

# Responding to COVID-19-related business issues in Latin America

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Latin America Initiative

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COVID-19's march across the globe arrived in Latin America on February 25 in Brazil, coming roughly a month after Europe and the United States. High inequality and variable medical capacity across the region are driving governments to rely heavily on social distancing and business restrictions to slow and prevent the spread of the virus. As a result of this timeline and different government responses to the pandemic, businesses operating in Latin America are having to navigate a varied patchwork of business restrictions, quarantines, and social distancing guidelines.

The region is poised to suffer severe economic damage from the pandemic and government responses to it, with analysts projecting Latin America will face its deepest contraction in the Post-War period. This means many companies, commercial relationships, and foreign investments are or will be adversely impacted.

As elsewhere around the globe, governments in Latin America are preparing for a protracted fight against the coronavirus, so businesses in the region will likely face periodic interruptions in commercial and industrial activity.

Covington's unique blend of public policy expertise on Latin America, combined with our top legal practices in Arbitration, White Collar and Anti-Corruption, Corporate, Private Equity, Insurance Recovery, Trade, Food, Drug and Devices, and Employment, have allowed us to bring multidisciplinary assistance to our clients across the region in this challenging time, both to confront the urgent business implications of the crisis and to prepare for a mid-term future where businesses must coexist with the coronavirus threat.

This article highlights some of the key issues on which Covington is assisting clients in Latin America.<sup>1</sup> For further guidance, we invite you to review our [COVID-19: Legal and Business Toolkit](#) and our [COVID-19 Checklist: Legal and Business Considerations](#).

## Supply Chain Continuity: Mexico

Mexico's first confirmed case of COVID-19 was a month after the first confirmed case in the United States. As a result, social distancing measures and business restrictions enacted by

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<sup>1</sup> Covington and Burling LLP is available to assist clients on the complex issues arising from the COVID-19 crisis pertaining to United States law, but cannot advise on issues of foreign law.

President López Obrador's government are likely to last beyond United States closures and restrictions, assuming the curves in each country continue to follow their current trajectories. Further, Mexico's list of sectors and activities deemed essential was initially more restrictive than the United States essential sectors list, meaning that some companies with cross-border supply chains are finding that their operations in Mexico may be more limited than their United States operations. Covington is providing advice to companies across various sectors on how to navigate the discrepancies and engage with government officials on both sides to support better alignment of key sectors and the stabilization of cross-border supply chains. Getting these supply chain issues right, now, is key toward ensuring that the economies can recover as quickly as possible when the health crisis ebbs.

### **Breaches of Contractual Obligations**

Many businesses across the region are facing disruptions in their commercial relationships as a result of government measures designed to slow and prevent the spread of COVID-19. Construction, infrastructure and mining projects have also been disrupted.

Businesses may be facing their own or their counter-parties' inability to perform. These businesses will want to review existing agreements to determine both (i) the rights available to them as against breaching parties, and (ii) their own risk of noncompliance and available remedies or waivers.

Businesses unable to meet their obligations should review *force majeure* provisions contractually available, which can excuse breaches arising from circumstances that (i) prevent a party's performance, and (ii) were reasonably unforeseeable or beyond the breaching party's reasonable control. *Force majeure* clauses may only cover certain obligations, and may impose additional requirements on the breaching party (such as mitigation efforts) before such remedy can be available.

Other legal doctrines, including the *impossibility or impracticability of performance* doctrine, which looks to whether the substance of the agreement or means for its performance has been destroyed, or alternatively the *frustration of purpose* doctrine, where a party's purpose for entering an agreement - rather than the means of accomplishing the same - has been destroyed, may also be available. In both cases, as with *force majeure*, the circumstances leading to such breach must not have been reasonably foreseeable.

Covington has put together helpful guidance on these different contractual remedies and their interpretation under various United States jurisdictions, and can advise clients on the complex issues arising under such legal frameworks, mitigation strategies, and litigation risk.

### **Insurance**

In addition to legal remedies, businesses should [assess their access to insurance policy recovery](#), in particular policies pertaining to the disruption of business, employee liability, D&O insurance and representation and warranty insurance. Policyholders should look for any coverage for communicable diseases, exclusions pertaining to epidemics or pandemics, and any specific requirements to make a claim. Policyholders will want to document the impact of the virus on their operations, including any supply chain disruptions, facility closures, layoffs, litigation or other claims, and lost profits/income. Covington's insurance practice group has ample experience helping policyholders recover losses arising from global events and disasters, such as hurricanes, terrorist attacks and environmental damage, and is assisting clients assess their access to insurance policy recovery due to the pandemic.

