

# Managing the commercial fallout of COVID-19 and the new reality

Much has been written about the unprecedented nature and long term impact of COVID-19 and the problems arising as a result. Businesses operating in multiple jurisdictions are not immunised or isolated from those risks.

The purpose of this update is to identify the issues, things to think about and to provide some practical solutions for businesses operating in Australia.

## CHANGES TO FOREIGN INVESTMENT REVIEW FRAMEWORK

All proposed foreign investments into Australia subject to the *Foreign Acquisitions and Takeovers Act 1975* (Cth) (**FATA**) will require approval, regardless of the value or the nature of the foreign investor. This will be achieved by reducing to \$0 the monetary screening thresholds for all foreign investments.

To deal with this additional administrative load on the Foreign Investment Review Board (**FIRB**) and the ATO, the Treasurer has stated that there will be an increase in the timeframe to review applications from 30 days to 6 months to ensure the FIRB and the ATO have enough time to screen applications.

Despite this, the FIRB has said it will seek to accommodate commercial deadlines wherever possible and will prioritise investments which the FIRB views to be in the nation's interest by building business and maintaining or creating Australian jobs.

The specific mechanics of the proposed changes are yet to be released. However, David Irvine has indicated that there may be a temporary change as to how the FIRB applies the national interest test "*these temporary measures are necessary to protect the national interest during a historically challenging time for the economy, businesses and the broader community*".

### **So what hasn't changed?**

The Treasurer and the FIRB Chair have stated that these measures are not intended to be a block on foreign investment, and will prioritise investments which are in the FIRB views to be in the 'nation's interest. Practically, of course, delays in approvals may hinder foreign investment.

The FIRB and ATO will still be applying a national interest test in considering whether a significant action to be taken by a foreign person will be approved, or any conditions on the acquisition.

There are still avenues for foreign investment that may not require FIRB approval however as always, extreme care should be taken in pursuing these options.

## PRACTICAL STEPS YOU CAN DO NOW

Below we share some practical things that businesses can do in response to COVID-19.

Tip	Steps to take
Talk to the bank – Hardship	<p>Talk to the bank. Australian banks have indicated their willingness to work with customers by offering loan extensions, repayment free periods and interest free periods.</p> <p>Particularly with the insolvency rule changes, banks are willing to speak to customers, even where customers are not strictly meeting the published "hardship" criteria.</p> <p>If you are a commercial landlord, the Australian Banking Association has announced a number of measures in relation to commercial tenancies. These measures include six month deferral of loan repayments. It is important to note that these measures may only be accessed where the commercial lease remains in place.</p>
Cashflow modelling – get accounting advice	<p>Understand what makes your business tick, and where its pressure points are.</p> <p>Do some modelling with your accountant so you can plan your cash flows over the next 3, 6, 9 and 12 months and have a plan in place to succeed.</p> <p>Accountants are a great resource to rely upon for access to the various stimulus packages and administrative relief afforded by Governments. Where businesses are eligible, you should seek to access those benefits. It is important to keep in mind that legislation relating to director penalty notices have not been stayed or removed. This means that that it is important to plan for any future exposure that might arise for deferring payments relating to PAYG, super and GST.</p>
Speak to landlords	<p>The recent announcements of temporary moratoriums on eviction for non-payment of rent. Speak to landlords to discuss rent relief (or reduction) and temporary amendments to the lease.</p> <p>The cost-sharing or deferral of losses between landlords and tenants, along with Commonwealth, state and territory governments, local government and financial institutions means that there are options available which can be used to ensure that your business continues "over the bridge".</p> <p>Matters which could be discussed include:</p> <ul style="list-style-type: none"> <li>• rental review (this may be short term or long term);</li> <li>• rental deferral;</li> <li>• rent and outgoing abatement (this would likely be short term);</li> <li>• drawdown on existing security deposits with no requirement to top them up (at all or for a period).</li> </ul> <p>In preparation for meeting with landlords, consider some other arrangements which could be offered including:</p> <ul style="list-style-type: none"> <li>• entering into a forbearance arrangement;</li> <li>• personal guarantees supported by mortgages or a security interest over assets (in our experience, many personal guarantees are not supported by security);</li> <li>• increase bank guarantee (if you can get agreement from your bank).</li> </ul>
Debtor management – start talking to debtors now	<p>The increase in the threshold (\$2,000 to \$20,000) and timeframes for bringing insolvency proceedings (21 days to 6 months) means aged</p>

