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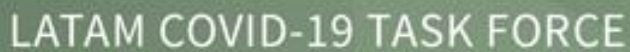

LATAM COVID-19 Task Force: Considerations for Private Equity Investors

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The outbreak of COVID-19 is causing disruption across the world. Willkie has been endeavoring to provide our clients, colleagues and friends with current information, insights and analysis of the challenges and issues that companies are facing globally. As part of those efforts, we have asked our colleagues at law firms in Latin America and Spain to join us in creating a LATAM COVID-19 Task Force to help clients navigate through this crisis and share their thoughts, views and insights on it.

As the full extent of the global effects of the outbreak remains to be seen, private equity funds are faced with managing the simultaneous demands and concerns of their portfolio companies, each with different needs, strategies and capabilities and varying levels of exposure to the instability caused by COVID-19. At the same time, fund managers are responding to a range of additional considerations given the impact of the pandemic on their funds and investors' interests. Areas at the fund level where we are seeing increased focus include liquidity management, increases in capital calls and management of investor concerns, limitations on exit activity and evaluation of new investments and strategies.

We have asked our colleagues in Brazil, Chile, Colombia, Mexico, Peru and Spain to share their thoughts on the main issues affecting the private equity industry as well as trends anticipated as a result of COVID-19. Please see below for our Q&A discussion with our colleagues, which also includes our observations on these topics based on what we are seeing in the United States at this time.

Brazil – Lefosse Advogados Q&A

Chile – Barros & Errázuriz Q&A

Colombia – Brigard Urrutia Q&A

Mexico – Mijares Angoitia Cortés y Fuentes, S.C. Q&A

Peru – Rebaza, Alcázar & De Las Casas Q&A

Spain – Pérez-Llorca Q&A

Certain Key Considerations

New Prospects for Investment

With a more diverse set of potential new opportunities for investments in sectors that are demonstrating resilience and, in some cases, growth as a result of COVID-19 (e.g., technology-forward businesses with services or products that can be leveraged under the circumstances, financial services, renewable energy, infrastructure, telecommunications, pharmaceutical and health science, etc.) as well as in sectors that are experiencing a downturn, we anticipate there will be certain common factors for private equity sponsors to consider in any market, including the following key factors:

- Consider for any multi-jurisdictional transaction, obtaining legal advice that is sufficiently comprehensive for all the jurisdictions involved, particularly with respect to the variety of regulations implemented locally in response to COVID-19. Certain countries have implemented stricter regulatory requirements as well as tax relief and financial aid measures, some of which are only temporary in nature. Other measures may still be under consideration depending on the effectiveness of the programs enacted to date. The collective result of these changes could significantly impact the thesis for the transaction.

- Consider when to invest and how much to invest to address lender concerns, liquidity risks and challenges anticipated for any businesses that may be more vulnerable to shutdowns and restart complications. The current scarcity of new debt financing commitments from banks will offer advantages to large sponsors able to fund an investment entirely with equity capital. Direct lenders and other alternative sources of capital will be another avenue outside of the traditional debt markets.

- Consider that shifting valuations may create challenges not only in the original decision to transact but also after closing as subsequent declines in portfolio company valuation may impact and trigger investors' rights under the fund agreements (e.g., potential clawbacks and adjustments in management fee payments as a result) as well as collateral value and compliance-related determinations with fund financing sources. There is no substitute for active and in-depth due diligence on all fronts in determining the appropriate valuation for a target business, taking into account its historical performance, the impact of COVID-19 on its operations, projected financial needs

and further potential risks and vulnerabilities (whether for the industry or unique to the business) and assessments of the possible outcomes for the investment in the medium- and long-term.

- Consider that certain regional markets may require sponsors to apply more creativity in their due diligence requirements to mitigate the challenges presented by COVID-19. In-person meetings and review of certain information and original documents may not be possible or at least limited for some time depending on the country and industry. For deals that do progress, particularly in jurisdictions where the traditional practice relies heavily on original documentation, parties may need to consider implementing other mechanisms that allow equal or similar certainty (as a key example, public notaries that certify the existence and validity of certain documents).

- Consider beneficial foreign exchange rates. Certain investments may become comparatively more attractive for sponsors due to the fluctuations of foreign exchange rates in certain markets, including a number of countries in Latin America. Such considerations should be balanced against the regulatory landscape of any given country in light of measures that governments may elect to adopt to protect domestic businesses as they recover from the pandemic.

- Consider regional markets that have opted in to global organizations where membership requires compliance with public policies reflecting high international standards. Recently, Colombia joined the Organisation for Economic Co-operation and Development as the third country in Latin America to become a member after Chile and Mexico. This decision will increase the investment potential in the region and may provide sponsors with further alternatives in sourcing investments.

- Consider that when the time is right again for an increase in M&A activity, some of the anticipated decrease in corporate buyer activity may remove some competition for private equity funds in future M&A processes. However, with many funds actively seeking investment opportunities, the extent to which negotiations with sellers may be reframed in light of COVID-19 remains to be seen.

Current Investments in Portfolio Companies

- Consider all current government financial programs. Most of the governments of the countries included in this Client Alert have implemented measures extending access to liquidity for portfolio companies. When assessing the need of a particular portfolio company to apply for governmental financial aid, eligibility requirements will vary across jurisdictions.

- Consider using strategic “add-on” acquisition, joint venture and similar opportunities as a means to jumpstart portfolio company activity, create synergies and reset leverage capacity for the given portfolio company.

- Consider that ESG commitments will continue to be important. While the pandemic context has forced businesses to focus on what is immediately ahead, we have seen that governmental authorities generally continue to support and advocate sustainable investment and climate and environmental risk management. Particularly in light of the sentiments expressed worldwide about the social disruption caused by COVID-19, we anticipate that investments in companies with strong ESG attributes and maintaining and strengthening current ESG policies will remain important considerations in the private equity industry.

- Consider enhanced business continuity and contingency plans based on lessons learned from the first phase of this crisis. Evaluating and understanding the extent of insurance coverage as it relates to COVID-19 related risks and business interruptions will be important. We anticipate heightened focus on “key person” provisions (whether in fund agreements, commercial contracts, insurance coverage or otherwise) and greater emphasis by investors on taking proactive steps to assess portfolio-level contingency planning. This may include developing and conducting test-run business disruption contingency plans with portfolios most affected by the pandemic and, in some instances, reaching out to key vendor and supply-chain relationships to better assess potential business disruption risk, as well as any vulnerabilities as to key person losses and contingency planning.

- Consider that additional bandwidth may be taken up by more ongoing and extensive reviews of operational and financing concerns. We have seen and continue to anticipate that private equity funds and portfolio companies alike will need to closely assess and potentially work with lenders to amend financial covenant requirements in existing debt financing agreements in cases where compliance may become tenuous. The review of force majeure provisions in commercial contracts (both upstream and downstream) will also be of continued importance, both to confirm the parameters for a given business’s contractual obligations and its rights in the event of any breaches that a counterparty connects to COVID-19.

Deal Terms

- Consider that in light of valuation uncertainties, earn-out structures with contingent purchase price may become more appealing to harmonize varying expectations and comfort levels, particularly in certain industries.

- Considering that the assertion of MAE may be challenged in light of what has become a fairly common practice of carving out the effects of pandemics and other market events in assessing if a MAE has occurred, we anticipate greater focus on pre-closing covenants (primarily “interim” or “ordinary course” operating covenants) and closing conditions by buyers seeking to terminate a transaction in which the target business has been impacted by COVID-19 and subsequently operated in a manner that may have further degraded the value of the business. To the extent the prospect of closing may be delayed or disputed, it will be important that parties keep in mind the applicable conditions, including the duration, of any debt financing commitments for the given transaction.

- Consider the interplay between MAE and force majeure in certain Latin American jurisdictions. As further explained by our colleagues, MAE provisions typically do not carry an equivalent remedy in local legal frameworks. By contrast, an aggrieved party may allege the occurrence of a force majeure event, subject to complying with the requirements applicable to force majeure, which is a statutory construct in these jurisdictions. This may occur even in the context of an M&A transaction such that the force majeure rights are incremental to MAE-related provisions; however, a party seeking to pursue force majeure rights will need to take into consideration that an excuse from performance will be appropriate only for so long as the event preventing performance is continuing. Accordingly, the relief available under applicable law to a party invoking force majeure is temporary and will not generally offer a buyer or investor a potential termination right in respect of the transaction unless the force majeure event in question makes performance impossible (i.e., closing) for an indefinite duration. Depending on the jurisdiction, while it may in some cases be common for a Latin American-based transaction to elect New York governing law and arbitration such that local courts will not serve as venue in any dispute, when drafting transaction documents, we recommend nevertheless taking into consideration the potential complications that may arise from including certain more U.S.-based concepts like MAE, which may be subject to being re-defined through local case law or assimilated with local remedies.
- Consider that the implications of a decision to obtain a representation and warranties insurance policy instead of using an escrow or holdback mechanism or vice versa may depend on the jurisdiction involved in the transaction. Traditionally, representation and warranties insurance policies have not been frequently used in Latin American transactions due to its high cost and broad coverage exclusions, and buyers have preferred to secure post-closing protection through an escrow or purchase price holdback. However, in light of the additional uncertainty and new risks created by the pandemic, including as it relates to the financial wherewithal of sellers who may be heavily impacted, this may require a re-assessment of previous post-closing recourse practices.

A. Brazil – Lefosse Advogados Q&A

Maurício Negri Paschoal, **Gonçalo Capela Godinho**, **André Mileski**, **Eduardo Carvalhaes**, **José Carlos Berardo**

1. Current Governmental Responses to COVID-19

In response to the shutdown orders in states and counties across the United States that have significantly curbed business activity across sectors in the past two months, the Coronavirus Aid, Relief, and Economic Security (CARES) Act established the Paycheck Protection Program ("PPP") on March 27, 2020, which, among other things, authorized up to an initial $349 billion (with an additional $310 billion of funding added on April 24, 2020) in loans aimed at providing liquidity to eligible small businesses, sole proprietorships, independent contractors and self-employed individuals. Subject to certain restrictions, a loan extended under the PPP will be forgiven to the extent employee and compensation levels are maintained and the proceeds are used within eight weeks after the loan is made for payroll costs and other approved purposes. For businesses seeking to apply, eligibility will depend on whether the applicant qualifies as a small business concern under one of the metrics (e.g., number of employees, total annual receipts) required by the Small Business Administration ("SBA"). The eligibility determination will, subject only to very limited exceptions, involve the application of the SBA's affiliation rules which aggregates the relevant metrics for the applicant and all of its applicable affiliates. As of April 24, 2020, the SBA issued an interim final rule indicating that the portfolio companies of a private equity fund ("PE fund") are not de facto excluded and may still be eligible to receive a PPP loan if they otherwise meet the eligibility criteria.

Are you seeing similar federal/national and/or local government decrees or measures (or a demand for such) that would benefit portfolio companies in terms of providing access to additional capital or other relief measures? Are there conditions applicable to obtaining such benefits (e.g., job protection, limits on size of business (whether measured by revenue and/or employee head count), etc.)? Are you seeing portfolio companies seeking government assistance and, if so, to what extent is it relevant if they are private equity backed?

Lefosse's Response: Yes, but such measures are still subject to certain limitations. The Brazilian Social and Economic Development Bank (BNDES) is extending credit lines in response to the COVID-19 pandemic, but eligible borrowers are, for the time being, limited to certain sectors (e.g., healthcare and airlines) and sizes, and the use of proceeds is also restricted. This is a small and limited response as the pandemic is having drastic effects on many sectors that are not eligible for these facilities, such as real estate, retail and entertainment. The resulting disruption to the underlying supply chain may ultimately lead to a deeper recession.

Utility companies are also taking a hit and demanding government aid. As utility concessions are deemed to be public services, following the outbreak, a number of court decisions preventing utility companies from interrupting services or readjusting prices or tariffs for a specific period of time have been awarded, and in some cases have been followed by specific regulation. While no one disputes that basic services, such as power, sanitation and telecommunications, should be maintained, utility companies will also need some sort of relief to avoid full service disruption.

In the healthcare sector, the regulators have allowed health insurance companies to lower their solvency margins in order to maintain appropriate liquidity levels to meet challenges presented by the pandemic.

In the U.S., the aforementioned SBA affiliation rules have generally limited the availability of access to governmental assistance through the PPP loans for many companies owned or controlled by PE or venture capital funds or alternative asset managers (including, in the case of minority investments, where control is inferred from certain consent rights held by the institutional investor). For your clients with U.S. operations who may be eligible, are you seeing any efforts to unwind or otherwise modify such arrangements so that they can more readily seek government assistance for their U.S. business operations?

Lefosse's Response: To date, we are not aware of such changes.

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2. *Changes in Deal Dynamics*

Prior to COVID-19, we had been facing a predominantly "seller's market" where deal terms had become increasingly favorable to sellers such that it became common that potential buyers, including private equity sponsors, needed to be willing to adopt more flexible positions to be competitive in sale processes. While competition between potential private equity and corporate buyers will remain, we anticipate that the volatility and disruption brought about by COVID-19 should result in a shift toward more buyer or investor favorable terms. We also anticipate that while speed and deal certainty should remain a priority, buyers will take comprehensive measures with respect to due diligence, particularly as it relates to understanding how a given target business has been altered by the pandemic and whether it is able to mitigate the effects now and in the longer term.

Recognizing that some industries may be impacted more than others, what do you expect with respect to changes in the negotiation leverage scale as well as market trends for PE sponsors as a result of COVID-19? Do you also anticipate that corporate buyers may take a step back in the near term as they focus on preserving their cash flow and operations or otherwise, thus reducing some competition for financial buyers? Given the current economic changes, we believe the current foreign exchange rates are also

favorable for foreign PE sponsors to invest in the Latin American region, if you could please comment on this aspect as well.

Lefosse's Response: We expect the negotiation leverage to be tipped towards PE sponsors to the extent new transactions are pursued, but the answer depends largely on their specific investment strategies and on the current exposure of the portfolio companies already operating in Brazil.

Commercial bank credit lines and other traditional sources of funds seem to be less available and more expensive at this time, even for companies that are less affected as a whole. This opens a significant window of opportunity for debt firms and private lending. We have seen a number of structured credit transactions sponsored by PE funds, especially those willing to be creative in terms of collateral arrangements. Concerns with higher spreads are diminishing, and companies seem to be willing to accept them if the transaction can be unwound at a later stage subject to a penalty. Companies have also shown more willingness to discuss hybrid structures and equity kickers with potential debt financing sources.

For PE funds seeking pure equity investments, there are of course numerous opportunities, especially for funds that can deploy capital quickly or that have U.S. or European limited partners given that the exchange rate will make a big difference in returns. Additionally, PE funds can address debt financing issues with all equity financing or over-equitized capital structures, and potentially hold their debt financing for when the markets improve. The choice of sectors will likely depend on how sensitive each fund is to the ideal time for exit, as some sectors will take longer to recover. We are already seeing new transactions involving more resilient sectors (certain healthcare and fintech businesses being good examples), and expect to see more PIPE transactions soon. Prior to the COVID-19 pandemic, Brazil had a long pipeline of companies seeking to go public, many of which will need to find alternative funding at this time.

Corporate investors of course have challenges of their own, especially in critically affected industries, both in terms of operations and cash preservation. However, opportunities may arise for well-capitalized corporate investors willing to explore well-positioned and niche acquisition targets that were caught off-guard by the pandemic and are in need of cash and/or cost-reducing synergies. All this may create a rich environment for market consolidation in some sectors.

The technology sector also presents another source of transactions for both corporate and financial investors. Many industries were already dealing with innovation and technology, both of which are growth drivers, especially in developing new distribution channels and improving logistics for businesses. The new social isolation conditions tend to accelerate this trend, as strategic companies seek to add new tools to their belts. This may lead to an increase in strategic deals, including add-ons, that have the potential of transforming industry patterns and providing exit opportunities for VC investors and, in some cases, PE funds.

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3. For Better or Worse: Industries Impacted by COVID-19

Within a short period of time, COVID-19 has caused disruption throughout all industries. On the one hand, the outbreak and the resulting shutdown orders in the U.S. have had a significant negative impact on sectors that are unable to deliver their core services and products, such as the oil and gas, tourism, airline, hotel and entertainment industries. At this time, it remains unclear as to when and to what extent consumer demand will return. On the other hand, the lockdowns and restraints imposed have resulted in unprecedented demand and new opportunities in light of how businesses have leveraged their use of technology (e.g., online retailers, video conferencing services, online learning, home fitness, delivery applications, pet products, etc.).

Are you seeing, or do you expect to see, increased investment and M&A activity involving local sectors or businesses that are benefiting from the COVID-19 outbreak, or that were active before COVID-19 and remain relevant at this time, e.g., the renewable energy sector?

Lefosse's Response: Definitely. Renewable energy (in particular greenfield projects), telecoms, agribusiness and healthcare would be notable examples in Brazil.

Increased activity in the renewal energy sector has been an important new trend in Brazil, as in other countries. Despite the short-term reduction in demand affecting prices, the industry is likely to bounce back soon. Infrastructure projects take long to develop, and Brazil, as an emerging market, is likely to need additional power sources. Renewable energy (in Brazil, especially hydroelectric, wind and solar power) will be the main driver.

In telecommunications, the operators are looking to expand the existing networks, investing in fiber optic, satellite capacity, submarine cables and upgrading of existing infrastructure.

Agribusiness has traditionally been one of the most important industries in Brazil. The industry has achieved substantial and sustainable growth in recent decades, as the world population grows and eating habits improve. COVID-19 has caused some disruption in supply chains (seeds, fertilizer, etc.), but this is not expected to last long, as food is just as important as healthcare. Most crops were not immediately affected in Brazil.

Another example is healthcare, an industry that has consistently grown over the past 15 years in Brazil. Consolidation created major players in the hospital and diagnostic sectors, but given the size of the country and the number of people, we still see a fairly active M&A market, which has slowed down because of COVID-19 but will certainly bounce back in the aftermath of the outbreak. We also expect to continue seeing a consolidation trend involving other healthcare sectors, such as pharmaceutical, distribution, home care and health insurance.

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4. ***Alternative Investment Opportunities***

For the industries most heavily impacted, we anticipate this may result in PE funds evaluating alternative opportunities given the limited traditional M&A buyout activity at this time. Similar to the trends observed during the 2008 financial crisis, we have already seen certain PE funds committing to significant investments in public companies in recent weeks with Apollo/Silver Lake's $3.2 billion investment in Expedia and Roark Capital's $200 million investment in the Cheesecake Factory as a few high-profile examples. There has also been discussion around increased opportunities for more carve-out transactions as strategic companies may divest their non-core assets in an effort to preserve liquidity. As the impacts of COVID-19 persist and businesses explore their strategic options, we would also anticipate greater focus on distressed and special situations investments.