## **Borrowing and Capital Injections**

With many borrowing options currently unavailable as lenders assess COVID-19 risks in a shifting environment, businesses with affiliates in the United States should review potential stimulus [resources available under the Coronavirus Aid, Relief, and Economic Security Act \(CARES Act\)](#), including [loans for small businesses](#) and modifications to the rules affecting net operating loss carryforward/carrybacks. Access to funds under such programs will likely become more limited as time progresses, and additional restrictions on the access to such funds may come into play as a result. Consideration should also be given to organizations where affiliates may be able to provide capital through equity-based solutions (such as equity issuances and stock buy-backs) as a means to provide capital injections. Covington has been advising clients on Small Business Administration loan opportunities and other features of the CARES Act, and has put together helpful guidance on government relief programs.

## **Interim Covenants and Future Drafting Considerations**

Parties with agreements that have been entered into but not yet closed may find themselves hard-pressed to follow pre-COVID-19 interim covenants, and require waivers or the renegotiation of certain terms, including to respond to new legal requirements or take advantage of potential stimulus assistance. Potential termination right triggers should also be reviewed, as well as the effects on deal value arising from covenant non-compliance, delayed regulatory approvals, and other COVID-19 disruptions. Covington is assisting clients in reviewing current agreements and finding solutions to these issues.

Future transactions will require additional diligence of such disruptions (including effects to supply chain and labor) and its impact on deal value. Agreement language is shifting and will continue to evolve to address COVID-19 effects, in particular as regards (i) “Material Adverse Effect” definitions and the carve-outs for pandemics, including measures of impact of the same industry or regional-wise, (ii) representations and warranties regarding the business during the COVID-19 crisis, and (iii) interim covenants and conditions to close, specifically as regards maintaining an “ordinary course of business” or “consistent with past practice” standard.

## **Valuations, Deal Currency and Earn Outs**

Looking ahead, businesses will have to carefully consider the valuation methods used to account for the volatility and uncertainty resulting from COVID-19 shocks, including loss lines specific to the effects of the virus on operations. Stock transactions have been on the rise and are likely to trend upward as stock valuation will be easier to accomplish and it decreases reliance on external borrowing, increasing deal certainty. Arrangements that take into account the future performance of the business (such as earn-outs and complex target-based adjustments) are also more likely to be used given uncertainty about underlying business valuations. The effect of foreign currency fluctuations become particularly relevant when it comes to such forward-looking price adjustment provisions, including the potential for sudden devaluations, as have occurred as a result of the pandemic. As some companies seek to take advantage of lower asset prices across the region, Covington's corporate team is assisting them in taking all the necessary contractual precautions to guard themselves against the effects of a protracted health and economic crisis.

## **Investor-State Arbitration**

In response to the pandemic, some governments in the region have taken or are planning to take measures that may adversely impact foreign investments. Covington is assisting clients to assess the effects of these measures and, through its team of public policy experts, engage with governments to raise awareness of their implications under international treaties.

## **Preventing Contractual and Commercial Disputes**

Covington is working with clients on how to communicate proactively with counter-parties and establish a process for mutually agreed amended performance to avoid disputes. Since the pandemic has resulted in the suspension of pending arbitration and court proceedings, as well as the use of new technologies to conduct proceedings in some cases, Covington is advising clients in those proceedings and on decisions regarding whether and on what terms to settle rather than litigate.

## **Corruption Risks**

In response to the COVID-19 pandemic, companies doing business in Latin America are seeking to respond to urgent procurement processes, adapt to disruptions in their supply chains, and comply with restrictions to their operations. For many companies, the level of engagement with government officials has escalated and compliance departments are facing new and significantly increased compliance risks. Covington's anti-corruption compliance team is assisting clients in assessing and managing this evolving risk environment.

In addition, companies across the region are looking for ways to support their communities, many of which were already embedded in systemic poverty prior to the current crisis, through charitable contributions. While engaging in these laudable efforts, companies must be mindful of corruption risks when making decisions about giving. Companies should be careful in verifying the identity of the donation's recipient and the origin of the donation request. Several enforcement actions under the Foreign Corrupt Practice Act (FCPA) have involved improper conduct related to charitable contributions made to organizations at the request of government officials, or to charities owned or managed by government officials or their relatives. Covington has put together a list of best practices to help companies mitigate risk and continue to make a positive impact during the pandemic.

*For further information on any of these topics or other questions, please reach out to Covington's COVID-19 Task Force, [COVID19@cov.com](mailto:COVID19@cov.com), Sergio Urias, [surias@cov.com](mailto:surias@cov.com), Miguel López Forastier, [mlopezforastier@cov.com](mailto:mlopezforastier@cov.com), or Kimberly Breier, [kbreier@cov.com](mailto:kbreier@cov.com).*