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	<p>debtors may live on for longer than they would have in the pre-COVID-19 world.</p> <p>Negotiating (and importantly, documenting) with your aged debtors for forbearance and modest instalment payment arrangements may see you keep some cash coming in the door whilst securing your position.</p>
<p>Security review - understand your security position</p>	<p>Where customers paying in arrears and there are existing securities in place (or where ones should be put in place), it is important to understand:</p> <ul style="list-style-type: none"> <li>• Can security be taken – what do your terms and conditions say?</li> <li>• Have registrations been done – if not, it is time to register?</li> <li>• Is there other security – personal guarantees, etc.?</li> </ul> <p>With the change to the thresholds and timeframes for bringing insolvency proceedings (21 days to 6 months), debtors will take longer to pay, so ensuring you have security will be key.</p> <p>A review of your security position is key for securing your position. A review will require:</p> <ul style="list-style-type: none"> <li>• a review of your terms and conditions of supply;</li> <li>• a review of securities registered by you against the assets of your customers (likely on the Personal Property Securities Register);</li> <li>• a review of your debtor lists;</li> <li>• a review of signed agreements provided by your customers.</li> </ul>
<p>Employees – implementing alternative work arrangements and steps where difficult decision have to be made</p>	<p>Make sure you are discharging all of your obligations to your employees, including:</p> <ul style="list-style-type: none"> <li>• discharging your duty of care to keep them safe, both at work and on their way to work;</li> <li>• if they are working from home, discharging your obligations to ensure they have a safe place to work;</li> <li>• adequately providing leave, where required.</li> </ul> <p>The recent announcements of the government means that some of the immediate pressures regarding employment costs have been reduced. However, there may be some circumstances where tough decisions may still need to be made. Some options open to employees include:</p> <ul style="list-style-type: none"> <li>• negotiated outcomes with your staff where they vary their employment agreements (in the short term or long term);</li> <li>• stand downs during periods of inactivity; and</li> <li>• redundancies.</li> </ul>
<p>Take advantage of administrative relief</p>	<p>Taking account of the comments regarding director penalty notices, etc., the Federal Government announced administrative relief which might be able to be accessed by business. To date, the ATO has identified the following as areas for potential relief:</p> <ul style="list-style-type: none"> <li>• Deferring by up to four months the payment date of amounts due through the business activity statement (including PAYG instalments), income tax assessments, fringe benefits tax assessments and excise.</li> <li>• Allowing businesses on a quarterly reporting cycle to opt into monthly GST reporting in order to get quicker access to GST refunds they may be entitled to.</li> <li>• Allowing businesses to vary PAYG instalment amounts to zero for the March 2020 quarter. Businesses that vary their PAYG instalment to zero can also claim a refund for any instalments made for the September 2019 and December 2019 quarters.</li> <li>• Remitting any interest and penalties, incurred on or after 23 January 2020, that have been applied to tax liabilities.</li> </ul>