To the extent more traditional M&A activity may have slowed, what are some alternative strategies that PE sponsors may be considering (or should consider) at this time (e.g., PIPEs, carve-outs, distressed acquisitions, etc.)?

Lefosse's Response: We are generally seeing an interesting array of opportunities presented by the current crisis that PE funds are assessing (or should assess). We see some PE investors still pursuing preexisting investment strategies in companies that operate in strong sectors, such as healthcare, and who are willing to complete transactions that had not yet closed prior to the outbreak; however, in some cases, investors are using the opportunity to renegotiate deal terms and conditions to reflect the new reality and new projections.

PIPEs are a first obvious choice. Listed companies will also suffer from the liquidity crunch and will seek alternative sources of funds. PIPE deals tend to be quick to execute and already provide a certain degree of liquidity, which makes them an ideal choice in circumstances like these. For similar reasons, we expect deals involving convertible debt to also soon be on the rise.

Another trend in Brazil relates to the sale of non-core assets, especially involving assets that are easy and quick to sell, such as real estate and subsidiaries that are not required for the operation of the core business. Carve-out deals are also being discussed and structured, but they are naturally more complex and need more time to plan and implement. We expect to see an increase in carve-outs at a later stage.

Brazil has seen a recent spike in the special situations industry and the current environment seems to be perfect for additional growth. We see room for innovative credit and equity (or hybrid) transactions, sale of legal claims, sale of NPLs, DIP financing and sale of assets in restructuring processes. However, once the playing field is leveled, the existing leverage in favor of special situation investors may fade (or even cease to exist).

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5. Post-COVID-19 Economy and Governmental Responses

As governments respond and businesses adapt to the changes caused by COVID-19, we anticipate that the "new normal" will reshape certain sectors, some of which may be particularly well-positioned to thrive to the extent they offer services and/or products that can provide solutions for the changes caused by COVID-19. Such sectors may present new and interesting opportunities but may also further draw additional governmental or regulatory response.

Based on your experience and discussions with market participants, what sectors do you see gaining the most and/or having a greater impact on the economy post-COVID-19? Given the difficulties that businesses have experienced, do you think the post-COVID 19 era may see a more favorable regulatory environment that enables and facilitates their recovery? For example, the Superintendency of Industry and Commerce of Colombia, which regulates fair competition and protects consumers, in December 2019 ruled that Uber had violated competition rules; Cornershop, a leading online grocery provider in Chile, Mexico, Peru, Brazil and Colombia, and Uber have been hampered by some antitrust regulators in Latin America; in 2018, the Mexican antitrust regulator did not approve Walmart's acquisition of Cornershop.

Lefosse's Response: COVID-19 is reshaping human interactions and how companies do business. Sectors that were already well positioned or are now moving fast to take advantage of the new setting will naturally benefit most. Companies that are typically technology-driven (for example, B2C, which relies heavily on online sales, logistics and supply chain and fintechs) are more prone to capitalize on the new forces and trends and, therefore, more likely to thrive in the new environment. This is not to say that more traditional businesses which are less technologically mature will disappear, but they will certainly need to adapt.

The question on the regulatory environment deserves a two-pronged answer. We do expect to see more business-friendly regulation, reducing the red tape and bureaucracy that make doing business in Brazil so expensive. A few examples here are the admission of electronic signatures in agreements and for certain public filings, electronic court filings, virtual shareholders' meetings and voting, and simplified licensing processes for low-risk types of business. A lighter approach towards regulation was already on the government's agenda before the pandemic, and we do not expect the initiative to fade; on the contrary, with COVID-19 an ongoing threat, the need for a more friendly regulatory environment has become even more apparent, particularly for small businesses.

On the antitrust side, we should expect existing standards to be preserved. The Brazilian Antitrust Agency is already investigating cases of possible price gouging in connection with the sale and distribution of medical

supplies during the pandemic and should have incremental (and in many cases, quite difficult) work as companies merge and consolidate to survive, which may lead to significant concentration in certain markets.

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6. COVID-19 Impact on Limited Partners

The current circumstances bring into question the likelihood of meeting expectations with respect to fundraising, especially for younger PE funds. Based on discussions to date, we anticipate that funds that lack a strong, established track record with limited partners ("LPs") who are seeking new investments in this environment could face greater challenges as they seek capital commitments from investors who may be less likely to deploy new capital in the first instance whether due to an inability to meet with and diligence the new(er) fund managers, changes in their asset allocations, a general preference to conserve capital at this time or other reasons. The limitations on meeting investors in person due to the travel restrictions and quarantine measures in the U.S. and worldwide may be more manageable for established PE funds given their existing relationships, but the use of Zoom and other video-conference methods is still unlikely to be a suitable substitute in all cases.

With respect to liquidity questions, PE funds may need to weigh their lender relationships and credit facility options against the impact of potential LP capital calls when LPs have their own liquidity considerations. Given the quarantine and work-from-home-restrictions, we anticipate that LPs may need more lead time generally, including for any required capital contributions, and it is reasonable to expect that anything beyond what is contemplated by the existing fund agreements may take longer than is typical.

Relative to the fundraising environment in 2008/09, for new funds being raised at this time, what are the main structural factors and considerations that may limit LPs' interest in committing capital to new ventures? Are you seeing, or do you expect to see, LPs change their allocations to PE as an asset class (whether in the U.S. and/or to funds with a Latin American or other international focus) during this downturn?

Lefosse's Response: Issues relating to foreign exchange volatility, the regulatory framework and changes in law are naturally sharpened on occasions such as the present pandemic. We believe it is still too soon to predict whether we can expect LPs to change their allocations to PE as an asset class in Brazil; however, at this point, we expect that LPs will already have digested and accounted for Brazil's country risk and acquainted themselves with the dynamics (and the historical fluctuations) of the Brazilian market and economy, and therefore will continue to commit capital.

It is likely too soon to tell, but are you concerned about potential LPs defaulting on their current commitments? Based on your discussions with clients, have LPs been increasingly reaching out with

capital call funding concerns (even if just prospectively)? Do they expect any pressure on fees typically earned by funds?

Lefosse's Response: Since the pandemic's surge, we have seen a few situations involving capital call funding concerns with respect to investment funds raised locally, which were addressed in different ways (the most delicate one was solved with the transfer of the commitment obligation to another investor). That being said, we have noticed that PE funds and other asset class vehicles with a focus on Brazil are avoiding making capital calls at least until we cross this initial phase and there is further clarity on the consequences brought by COVID-19.

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7. Availability of Debt Financing

As we have seen to date, PE funds and their portfolio companies have taken various measures to secure debt financing from commercial banks to stabilize cash flows in light of the uncertainty of the current financial climate. In the past and of relevance now, non-bank lenders in the private credit industry have shown more willingness to provide financing, albeit on more expensive terms and likely with more scrutiny from the lending party.

Based on your discussions with clients and contacts in the industry, are they seeing, or do they expect to see, significant liquidity concerns within their portfolio companies? Have you advised portfolio companies to draw down on credit facilities? If so, are they seeing any resistance from their lenders at this stage? Please also comment on the extent to which you anticipate commercial banks taking a more conservative approach to lending during and after the pandemic, as well as the best strategies, including alternative sources of financing, available to PE sponsors and their portfolio companies as they seek alternative cash flows to weather the downturn.

Lefosse's Response: Based on our discussions, access to traditional banking lines is becoming more challenging and expensive. We see this as a natural consequence of the current environment, as more clients are tapping credit lines, global liquidity is decreasing and credit rates are dropping (or are harder to evaluate). As a consequence, spreads in new loans tend to be higher, which reduces access to other sources of credit. This may lead to a number of trends.

One trend is that businesses are optimizing themselves by reducing expenses, which in turn may lead to mergers and acquisitions (especially in the technology sector). Another expected trend is that borrowers will seek financing from alternative credit sources, such as financial institutions and special situation funds. We see a number of active funds willing to enter into credit transactions, and we see room for newcomers. Special situations investors are also expected to gain traction and become more active, especially when dealing with companies with illiquid assets to offer as collateral.

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8. <u>ESG Initiatives</u>

Leading up to COVID-19, environmental, social and governance-related ("ESG") initiatives were becoming a strong area of focus for investors as part of the criteria used to assess the long-term quality and sustainability of potential investments. The growing view was that a strong ESG proposition can create long-term value for companies, their employees, stakeholders and ultimately communities. As an example of the various recognitions given acknowledging the value of ESG in recent years, the U.S. Business Roundtable had released a new statement in August 2019 affirming businesses' commitments to ESG. This statement was signed by CEOs of a number of Fortune 100 companies, including a number of companies that have since received significant attention in light of COVID-19, such as Amazon, American Airlines, 3M, Boeing, Marriott, Target and Walmart. Given the public perceptions and expectations of a corporation's role at this time, we would anticipate that ESG commitments will continue to remain highly relevant across all sectors.

In consideration of the current business concerns and priorities around preserving cash flow and stabilizing operations, as well as the social consequences of the disruption caused by COVID-19, to what extent do you anticipate that ESG principles remain relevant in guiding new investment opportunities and management of existing investments at this time?

<u>Lefosse's Response</u>: We see an increasing focus on ESG initiatives, and expect the post-COVID-19 era to be marked by additional pressure to pursue companies that commit to ESG standards as part of investment policies.

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9. <u>"Key Person" Focus</u>

Even for established funds with close, long-term relationships with their investors, the nature of COVID-19 has been so unprecedented that we are seeing investors focus closely on obtaining the clarity needed and further insights on measures taken by PE sponsors to protect their investments. We have seen significant focus on ensuring that business continuity plans are updated in a manner that takes into consideration the possibility of further operational changes imposed by applicable government requirements and recommendations such that appropriate risk management protocols are in place, including as to key persons whether at the business or involved with any number of a given business's vendors. Given the unpredictability of COVID-19, which has already impacted leaders at the highest levels of government and business (UK Prime Minister Boris Johnson and Morgan Stanley CEO James Gorman being two notable examples), understanding "key person" triggers at the portfolio company level for insurance coverage and/or commercial contracts will be of heightened importance. Similarly, in more extreme cases at the fund level, the "key person" triggers in fund documents may become

relevant in the case of extended unavailability (e.g., what constitutes "incapacitation"), including which investor rights may vest upon a "key person event" (such as redemption rights or other protections). In either case, parties may seek to broaden key person clauses going forward to address relevant commercial considerations due to these experiences to date with COVID-19.

As it relates to business continuity, are you seeing, or do you expect to see, additional succession or contingency plans that provide assurances if certain key people are unable to meet their obligations for an extended period of time? At the fund level, what would generally be needed to trigger a "key person event" and what are the rights in favor of the investors should such an event occur? Based on your discussions with clients and contacts in the industry, what are the measures you would advise clients to take regarding how best to prepare for and manage the risk surrounding any key person changes caused by COVID-19?

Lefosse's Response: This will ultimately depend on the PE fund and its structure. For the time being, we are not seeing an increase in succession or contingency planning.

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10. "Material Adverse Effect" and Other Concepts

While the full impact of COVID-19 remains to be seen, it is not surprising that parties are now actively initiating a closer review of material adverse effect ("MAE") provisions as well as potential issues with pre-closing covenant compliance and closing condition satisfaction for transactions that signed but have not yet closed. Given the disruption to date, buyers may conclude that earlier valuations agreed to pre-COVID-19 need to be revisited. In more severe cases, a buyer may believe that terminating the transaction is the most appropriate path forward, whether on the basis that the target business has suffered an MAE and/or has breached the agreement and is otherwise unable to satisfy its closing conditions. While no quantifiable test exists as to whether an MAE has occurred and courts are generally reluctant to make such a determination, both Delaware and New York law do require that the adverse effects be "durationally significant". To date, MAE has been invoked successfully only once in Delaware court. In view of the usual practices for defining MAE (which, among other things, generally involve an absence of specific events or dollar thresholds), we see MAE provisions being used as a negotiation tool for buyers who believe that re-negotiation of a deal is appropriate. In the case of COVID-19 in particular, buyers looking to terminate will also need to address common exclusions in the definition of a MAE for industry-wide or "systemic" events such as pandemics, "Acts of God", changes in law or government actions unless the business was disproportionately impacted. Accordingly, we anticipate that parties, in seeking remedies, will increase their attention on whether closing conditions cannot be satisfied for other reasons, such as in the case where pre-closing interim operating covenants are breached in a manner that would impede closing. Sycamore

Partners' recent termination of its agreement with L Brands, the owner of Victoria's Secret, is one high-profile example of a decision to terminate based largely on analysis regarding the target's covenant compliance and ability to satisfy closing conditions.

For existing deals in progress that have been signed but not yet closed, we are seeing an increase in efforts to use material adverse change provisions and other conditions to either unwind or renegotiate transactions. Are you experiencing similar situations with respect to your existing deals, whether on the buy or sell side? What, in your experience, would be the level of change required (and for what duration) in order for a buyer to be well-positioned to prevail on invoking a material adverse change provision? Going forward, do you anticipate any changes to how parties may wish to define MAE in an acquisition agreement as a result of the effects of COVID-19?

Lefosse's Response: This is probably one of the top issues on the agenda of both corporate and litigation lawyers. The current situation falls into the definition of an MAE in most M&A agreements in Brazil, except where pandemics are expressly excluded. Adding to the discussions, in many cases the circumstances for a statutory force majeure event would also be met. Typically, this is a case-by-case evaluation, which should consider the specifics of the deal, the impacts on the parties involved, the level of sophistication of the parties (which should be deemed to be high in transactions involving PE players) and how the relevant industry is affected as a whole.

Brazilian law imposes a duty to engage in good faith negotiation when unforeseen and extreme circumstances change the economic rationale of the deal. This has potential implications to both the discussions involving MAE clauses (easier to trigger due to the more objective standards) and force majeure. As a rule of thumb, parties should try to renegotiate rather than terminate agreements, including in the M&A context.

MAE clauses are typically pro-buyer, but having them well-crafted obviously works to the benefit of both parties, due to the more precise allocation of risks. In the pandemic aftermath, we expect most, if not all, MAE provisions to expressly carve out "pandemics" like they do tsunamis or terrorist attacks, as a way to allocate deal certainty risk. However, COVID-19 is proving to be something different, as it affects businesses on a global scale, as opposed to the typical MAE circumstances which tend to be construed in local or national contexts. This poses a challenge to deal making. Other than in very well-crafted hell-or-high-water provisions, it is hard to argue that a situation such as the current one would not qualify as a force majeure event, as the office of the Attorney General has recently acknowledged in a formal opinion.

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11. <u>IPO and Exit Prospects</u>

On the eve of the COVID-19 outbreak, market conditions in many regions in Latin America were favorable for PE funds seeking exit opportunities for their most successful investments, with several notable companies planning to launch IPOs or follow-on offerings. As we have seen the pandemic bring on a wave of uncertainty, such exit plans have been put on hold and the extent of the delay and whether other exit opportunities may be pursued are both unclear.

With the outbreak, are you seeing companies delaying or withdrawing their IPO plans or follow-on offerings? Recognizing that this may vary by industry, are companies and investors seeing the IPO window opening back up in the short term and, if so, how do you see the time lag impacting the terms and pricing of offerings? To the extent not, what are the alternatives you are seeing on exit considerations?

<u>Lefosse's Response</u>: At the beginning of 2020, prior to the global COVID-19 outbreak, Brazil had a substantial pipeline of companies pursuing IPOs (especially after the approval of much-needed structural economic reforms). These IPOs were mainly driven by (i) PE funds seeking an exit or (ii) companies seeking growth-related liquidity. In general, the market seemed to be very optimistic about the prospects of these deals. Current circumstances seem to have placed the IPO window on hold for the near future (until potentially 2021). Pricing implications, both industry- and asset-specific, are hard to predict, and will depend mostly on the level and speed of general economic recovery.

The market's reaction to reduced IPO prospects will depend on a number of different factors. Companies seeking growth liquidity will most likely have to defer their growth plans or seek alternative funding. PE-backed companies (and other companies with wealthy shareholders or sponsors) can always seek over-equitized capital structures.

That said, this scenario creates great opportunities for PE investments, especially as cash-deprived companies are still willing to seek expansion plans, either organically or by acquisition. Seeking a PE investor (or adding another one) may be a quick and efficient way to raise cash, and other IPO windows should be available in the near (though not foreseeable) future.

B. Chile – Barros & Errázuriz Q&A

Pablo Guerrero Valenzuela

1. Current Governmental Responses to COVID-19

In response to the shutdown orders in states and counties across the United States that have significantly curbed business activity across sectors in the past two months, the Coronavirus Aid, Relief, and Economic Security (CARES) Act established the Paycheck Protection Program ("PPP") on March 27, 2020, which, among other things, authorized up to an initial $349 billion (with an additional $310 billion of funding added on April 24, 2020) in loans aimed at providing liquidity to eligible small businesses, sole proprietorships, independent contractors and self-employed individuals. Subject to certain restrictions, a loan extended under the PPP will be forgiven to the extent employee and compensation levels are maintained and the proceeds are used within eight weeks after the loan is made for payroll costs and other approved purposes. For businesses seeking to apply, eligibility will depend on whether the applicant qualifies as a small business concern under one of the metrics (e.g., number of employees, total annual receipts) required by the Small Business Administration ("SBA"). The eligibility determination will, subject only to very limited exceptions, involve the application of the SBA's affiliation rules which aggregates the relevant metrics for the applicant and all of its applicable affiliates. As of April 24, 2020, the SBA issued an interim final rule indicating that the portfolio companies of a private equity fund ("PE fund") are not de facto excluded and may still be eligible to receive a PPP loan if they otherwise meet the eligibility criteria.

Are you seeing similar federal/national and/or local government decrees or measures (or a demand for such) that would benefit portfolio companies in terms of providing access to additional capital or other relief measures? Are there conditions applicable to obtaining such benefits (e.g., job protection, limits on size of business (whether measured by revenue and/or employee head count), etc.)? Are you seeing portfolio companies seeking government assistance and, if so, to what extent is it relevant if they are private equity backed?

Barros & Errázuriz's Response: In response to the COVID-19 crisis, the Chilean government has implemented several successive nationwide economic plans that are designed to provide economic relief and protect employment stability within Chile.

