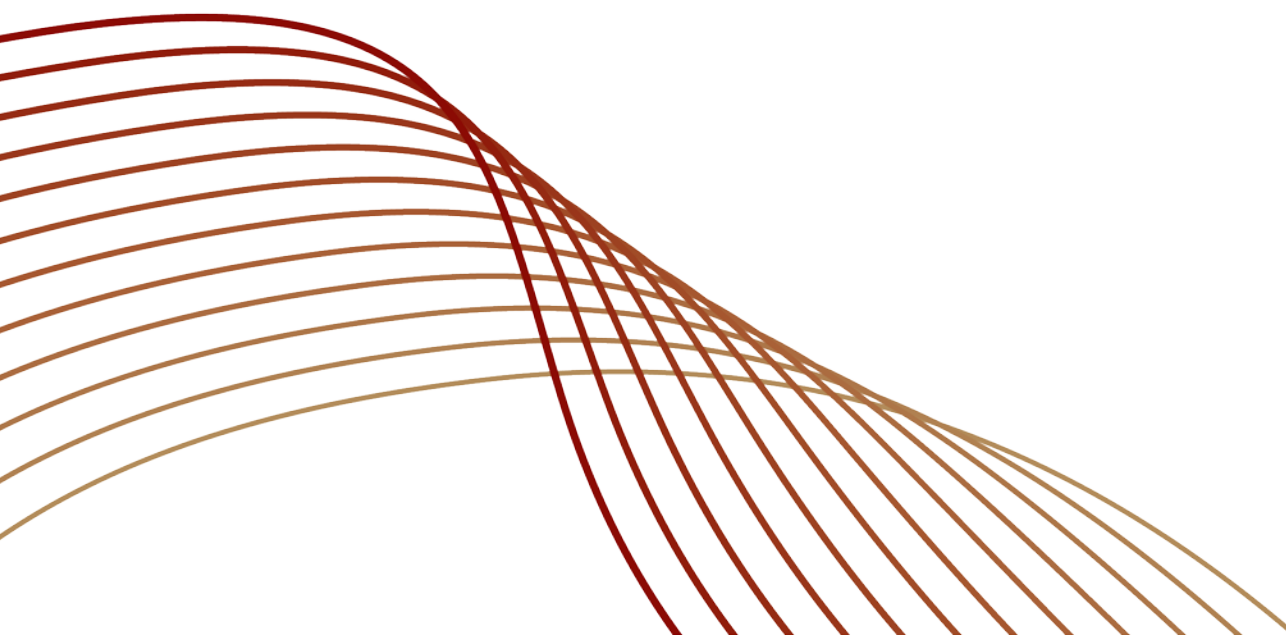


# SEC DISCLOSURES AND LIABILITY IN LIGHT OF COVID-19

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Thursday, April 2, 2020



**PAUL**  
**HASTINGS**

- Introduction
- Disclosure Trends Around COVID-19
- Current SEC Guidance
- Liability Considerations
- Planning for Q1 Financial Reporting
- FAQs for COVID-19 Disclosures

- **Risk Factors:** By early March, companies were taking different approaches. Companies that have significant operations or supply chains involving China, or that are particularly vulnerable to the impact of COVID-19, were including more tailored disclosures. As the situation has progressed since late January, we have seen an increase in registrants that include disclosure of risks related to COVID-19 in their annual reports on Form 10-K or Form 20-F, and such disclosures have become much more specific as to the likely ramifications of the global pandemic impact on their business.
- **MD&A:** Companies began including COVID-19-related disclosures in their MD&A that were customized for their business and industry. This disclosure often covered potential trends or uncertainties affecting subsequent periods, and it identified any direct business connection to China or surrounding areas, as well as any negative impact expected as a result of a reduction in people's ability or willingness to travel. The language usually tracked the related risk factor or, where included, the financial statement subsequent events footnote.
- **Financial Statement Subsequent Events Footnote:** On February 19, 2020, SEC Chairman Jay Clayton noted in a public statement that companies and their auditors should consider whether financial statement disclosure about COVID-19 is appropriate in the subsequent events footnote. As of early March, most companies that included such disclosure were heavily concentrated in the travel and hospitality industries, but some companies with significant operations or supply chains involving China also included such disclosure. In each case, the subsequent events disclosure was tailored to the specific circumstances and operations of the company.