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	<ul style="list-style-type: none"> <li>Working with affected businesses to help them pay their existing and ongoing tax liabilities by allowing them to enter into low interest payment plans.</li> </ul>
Insurance review	<p>Businesses should review their insurance policies to determine if there is business continuity insurance which responds to the current situation.</p> <p>As all insurance policies are not the same, it is important to consider that each policy will turn on its wording, in particular, the exclusions and individual endorsements need to be considered.</p> <p>If you are unsure whether there is coverage or whether it is excluded, you should speak with your insurance broker.</p>
Cyber security – managing risk	<p>Cyber-criminals have become creative in capitalising on Coronavirus to corrupt 'users' computers, so knowing the signs of a potential attack is key. Some recent examples include:</p> <ul style="list-style-type: none"> <li><i>phishing emails which contain attachments claiming to offer Coronavirus safety information</i>, that install destructive files on users' devices when downloaded;</li> <li><i>phishing emails which appear to have come from trusted advisors such as government departments and health authorities</i>, with links that take users to generic looking Microsoft login pages and ask them to enter their user credentials; and</li> <li><i>websites which lure users in with Coronavirus-related domain names</i> and then encourage them to click on malicious links or download unsafe documents.</li> </ul> <p>Now is a time to check your current practices and where possible, improve security so that the risk of a successful attack is minimised.</p> <p>Strategies that employees can use to identify cyber-threats include:</p> <ul style="list-style-type: none"> <li>checking the URL of websites, they access for incorrect spelling or unusual domain names;</li> <li>being cautious about emails or websites which encourage them to click on links to new pages; and</li> <li>monitoring email and website content for indicators that it may be illegitimate, including spelling or grammatical errors, incorrect language translations, and the use of low resolution images or graphics.</li> </ul> <p>Businesses can also:</p> <ul style="list-style-type: none"> <li>institute a data breach response plan, which includes what might constitute a data breach, who should be notified, and how to respond to any media attention;</li> <li>map what data your business stores, its location, and how it flows from one place to the next;</li> <li>encrypting and de-identifying any data stored by the business if possible; and</li> <li>ensuring compliance with the standards in the Privacy Act 1988 if the business collects and stores data containing customer information.</li> </ul>
Being proactive in ongoing commercial negotiations	<p>If you are in the middle of negotiating agreements, things to keep in mind when negotiating include:</p> <ul style="list-style-type: none"> <li><i>due diligence</i> – include due diligence as a requirement of the agreement and give yourself sufficient time to undertake the review. Given the economic conditions, it is important that more detailed due diligence should be undertaken.</li> </ul>

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	<ul style="list-style-type: none"> <li>• <i>conditions precedent</i> – plan for and manage delays that will likely occur. Also, consider whether the normal conditions which you would expect should be expanded so as best as possible to protect the parties or that they go into the arrangements with eyes wide open.</li> <li>• <i>termination rights</i> – the parties should carefully consider any proposed termination rights exercisable in the period between signing and completion. Sellers should be arguing against the inclusion of any material adverse change provisions. Although the true impacts of the virus are not yet known it is still a known risk and sellers should avoid taking any risk of the buyer attempting to rely on the impacts of the virus as a means to terminate the agreement. Buyers should seek rights to terminate the agreement in circumstances where the sellers have not properly disclosed the existing impact of the pandemic on their business.</li> <li>• <i>conditions</i> - While sellers will resist diminished deal certainty arising from specific crisis related conditions, if M&amp;A activity slows, leverage of buyers is likely to increase. If so, specific conditions tailored to the expectations of the crisis may become a part of purchase agreements.</li> <li>• <i>warranties and indemnities</i> – sellers should consider limiting the scope of warranties and indemnities given and avoid giving any assurances regarding the impact of the virus on your business. For buyers, seek specific warranties relating to the impact of the virus on the target to date to ensure you have all available information in making a decision whether to proceed with the transaction.</li> <li>• <i>Locked Box</i> – Given uncertainties around performance and receivables, we may see deals which initially contemplated locked box mechanics revert to the traditional working capital adjustment provision to limit risks in declining working capital for buyers.</li> <li>• <i>Material Adverse Change or Effect</i> – It is common to carve-out from this definition known events that are impacting a business. Therefore, we are seeing specific references to COVID-19, epidemics and pandemics as a carve-out from the circumstances which would cause or have a material adverse effect. However, deal participants should seek to tailor this definition in the context of COVID-19 and other situations, to take into account the worsening of existing conditions due to the crisis in geographic areas in which the target operates or the world in general.</li> </ul>

## SUPPLY CHAIN ISSUES

Industrials, manufacturing and transportation (**IMT**) companies are particularly hard hit by quarantines, travel restrictions, and other disruptions caused by the COVID-19.