As the first of these measures, the Chilean government passed Law No. 21,227 on March 31, 2020 in an effort to mitigate the economic effects of the COVID-19 pandemic, particularly with respect to employment. As a matter of law, the prohibitions or suspensions on business activities as a result of COVID-19 have resulted in suspension of employment for the affected companies' employees. Consequently, commencing on April 6, 2020 for a period of six months, employees will be able to access unemployment insurance benefits while the employment

relationship is in force so long as the employee has made the required social security contributions in the immediately preceding months. In addition, this law allows companies that are affected, but whose activities are not otherwise prohibited or suspended by law, to agree to a suspension of employment with their employees such that the employees may access the benefits provided under the law. As an alternative, the law also affords the companies that fall within the scope of the law the ability to agree with their employees on a reduced work schedule for a minimum of one month and a maximum of five months (in the case of employment agreements of indefinite duration) or three months (in the case of employment agreements with fixed terms). In such cases, employees will be able to supplement their salary with unemployment insurance under the law. During the term of any such suspension, the employer will be obligated only to pay social security contributions. The unemployment payments received will not be taxable.

In addition to the foregoing measures, on April 12, 2020, President Sebastián Piñera announced the “Historic Plan of State Guarantees”, which is primarily intended to promote, ease and extend access to liquidity for small and medium size companies in need of working capital to overcome the disruption of COVID-19. On April 25, 2020, the corresponding bill was enacted by the Ministry of Finance.

The main feature of this bill is to facilitate the access of affected companies to the Small and Medium Companies Guarantee Fund (“FOGAPE”) through April 30, 2021. The FOGAPE will receive an additional USD $3 billion in funding and will guarantee loans made by commercial banks to affected companies with working capital needs.

With respect to eligibility, companies with annual sales between approximately USD $3.3 million to USD $33.5 million will be allowed to access bank funding guaranteed by FOGAPE. In the case of export companies, access is limited to those which have exported goods with at least an average of USD $16.7 million annually in the two previous years. There is no other criteria other than annual sales receipts. The funding guaranteed by FOGAPE will be granted in local currency, except for funding intended to finance export and import companies, which could be granted in foreign currency.

The foregoing will allow the banks to provide working capital credit facilities to affected companies for up to USD $24 million. The maximum principal amount of the credit line will be the equivalent of three months of the company’s annual sales, considering, as a reference point, the period between October 2018 and September 2019 (although banks may opt to choose a different reference period, such as fiscal year 2019 or the twelve months prior to the funding approval). The maximum amount of the FOGAPE guarantee for each affected company will range from up to of 85% of the credit line for micro and small enterprises (annual sales up to USD $836,000) to 60% for larger enterprises (annual sales up to USD $33,450,000). Each credit line will bear a nominal interest rate of 3.5% and feature a six-month grace period. Repayment will occur in installments with a maturity date ranging from 24 to 48 months.

The Employment Protection Act and the credit lines guaranteed by FOGAPE present no restrictions with respect to the ownership structure of the beneficiary companies. Accordingly, any company that meets the legal requirements will be eligible to apply for assistance under these programs. As of this date, we have seen different types of companies apply the terms of the Employment Protection Act for their operations given that the debt markets have been closed and such companies are foreseeing cash flows constraints. On the other hand, with respect to the FOGAPE-backed credit lines, it is too early to provide an assessment on the extent to which companies will utilize them, notwithstanding our belief that many of the eligible companies will do so.

In the U.S., the aforementioned SBA affiliation rules have generally limited the availability of access to governmental assistance through the PPP loans for many companies owned or controlled by PE or venture capital funds or alternative asset managers (including, in the case of minority investments, where control is inferred from certain consent rights held by the institutional investor). For your clients with U.S. operations who may be eligible, are you seeing any efforts to unwind or otherwise modify such arrangements so that they can more readily seek government assistance for their U.S. business operations?

Barros & Errázuriz's Response: In general, we have not seen changes in how our clients with investments in the U.S. have been operating their businesses or in the manner in which they have approached the market. However, it is important to note that, with the exception of certain real estate developers, the number of Chilean PE funds or investment funds with operating assets in the U.S. is very limited at this time.

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2. *Changes in Deal Dynamics*

Prior to COVID-19, we had been facing a predominantly "seller's market" where deal terms had become increasingly favorable to sellers such that it became common that potential buyers, including private equity sponsors, needed to be willing to adopt more flexible positions to be competitive in sale processes. While competition between potential private equity and corporate buyers will remain, we anticipate that the volatility and disruption brought about by COVID-19 should result in a shift toward more buyer or investor favorable terms. We also anticipate that while speed and deal certainty should remain a priority, buyers will take comprehensive measures with respect to due diligence, particularly as it relates to understanding how a given target business has been altered by the pandemic and whether it is able to mitigate the effects now and in the longer term.

Recognizing that some industries may be impacted more than others, what do you expect with respect to changes in the negotiation leverage scale as well as market trends for PE sponsors as a result of COVID-19? Do you also anticipate that corporate buyers may take a step back in the near term as they focus on

preserving their cash flow and operations or otherwise, thus reducing some competition for financial buyers? Given the current economic changes, we believe the current foreign exchange rates are also favorable for foreign PE sponsors to invest in the Latin American region, if you could please comment on this aspect as well.

Barros & Errázuriz's Response: While we believe it is too early to assess the impact of COVID-19 in driving new M&A trends, based on discussions that we regularly hold with clients and key players in the market, we foresee that PE sponsors will play an active role in the market once the peak of the crisis has passed. This is mainly due to a combination of the availability of cash to be invested, a reduction on prices that we anticipate and less competition from corporate strategic investors.

With respect to strategic companies, we anticipate they will be focused on stabilizing their current operations and preserving cash to ensure their financial stability rather than seeking to acquire new assets. In that light, we have seen that our major corporate clients are dealing with keeping their businesses operating in the best possible manner and concerned with keeping their labor force in place. Accordingly, we believe that PE funds will have a predominant role in future M&A processes.

In terms of foreign exchange rates, it is not a secret that those PE funds that are funded in foreign currencies (especially in U.S. dollars) will have more attractive conditions with respect to the pricing of potential acquisition targets, considering that in the past six months the U.S. dollar has gained around 20-25% against the Chilean peso due not only to the COVID-19 situation but also due to the civil protests and unrest that occurred in October 2019.

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3. ***For Better or Worse: Industries Impacted by COVID-19***

Within a short period of time, COVID-19 has caused disruption throughout all industries. On the one hand, the outbreak and the resulting shutdown orders in the U.S. have had a significant negative impact on sectors that are unable to deliver their core services and products, such as the oil and gas, tourism, airline, hotel and entertainment industries. At this time, it remains unclear as to when and to what extent consumer demand will return. On the other hand, the lockdowns and restraints imposed have resulted in unprecedented demand and new opportunities in light of how businesses have leveraged their use of technology (e.g., online retailers, video conferencing services, online learning, home fitness, delivery applications, pet products, etc.).

Are you seeing, or do you expect to see, increased investment and M&A activity involving local sectors or businesses that are benefiting from the COVID-19 outbreak, or that were active before COVID-19 and remain relevant at this time, e.g., the renewable energy sector?

Barros & Errázuriz's Response: We expect that M&A industry trends from the past few years will continue in the same direction with the predominant portion of major transactions occurring in areas related to the infrastructure, energy and renewable energy sectors; however, we may see an increase in the range of portfolios or assets related to those sectors that will require fresh equity, which may result in a greater number of M&A transactions than was projected prior to COVID-19.

The foregoing is notwithstanding our belief that we will also expect to see transactions in other industries such as health insurance, salmon farming, retail, industrials, food and beverage, etc. In certain of these industries, such as food, beverage and salmon farming, there will be enhanced opportunities for consolidation, particularly in consideration that owners may be facing cash constraints given the current dislocation.

As in most parts of the world, the most affected industries currently are related to tourism, travel, restaurants and retail, particularly those who lack an online platform. Not surprisingly, there are also businesses such as car dealers, service providers and real estate that have been directly impacted by the lockdowns.

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4. ***Alternative Investment Opportunities***

For the industries most heavily impacted, we anticipate this may result in PE funds evaluating alternative opportunities given the limited traditional M&A buyout activity at this time. Similar to the trends observed during the 2008 financial crisis, we have already seen certain PE funds committing to significant investments in public companies in recent weeks with Apollo/Silver Lake's $3.2 billion investment in Expedia and Roark Capital's $200 million investment in the Cheesecake Factory as a few high-profile examples. There has also been discussion around increased opportunities for more carve-out transactions as strategic companies may divest their non-core assets in an effort to preserve liquidity. As the impacts of COVID-19 persist and businesses explore their strategic options, we would also anticipate greater focus on distressed and special situations investments.

To the extent more traditional M&A activity may have slowed, what are some alternative strategies that PE sponsors may be considering (or should consider) at this time (e.g., PIPEs, carve-outs, distressed acquisitions, etc.)?

Barros & Errázuriz's Response: While we may be seeing a slowdown in the M&A dealflow in the upcoming months, in some cases as a result of delays in sale processes announced prior to the COVID-19 outbreak, we expect that after the peak of the COVID-19 outbreak, M&A activity will increase significantly in Q3 and Q4 of 2020 and during 2021.

In addition, in terms of alternative transactions, we have for some time observed the trend in increased carve-outs acquisitions where strategic companies move forward with the sale of those assets that are not core for their business (e.g., infrastructure for mining activities; gas terminals, among others). This is a trend that we would expect will continue and may be accelerated after COVID-19.

We also expect to see more activity in involving distressed assets with an increase in the number of distressed financing solutions, including more preferred equity structures with investor-favorable terms as an example. In terms of PIPE transactions, we believe that, if it happens, it will be very limited to specific industries that have been and will continue to be heavily impacted by the COVID-19 outbreak. Ultimately, we see that major Chilean publicly traded corporations, as well as financial institutions, have fundamentals that are financially healthy and with sufficiently capacity to overcome the current situation.

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5. Post-COVID-19 Economy and Governmental Responses

As governments respond and businesses adapt to the changes caused by COVID-19, we anticipate that the "new normal" will reshape certain sectors, some of which may be particularly well-positioned to thrive to the extent they offer services and/or products that can provide solutions for the changes caused by COVID-19. Such sectors may present new and interesting opportunities but may also further draw additional governmental or regulatory response.

Based on your experience and discussions with market participants, what sectors do you see gaining the most and/or having a greater impact on the economy post-COVID-19? Given the difficulties that businesses have experienced, do you think the post-COVID 19 era may see a more favorable regulatory environment that enables and facilitates their recovery? For example, the Superintendency of Industry and Commerce of Colombia, which regulates fair competition and protects consumers, in December 2019 ruled that Uber had violated competition rules; Cornershop, a leading online grocery provider in Chile, Mexico, Peru, Brazil and Colombia, and Uber have been hampered by some antitrust regulators in Latin America; in 2018, the Mexican antitrust regulator did not approve Walmart's acquisition of Cornershop.

Barros & Errázuriz's Response: While we expect an increase in M&A activity across different sectors, we have no evidence and we do not believe that there will be significant changes in the regulatory requirements for parties seeking to complete acquisitions. In Chile, consumer protection and competition matters have become very sensitive topics in recent years across different industries and from a social stability point of view, we do not expect to gain flexibility on those fronts simply because of the current situation. We also have not yet seen any protectionist measures in favor of domestic companies nor any measures that may be less favorable for foreign

direct investments at this time. We expect that the government will continue with the same approach of the past decades in boosting foreign investments in different sectors.

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6. COVID-19 Impact on Limited Partners

The current circumstances bring into question the likelihood of meeting expectations with respect to fundraising, especially for younger PE funds. Based on discussions to date, we anticipate that funds that lack a strong, established track record with limited partners ("LPs") who are seeking new investments in this environment could face greater challenges as they seek capital commitments from investors who may be less likely to deploy new capital in the first instance whether due to an inability to meet with and diligence the new(er) fund managers, changes in their asset allocations, a general preference to conserve capital at this time or other reasons. The limitations on meeting investors in person due to the travel restrictions and quarantine measures in the U.S. and worldwide may be more manageable for established PE funds given their existing relationships, but the use of Zoom and other video-conference methods is still unlikely to be a suitable substitute in all cases.

With respect to liquidity questions, PE funds may need to weigh their lender relationships and credit facility options against the impact of potential LP capital calls when LPs have their own liquidity considerations. Given the quarantine and work-from-home-restrictions, we anticipate that LPs may need more lead time generally, including for any required capital contributions, and it is reasonable to expect that anything beyond what is contemplated by the existing fund agreements may take longer than is typical.

Relative to the fundraising environment in 2008/09, for new funds being raised at this time, what are the main structural factors and considerations that may limit LPs' interest in committing capital to new ventures? Are you seeing, or do you expect to see, LPs change their allocations to PE as an asset class (whether in the U.S. and/or to funds with a Latin American or other international focus) during this downturn?

Barros & Errázuriz's Response: It is difficult to say whether the change is structural or not, but based on our regular conversations with fund managers, we are seeing that LPs are certainly struggling with liquidity issues given a wave of capital calls these days from Chilean LPs of both global funds as well as Latin America based funds. At this time, we have not seen LPs materially change their commitments with investment funds. We anticipate that it is probable this will remain in the back of their heads when considering new commitments in the future. Given this, we would expect allocations to PE funds as an asset class in general to decrease over the coming months until this COVID-19 episode, as many other episodes in the past, is forgotten.

Notwithstanding the foregoing, it is important to note that the Central Bank recently announced an increase on the limits of the level of resources that Chilean pension funds may allocate to alternative assets which we believe, in the medium-term, will have an impact on fundraising, since the pension funds usually invest through asset managers that have specific capabilities for this sort of investment. These restrictions will allow Chilean pension funds to increase their positions in assets such as infrastructure and real estate, which offer long-term cash flows.

We have not seen any additional pressure on fees from LPs. The pressure has always been there.

It is likely too soon to tell, but are you concerned about potential LPs defaulting on their current commitments? Based on your discussions with clients, have LPs been increasingly reaching out with capital call funding concerns (even if just prospectively)? Do they expect any pressure on fees typically earned by funds?

Barros & Errázuriz's Response: We have heard from the market that more LPs are taking issue with the amount of capital calls they have been receiving, both due to liquidity issues and concentration on the PE asset class, which may trigger a breach of existing regulatory limits. However, we have not yet heard any concerns about potential defaults on commitments.

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7. Availability of Debt Financing

As we have seen to date, PE funds and their portfolio companies have taken various measures to secure debt financing from commercial banks to stabilize cash flows in light of the uncertainty of the current financial climate. In the past and of relevance now, non-bank lenders in the private credit industry have shown more willingness to provide financing, albeit on more expensive terms and likely with more scrutiny from the lending party.

Based on your discussions with clients and contacts in the industry, are they seeing, or do they expect to see, significant liquidity concerns within their portfolio companies? Have you advised portfolio companies to draw down on credit facilities? If so, are they seeing any resistance from their lenders at this stage? Please also comment on the extent to which you anticipate commercial banks taking a more conservative approach to lending during and after the pandemic, as well as the best strategies, including alternative sources of financing, available to PE sponsors and their portfolio companies as they seek alternative cash flows to weather the downturn.

Barros & Errázuriz's Response: As far as we have been informed, portfolio companies have been working on their liquidity but we have not yet heard of any major concerns, assuming the downturn is limited to the upcoming months.

While banks are taking a more conservative approach to lending both due to the COVID-19 and October 2019 social unrest issues, local banks have still been very supportive of their clients in an effort to help them overcome this situation and also to navigate the new economic measures taken by the government (e.g., FOGAPE-backed working capital credit lines at low interest rate).

Based on the foregoing, we believe that international lending will increase as a source of financing to counterbalance the more conservative approach from the local financial system. Private lending will also become a more common financing source.

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8. ESG Initiatives

Leading up to COVID-19, environmental, social and governance-related ("ESG") initiatives were becoming a strong area of focus for investors as part of the criteria used to assess the long-term quality and sustainability of potential investments. The growing view was that a strong ESG proposition can create long-term value for companies, their employees, stakeholders and ultimately communities. As an example of the various recognitions given acknowledging the value of ESG in recent years, the U.S. Business Roundtable had released a new statement in August 2019 affirming businesses' commitments to ESG. This statement was signed by CEOs of a number of Fortune 100 companies, including a number of companies that have since received significant attention in light of COVID-19, such as Amazon, American Airlines, 3M, Boeing, Marriott, Target and Walmart. Given the public perceptions and expectations of a corporation's role at this time, we would anticipate that ESG commitments will continue to remain highly relevant across all sectors.

In consideration of the current business concerns and priorities around preserving cash flow and stabilizing operations, as well as the social consequences of the disruption caused by COVID-19, to what extent do you anticipate that ESG principles remain relevant in guiding new investment opportunities and management of existing investments at this time?

Barros & Errázuriz's Response: We are certain that investors generally and particularly PE funds will prefer to invest in companies with strong ESG policies, considering that any social and/or governance-related issue may heavily impact the eventual exit on the investment.

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9. <u>"Key Person" Focus</u>

Even for established funds with close, long-term relationships with their investors, the nature of COVID-19 has been so unprecedented that we are seeing investors focus closely on obtaining the clarity needed and further insights on measures taken by PE sponsors to protect their investments. We have seen significant focus on ensuring that business continuity plans are updated in a manner that takes into consideration the possibility of further operational changes imposed by applicable government requirements and recommendations such that appropriate risk management protocols are in place, including as to key persons whether at the business or involved with any number of a given business's vendors. Given the unpredictability of COVID-19, which has already impacted leaders at the highest levels of government and business (UK Prime Minister Boris Johnson and Morgan Stanley CEO James Gorman being two notable examples), understanding "key person" triggers at the portfolio company level for insurance coverage and/or commercial contracts will be of heightened importance. Similarly, in more extreme cases at the fund level, the "key person" triggers in fund documents may become relevant in the case of extended unavailability (e.g., what constitutes "incapacitation"), including which investor rights may vest upon a "key person event" (such as redemption rights or other protections). In either case, parties may seek to broaden key person clauses going forward to address relevant commercial considerations due to these experiences to date with COVID-19.

As it relates to business continuity, are you seeing, or do you expect to see, additional succession or contingency plans that provide assurances if certain key people are unable to meet their obligations for an extended period of time? At the fund level, what would generally be needed to trigger a "key person event" and what are the rights in favor of the investors should such an event occur? Based on your discussions with clients and contacts in the industry, what are the measures you would advise clients to take regarding how best to prepare for and manage the risk surrounding any key person changes caused by COVID-19?

<u>Barros & Errázuriz's Response</u>: In general, based on what we have seen with our PE clients, we do not foresee major changes in succession plans or contingency plans to cover this sort of event. As to key person triggers, usually at the fund level, a "Key Person Event" will be triggered when one or more of the Key Persons dies or leaves the management company for any reason and, sometimes, when one or more of them do not dedicate a sufficient amount of time to the business affairs of the fund for an extended period of time. Once a Key Person Event is triggered, there are different types of rights in favor of investors such as the termination of the commitment period or other similar measures that we always recommend to our LP clients. We do not expect any major changes in LPs pushing for broadened "Key Person" triggers and rights in response to the pandemic.