- Recent public company filing/disclosures trends:
  - Form 10-K and Form 10-Q filings including risk factors relating to COVID-19, discussion of COVID-19 as a trend or factor affecting results in MD&A, and subsequent event footnote disclosures relating to COVID-19;
  - Form 8-K filings updating or withdrawing previously provided guidance as a result of the impacts of COVID-19, as well as earnings press releases where companies have opted not to provide guidance for 2020 or interim periods given the uncertainty created by COVID-19;
  - Form 8-K filings providing business operations updates (such as store closures, supply chain interruptions, etc.), typically as Regulation FD disclosure under Item 7.01, that provide specific and detailed information about the business and operational impacts of COVID-19 faced by particular companies or industries;
  - Form 8-K filings reporting new material commercial contracts for businesses engaged in providing goods, pharmaceuticals, medical devices, or other supplies that may be used in combatting the pandemic;
  - Form 8-K filings disclosing draws on revolving credit facilities as part of a company's COVID-19 preparedness strategy;

# SEC DISCLOSURE TRENDS

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- Form 8-K filings disclosing capital structure updates, such as dividend suspensions, the suspension of share buyback programs, and the implementation of share buyback programs;
- Form 8-K filings including updated risk factors and/or trends and factors affecting MD&A disclosures from previously filed periodic reports;
- Form 8-K filings disclosing the temporary departure of an executive officer due to COVID-19;
- Form 8-K filings disclosing voluntary and involuntary salary or compensation reductions taken by Named Executive Officers (“NEOs”) in response to COVID-19; and
- Form 8-K filings and proxy statement disclosures regarding upcoming annual meetings—either being held using virtual means, or reserving the right to change to a virtual meeting depending on the developments with COVID-19—as well as bylaw amendments to allow for virtual meetings.

- March 25 Disclosure Topic 9 on COVID-19 Disclosures.
- While the SEC Staff Guidance recognizes that it may be difficult for a company to assess or predict with certainty the broad effects that COVID-19 will ultimately have on its business or operations (as many factors are beyond a company's control), the guidance reminds companies that the risks and effects that they have experienced to date, or expect to experience in the future, and the ways in which their management is responding to the evolving circumstances may be material to investors and market participants.

- How has COVID-19 impacted your financial condition and results of operations? In light of changing trends and the overall economic outlook, how do you expect COVID-19 to impact your future operating results and near-and-long-term financial condition? Do you expect that COVID-19 will impact future operations differently than how it affected the current period?
- How has COVID-19 impacted your capital and financial resources, including your overall liquidity position and outlook? Has your cost of or access to capital and funding sources, such as revolving credit facilities or other sources changed, or is it reasonably likely to change? Have your sources or uses of cash otherwise been materially impacted? Is there a material uncertainty about your ongoing ability to meet the covenants of your credit agreements? If a material liquidity deficiency has been identified, what course of action has the company taken or proposed to take to remedy the deficiency? Consider the requirement to disclose known trends and uncertainties as it relates to your ability to service your debt or other financial obligations, access the debt markets, including commercial paper or other short-term financing arrangements, maturity mismatches between borrowing sources and the assets funded by those sources, changes in terms requested by counterparties, changes in the valuation of collateral, and counterparty or customer risk. Do you expect to disclose or incur any material COVID-19-related contingencies?
- How do you expect COVID-19 to affect assets on your balance sheet and your ability to timely account for those assets? For example, will there be significant changes in judgments in determining the fair-value of assets measured in accordance with U.S GAAP or IFRS?

- Do you anticipate any material impairments (e.g., with respect to goodwill, intangible assets, long-lived assets, right-of-use assets, investment securities), increases in allowances for credit losses, restructuring charges, other expenses, or changes in accounting judgments that have had or are reasonably likely to have a material impact on your financial statements?
- Have COVID-19-related circumstances such as remote work arrangements adversely affected your ability to maintain operations, including financial reporting systems, internal control over financial reporting and disclosure controls and procedures? If so, what changes in your controls have occurred during the current period that materially affect or are reasonably likely to materially affect your internal control over financial reporting? What challenges do you anticipate in your ability to maintain these systems and controls?
- Have you experienced challenges in implementing your business continuity plans or do you foresee requiring material expenditures to do so? Do you face any material resource constraints in implementing these plans?
- Do you expect COVID-19 to materially affect the demand for your products or services?
- Do you anticipate a material adverse impact of COVID-19 on your supply chain or the methods used to distribute your products or services? Do you expect the anticipated impact of COVID-19 to materially change the relationship between costs and revenues?
- Will your operations be materially impacted by any constraints or other impacts on your human capital resources and productivity?
- Are travel restrictions and border closures expected to have a material impact on your ability to operate and achieve your business goals?



