conditions that need not only to be assessed as a commercial matter but also evaluated for purposes of impact on disclosures (dividend and share repurchase restrictions being obvious important issues). Many funding programs are also conditioned on some showing that funds are not otherwise available to the business in question, and market volatility will complicate that inquiry. If the high yield market, for example, is open sporadically, will government funding programs, or businesses' appetite to take that funding, vacillate?

For further information or thought leadership in relation to the COVID-19 Crisis, please visit our Coronavirus: S&C Updates webpage. Our partners are happy to answer your questions and provide further support.