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10. <u>"Material Adverse Effect" and Other Concepts</u>

While the full impact of COVID-19 remains to be seen, it is not surprising that parties are now actively initiating a closer review of material adverse effect ("MAE") provisions as well as potential issues with pre-closing covenant compliance and closing condition satisfaction for transactions that signed but have not yet closed. Given the disruption to date, buyers may conclude that earlier valuations agreed to pre-COVID-19 need to be revisited. In more severe cases, a buyer may believe that terminating the transaction is the most appropriate path forward, whether on the basis that the target business has suffered an MAE and/or has breached the agreement and is otherwise unable to satisfy its closing conditions. While no quantifiable test exists as to whether an MAE has occurred and courts are generally reluctant to make such a determination, both Delaware and New York law do require that the adverse effects be "durationally significant". To date, MAE has been invoked successfully only once in Delaware court. In view of the usual practices for defining MAE (which, among other things, generally involve an absence of specific events or dollar thresholds), we see MAE provisions being used as a negotiation tool for buyers who believe that re-negotiation of a deal is appropriate. In the case of COVID-19 in particular, buyers looking to terminate will also need to address common exclusions in the definition of a MAE for industry-wide or "systemic" events such as pandemics, "Acts of God", changes in law or government actions unless the business was disproportionately impacted. Accordingly, we anticipate that parties, in seeking remedies, will increase their attention on whether closing conditions cannot be satisfied for other reasons, such as in the case where pre-closing interim operating covenants are breached in a manner that would impede closing. Sycamore Partners' recent termination of its agreement with L Brands, the owner of Victoria's Secret, is one high-profile example of a decision to terminate based largely on analysis regarding the target's covenant compliance and ability to satisfy closing conditions.

For existing deals in progress that have been signed but not yet closed, we are seeing an increase in efforts to use material adverse change provisions and other conditions to either unwind or renegotiate transactions. Are you experiencing similar situations with respect to your existing deals, whether on the buy or sell side? What, in your experience, would be the level of change required (and for what duration) in order for a buyer to be well-positioned to prevail on invoking a material adverse change provision? Going forward, do you anticipate any changes to how parties may wish to define MAE in an acquisition agreement as a result of the effects of COVID-19?

<u>Barros & Errázuriz's Response</u>: We have not experienced similar observations at this time. We believe that deals signed prior to the COVID-19 pandemic will not be unwound prior to closing due to any MAE-related reasons arising from COVID-19. In contrast, what we have seen in the market is that deals in more preliminary stages have been put on hold or renegotiated on their terms.

Aside from MAE, it is important to note that Chilean law establishes statutory force majeure rights that may apply under certain circumstances in agreements governed by Chilean law even without an explicit reference to the concept. However, there are certain cases where parties define force majeure as well as its application in the agreement with the purpose of limiting (or increasing) its applicability depending on the facts. As such, the applicability of force majeure needs to be assessed case by case. With respect to MAE provisions, we would take the same approach. Typically, MAE is defined to cover impacts on business operations and/or prospects taken into account for a particular transaction, including monetary thresholds, and would not be considered a force majeure event.

There is currently no established case law with respect to the MAE concept. Although we have been approached by clients asking about the potential application of force majeure and/or MAE provisions, we expect to have more specific case law in the near future that may be useful in helping to assess any potential changes in approach to these sorts of clauses going forward. We expect that courts will eventually apply a very high standard for an MAE determination given the significant consequences that an MAE finding would have on a transaction. In any case, the courts will judge applying Chilean contractual law principles such as good faith, autonomy of will and obligatory force of the agreement between the parties.

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11. <u>IPO and Exit Prospects</u>

On the eve of the COVID-19 outbreak, market conditions in many regions in Latin America were favorable for PE funds seeking exit opportunities for their most successful investments, with several notable companies planning to launch IPOs or follow-on offerings. As we have seen the pandemic bring on a wave of uncertainty, such exit plans have been put on hold and the extent of the delay and whether other exit opportunities may be pursued are both unclear.

With the outbreak, are you seeing companies delaying or withdrawing their IPO plans or follow-on offerings? Recognizing that this may vary by industry, are companies and investors seeing the IPO window opening back up in the short term and, if so, how do you see the time lag impacting the terms and pricing of offerings? To the extent not, what are the alternatives you are seeing on exit considerations?

Barros & Errázuriz's Response: Considering that Chile is a small market, the number of IPOs of domestic companies each year is very limited. Nevertheless, we believe that any IPO that has been discussed prior to the COVID-19 outbreak should be postponed until markets reopen and are more stable. As an alternative, we may see in the future PE funds preferring to initiate partial cash-outs through the sale of non-controlling positions (e.g.,

minority investments) and postponing IPO and/or other exit plans of their control investments for the medium term. Such measures would allow PE funds to return some cash to the LPs without sacrificing more upside given the current circumstances.

C. Colombia – Brigard Urrutia Q&A

Jaime Robledo Vásquez

1. Current Governmental Responses to COVID-19

In response to the shutdown orders in states and counties across the United States that have significantly curbed business activity across sectors in the past two months, the Coronavirus Aid, Relief, and Economic Security (CARES) Act established the Paycheck Protection Program ("PPP") on March 27, 2020, which, among other things, authorized up to an initial $349 billion (with an additional $310 billion of funding added on April 24, 2020) in loans aimed at providing liquidity to eligible small businesses, sole proprietorships, independent contractors and self-employed individuals. Subject to certain restrictions, a loan extended under the PPP will be forgiven to the extent employee and compensation levels are maintained and the proceeds are used within eight weeks after the loan is made for payroll costs and other approved purposes. For businesses seeking to apply, eligibility will depend on whether the applicant qualifies as a small business concern under one of the metrics (e.g., number of employees, total annual receipts) required by the Small Business Administration ("SBA"). The eligibility determination will, subject only to very limited exceptions, involve the application of the SBA's affiliation rules which aggregates the relevant metrics for the applicant and all of its applicable affiliates. As of April 24, 2020, the SBA issued an interim final rule indicating that the portfolio companies of a private equity fund ("PE fund") are not de facto excluded and may still be eligible to receive a PPP loan if they otherwise meet the eligibility criteria.

Are you seeing similar federal/national and/or local government decrees or measures (or a demand for such) that would benefit portfolio companies in terms of providing access to additional capital or other relief measures? Are there conditions applicable to obtaining such benefits (e.g., job protection, limits on size of business (whether measured by revenue and/or employee head count), etc.)? Are you seeing portfolio companies seeking government assistance and, if so, to what extent is it relevant if they are private equity backed?

Brigard Urrutia's Response: The Colombian government has approved a number of relief packages to companies and businesses in the form of decrees and other measures. These relief measures apply equally to companies across all industries and of all sizes and eligibility is not contingent on whether a given company is venture capital or private equity-backed.

To increase liquidity for affected businesses, the Colombian government has opened several lines of credit through *Bancoldex* (National Bank for Foreign Trade) and *Findeter* (National Development Agency) for small, medium and large companies in any industry that are undergoing financial difficulties derived from COVID-19. Generally, the lines of credit are repayable within three to 10 years, with a grace period ranging from three to 12

months. The loans are not subject to any eligibility requirements, such as based on revenue or headcount, nor is there any cap on borrowed volume. The use of proceeds may be subject to different requirements or restrictions depending on the type of credit for which the company applied. However, most of the lines of credit require that the proceeds be used for working capital or debt refinancing purposes.

In addition to the line of credit program, Decree 560 of 2020 issued on April 15, 2020 (the "Decree") established an emergency insolvency regime. This Decree has broadened the scope of the insolvency regime to include formerly excluded companies and changed some of the previous insolvency criteria, such as the ratio of allowed losses and paid-in capital. Among others, the Decree addresses four main topics:

(a) *Increased the flexibility of insolvency regulations to relieve debtor's cash flow and allow expedited insolvency proceedings.* The debtor may obtain credit during the negotiation of the reorganization process to be used for ordinary course purposes, without prior court authorization. The Decree also simplifies the process of admission to reorganization mechanisms, namely by providing that the court will not audit the content or accuracy of the documents provided or the financial information or compliance with the accounting policies of the applicant debtor.

(b) *Distressed M&A.* The Decree contains additional provisions governing any proposed acquisition of the insolvent company or its assets. Any creditor may now capitalize a company whose equity value is negative and, as a result thereof, keep all of the shares in its capital.

(c) *DIP financing*. The debtor may obtain credit during the negotiation of the reorganization process to be used for ordinary course purposes, without prior court authorization.

(d) *Tax relief measures.* The Decree provides certain tax relief measures for companies that are undergoing a reorganization proceeding and for companies in the process of executing a reorganization agreement entered into prior to the issuance of the Decree. Among others, these measures include certain exemptions from tax withholding and from liquidation and advance payment of income tax.

Additionally, on April 28, 2020, Colombia became an official member of the Organisation for Economic Co-operation and Development. As such, Colombia became the third Latin-American country to join this organization and ratified its commitment to guarantee the highest standards on public policies. Several legal reforms regarding labor and employment matters, the judicial system and anti-bribery regulations, among others, have been implemented in response to this commitment.

These are the only governmental measures adopted that could benefit portfolio companies at this time. However, we believe that the Colombian government will implement further measures in the near future.

In the U.S., the aforementioned SBA affiliation rules have generally limited the availability of access to governmental assistance through the PPP loans for many companies owned or controlled by PE or venture capital funds or alternative asset managers (including, in the case of minority investments, where control is inferred from certain consent rights held by the institutional investor). For your clients with U.S. operations who may be eligible, are you seeing any efforts to unwind or otherwise modify such arrangements so that they can more readily seek government assistance for their U.S. business operations?

Brigard Urrutia's Response: No, we have not seen these types of efforts from our clients with U.S. operations at this time.

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2. Changes in Deal Dynamics

Prior to COVID-19, we had been facing a predominantly "seller's market" where deal terms had become increasingly favorable to sellers such that it became common that potential buyers, including private equity sponsors, needed to be willing to adopt more flexible positions to be competitive in sale processes. While competition between potential private equity and corporate buyers will remain, we anticipate that the volatility and disruption brought about by COVID-19 should result in a shift toward more buyer or investor favorable terms. We also anticipate that while speed and deal certainty should remain a priority, buyers will take comprehensive measures with respect to due diligence, particularly as it relates to understanding how a given target business has been altered by the pandemic and whether it is able to mitigate the effects now and in the longer term.

Recognizing that some industries may be impacted more than others, what do you expect with respect to changes in the negotiation leverage scale as well as market trends for PE sponsors as a result of COVID-19? Do you also anticipate that corporate buyers may take a step back in the near term as they focus on preserving their cash flow and operations or otherwise, thus reducing some competition for financial buyers? Given the current economic changes, we believe the current foreign exchange rates are also favorable for foreign PE sponsors to invest in the Latin American region, if you could please comment on this aspect as well.

Brigard Urrutia's Response: Prior to the pandemic, the leverage scale was very seller-friendly. Due to COVID-19, we expect that the scale will shift and present the investors and the market in general with deal terms that are more buyer/investor-friendly.

We also anticipate that corporate buyers will slow down their acquisition and investment activities and be a lot more cautious in the cash management of their operations. However, we believe that due to the economic situation in which most companies will find themselves after the pandemic, it is possible that there will be a significant number of transactions with lower economic valuations that will favor PE investors and, in a certain way, propel the number of distressed M&A transactions. Ultimately, we do not foresee that PE sponsors will be ceding more space to corporate/strategic buyers.

Finally, we consider that due to the recent Colombian peso depreciation, one of the currencies that has suffered the sharpest decline worldwide, Colombian targets will be cheaper for foreign PE sponsors. Consequently, the foreign exchange rates will be a key factor in M&A and venture capital transactions for foreign investors who will see the favorable exchange rate as a significant business advantage.

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3. For Better or Worse: Industries Impacted by COVID-19

Within a short period of time, COVID-19 has caused disruption throughout all industries. On the one hand, the outbreak and the resulting shutdown orders in the U.S. have had a significant negative impact on sectors that are unable to deliver their core services and products, such as the oil and gas, tourism, airline, hotel and entertainment industries. At this time, it remains unclear as to when and to what extent consumer demand will return. On the other hand, the lockdowns and restraints imposed have resulted in unprecedented demand and new opportunities in light of how businesses have leveraged their use of technology (e.g., online retailers, video conferencing services, online learning, home fitness, delivery applications, pet products, etc.).

Are you seeing, or do you expect to see, increased investment and M&A activity involving local sectors or businesses that are benefiting from the COVID-19 outbreak, or that were active before COVID-19 and remain relevant at this time, e.g., the renewable energy sector?

Brigard Urrutia's Response: As we mentioned, investment and M&A activity in sectors that were active before COVID-19, such as the renewable energy sector, have not been affected; in this sense our clients have continued their ongoing transactions and we have received further requests to advise in investments or structuring of renewable energy projects.

Notwithstanding the foregoing, it is unclear whether COVID-19 will play a part in the increase or even interest in investment and M&A activity in other local business sectors that may have been currently benefiting from COVID-19 outbreak.

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4. Alternative Investment Opportunities

For the industries most heavily impacted, we anticipate this may result in PE funds evaluating alternative opportunities given the limited traditional M&A buyout activity at this time. Similar to the trends observed during the 2008 financial crisis, we have already seen certain PE funds committing to significant investments in public companies in recent weeks with Apollo/Silver Lake's $3.2 billion investment in Expedia and Roark Capital's $200 million investment in the Cheesecake Factory as a few high-profile examples. There has also been discussion around increased opportunities for more carve-out transactions as strategic companies may divest their non-core assets in an effort to preserve liquidity. As the impacts of COVID-19 persist and businesses explore their strategic options, we would also anticipate greater focus on distressed and special situations investments.

To the extent more traditional M&A activity may have slowed, what are some alternative strategies that PE sponsors may be considering (or should consider) at this time (e.g., PIPEs, carve-outs, distressed acquisitions, etc.)?

Brigard Urrutia's Response: Considering how the current situation has impacted the exchange rate and the depreciation of the Colombian peso, an increase in foreign investment through PE rather than local investments as well as through other distressed acquisitions is possible; however, market behavior is still too uncertain to be able to make a more accurate prediction at this time.

We believe the current government will probably support the pursuit of new foreign investments as one of the key tactics to promote domestic recovery and that it will not take a protectionist approach by creating further restrictions to foreign investments.

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5. Post-COVID-19 Economy and Governmental Responses

As governments respond and businesses adapt to the changes caused by COVID-19, we anticipate that the "new normal" will reshape certain sectors, some of which may be particularly well-positioned to thrive to the extent they offer services and/or products that can provide solutions for the changes caused by COVID-19. Such sectors may present new and interesting opportunities but may also further draw additional governmental or regulatory response.

Based on your experience and discussions with market participants, what sectors do you see gaining the most and/or having a greater impact on the economy post-COVID-19? Given the difficulties that businesses have experienced, do you think the post-COVID 19 era may see a more favorable regulatory environment that enables and facilitates their recovery? For example, the Superintendency of Industry

and Commerce of Colombia, which regulates fair competition and protects consumers, in December 2019 ruled that Uber had violated competition rules; Cornershop, a leading online grocery provider in Chile, Mexico, Peru, Brazil and Colombia, and Uber have been hampered by some antitrust regulators in Latin America; in 2018, the Mexican antitrust regulator did not approve Walmart's acquisition of Cornershop.

Brigard Urrutia's Response: We consider that the e-commerce, technology, pharmaceuticals and food sectors will be the sectors having a greater impact in the post COVID-19 economy.

In regards to the regulatory environment after the pandemic, it is too early to predict whether the Colombian government will relax any regulations in response to the challenges brought by COVID-19. Some industrial sectors have initiated this discussion by delivering letters to the government seeking more flexibility in connection with the environmental licensing process and the satisfaction of mandatory prior consultation requirements with certain ethnic groups who hold rights to participate in decisions, activities or projects that could have an impact in their territories. However, such changes would require passing new legislation and might be subject to constitutional control. We do not expect changes on fair competition and consumer protection regulation.

Notwithstanding the above, we do anticipate more political interest and haste to work on the regulation of shared economic platforms. There has been a debate in Colombia about whether it would be necessary to pass new regulations addressing the particularities of services rendered through shared economy platforms, such as Uber or Cabify, or to consider that such platforms render transportation services and are therefore subject to the regulations already in place. Ultimately, after the downturn, there may be more political interest to pass new regulations to stimulate the development of businesses based on shared economies and attract foreign investment.

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6. COVID-19 Impact on Limited Partners

The current circumstances bring into question the likelihood of meeting expectations with respect to fundraising, especially for younger PE funds. Based on discussions to date, we anticipate that funds that lack a strong, established track record with limited partners ("LPs") who are seeking new investments in this environment could face greater challenges as they seek capital commitments from investors who may be less likely to deploy new capital in the first instance whether due to an inability to meet with and diligence the new(er) fund managers, changes in their asset allocations, a general preference to conserve capital at this time or other reasons. The limitations on meeting investors in person due to the travel restrictions and quarantine measures in the U.S. and worldwide may be more manageable for established PE funds given their existing relationships, but the use of Zoom and other video-conference methods is still unlikely to be a suitable substitute in all cases.

With respect to liquidity questions, PE funds may need to weigh their lender relationships and credit facility options against the impact of potential LP capital calls when LPs have their own liquidity considerations. Given the quarantine and work-from-home-restrictions, we anticipate that LPs may need more lead time generally, including for any required capital contributions, and it is reasonable to expect that anything beyond what is contemplated by the existing fund agreements may take longer than is typical.

Relative to the fundraising environment in 2008/09, for new funds being raised at this time, what are the main structural factors and considerations that may limit LPs' interest in committing capital to new ventures? Are you seeing, or do you expect to see, LPs change their allocations to PE as an asset class (whether in the U.S. and/or to funds with a Latin American or other international focus) during this downturn?

Brigard Urrutia's Response: It is too soon to predict how LPs and PE funds will manage their allocations to new ventures. However, PE funds have been struggling with the depreciation of the Colombian peso during the last few years. After this downturn, we do not expect this situation to change. We anticipate that PE funds will be even more cautious about their investments in Colombia.

It is likely too soon to tell, but are you concerned about potential LPs defaulting on their current commitments? Based on your discussions with clients, have LPs been increasingly reaching out with capital call funding concerns (even if just prospectively)? Do they expect any pressure on fees typically earned by funds?

Brigard Urrutia's Response: It is too early to tell. We have not heard about LPs potentially defaulting on their current commitments or any increase in frequency of capital calls at this time.

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7. Availability of Debt Financing

As we have seen to date, PE funds and their portfolio companies have taken various measures to secure debt financing from commercial banks to stabilize cash flows in light of the uncertainty of the current financial climate. In the past and of relevance now, non-bank lenders in the private credit industry have shown more willingness to provide financing, albeit on more expensive terms and likely with more scrutiny from the lending party.