- Helpful reminders, from an SEC enforcement and litigator's perspective
  - Demonstrate good faith
    - Involve counsel – internal and external
    - Pick up the phone and discuss the issues
    - Collaborate with others and designate point personnel
    - Follow designed policies and procedures
    - Listen to the whistleblowers
  - Considerations about the process and the disclosures
    - Duty to update and duty to correct
    - Affirmative statements vs. omissions
    - Embrace qualifying statements
      - Forward-looking statements / bespeaks caution doctrine

- False and misleading statements
  - Impact on the business
  - Risk disclosures
  - Accounting disclosures
  - Sales figures
- Inquiries related to MNPI and the disclosure process
  - Insider trading
  - Reg FD
- Controls Inquiries
  - Internal controls
  - Disclosure controls

## Inovio Pharmaceuticals, Inc.

- Asserts claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934.
- Focuses on statements made by CEO concerning the company's ability to produce a COVID-19 vaccine.
  - CEO stated in public that Inovio had developed a COVID-19 vaccine within “three hours” and expected to start testing the vaccine in the coming months.
- Following these statements, stock price more than quadrupled. However, after one research outlet publicly challenged CEO's claims, CEO disclosed that Inovio did not possess a vaccine, but instead had “designed a vaccine construct”—a precursor to a vaccine.
- Stock price dropped 71% on this news.

## Norwegian Cruise Lines

- Asserts claims under Sections 10(b) and 20(a) of the Securities Exchange Act of 1934.
- Complaint alleges that company issued a series of disclosures in February 2020 that discussed a positive outlook for the company and “touted” the company’s procedures to protect the health and safety of guests and crew.
- These statements were allegedly false because company was allegedly “providing customers with unproven and/or blatantly false statements about COVID-19 to entice the purchase of cruises.”
  - News articles cited “leaked” documents from company, purportedly suggesting that it directed its salesforce to lie to customers about COVID-19, including that the virus cannot live in “tropical temperatures” and was an “overhyped pandemic scare.”
- Following these reports, stock fell roughly 60%.

- What to expect?
  - Event-driven securities litigation
  - Accuracy is paramount
  - Undisclosed materialized risks a potential fertile ground
  - The generic versus the specific
  - Causation conundrum

- The SEC Staff Guidance contemplates that issuers may reflect the nonrecurring charges and expenses associated with COVID-19 in their non-GAAP financial measures. However, issuers must ensure that any non-GAAP financial measures comply with Item 10 of Regulation S-K and Regulation G, including the following:
  - highlighting why the measure or metric is useful and how it helps investors assess the impact of COVID-19 on the company's financial position and results of operations;
  - taking care to afford equal or greater prominence to the most comparable GAAP measures;
  - reconciling non-GAAP measures to the most comparable GAAP measures; the Staff will, for purposes of COVID-19 related disclosures, allow issuers to reconcile non-GAAP financial measures to preliminary GAAP results, or a range of preliminary GAAP results, that may require additional information and analysis to complete;
  - if a company presents non-GAAP financial measures that are reconciled to provisional amount(s) or an estimated range of GAAP financial measures in reliance on the above position, it should limit the measures in its presentation to those non-GAAP financial measures it is using to report financial results to its board of directors; and
  - if a company presents non-GAAP financial measures that are reconciled to provisional amount(s) or an estimated range of GAAP financial measures, it should explain, to the extent practicable, why the line item(s) or accounting is incomplete, and what additional information or analysis may be needed to complete the accounting.

- *Q: Are we obligated under SEC rules to update investors about the impacts of COVID-19 on our business?*
- *Q: How frequently are we obligated to update investors about impacts, particularly where our business is changing day-to-day?*
- *Q: Should we close our trading window for insiders?*
- *Q: What liability do we have for statements made relating to COVID-19? Are the forward-looking statements we make protected from liability?*
- *Q: We previously released guidance—do we have to update it?*

## THE AMERICAS

Atlanta  
Century City  
Chicago  
Houston  
Los Angeles  
New York

Orange County  
Palo Alto  
San Diego  
San Francisco  
São Paulo  
Washington, D.C.