The IMT sector also includes companies that provide the transportation and services necessary for an effective supply chain, such as airfreight, rail, shipping, and logistics.

Significant issues IMT companies are wrestling with include the following:

- Actions to close borders and restrict movements affect not only people, but also transportation of goods, both between and within countries. Companies will experience

delays and shortages, making it difficult to resume and maintain operations even after the virus has waned in some countries.

- Complex supply chains make it more difficult to identify where the "pinch" points are, in particular given the dynamic nature of the impacts of COVID-19 as it moves across the globe. To get ahead of this impact, IMT companies will need to continually update their supply chain risk assessment with new information.
- Changing manufacturing locations or suppliers quickly raises additional risks, especially because of time constraints on properly vetting such supply chain shifts to ensure technical product compliance.

Steps to alleviate pressure on supply chains include:

- Conduct a full risk assessment on the impact of the outbreak on business activities.
- Evaluate options when core supply chains are disrupted.
- Consider whether there are alternative ways of performing the contractual obligations.
- Consider whether there are ways of mitigating the effects.
- If entering into new contracts, draft provisions clearly and comprehensively to cover eventualities such as the present outbreak, and understand implications of the law governing the contract.
- Consider the possibility of invoking force majeure clauses (see below for further considerations).
- Monitor the announcement of any new governmental or regulatory policies.

## TRAVEL RESTRICTIONS – BUSINESS AND FREIGHT

Latest updates provided by the Department of Home Affairs (Australian government), Australian Border Force and Smart Traveller (Federal Government body) in respect of the restrictions coming into Australia:

- Only Australia citizens, residents and immediate family members are being allowed to travel to Australia, to which they will be in quarantine for:
  - From 21:00 AEDT 20 March 2020, only Australian citizens, residents and immediate family members can travel to Australia
  - From 23:59 AEDT on 28 March 2020, all travellers arriving in Australia will be required to undertake a mandatory 14-day quarantine at designated facilities (for example, a hotel), in their port of arrival
- These travel restrictions are subject to change – best to keep checking for updates (likely to become more restrictive as time progresses)

There have been additional exemptions provided by the Commissioner of the Australian Border Force, if someone is entering Australia (that is not an Australian citizen, resident or family member):

These categories of exemptions must be granted prior to these below travellers undertaking travel to Australia:

- foreign nationals travelling at the invitation of the Australian Commonwealth Government for the purpose of assisting in the COVID-19 response or whose entry would be in the national interest;
- critical medical services, including air ambulance and delivery of supplies, that regularly arrive into Australia from international ports;

- persons with critical skills (for example, medical specialists, engineers, marine pilots and crews) by exception;
- diplomats accredited to Australia and currently resident in Australia and their immediate family;
- case-by-case exceptions may also be granted for humanitarian or compassionate reasons.

#### Restrictions travelling from Australia:

- Australian citizens and Australian permanent residents are restricted from travelling overseas from 25 March 2020 at 12:00hrs AEDST.
- This international travel restriction does not apply to the following:
  - people ordinarily resident in a country other than Australia;
  - airline and maritime crew and associated safety workers;
  - New Zealand citizens holding a Special Category (Subclass 444) Visa are not permanent residents for the purposes of the Biosecurity Determination and are permitted to depart Australia. New Zealand citizens who are permanent visa holders may apply for a Commissioner's discretion;
  - people engaged in the day to day conduct of outbound and inbound freight;
  - people whose travel is associated with essential work at offshore facilities; and
  - people travelling on official government business, including members of the Australian Defence Force.

#### HOW CAN WE HELP YOU?

- Negotiating relief with your landlord, your bank or the ATO.
- Advising on the application Director Penalty Notice regime.
- Drafting forbearance deeds with your debtors and assisting you to take adequate security.
- Reviewing your terms and conditions and registrations of securities on the PPSR or the Land Titles Office.
- Drafting security documents such as guarantees, mortgages and general security agreements.
- Documenting any agreement with your employees to vary the terms of their employment.
- Managing redundancies or stand down of employees.
- Advising on structure issues or Government incentives.