Based on your discussions with clients and contacts in the industry, are they seeing, or do they expect to see, significant liquidity concerns within their portfolio companies? Have you advised portfolio companies to draw down on credit facilities? If so, are they seeing any resistance from their lenders at this stage? Please also comment on the extent to which you anticipate commercial banks taking a more

conservative approach to lending during and after the pandemic, as well as the best strategies, including alternative sources of financing, available to PE sponsors and their portfolio companies as they seek alternative cash flows to weather the downturn.

Brigard Urrutia's Response: Although it is not customary in Colombia for portfolio companies to seek financial loans, we do know that certain financial institutions will take a more conservative approach to making long-term loans. Given the new circumstances, our advice would be for companies in need of capital to access the lines of credit granted by the Colombian government, as further described in Section 1. - *Current Governmental Responses to COVID-19* above.

We have also seen the Colombian Superintendence of Finance (the "SFC") take on a very active role in aiming to mitigate the impact of COVID-19. By means of both written and oral requests, the SFC mandated local administrators to closely monitor and surveil the actions being implemented by sponsors to mitigate the problems derived from the current situation. In addition, sponsors and local administrators are seeking frequent updates from local experts on the measures being adopted by the Colombian government. This will allow sponsors to gather sufficient information to make informed decisions and avoid further economic and social missteps. It is important to point out that a fluent and open communication channel between the sponsors and the LPs is key to maintaining a healthy relationship that allows proper measures to be implemented throughout the crisis.

As a final comment on this matter, please note that, considering the current pandemic, the Decree has established an "emergency negotiation" proceeding for companies. The emergency negotiation grants companies three months to negotiate a reorganization agreement, provided that (i) the debtor is in default or has an imminent inability to pay and (ii) the court has authorized the emergency negotiation proceeding. During this negotiation, the processes of execution, coercive collection, restitution of possession and execution of guarantees against the debtor are suspended. Payments of obligations for administrative expenses that the debtor deems necessary may be deferred, except for payment of salaries, payroll taxes and social security contributions.

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8. ESG Initiatives

Leading up to COVID-19, environmental, social and governance-related ("ESG") initiatives were becoming a strong area of focus for investors as part of the criteria used to assess the long-term quality and sustainability of potential investments. The growing view was that a strong ESG proposition can create long-term value for companies, their employees, stakeholders and ultimately communities. As an example of the various recognitions given acknowledging the value of ESG in recent years, the U.S. Business Roundtable had released a new statement in August 2019 affirming businesses' commitments to ESG. This statement was signed by CEOs of a

number of Fortune 100 companies, including a number of companies that have since received significant attention in light of COVID-19, such as Amazon, American Airlines, 3M, Boeing, Marriott, Target and Walmart. Given the public perceptions and expectations of a corporation's role at this time, we would anticipate that ESG commitments will continue to remain highly relevant across all sectors.

In consideration of the current business concerns and priorities around preserving cash flow and stabilizing operations, as well as the social consequences of the disruption caused by COVID-19, to what extent do you anticipate that ESG principles remain relevant in guiding new investment opportunities and management of existing investments at this time?

Brigard Urrutia's Response: Based on our experience, we anticipate that ESG principles will acquire more relevance in light of the current pandemic. As a matter of fact, most of our clients have been making extraordinary efforts to survive – trying to minimize, to the greatest extent possible, any negative effects brought by COVID-19, and preserving cash flow and trying to stabilize their operations – without making material changes to ESG commitments.

In our opinion, the manner in which companies handle the crisis, including their ESG management, will mark and differentiate themselves as they are under the scrutiny of public opinion. Interest in stakeholder value in addition to shareholder value was already a matter of importance and on companies' agendas, especially publicly traded ones. LPs seeking to diversify their portfolios and further a reputation that they are committed to ESG and impact investing may likely put pressure on sponsors to engage more and more in this kind of investments.

At this time, governmental entities in Colombia are also encouraging socially responsible management of funds. The SFC has publicly promoted that LPs should be mindful in reviewing their existing portfolios and consider under better market practice guidelines that pensioners' money be invested responsibly and in funds that care for additional social and environmental returns.

Finally, increasing international pressure for companies to adopt sustainability programs in a medium or long-term basis, and for PE firms and funds to focus their investments on ESG-responsible businesses, is very likely. Thus, companies interested in attracting major private investors will adapt their strategies to include tangible actions under ESG principles.

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9. *“Key Person” Focus*

Even for established funds with close, long-term relationships with their investors, the nature of COVID-19 has been so unprecedented that we are seeing investors focus closely on obtaining the clarity needed and further

insights on measures taken by PE sponsors to protect their investments. We have seen significant focus on ensuring that business continuity plans are updated in a manner that takes into consideration the possibility of further operational changes imposed by applicable government requirements and recommendations such that appropriate risk management protocols are in place, including as to key persons whether at the business or involved with any number of a given business's vendors. Given the unpredictability of COVID-19, which has already impacted leaders at the highest levels of government and business (UK Prime Minister Boris Johnson and Morgan Stanley CEO James Gorman being two notable examples), understanding "key person" triggers at the portfolio company level for insurance coverage and/or commercial contracts will be of heightened importance. Similarly, in more extreme cases at the fund level, the "key person" triggers in fund documents may become relevant in the case of extended unavailability (e.g., what constitutes "incapacitation"), including which investor rights may vest upon a "key person event" (such as redemption rights or other protections). In either case, parties may seek to broaden key person clauses going forward to address relevant commercial considerations due to these experiences to date with COVID-19.

As it relates to business continuity, are you seeing, or do you expect to see, additional succession or contingency plans that provide assurances if certain key people are unable to meet their obligations for an extended period of time? At the fund level, what would generally be needed to trigger a "key person event" and what are the rights in favor of the investors should such an event occur? Based on your discussions with clients and contacts in the industry, what are the measures you would advise clients to take regarding how best to prepare for and manage the risk surrounding any key person changes caused by COVID-19?

Brigard Urrutia's Response: Since the COVID-19 outbreak began, local governments have responded by taking various measures that include imposing quarantines and medical screenings, restricting travel, limiting public gatherings and suspending certain activities that may directly affect the work carried out by fund managers, but none that may affect virtual working or keeping surveillance over assets by electronic means. Having this in mind, we do foresee that the current situation will generate new contingency plans that would guarantee LPs the continuity of the given fund's activities should certain key people be restricted or unavailable to successfully carry on with the fund's main functions for an extended period of time.

It is important to point out that private equity regulations in Colombia do not have any provisions related to "key person events"; however, it has become a market practice to address these sorts of provisions for PE funds in the parties' agreements. Therefore, at the fund level a "key person event" is usually triggered when a member of the general partner ("GP") team that has been designated as a "key person" either resigns, is no longer able to participate in the fund's activities (typically, a "key person" event will only be triggered after the person is not available to perform his or her duties for the fund for a period that exceeds 60 days) or dies. As a general rule, the

fund's bylaws usually seek to restrain the application of the "key person" event to those cases where more than two or three key persons are missing. This kind of event would usually trigger a fund's bylaws (*Reglamento*) clause by which the investment period would be suspended.

With respect to COVID-19, while it may cause key persons to be quarantined and far away from transportation systems that enable proper travel to the location where investments are based, GPs still have access to different technological means and tools that allow them to properly surveil the fund's investments. This would generally keep the "key person" provision from being triggered. However, in case the virus causes severe health issues to the key persons for a period longer than 60 days, GPs may need to prepare for potential requests of suspension of the investment period.

In a worst case scenario, the suspension of the investment period will usually be in force until (i) the key person is replaced by the LPs following the standards and profile set by the fund's bylaws; (ii) the LPs decide to resume the investment period; (iii) the LPs decide to terminate the investment period, in which case they will be able to replace the GP or establish a limited period for the GP to carry out the fund's exits; or (iv) the investment period is terminated prematurely after not being able to replace the missing key person. It is important to point out that is common for the fund's bylaws to include a list of characteristics and requirements that the key person's replacement must fulfill. Following the occurrence of these events, the GP would be entitled to submit a list of candidates to the LPs, whose appointment could only be objected to if the candidates do not comply with the listed requirements.

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10. "Material Adverse Effect" and Other Concepts

While the full impact of COVID-19 remains to be seen, it is not surprising that parties are now actively initiating a closer review of material adverse effect ("MAE") provisions as well as potential issues with pre-closing covenant compliance and closing condition satisfaction for transactions that signed but have not yet closed. Given the disruption to date, buyers may conclude that earlier valuations agreed to pre-COVID-19 need to be revisited. In more severe cases, a buyer may believe that terminating the transaction is the most appropriate path forward, whether on the basis that the target business has suffered an MAE and/or has breached the agreement and is otherwise unable to satisfy its closing conditions. While no quantifiable test exists as to whether an MAE has occurred and courts are generally reluctant to make such a determination, both Delaware and New York law do require that the adverse effects be "durationally significant". To date, MAE has been invoked successfully only once in Delaware court. In view of the usual practices for defining MAE (which, among other things, generally involve an absence of specific events or dollar thresholds), we see MAE provisions being used as a negotiation tool for buyers who believe that re-negotiation of a deal is appropriate. In the case of COVID-19 in particular,

buyers looking to terminate will also need to address common exclusions in the definition of a MAE for industry-wide or "systemic" events such as pandemics, "Acts of God", changes in law or government actions unless the business was disproportionately impacted. Accordingly, we anticipate that parties, in seeking remedies, will increase their attention on whether closing conditions cannot be satisfied for other reasons, such as in the case where pre-closing interim operating covenants are breached in a manner that would impede closing. Sycamore Partners' recent termination of its agreement with L Brands, the owner of Victoria's Secret, is one high-profile example of a decision to terminate based largely on analysis regarding the target's covenant compliance and ability to satisfy closing conditions.

For existing deals in progress that have been signed but not yet closed, we are seeing an increase in efforts to use material adverse change provisions and other conditions to either unwind or renegotiate transactions. Are you experiencing similar situations with respect to your existing deals, whether on the buy or sell side? What, in your experience, would be the level of change required (and for what duration) in order for a buyer to be well-positioned to prevail on invoking a material adverse change provision? Going forward, do you anticipate any changes to how parties may wish to define MAE in an acquisition agreement as a result of the effects of COVID-19?

Brigard Urrutia's Response: Indeed. Several clients with signed deals but not yet closed have approached us with questions in connection with the MAE clause, both from the sell side and buy side. Yet no client or counterparty has invoked such clause to avoid closing at this time.

Based on our experience, a significant number of M&A contracts contain MAE definitions with express carve-outs for "national emergencies." Colombia was put under a state of economic, social and environmental emergency by the government on March 17, 2020; as a result, no buyer under the aforementioned contracts would be able to enforce an MAE provision based on the pandemic. Consequently, this is protective of sellers who are contractually entitled to sue to force buyers to close, regardless of the fact that the national emergency may affect buyers' financial interest in closing. Buyer will also have less leverage to argue, for example, that the price should be renegotiated in the case that national emergencies are specifically excluded as an MAE event.

Similarly, if a contract specifies that a pandemic is not an MAE, this also means that the parties are waiving their right to claim a force majeure event derived from the pandemic. Therefore, in order to avoid having pre-closing disputes be subject to the statutory force majeure rule and to knowingly allocate deal certainty risk between the parties, M&A contracts will expressly need to ascertain whether the definition of MAE includes or excludes certain events, such as pandemics or national emergencies.

For contracts that do not currently expressly carve out national emergencies, pandemics or similar events, we believe it is possible that COVID-19 will be deemed a force majeure event and therefore, buyer may refuse to

close the respective transaction. Moreover, even though force majeure may last for as long as the pandemic lasts, it is possible that buyers will start pursuing a theory under which the effects of the pandemic will last longer (due to the economic impact it will have) and therefore, seek a full exit of the corresponding agreement.

Under Colombian laws and case law, there are no thresholds nor quantifiable criteria to determine whether an MAE has occurred. A court would analyze the particular wording of an MAE clause to get a sense of the parties' intentions, and subsequently render its decision based on force majeure regulations. As to force majeure, under Colombian law, the Colombian Supreme Court of Justice (the "CSCJ") has found that a force majeure event must be (i) external, (ii) unforeseeable and (iii) an irresistible event that makes it impossible for the party to fulfill its obligations. Courts have developed this criteria by defining the scope of such adjectives, rather than applying thresholds or quantifiable requisites. Based on case law, there is a duty of diligence and care imposed on the affected party that goes beyond merely proving that the fact was external but also requires the party to demonstrate that the inability to perform was not even partially attributable to its negligence. Notwithstanding the above, the CSCJ has stated that the decision on whether an event qualifies as force majeure must be assessed on a case-by-case basis. Consequently, the outbreak of a virus is not itself an event of force majeure.

We further note that upon the declaration of the state of economic, social and environmental emergency, the government expressly stated that the spread of COVID-19 was a "sudden and unexpected" circumstance. Thus, parties to agreements entered into prior to the issuance of Decree 417 could argue that force majeure provisions are applicable since COVID-19 was an unforeseeable event, subject to proving it was also external and impossible to resist and not otherwise carved out of MAE. As described above, the applicability of this remedy would be assessed on a case-by-case basis.

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11. IPO and Exit Prospects

On the eve of the COVID-19 outbreak, market conditions in many regions in Latin America were favorable for PE funds seeking exit opportunities for their most successful investments, with several notable companies planning to launch IPOs or follow-on offerings. As we have seen the pandemic bring on a wave of uncertainty, such exit plans have been put on hold and the extent of the delay and whether other exit opportunities may be pursued are both unclear.

With the outbreak, are you seeing companies delaying or withdrawing their IPO plans or follow-on offerings? Recognizing that this may vary by industry, are companies and investors seeing the IPO window opening back up in the short term and, if so, how do you see the time lag impacting the terms

and pricing of offerings? To the extent not, what are the alternatives you are seeing on exit considerations?

Brigard Urrutia's Response: As Colombia's capital markets are characterized by ownership concentration and the fact that few companies are listed, the strength of the IPO market is limited and restrained under normal conditions. This is especially true for PE/venture capital-backed companies. As a result, over the last six years there has not been any IPO of PE or venture capital-backed companies.

Coincidentally, we were recently reviewing a potential IPO of a portfolio company, and due to the COVID-19 outbreak, the sponsor postponed the IPO plan (which we believe would have happened irrespective of the industry) due to the lack of appetite among investors because of the increased market volatility and weak market conditions, which have made it riskier for PE funds to utilize the IPO exit window. Consequently, our view is that companies are not expecting the IPO window to open back up in the very near term. However, we have also seen that institutional investors, such as pension funds with the liquidity to invest and interest in diversifying their portfolio, are willing to invest in portfolio companies with IPO potential. Likewise, regulators and the Colombian Securities Exchange are very focused on the stock market bouncing back such that market conditions for IPOs should improve in the near term. With respect to the impact on the terms and pricing of offerings, there may be an impact in the pricing of offerings because of the lockdown, mostly for companies affected by the pandemic. As to the alternatives on exit considerations, we do see that PE funds are seeking strategic sales to large companies with enough liquidity to acquire those companies rather than an exit through the public markets.

D. Mexico – Mijares Angoitia Cortés y Fuentes, S.C. Q&A

Pablo Mijares, **Martín Sánchez**, **Francisco Glennie**

1. Current Governmental Responses to COVID-19

In response to the shutdown orders in states and counties across the United States that have significantly curbed business activity across sectors in the past two months, the Coronavirus Aid, Relief, and Economic Security (CARES) Act established the Paycheck Protection Program ("PPP") on March 27, 2020, which, among other things, authorized up to an initial $349 billion (with an additional $310 billion of funding added on April 24, 2020) in loans aimed at providing liquidity to eligible small businesses, sole proprietorships, independent contractors and self-employed individuals. Subject to certain restrictions, a loan extended under the PPP will be forgiven to the extent employee and compensation levels are maintained and the proceeds are used within eight weeks after the loan is made for payroll costs and other approved purposes. For businesses seeking to apply, eligibility will depend on whether the applicant qualifies as a small business concern under one of the metrics (e.g., number of employees, total annual receipts) required by the Small Business Administration ("SBA"). The eligibility determination will, subject only to very limited exceptions, involve the application of the SBA's affiliation rules which aggregates the relevant metrics for the applicant and all of its applicable affiliates. As of April 24, 2020, the SBA issued an interim final rule indicating that the portfolio companies of a private equity fund ("PE fund") are not de facto excluded and may still be eligible to receive a PPP loan if they otherwise meet the eligibility criteria.

Are you seeing similar federal/national and/or local government decrees or measures (or a demand for such) that would benefit portfolio companies in terms of providing access to additional capital or other relief measures? Are there conditions applicable to obtaining such benefits (e.g., job protection, limits on size of business (whether measured by revenue and/or employee head count), etc.)? Are you seeing portfolio companies seeking government assistance and, if so, to what extent is it relevant if they are private equity backed?

Mijares' Response: In contrast to the measures taken by many governments in response to COVID-19, including the U.S., the Mexican government has not granted or proposed any fiscal stimulus and/or relief measures to businesses in Mexico that have been negatively impacted by the pandemic. This will undoubtedly have an impact on the pace at which the Mexican economy will recover. However, on a more limited basis, the Bank of Mexico has announced that it will implement a program to support banking institutions and provide liquidity to the market by facilitating lending to both individuals and small-to-midsized businesses.

In parallel, other market participants are also weighing in, to see how they can get involved and contribute. For example, the AFOREs (Mexican Employee Savings Plans) have also expressed interest in investing in existing

government projects, such as toll-roads and other infrastructure projects. Considering the investment restrictions of the AFOREs, this could be a boost to Development Capital Certificates known as "CKDs", which are publicly traded funds, and which are common instruments through which AFOREs invest in this type of projects. However, this would need an active role of the new administration in promoting and being open to new infrastructure projects sponsored by the private sector, which has not been their policy so far.

In the U.S., the aforementioned SBA affiliation rules have generally limited the availability of access to governmental assistance through the PPP loans for many companies owned or controlled by PE or venture capital funds or alternative asset managers (including, in the case of minority investments, where control is inferred from certain consent rights held by the institutional investor). For your clients with U.S. operations who may be eligible, are you seeing any efforts to unwind or otherwise modify such arrangements so that they can more readily seek government assistance for their U.S. business operations?

Mijares' Response: To date, we have not seen these types of efforts.