## ASIA

Beijing  
Hong Kong  
Seoul  
Shanghai  
Tokyo

## EUROPE

Brussels  
Frankfurt  
London  
Paris



21 Offices

ACROSS THE AMERICAS, ASIA,  
AND EUROPE

1 Legal Team

TO INTEGRATE WITH THE STRATEGIC  
GOALS OF YOUR BUSINESS

PAUL  
HASTINGS



# OUR OFFICES

## THE AMERICAS

### Atlanta

1170 Peachtree Street, N.E.  
Suite 100  
Atlanta, GA 30309  
t: +1.404.815.2400  
f: +1.404.815.2424

### Century City

1999 Avenue of the Stars  
Los Angeles, CA 90067  
t: +1.310.620.5700  
f: +1.310.620.5899

### Chicago

71 S. Wacker Drive  
Forty-fifth Floor  
Chicago, IL 60606  
t: +1.312.499.6000  
f: +1.312.499.6100

### Houston

600 Travis Street  
Fifty-Eighth Floor  
Houston, TX 77002  
t: +1.713.860.7300  
f: +1.713.353.3100

### Los Angeles

515 South Flower Street  
Twenty-Fifth Floor  
Los Angeles, CA 90071  
t: +1.213.683.6000  
f: +1.213.627.0705

### New York

200 Park Avenue  
New York, NY 10166  
t: +1.212.318.6000  
f: +1.212.319.4090

### Orange County

695 Town Center Drive  
Seventeenth Floor  
Costa Mesa, CA 92626  
t: +1.714.668.6200  
f: +1.714.979.1921

### Palo Alto

1117 S. California Ave.  
Palo Alto, CA 94304  
t: +1.650.320.1800  
f: +1.650.320.1900

### San Diego

4747 Executive Drive  
Twelfth Floor  
San Diego, CA 92121  
t: +1.858.458.3000  
f: +1.858.458.3005

### San Francisco

101 California Street  
Forty-Eighth Floor  
San Francisco, CA 94111  
t: +1.415.856.7000  
f: +1.415.856.7100

### São Paulo

Av. Presidente Juscelino Kubitschek, 2041  
Torre D, 21º andar  
Sao Paulo, SP  
04543-011  
Brazil  
t: +55.11.3521.7109  
f: +1.212.230.7647

### Washington, D.C.

875 15th Street, N.W.  
Washington, D.C. 20005  
t: +1.202.551.1700  
f: +1.202.551.1705

## ASIA

### Beijing

Suite 2601, 26/F  
Yintai Center Office Tower  
2 Jianguomenwai Avenue  
Chaoyang District  
Beijing 100022 PRC  
t: +86.10.8567.5300  
f: +86.10.8567.5400

### Hong Kong

21-22/F Bank of China Tower  
1 Garden Road  
Central Hong Kong  
t: +852.2867.1288  
f: +852.2526.2119

### Seoul

33/F West Tower  
Mirae Asset Center1  
26, Eulji-ro 5-gil, Jung-gu  
Seoul, 04539, Korea  
t: +82.2.6321.3800  
f: +82.2.6321.3900

### Shanghai

43/F Jing An Kerry Center Tower II  
1539 Nanjing West Road  
Shanghai 200040, PRC  
t: +86.21.6103.2900  
f: +86.21.6103.2990

### Tokyo

Ark Hills Sengokuyama Mori Tower  
40th Floor, 1-9-10 Roppongi  
Minato-ku, Tokyo 106-0032  
Japan  
t: +81.3.6229.6100  
f: +81.3.6229.7100

## EUROPE

### Brussels

Avenue Louise 222  
1050 Brussels  
Belgium  
t: +32.2.641.7460  
f: +32.2.641.7461

### Frankfurt

TaunusTurm  
Taunustor 1  
60310 Frankfurt am Main  
Germany  
t: +49.69.907485.0  
f: +49.69.907485.499

### London

100 Bishopsgate  
London EC2N 4AG  
United Kingdom  
t: +44.20.3023.5100  
f: +44.20.3023.5109

### Paris

32, rue de Monceau  
75008 Paris  
France  
t: +33.1.42.99.04.50  
f: +33.1.45.63.91.49

For further information, you may visit our home page at  
[www.paulhastings.com](http://www.paulhastings.com) or email us at [info@paulhastings.com](mailto:info@paulhastings.com)