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2. ***Changes in Deal Dynamics***

Prior to COVID-19, we had been facing a predominantly "seller's market" where deal terms had become increasingly favorable to sellers such that it became common that potential buyers, including private equity sponsors, needed to be willing to adopt more flexible positions to be competitive in sale processes. While competition between potential private equity and corporate buyers will remain, we anticipate that the volatility and disruption brought about by COVID-19 should result in a shift toward more buyer or investor favorable terms. We also anticipate that while speed and deal certainty should remain a priority, buyers will take comprehensive measures with respect to due diligence, particularly as it relates to understanding how a given target business has been altered by the pandemic and whether it is able to mitigate the effects now and in the longer term.

Recognizing that some industries may be impacted more than others, what do you expect with respect to changes in the negotiation leverage scale as well as market trends for PE sponsors as a result of COVID-19? Do you also anticipate that corporate buyers may take a step back in the near term as they focus on preserving their cash flow and operations or otherwise, thus reducing some competition for financial buyers? Given the current economic changes, we believe the current foreign exchange rates are also favorable for foreign PE sponsors to invest in the Latin American region, if you could please comment on this aspect as well.

Mijares' Response: We expect buyers and investors to regain leverage in this new market and sellers to accept more "buyer-friendly" terms, both in the case of minority investments and control acquisitions.

We expect corporate buyers to slow down in terms of deal activity and to be significantly more cautious in their cash management practices. Nevertheless, we also expect the COVID-19 crisis to create many attractive opportunities for strategic transactions at lower prices. The trend for concentrations in certain sectors (e.g., energy and infrastructure) over the past two years may also increase and provide an opportunity to well-positioned funds or companies to acquire businesses and assets on more favorable terms. We also anticipate that potential buyers may benefit from the fact that some CKDs are entering their divestment periods. Absent a quick change in the current circumstances, they will need to sell their assets and investments at buyer-friendly terms.

We foresee that foreign exchange rates will be a key factor for parties in all transactions in the near future. As a result of the recent Mexican peso depreciation, one of the currencies that has suffered the sharpest decline worldwide, Mexican targets will be less expensive for foreign PE sponsors pursuing acquisitions. Having said this, we also believe that factors such as the uncertainty of further currency depreciation in the future, as well as the resulting decrease in targets' projections and valuations in U.S. dollars, may offset the advantages otherwise created by a foreign exchange rate that is favorable to potential buyers.

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3. ***For Better or Worse: Industries Impacted by COVID-19***

Within a short period of time, COVID-19 has caused disruption throughout all industries. On the one hand, the outbreak and the resulting shutdown orders in the U.S. have had a significant negative impact on sectors that are unable to deliver their core services and products, such as the oil and gas, tourism, airline, hotel and entertainment industries. At this time, it remains unclear as to when and to what extent consumer demand will return. On the other hand, the lockdowns and restraints imposed have resulted in unprecedented demand and new opportunities in light of how businesses have leveraged their use of technology (e.g., online retailers, video conferencing services, online learning, home fitness, delivery applications, pet products, etc.).

Are you seeing, or do you expect to see, increased investment and M&A activity involving local sectors or businesses that are benefiting from the COVID-19 outbreak, or that were active before COVID-19 and remain relevant at this time, e.g., the renewable energy sector?

Mijares' Response: While we do expect transactions in these sectors to increase in frequency, particularly in the pharmaceutical, technology and food sectors, we believe it is still too early to tell when this activity will begin.

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4. ***Alternative Investment Opportunities***

For the industries most heavily impacted, we anticipate this may result in PE funds evaluating alternative opportunities given the limited traditional M&A buyout activity at this time. Similar to the trends observed during the 2008 financial crisis, we have already seen certain PE funds committing to significant investments in public companies in recent weeks with Apollo/Silver Lake's $3.2 billion investment in Expedia and Roark Capital's $200 million investment in the Cheesecake Factory as a few high-profile examples. There has also been discussion around increased opportunities for more carve-out transactions as strategic companies may divest their non-core assets in an effort to preserve liquidity. As the impacts of COVID-19 persist and businesses explore their strategic options, we would also anticipate greater focus on distressed and special situations investments.

To the extent more traditional M&A activity may have slowed, what are some alternative strategies that PE sponsors may be considering (or should consider) at this time (e.g., PIPEs, carve-outs, distressed acquisitions, etc.)?

Mijares' Response: We are expecting distressed investments to spike as a result of this crisis and we have already started to see companies engaging in discussions of alternative strategies as part of their potential restructuring plans to mitigate the effects of the COVID-19 crisis. As mentioned above, special consideration should be made to divestments that will be made by CKDs. Aside from these early observations, we believe it is still too early to tell if other types of transactions will increase.

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5. ***Post-COVID-19 Economy and Governmental Responses***

As governments respond and businesses adapt to the changes caused by COVID-19, we anticipate that the "new normal" will reshape certain sectors, some of which may be particularly well-positioned to thrive to the extent they offer services and/or products that can provide solutions for the changes caused by COVID-19. Such sectors may present new and interesting opportunities but may also further draw additional governmental or regulatory response.

Based on your experience and discussions with market participants, what sectors do you see gaining the most and/or having a greater impact on the economy post-COVID-19? Given the difficulties that businesses have experienced, do you think the post-COVID 19 era may see a more favorable regulatory environment that enables and facilitates their recovery? For example, the Superintendency of Industry and Commerce of Colombia, which regulates fair competition and protects consumers, in December 2019

ruled that Uber had violated competition rules; Cornershop, a leading online grocery provider in Chile, Mexico, Peru, Brazil and Colombia, and Uber have been hampered by some antitrust regulators in Latin America; in 2018, the Mexican antitrust regulator did not approve Walmart's acquisition of Cornershop.

Mijares' Response: We believe the pharmaceutical, technology and food sectors will be among the main sectors to benefit in both the COVID-19 and post COVID-19 eras.

As a result of the impact of COVID-19, several governmental authorities (e.g., Federal Telecommunications Institute, Energy Regulatory Commission, the Banking and Securities Commission and the Federal Economic Competition Commission (COFECE)) have temporarily suspended certain procedures and formalities ordinarily required of companies (such as delivering hard copies of documents) as well as timing deadlines in some cases. In the M&A context, COFECE is still substantively involved in resolving antitrust-related matters. Prior clearance by COFECE for transactions that require antitrust approval remains a firm requirement. Overall, we do not expect that COFECE will relax its assessments of the transactions that require such clearance. Other than in the instances mentioned here, we do not see COVID-19 affecting the general stance of the government towards investments in general, either domestic or foreign, or enacting special measures that would benefit companies directly in their recovery.

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6. COVID-19 Impact on Limited Partners

The current circumstances bring into question the likelihood of meeting expectations with respect to fundraising, especially for younger PE funds. Based on discussions to date, we anticipate that funds that lack a strong, established track record with limited partners ("LPs") who are seeking new investments in this environment could face greater challenges as they seek capital commitments from investors who may be less likely to deploy new capital in the first instance whether due to an inability to meet with and diligence the new(er) fund managers, changes in their asset allocations, a general preference to conserve capital at this time or other reasons. The limitations on meeting investors in person due to the travel restrictions and quarantine measures in the U.S. and worldwide may be more manageable for established PE funds given their existing relationships, but the use of Zoom and other video-conference methods is still unlikely to be a suitable substitute in all cases.

With respect to liquidity questions, PE funds may need to weigh their lender relationships and credit facility options against the impact of potential LP capital calls when LPs have their own liquidity considerations. Given the quarantine and work-from-home-restrictions, we anticipate that LPs may need more lead time generally, including for any required capital contributions, and it is reasonable to expect that anything beyond what is contemplated by the existing fund agreements may take longer than is typical.

Relative to the fundraising environment in 2008/09, for new funds being raised at this time, what are the main structural factors and considerations that may limit LPs' interest in committing capital to new ventures? Are you seeing, or do you expect to see, LPs change their allocations to PE as an asset class (whether in the U.S. and/or to funds with a Latin American or other international focus) during this downturn?

Mijares' Response: It is difficult to predict how LPs will react to this downturn; however, once the government-mandated lock-downs are lifted around the world, we do not believe that LPs will decrease their allocations to PE as an asset class. Having said this, the pressure on PE funds to be cautious in their investments in the region will certainly increase, specifically in sectors that were more affected by the pandemic or in countries that have created uncertainty for investors as a result of the erratic measures that have been adopted by their governments in response to COVID-19.

It is likely too soon to tell, but are you concerned about potential LPs defaulting on their current commitments? Based on your discussions with clients, have LPs been increasingly reaching out with capital call funding concerns (even if just prospectively)? Do they expect any pressure on fees typically earned by funds?

Mijares' Response: We agree it is likely too early to tell. At this time, we have not yet heard any capital call funding concerns, either by LPs or PE funds.

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7. *Availability of Debt Financing*

As we have seen to date, PE funds and their portfolio companies have taken various measures to secure debt financing from commercial banks to stabilize cash flows in light of the uncertainty of the current financial climate. In the past and of relevance now, non-bank lenders in the private credit industry have shown more willingness to provide financing, albeit on more expensive terms and likely with more scrutiny from the lending party.

Based on your discussions with clients and contacts in the industry, are they seeing, or do they expect to see, significant liquidity concerns within their portfolio companies? Have you advised portfolio companies to draw down on credit facilities? If so, are they seeing any resistance from their lenders at this stage? Please also comment on the extent to which you anticipate commercial banks taking a more conservative approach to lending during and after the pandemic, as well as the best strategies, including alternative sources of financing, available to PE sponsors and their portfolio companies as they seek alternative cash flows to weather the downturn.

Mijares' Response: Yes, liquidity has been a key concern for many portfolio companies. Fortunately for them, we have not seen any meaningful limitations at this point with respect to their access to either the commercial banking or private lending sector. Many clients have recently drawn on existing credit facilities and/or negotiated new credit facilities with no relevant hurdles or resistance from lenders at this stage. Notwithstanding the above, we have seen commercial banks taking a more conservative approach, including in instances in which the banks had long-standing relationships with the impacted company. This may open the possibility for mezzanine funds or non-bank financial institutions such as "*SOFOMs*" (*Sociedad Financiera de Objeto Múltiple)* to be considered as an alternative source of funding.

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8. ESG Initiatives

Leading up to COVID-19, environmental, social and governance-related ("ESG") initiatives were becoming a strong area of focus for investors as part of the criteria used to assess the long-term quality and sustainability of potential investments. The growing view was that a strong ESG proposition can create long-term value for companies, their employees, stakeholders and ultimately communities. As an example of the various recognitions given acknowledging the value of ESG in recent years, the U.S. Business Roundtable had released a new statement in August 2019 affirming businesses' commitments to ESG. This statement was signed by CEOs of a number of Fortune 100 companies, including a number of companies that have since received significant attention in light of COVID-19, such as Amazon, American Airlines, 3M, Boeing, Marriott, Target and Walmart. Given the public perceptions and expectations of a corporation's role at this time, we would anticipate that ESG commitments will continue to remain highly relevant across all sectors.

In consideration of the current business concerns and priorities around preserving cash flow and stabilizing operations, as well as the social consequences of the disruption caused by COVID-19, to what extent do you anticipate that ESG principles remain relevant in guiding new investment opportunities and management of existing investments at this time?

Mijares' Response: We absolutely believe that ESG principles will remain relevant in guiding new investment opportunities and do not expect the COVID-19 disruption to impact that. This is especially true for companies that are publicly traded or have issued debt in the public markets in response to ESG standards having been increased earlier this year with the Dow Jones sustainability index adopting the RobecoSAM methodology to measure companies. For Mexican pension funds especially, the requirements in their investment regime now include the extent to which a company has complied with ESG standards. Accordingly, companies seeking investments from PE or Mexican pension funds are incorporating ESG principles as part of their day-to-day operations in order to attract these type of investments.

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9. <u>"Key Person" Focus</u>

Even for established funds with close, long-term relationships with their investors, the nature of COVID-19 has been so unprecedented that we are seeing investors focus closely on obtaining the clarity needed and further insights on measures taken by PE sponsors to protect their investments. We have seen significant focus on ensuring that business continuity plans are updated in a manner that takes into consideration the possibility of further operational changes imposed by applicable government requirements and recommendations such that appropriate risk management protocols are in place, including as to key persons whether at the business or involved with any number of a given business's vendors. Given the unpredictability of COVID-19, which has already impacted leaders at the highest levels of government and business (UK Prime Minister Boris Johnson and Morgan Stanley CEO James Gorman being two notable examples), understanding "key person" triggers at the portfolio company level for insurance coverage and/or commercial contracts will be of heightened importance. Similarly, in more extreme cases at the fund level, the "key person" triggers in fund documents may become relevant in the case of extended unavailability (e.g., what constitutes "incapacitation"), including which investor rights may vest upon a "key person event" (such as redemption rights or other protections). In either case, parties may seek to broaden key person clauses going forward to address relevant commercial considerations due to these experiences to date with COVID-19.

As it relates to business continuity, are you seeing, or do you expect to see, additional succession or contingency plans that provide assurances if certain key people are unable to meet their obligations for an extended period of time? At the fund level, what would generally be needed to trigger a "key person event" and what are the rights in favor of the investors should such an event occur? Based on your discussions with clients and contacts in the industry, what are the measures you would advise clients to take regarding how best to prepare for and manage the risk surrounding any key person changes caused by COVID-19?

<u>Mijares' Response</u>: We do expect the COVID-19 pandemic to make people more conscious as to availability and succession plans with respect to their key persons. In our experience, "key person events" are typically triggered when "key persons" die, are disabled or cease to participate in the fund (i.e., where it is clear the person's lack of continuing involvement will be permanent). This usually results in the commitment period being suspended. We would advise LPs to try to broaden the scope of these clauses, to reflect the new reality and concerns brought by COVID-19.

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10. “Material Adverse Effect” and Other Concepts

While the full impact of COVID-19 remains to be seen, it is not surprising that parties are now actively initiating a closer review of material adverse effect (“MAE”) provisions as well as potential issues with pre-closing covenant compliance and closing condition satisfaction for transactions that signed but have not yet closed. Given the disruption to date, buyers may conclude that earlier valuations agreed to pre-COVID-19 need to be revisited. In more severe cases, a buyer may believe that terminating the transaction is the most appropriate path forward, whether on the basis that the target business has suffered an MAE and/or has breached the agreement and is otherwise unable to satisfy its closing conditions. While no quantifiable test exists as to whether an MAE has occurred and courts are generally reluctant to make such a determination, both Delaware and New York law do require that the adverse effects be “durationally significant”. To date, MAE has been invoked successfully only once in Delaware court. In view of the usual practices for defining MAE (which, among other things, generally involve an absence of specific events or dollar thresholds), we see MAE provisions being used as a negotiation tool for buyers who believe that re-negotiation of a deal is appropriate. In the case of COVID-19 in particular, buyers looking to terminate will also need to address common exclusions in the definition of a MAE for industry-wide or “systemic” events such as pandemics, “Acts of God”, changes in law or government actions unless the business was disproportionately impacted. Accordingly, we anticipate that parties, in seeking remedies, will increase their attention on whether closing conditions cannot be satisfied for other reasons, such as in the case where pre-closing interim operating covenants are breached in a manner that would impede closing. Sycamore Partners’ recent termination of its agreement with L Brands, the owner of Victoria’s Secret, is one high-profile example of a decision to terminate based largely on analysis regarding the target’s covenant compliance and ability to satisfy closing conditions.

For existing deals in progress that have been signed but not yet closed, we are seeing an increase in efforts to use material adverse change provisions and other conditions to either unwind or renegotiate transactions. Are you experiencing similar situations with respect to your existing deals, whether on the buy or sell side? What, in your experience, would be the level of change required (and for what duration) in order for a buyer to be well-positioned to prevail on invoking a material adverse change provision? Going forward, do you anticipate any changes to how parties may wish to define MAE in an acquisition agreement as a result of the effects of COVID-19?

Mijares’ Response: Yes. While we have yet to see any buyer invoke an MAE to terminate a transaction as a result of COVID-19, we have seen buyers using that argument to initiate renegotiations of pending transactions. In Mexico, there is currently no judicial precedent with respect to the applicable threshold at which an MAE may occur. However, in light of the principle of will autonomy in Mexico, which establishes that what has been agreed to between the parties must be complied with, it may be advisable for parties to include a monetary threshold in MAE definitions. Ultimately, we expect both buyers and sellers to take a much closer look at the way they define

MAE with COVID-19, but also with pandemics and outbreaks generally in mind. Furthermore, regardless of the MAE clause, we are also now seeing sellers express more concern that force majeure or "Acts of God" may be argued by buyers.

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11. IPO and Exit Prospects

On the eve of the COVID-19 outbreak, market conditions in many regions in Latin America were favorable for PE funds seeking exit opportunities for their most successful investments, with several notable companies planning to launch IPOs or follow-on offerings. As we have seen the pandemic bring on a wave of uncertainty, such exit plans have been put on hold and the extent of the delay and whether other exit opportunities may be pursued are both unclear.

With the outbreak, are you seeing companies delaying or withdrawing their IPO plans or follow-on offerings? Recognizing that this may vary by industry, are companies and investors seeing the IPO window opening back up in the short term and, if so, how do you see the time lag impacting the terms and pricing of offerings? To the extent not, what are the alternatives you are seeing on exit considerations?

Mijares' Response: Unfortunately, we are not seeing the IPOs or follow-on window opening in the short term. We are currently seeing exits involving sales to other PE funds or strategic buyers as the most viable option; however, strong bidding processes have been hampered as a result of the general economic context, and we generally believe PE portfolio exits in the short term will face significant hurdles. As mentioned above, the only sector in which we foresee more frequent transactions in the M&A market at this time is with respect to portfolios of CKDs with the right characteristics to roll over into a different type of long-term investment platform. For example, this could be the case for infrastructure or energy assets that could be contributed, at a reasonable valuation, to a Fibra-E (Mexican MLP) structure.

E. Peru – Rebaza, Alcázar & De Las Casas Q&A

Alberto Rebaza, Felipe Boisset

1. Current Governmental Responses to COVID-19

In response to the shutdown orders in states and counties across the United States that have significantly curbed business activity across sectors in the past two months, the Coronavirus Aid, Relief, and Economic Security (CARES) Act established the Paycheck Protection Program ("PPP") on March 27, 2020, which, among other things, authorized up to an initial $349 billion (with an additional $310 billion of funding added on April 24, 2020) in loans aimed at providing liquidity to eligible small businesses, sole proprietorships, independent contractors and self-employed individuals. Subject to certain restrictions, a loan extended under the PPP will be forgiven to the extent employee and compensation levels are maintained and the proceeds are used within eight weeks after the loan is made for payroll costs and other approved purposes. For businesses seeking to apply, eligibility will depend on whether the applicant qualifies as a small business concern under one of the metrics (e.g., number of employees, total annual receipts) required by the Small Business Administration ("SBA"). The eligibility determination will, subject only to very limited exceptions, involve the application of the SBA's affiliation rules which aggregates the relevant metrics for the applicant and all of its applicable affiliates. As of April 24, 2020, the SBA issued an interim final rule indicating that the portfolio companies of a private equity fund ("PE fund") are not de facto excluded and may still be eligible to receive a PPP loan if they otherwise meet the eligibility criteria.

Are you seeing similar federal/national and/or local government decrees or measures (or a demand for such) that would benefit portfolio companies in terms of providing access to additional capital or other relief measures? Are there conditions applicable to obtaining such benefits (e.g., job protection, limits on size of business (whether measured by revenue and/or employee head count), etc.)? Are you seeing portfolio companies seeking government assistance and, if so, to what extent is it relevant if they are private equity backed?

Rebaza's Response: Yes. The Peruvian government has issued a series of relief measures, most notably the *"Reactiva Perú"* plan (the "Program"), which aims to alleviate the impact of the COVID-19 outbreak on Peruvian businesses and preserve their ability to meet their short and medium-term obligations. The Program relies on a government guarantee of up to 30 billion Peruvian soles (approximately USD $8.8 billion) on the issuance of new loans aimed at providing funds to be used for payroll, working capital and other capital relief purposes to eligible businesses. In order to be eligible for the Program, applicants must, among other things: (i) be free of any enforceable tax debt in excess of approximately USD $1,200; (ii) have an eligible credit score; (iii) not be an affiliate of the financial lender or of any company that pursuant to Law 30737 has either been found guilty of corruption or is currently subject of an anticorruption investigation; and (iv) not distribute profits during the term of

the loan other than pursuant to any existing mandatory profit sharing agreement. Additionally, eligible participants will not be able to use the loans granted under the Program to pay (or prepay) other financial obligations prior to the repayment of the funds provided by the Program.

Apart from the business eligibility conditions, the Program contemplates the following key terms:

- A maximum aggregate principal amount of 10 million Peruvian soles (approximately USD $3 million) for each eligible company.

- The guarantees issued by the Program that secure the loan may range between securing 80-98% of the aggregate principal amount depending on the applicable principal amount. Nevertheless, given the loan coverage cap, the guarantee will only cover an eligible company's loan of up to the lesser of (x) three times the company's annual contribution to *EsSalud* in 2019; and (y) the equivalent of the 2019 average monthly sales of the eligible company as reflected in the Peruvian tax authority's records.

- There is a 36-month term on the loans issued under the Program, including a 12-month grace period on repayment of the principal amount and interest accrued thereon.

In the U.S., the aforementioned SBA affiliation rules have generally limited the availability of access to governmental assistance through the PPP loans for many companies owned or controlled by PE or venture capital funds or alternative asset managers (including, in the case of minority investments, where control is inferred from certain consent rights held by the institutional investor). For your clients with U.S. operations who may be eligible, are you seeing any efforts to unwind or otherwise modify such arrangements so that they can more readily seek government assistance for their U.S. business operations?

Rebaza's Response: To our knowledge, no restrictions of this sort have been imposed to date.

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2. Changes in Deal Dynamics

Prior to COVID-19, we had been facing a predominantly "seller's market" where deal terms had become increasingly favorable to sellers such that it became common that potential buyers, including private equity sponsors, needed to be willing to adopt more flexible positions to be competitive in sale processes. While competition between potential private equity and corporate buyers will remain, we anticipate that the volatility and disruption brought about by COVID-19 should result in a shift toward more buyer or investor favorable terms. We also anticipate that while speed and deal certainty should remain a priority, buyers will take comprehensive

measures with respect to due diligence, particularly as it relates to understanding how a given target business has been altered by the pandemic and whether it is able to mitigate the effects now and in the longer term.

Recognizing that some industries may be impacted more than others, what do you expect with respect to changes in the negotiation leverage scale as well as market trends for PE sponsors as a result of COVID-19? Do you also anticipate that corporate buyers may take a step back in the near term as they focus on preserving their cash flow and operations or otherwise, thus reducing some competition for financial buyers? Given the current economic changes, we believe the current foreign exchange rates are also favorable for foreign PE sponsors to invest in the Latin American region, if you could please comment on this aspect as well.

Rebaza's Response: Corporate buyers are in reality taking a step back and reevaluating investment decisions in order to preserve cash flow. M&A activity in Peru has been brought to a halt as a result of the COVID-19 outbreak, and corporate buyers either have put or are preparing to put their acquisition plans on hold in order to preserve their business operations. Such circumstances could indeed reduce competition for financial buyers, especially in a scenario where the restrictive lockdown measures mandated by the Peruvian government severely impact otherwise healthy businesses, reducing their values to all-time lows and creating particularly advantageous opportunities for PE funds to acquire and participate in such businesses' recovery.

Additionally, the current foreign exchange rate is relatively stable and favorable to foreign PE sponsors, sitting comfortably along the 3.30 – 3.40 Peruvian soles per dollar range.

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3. For Better or Worse: Industries Impacted by COVID-19

Within a short period of time, COVID-19 has caused disruption throughout all industries. On the one hand, the outbreak and the resulting shutdown orders in the U.S. have had a significant negative impact on sectors that are unable to deliver their core services and products, such as the oil and gas, tourism, airline, hotel and entertainment industries. At this time, it remains unclear as to when and to what extent consumer demand will return. On the other hand, the lockdowns and restraints imposed have resulted in unprecedented demand and new opportunities in light of how businesses have leveraged their use of technology (e.g., online retailers, video conferencing services, online learning, home fitness, delivery applications, pet products, etc.).

Are you seeing, or do you expect to see, increased investment and M&A activity involving local sectors or businesses that are benefiting from the COVID-19 outbreak, or that were active before COVID-19 and remain relevant at this time, e.g., the renewable energy sector?

Rebaza's Response: We expect to see an increase in distressed M&A activity in the months after the COVID-19-related restrictive measures are lifted, as it is largely expected that the vast majority of industry sectors will have been moderately or severely impacted by such measures, leaving only a small portion of industry sectors predicted to either benefit or experience only limited impacts as a result of such measures. Many of the most severely impacted industry sectors due to COVID-19 (namely, tourism, entertainment, construction and other labor-intensive producers of non-essential products) represent some of Peru's core industries which comprise a large portion of the country's GDP. As such, it would be natural for businesses in these sectors that are particularly distressed as a result of the circumstances to go through restructuring or distressed M&A processes. With respect to businesses that have remained widely active during the outbreak, while only time will tell, one scenario may involve their participation as potential buyers in this potential post-COVID-19 distressed M&A to further the aim of achieving synergies at severely discounted prices.

Additionally, for most of the past three decades or so, the Peruvian government has been very open to foreign investment in the country. At this time, there is a large percentage of foreign ownership in essential sectors, such as energy and mining, and we do not expect a change in the policy towards foreign investor control and/or ownership of key businesses even with the disruption caused by COVID-19.

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4. Alternative Investment Opportunities

For the industries most heavily impacted, we anticipate this may result in PE funds evaluating alternative opportunities given the limited traditional M&A buyout activity at this time. Similar to the trends observed during the 2008 financial crisis, we have already seen certain PE funds committing to significant investments in public companies in recent weeks with Apollo/Silver Lake's $3.2 billion investment in Expedia and Roark Capital's $200 million investment in the Cheesecake Factory as a few high-profile examples. There has also been discussion around increased opportunities for more carve-out transactions as strategic companies may divest their non-core assets in an effort to preserve liquidity. As the impacts of COVID-19 persist and businesses explore their strategic options, we would also anticipate greater focus on distressed and special situations investments.

To the extent more traditional M&A activity may have slowed, what are some alternative strategies that PE sponsors may be considering (or should consider) at this time (e.g., PIPEs, carve-outs, distressed acquisitions, etc.)?

Rebaza's Response: Transactional Track Record estimates a 58% drop in M&A activity in the Peruvian market in Q1 2020 as compared to Q1 2019. We certainly believe that some alternative strategies will gain momentum as a result of the COVID-19 crisis in an effort to reactivate M&A activity in the following months. In particular, we

believe earn-outs will prove to be key in structuring successful deals where the target company's cash flow and/or capacity to take on leverage have been heavily impacted by the restrictive measures imposed by the Peruvian government. Other key provisions may include (i) carve-outs to indemnity provisions, seeking to limit or exclude certain matters pertaining to the implementation of some of the labor and tax breaks that the government has announced during the lockdown period (especially considering that most of such labor or tax breaks depend on businesses meeting very specific conditions that are yet not entirely clear given the unprecedented nature of these measures, making businesses more prone to inadvertently generating contingencies that may materialize in the future); (ii) bolstered material adverse effect (MAE) provisions to limit or extend their scope (we expect buyers to employ general language and be more reluctant to accept carve-outs on effects originating from unforeseeable force majeure events, for instance, giving them some leeway to walk out of an ongoing deal); (iii) conditions precedent pertaining to the attainability of certain key business health metrics indicative of such businesses' capacity to recover in the aftermath of the COVID-19 crisis; and (iv) a deepened analysis of force majeure provisions to specifically regulate scenarios such as a health crisis.

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5. Post-COVID-19 Economy and Governmental Responses

As governments respond and businesses adapt to the changes caused by COVID-19, we anticipate that the "new normal" will reshape certain sectors, some of which may be particularly well-positioned to thrive to the extent they offer services and/or products that can provide solutions for the changes caused by COVID-19. Such sectors may present new and interesting opportunities but may also further draw additional governmental or regulatory response.

Based on your experience and discussions with market participants, what sectors do you see gaining the most and/or having a greater impact on the economy post-COVID-19? Given the difficulties that businesses have experienced, do you think the post-COVID 19 era may see a more favorable regulatory environment that enables and facilitates their recovery? For example, the Superintendency of Industry and Commerce of Colombia, which regulates fair competition and protects consumers, in December 2019 ruled that Uber had violated competition rules; Cornershop, a leading online grocery provider in Chile, Mexico, Peru, Brazil and Colombia, and Uber have been hampered by some antitrust regulators in Latin America; in 2018, the Mexican antitrust regulator did not approve Walmart's acquisition of Cornershop.

Rebaza's Response: We are already seeing certain sectors, albeit a minority of them, gaining momentum from the COVID-19 crisis and the restrictive measures imposed by the Peruvian government. We fully expect this trend to continue after the peak of the crisis has passed given that the post-COVID-19 era will impose a "new normal" in many different aspects of day-to-day life across all industry sectors, particularly pertaining to social

distancing. Accordingly, we expect the logistics and delivery solutions and fintech sectors to benefit the most in the post-COVID-19 era in a push to promote e-commerce and "contactless" transactions. However, at this point any scenario remains uncertain as different government agencies have made contradictory statements, most notably the latest statements issued by the Ministry of Production and the Ministry of Foreign Trade and Tourism, wherein the latter announced that specific safety guidelines and regulations would be put in place to enable and promote delivery services, while the former declared the unlawfulness of home delivery of goods (even so-called essential items) during the lockdown and condemned businesses engaging in such activities.

With respect to those businesses more negatively affected by the crisis and the restrictive measures imposed by the government, several labor and tax-related regulations (in addition to the Program) have already been put in place to alleviate the impact of those measures in order to enable prompt business recovery, most notably, measures allowing employers to suspend employment of certain employees, defer annual tax return filings and, in connection with the tax deductions system, allow companies to pre-liquidate and withdraw funds reserved for the payment of taxes from their drawdown accounts with Banco de la Nación, amongst others.

Additionally, while new antitrust regulation was expected to come into force in the coming months, this has now been put on hold. This delay is positive and presumably will allow the M&A market to recover without the burden of a lengthy antitrust procedure that may hinder transactions. Prior to this new regulation, Peru only had an *ex ante* antitrust procedure in place for transactions in the energy sector. We believe that introducing a comprehensive antitrust regime, with all of its complexities and the lack of previous experience for M&A buyers and sellers, would hardly be ideal in the current situation, putting virtually all relevant transactions derived from this crisis on unchartered territory.

The following are amongst the most relevant terms of this new antitrust regulation:

- It establishes a new *ex ante* procedure for all business-concentration transactions, whereby INDECOPI's (Peru's antithrust authority) prior approval would be required if: (x) the total sum of the value of domestic sales, during the previous fiscal year, of the companies involved in the transaction, is equal to or greater than 118,000 tax units ("UIT") (approximately USD $ 150 million); or (y) the value of domestic sales, during the previous fiscal year, of at least two of the companies involved in the transaction (where applicable), is equal to or greater than 25,000 UIT (approximately USD $ 30 million) each.
- Consummating transactions that would otherwise be subject to INDECOPI's prior approval can result in a fine to the involved parties ranging from USD $ 600,000 to USD $ 1.3 million approximately.

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6. <u>COVID-19 Impact on Limited Partners</u>

The current circumstances bring into question the likelihood of meeting expectations with respect to fundraising, especially for younger PE funds. Based on discussions to date, we anticipate that funds that lack a strong, established track record with limited partners ("LPs") who are seeking new investments in this environment could face greater challenges as they seek capital commitments from investors who may be less likely to deploy new capital in the first instance whether due to an inability to meet with and diligence the new(er) fund managers, changes in their asset allocations, a general preference to conserve capital at this time or other reasons. The limitations on meeting investors in person due to the travel restrictions and quarantine measures in the U.S. and worldwide may be more manageable for established PE funds given their existing relationships, but the use of Zoom and other video-conference methods is still unlikely to be a suitable substitute in all cases.

With respect to liquidity questions, PE funds may need to weigh their lender relationships and credit facility options against the impact of potential LP capital calls when LPs have their own liquidity considerations. Given the quarantine and work-from-home-restrictions, we anticipate that LPs may need more lead time generally, including for any required capital contributions, and it is reasonable to expect that anything beyond what is contemplated by the existing fund agreements may take longer than is typical.

Relative to the fundraising environment in 2008/09, for new funds being raised at this time, what are the main structural factors and considerations that may limit LPs' interest in committing capital to new ventures? Are you seeing, or do you expect to see, LPs change their allocations to PE as an asset class (whether in the U.S. and/or to funds with a Latin American or other international focus) during this downturn?

<u>Rebaza's Response</u>: We are not aware of any changes in LPs allocations at this time.

It is likely too soon to tell, but are you concerned about potential LPs defaulting on their current commitments? Based on your discussions with clients, have LPs been increasingly reaching out with capital call funding concerns (even if just prospectively)? Do they expect any pressure on fees typically earned by funds?

<u>Rebaza's Response</u>: No such discussions have been held with clients at this time.

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7. Availability of Debt Financing

As we have seen to date, PE funds and their portfolio companies have taken various measures to secure debt financing from commercial banks to stabilize cash flows in light of the uncertainty of the current financial climate. In the past and of relevance now, non-bank lenders in the private credit industry have shown more willingness to provide financing, albeit on more expensive terms and likely with more scrutiny from the lending party.

Based on your discussions with clients and contacts in the industry, are they seeing, or do they expect to see, significant liquidity concerns within their portfolio companies? Have you advised portfolio companies to draw down on credit facilities? If so, are they seeing any resistance from their lenders at this stage? Please also comment on the extent to which you anticipate commercial banks taking a more conservative approach to lending during and after the pandemic, as well as the best strategies, including alternative sources of financing, available to PE sponsors and their portfolio companies as they seek alternative cash flows to weather the downturn.

Rebaza's Response: While we have not yet advised any of our clients facing such circumstances, we do anticipate that portfolio companies will struggle with liquidity, like most other businesses, due to the lockdown. Likewise, we expect banking institutions to take a more conservative approach when issuing new credit facilities and loans in the coming months.

Notwithstanding the foregoing, and given the frail state in which many target companies will be immediately after the COVID-19 crisis, to the extent transactions are pursued, we expect alternative M&A financing options to be explored, in the form of seller's financing schemes and/or earn-out structures, among other options.

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8. ESG Initiatives

Leading up to COVID-19, environmental, social and governance-related ("ESG") initiatives were becoming a strong area of focus for investors as part of the criteria used to assess the long-term quality and sustainability of potential investments. The growing view was that a strong ESG proposition can create long-term value for companies, their employees, stakeholders and ultimately communities. As an example of the various recognitions given acknowledging the value of ESG in recent years, the U.S. Business Roundtable had released a new statement in August 2019 affirming businesses' commitments to ESG. This statement was signed by CEOs of a number of Fortune 100 companies, including a number of companies that have since received significant attention in light of COVID-19, such as Amazon, American Airlines, 3M, Boeing, Marriott, Target and Walmart. Given the public perceptions and expectations of a corporation's role at this time, we would anticipate that ESG commitments will continue to remain highly relevant across all sectors.

In consideration of the current business concerns and priorities around preserving cash flow and stabilizing operations, as well as the social consequences of the disruption caused by COVID-19, to what extent do you anticipate that ESG principles remain relevant in guiding new investment opportunities and management of existing investments at this time?

Rebaza's Response: While the need for companies to prioritize cash flow and operations in the near-term may draw some attention away from compliance with ESG commitments, we believe such commitments will remain relevant in guiding new investment opportunities for investors, especially for foreign investors subject to more scrutinized compliance programs. As such, ESG factors will continue to be a relevant risk metric once the crisis winds down and operations go back to more stable levels.

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9. “Key Person” Focus

Even for established funds with close, long-term relationships with their investors, the nature of COVID-19 has been so unprecedented that we are seeing investors focus closely on obtaining the clarity needed and further insights on measures taken by PE sponsors to protect their investments. We have seen significant focus on ensuring that business continuity plans are updated in a manner that takes into consideration the possibility of further operational changes imposed by applicable government requirements and recommendations such that appropriate risk management protocols are in place, including as to key persons whether at the business or involved with any number of a given business's vendors. Given the unpredictability of COVID-19, which has already impacted leaders at the highest levels of government and business (UK Prime Minister Boris Johnson and Morgan Stanley CEO James Gorman being two notable examples), understanding “key person” triggers at the portfolio company level for insurance coverage and/or commercial contracts will be of heightened importance. Similarly, in more extreme cases at the fund level, the “key person” triggers in fund documents may become relevant in the case of extended unavailability (e.g., what constitutes “incapacitation”), including which investor rights may vest upon a “key person event” (such as redemption rights or other protections). In either case, parties may seek to broaden key person clauses going forward to address relevant commercial considerations due to these experiences to date with COVID-19.

As it relates to business continuity, are you seeing, or do you expect to see, additional succession or contingency plans that provide assurances if certain key people are unable to meet their obligations for an extended period of time? At the fund level, what would generally be needed to trigger a “key person event” and what are the rights in favor of the investors should such an event occur? Based on your discussions with clients and contacts in the industry, what are the measures you would advise clients to

take regarding how best to prepare for and manage the risk surrounding any key person changes caused by COVID-19?

Rebaza's Response: Lately, we have seen a wider inclusion of key person provisions in VC-related (but not private equity) transactions, where the know-how required for the business' success resides with the founders. While absence or incapacity of key persons has typically not been a focal point in the negotiation of such provisions (other than as it relates to departures from the company, death and taking out key person insurance), we anticipate that closer scrutiny of such scenarios while drafting the conditions that must be met in order to trigger a "key person event" will become the new normal.

Notwithstanding the foregoing, we have not yet seen parties invoke any key person provisions during the COVID-19 crisis.

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10. "Material Adverse Effect" and Other Concepts

While the full impact of COVID-19 remains to be seen, it is not surprising that parties are now actively initiating a closer review of material adverse effect ("MAE") provisions as well as potential issues with pre-closing covenant compliance and closing condition satisfaction for transactions that signed but have not yet closed. Given the disruption to date, buyers may conclude that earlier valuations agreed to pre-COVID-19 need to be revisited. In more severe cases, a buyer may believe that terminating the transaction is the most appropriate path forward, whether on the basis that the target business has suffered an MAE and/or has breached the agreement and is otherwise unable to satisfy its closing conditions. While no quantifiable test exists as to whether an MAE has occurred and courts are generally reluctant to make such a determination, both Delaware and New York law do require that the adverse effects be "durationally significant". To date, MAE has been invoked successfully only once in Delaware court. In view of the usual practices for defining MAE (which, among other things, generally involve an absence of specific events or dollar thresholds), we see MAE provisions being used as a negotiation tool for buyers who believe that re-negotiation of a deal is appropriate. In the case of COVID-19 in particular, buyers looking to terminate will also need to address common exclusions in the definition of a MAE for industry-wide or "systemic" events such as pandemics, "Acts of God", changes in law or government actions unless the business was disproportionately impacted. Accordingly, we anticipate that parties, in seeking remedies, will increase their attention on whether closing conditions cannot be satisfied for other reasons, such as in the case where pre-closing interim operating covenants are breached in a manner that would impede closing. Sycamore Partners' recent termination of its agreement with L Brands, the owner of Victoria's Secret, is one high-profile example of a decision to terminate based largely on analysis regarding the target's covenant compliance and ability to satisfy closing conditions.

For existing deals in progress that have been signed but not yet closed, we are seeing an increase in efforts to use material adverse change provisions and other conditions to either unwind or renegotiate transactions. Are you experiencing similar situations with respect to your existing deals, whether on the buy or sell side? What, in your experience, would be the level of change required (and for what duration) in order for a buyer to be well-positioned to prevail on invoking a material adverse change provision? Going forward, do you anticipate any changes to how parties may wish to define MAE in an acquisition agreement as a result of the effects of COVID-19?

Rebaza's Response: As described in Section 2. - *Changes in Deal Dynamics*, certain corporate buyers are taking a step back in their acquisitions. One way we have experienced this trend has been through the active use of MAE provisions in ongoing transactions. As a seller, the analysis of the MAE provisions becomes central to the negotiations in such situations, and on rare occasion the use of MAE provisions has been prevented as a result of specific force majeure carve-outs present in the MAE definition, which is not uncommon in Peruvian transactions. Likewise, MAE provisions customarily included in Peruvian acquisition agreements are commonly triggered by a quantifiable percentage loss in cash flow or sales, making them generally applicable without much expression of cause. However, and as abovementioned, it is just as common for such provisions to exclude force majeure (i.e. a pandemic) and other unforeseeable events from the scope of application of MAE provisions even though sometimes said exceptions will only operate so long as such force majeure event does not remain in place for an extended period of time, in which case it would be deemed a valid MAE.

As we previewed earlier in Section 4. - *Alternative Investment Opportunities*, we anticipate MAE provisions to continue to be central to many negotiations in the coming months, and otherwise standard provisions will surely feature bolstered terms in future acquisition agreements in an effort to mitigate against COVID-19 related circumstances.

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11. IPO and Exit Prospects

On the eve of the COVID-19 outbreak, market conditions in many regions in Latin America were favorable for PE funds seeking exit opportunities for their most successful investments, with several notable companies planning to launch IPOs or follow-on offerings. As we have seen the pandemic bring on a wave of uncertainty, such exit plans have been put on hold and the extent of the delay and whether other exit opportunities may be pursued are both unclear.

With the outbreak, are you seeing companies delaying or withdrawing their IPO plans or follow-on offerings? Recognizing that this may vary by industry, are companies and investors seeing the IPO

window opening back up in the short term and, if so, how do you see the time lag impacting the terms and pricing of offerings? To the extent not, what are the alternatives you are seeing on exit considerations?

Rebaza's Response: IPOs are very uncommon in Peru due to the absence of a significant public market volume, which makes it hard for a company seeking to go public to amass enough investors to fill, and let alone overbook, an entire order book in an offering. Peruvian companies seeking public funding have long since done so through the international stock exchanges, and we do not foresee this changing any time soon.

F. Spain – Pérez-Llorca Q&A

Francisco Iso, Iván Delgado

1. Current Governmental Responses to COVID-19

In response to the shutdown orders in states and counties across the United States that have significantly curbed business activity across sectors in the past two months, the Coronavirus Aid, Relief, and Economic Security (CARES) Act established the Paycheck Protection Program ("PPP") on March 27, 2020, which, among other things, authorized up to an initial $349 billion (with an additional $310 billion of funding added on April 24, 2020) in loans aimed at providing liquidity to eligible small businesses, sole proprietorships, independent contractors and self-employed individuals. Subject to certain restrictions, a loan extended under the PPP will be forgiven to the extent employee and compensation levels are maintained and the proceeds are used within eight weeks after the loan is made for payroll costs and other approved purposes. For businesses seeking to apply, eligibility will depend on whether the applicant qualifies as a small business concern under one of the metrics (e.g., number of employees, total annual receipts) required by the Small Business Administration ("SBA"). The eligibility determination will, subject only to very limited exceptions, involve the application of the SBA's affiliation rules which aggregates the relevant metrics for the applicant and all of its applicable affiliates. As of April 24, 2020, the SBA issued an interim final rule indicating that the portfolio companies of a private equity fund ("PE fund") are not de facto excluded and may still be eligible to receive a PPP loan if they otherwise meet the eligibility criteria.

Are you seeing similar federal/national and/or local government decrees or measures (or a demand for such) that would benefit portfolio companies in terms of providing access to additional capital or other relief measures? Are there conditions applicable to obtaining such benefits (e.g., job protection, limits on size of business (whether measured by revenue and/or employee head count), etc.)? Are you seeing portfolio companies seeking government assistance and, if so, to what extent is it relevant if they are private equity backed?

Pérez-Llorca's Response: As of this date, Spain has approved and is progressively implementing certain urgent and extraordinary measures under Royal Decree Law 8/2020 in order to mitigate the economic and social impact of COVID-19 and support the country's economic activity. Such measures include: (i) a scheme whereby the Spanish government will guarantee up to EUR 100 billion in loans or other types of financing (whether new financings or renewals) extended by regulated financial institutions to companies and self-employed individuals for working capital and general liquidity purposes (such that, unlike the PPP, it is not strictly limited to small businesses); (ii) increasing the net borrowing capacity of the Spanish Official Credit Institute (*Instituto de Crédito Oficial*) in the General State Budget Law by EUR 10 billion, in order to provide additional liquidity to self-employed individuals and companies, especially small and medium size companies ("SMEs"); and (iii) the creation of an

insurance coverage facility of up to EUR 2 billion to be borne by the Spanish Internationalisation Risk Reserve Fund (*Fondo de Reserva de los Riesgos de la Internacionalización*) – not available to publicly listed companies.

Those measures do indeed provide (or indicate that future regulation may provide) eligibility requirements that are aimed at distributing such aid among self-employed individuals, SMEs and larger companies which meet certain requirements (including, among other things: (a) solvency requirements and compliance with certain laws; and (b) that the aid be justified as a financial need resulting from the COVID-19 crisis and not from any pre-existing situation); however, for eligibility purposes, such measures do not distinguish based on whether or not the beneficiaries are private equity-backed companies.

As of this date, the Spanish Council of Ministers has also announced that the Spanish government will offer EUR 40 billion of lines of guarantee in two tranches. The first tranche of EUR 30 billion is intended to secure loans for self-employed individuals and SMEs, and the second tranche of EUR 10 billion is intended for large companies only. Additionally, the scope of this guarantee scheme has been extended to also cover counter-guarantees granted by CERSA (a Spanish public entity providing guarantee coverage to SMEs and self-employed individuals) and promissory notes issued by Spanish companies and listed in the Spanish markets for corporate debt and private fixed income (AIAF or MARF). Additional tranches of this guarantee scheme are expected in the future.

The regulations impose limitations on the aggregate principal amount per borrower that can be secured by such lines of guarantees, which are calculated on a consolidated group basis for each borrower. The maximum percentage of the principal amount of the financings to be guaranteed by this guarantee scheme will be (i) 80% in respect of both new financing transactions or the renewal of existing financial transactions undertaken by the self-employed individuals and SMEs; (ii) 70% of new financing transactions undertaken by large companies; and (iii) 60% of renewals of financing transactions undertaken by large companies. Interest rates will take into account the government guarantee so that they will be lower than the interest rate applied by banks to similar financings prior to the COVID-19 outbreak. The duration of the guarantee will equal the term of the underlying financing commitments, up to a maximum of five years.

We are aware of Spanish portfolio companies that are requesting additional financing under the governmental relief packages described above.

In the U.S., the aforementioned SBA affiliation rules have generally limited the availability of access to governmental assistance through the PPP loans for many companies owned or controlled by PE or venture capital funds or alternative asset managers (including, in the case of minority investments, where control is inferred from certain consent rights held by the institutional investor). For your clients with U.S. operations who may be eligible, are you seeing any efforts to unwind or otherwise modify such

arrangements so that they can more readily seek government assistance for their U.S. business operations?

Pérez-Llorca's Response: To date, not as far as we are concerned.

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2. Changes in Deal Dynamics

Prior to COVID-19, we had been facing a predominantly "seller's market" where deal terms had become increasingly favorable to sellers such that it became common that potential buyers, including private equity sponsors, needed to be willing to adopt more flexible positions to be competitive in sale processes. While competition between potential private equity and corporate buyers will remain, we anticipate that the volatility and disruption brought about by COVID-19 should result in a shift toward more buyer or investor favorable terms. We also anticipate that while speed and deal certainty should remain a priority, buyers will take comprehensive measures with respect to due diligence, particularly as it relates to understanding how a given target business has been altered by the pandemic and whether it is able to mitigate the effects now and in the longer term.

Recognizing that some industries may be impacted more than others, what do you expect with respect to changes in the negotiation leverage scale as well as market trends for PE sponsors as a result of COVID-19? Do you also anticipate that corporate buyers may take a step back in the near term as they focus on preserving their cash flow and operations or otherwise, thus reducing some competition for financial buyers? Given the current economic changes, we believe the current foreign exchange rates are also favorable for foreign PE sponsors to invest in the Latin American region, if you could please comment on this aspect as well.

Pérez-Llorca's Response: The combination of an abrupt market dislocation across different sectors, record amounts of dry powder by PE sponsors, and the historical correlation between PE fund and public market performance, may favor PE sponsors interested in taking advantage of the initial stages of the downturn recovery phase. We anticipate a shift back to more investor favorable terms for such transactions.

By contrast, we expect to see strategic companies more focused on preserving liquidity and cash flows in the effort to stabilize operations, including maintaining employee headcount, a factor that is now subject to increasing social scrutiny.

In contrast with what may develop in certain regions of Latin America, the Eurozone will not be offering favorable foreign exchanges to foreign PE funds (US particularly) because of the coordination between the Federal Reserve and the European Central Bank.

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3. For Better or Worse: Industries Impacted by COVID-19

Within a short period of time, COVID-19 has caused disruption throughout all industries. On the one hand, the outbreak and the resulting shutdown orders in the U.S. have had a significant negative impact on sectors that are unable to deliver their core services and products, such as the oil and gas, tourism, airline, hotel and entertainment industries. At this time, it remains unclear as to when and to what extent consumer demand will return. On the other hand, the lockdowns and restraints imposed have resulted in unprecedented demand and new opportunities in light of how businesses have leveraged their use of technology (e.g., online retailers, video conferencing services, online learning, home fitness, delivery applications, pet products, etc.).

Are you seeing, or do you expect to see, increased investment and M&A activity involving local sectors or businesses that are benefiting from the COVID-19 outbreak, or that were active before COVID-19 and remain relevant at this time, e.g., the renewable energy sector?

Pérez-Llorca's Response: Yes, we expect to see increased M&A activity in the infrastructure (mainly ports and logistics), clean energies, healthcare, pharmaceutical and B2B software sectors (i.e., businesses that are resilient to abrupt changes such as those brought upon by the COVID-19 outbreak).

Other sectors more directly dependent on consumer patterns are being heavily hit by the COVID-19 outbreak.

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4. Alternative Investment Opportunities

For the industries most heavily impacted, we anticipate this may result in PE funds evaluating alternative opportunities given the limited traditional M&A buyout activity at this time. Similar to the trends observed during the 2008 financial crisis, we have already seen certain PE funds committing to significant investments in public companies in recent weeks with Apollo/Silver Lake's $3.2 billion investment in Expedia and Roark Capital's $200 million investment in the Cheesecake Factory as a few high-profile examples. There has also been discussion around increased opportunities for more carve-out transactions as strategic companies may divest their non-core assets in an effort to preserve liquidity. As the impacts of COVID-19 persist and businesses explore their strategic options, we would also anticipate greater focus on distressed and special situations investments.

To the extent more traditional M&A activity may have slowed, what are some alternative strategies that PE sponsors may be considering (or should consider) at this time (e.g., PIPEs, carve-outs, distressed acquisitions, etc.)?

Pérez-Llorca's Response: We should pay attention to carve-outs of non-core divisions of corporate conglomerates focused on preserving liquidity and shoring up the short- and medium-term growth prospects of their core activities. Available cash will offer portfolio companies of PE funds potential opportunities for bolt-ons as well.

We also expect to see higher interest by PE sponsors in PIPEs or in acquisitions of already devalued-debt as a first step to be taken in anticipation of a take-private strategy for the target company. The lower valuations of large publicly listed companies represent a historical opportunity for PE sponsors, which may pursue the traditional activist playbook of getting a toehold interest in a large corporation in order to open discussions for a take-private or, failing such, to rely on a hostile takeover.

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5. Post-COVID-19 Economy and Governmental Responses

As governments respond and businesses adapt to the changes caused by COVID-19, we anticipate that the "new normal" will reshape certain sectors, some of which may be particularly well-positioned to thrive to the extent they offer services and/or products that can provide solutions for the changes caused by COVID-19. Such sectors may present new and interesting opportunities but may also further draw additional governmental or regulatory response.

Based on your experience and discussions with market participants, what sectors do you see gaining the most and/or having a greater impact on the economy post-COVID-19? Given the difficulties that businesses have experienced, do you think the post-COVID 19 era may see a more favorable regulatory environment that enables and facilitates their recovery? For example, the Superintendency of Industry and Commerce of Colombia, which regulates fair competition and protects consumers, in December 2019 ruled that Uber had violated competition rules; Cornershop, a leading online grocery provider in Chile, Mexico, Peru, Brazil and Colombia, and Uber have been hampered by some antitrust regulators in Latin America; in 2018, the Mexican antitrust regulator did not approve Walmart's acquisition of Cornershop.

Pérez-Llorca's Response: As noted above, we expect to see an increase in M&A activity in the infrastructure (mainly ports and logistics), clean energies, healthcare, pharmaceutical and B2B software sectors, (i.e., businesses that are resilient to abrupt changes such as COVID-19 outbreak).

By contrast, however, we are facing a less-friendly regulatory environment with respect to foreign investment in Spain. As a matter of public policy intended to favor the recovery of Spanish companies operating in critical sectors, the Spanish foreign direct investment regime (in force since 1999) has been suspended in respect of a number of sectors and participants. Prior to the suspension, prior authorization was required only for a limited set

of sectors and circumstances (e.g., defense and insurance). Certain previously exempt sectors are now subject to prior governmental authorization as a result of certain transactions, such as in the case of: (i) a non-EU/EFTA investor gaining ownership of 10% or more of a Spanish company's share capital; or (ii) a corporate transaction or act, or legal transaction giving rise to a non-EU/EFTA investor acquiring control or effectively participating in the management of a company. In assessing ownership, the government will consider the investor's ultimate shareholder base. In the case of PE sponsors, the understanding at this time is that the focus will be on the general partner (i.e., as opposed to the limited partners). The suspension has been in effect since mid-March and we expect the Spanish government to issue further guidance in this regard.

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6. <u>COVID-19 Impact on Limited Partners</u>

The current circumstances bring into question the likelihood of meeting expectations with respect to fundraising, especially for younger PE funds. Based on discussions to date, we anticipate that funds that lack a strong, established track record with limited partners ("LPs") who are seeking new investments in this environment could face greater challenges as they seek capital commitments from investors who may be less likely to deploy new capital in the first instance whether due to an inability to meet with and diligence the new(er) fund managers, changes in their asset allocations, a general preference to conserve capital at this time or other reasons. The limitations on meeting investors in person due to the travel restrictions and quarantine measures in the U.S. and worldwide may be more manageable for established PE funds given their existing relationships, but the use of Zoom and other video-conference methods is still unlikely to be a suitable substitute in all cases.

With respect to liquidity questions, PE funds may need to weigh their lender relationships and credit facility options against the impact of potential LP capital calls when LPs have their own liquidity considerations. Given the quarantine and work-from-home-restrictions, we anticipate that LPs may need more lead time generally, including for any required capital contributions, and it is reasonable to expect that anything beyond what is contemplated by the existing fund agreements may take longer than is typical.

Relative to the fundraising environment in 2008/09, for new funds being raised at this time, what are the main structural factors and considerations that may limit LPs' interest in committing capital to new ventures? Are you seeing, or do you expect to see, LPs change their allocations to PE as an asset class (whether in the U.S. and/or to funds with a Latin American or other international focus) during this downturn?

<u>Pérez-Llorca's Response</u>: The bifurcated pattern among PE sponsors that we have been witnessing in the past years will be enhanced in the post-COVID-19 environment. Consolidated PE sponsors with substantial track

records or sector-specific PE sponsors will likely not be affected. By contrast, newly established PE sponsors are likely to be impacted (e.g., pre-seed investments with current lower valuations will make future fundraising difficult) and forced to rely on less standard structures, such as deal-to-deal or co-investment approaches.

The lower valuations of public market equities are likely to cause LPs, such as insurance companies or pension funds, to limit their allocations to PE as an asset clause in order to comply with internal ratios. We expect to see more investments into PE by family offices and sovereign wealth funds.

Lastly, we expect to see increasing interest from insurance companies and pension funds in investing in PE funds focused on Spain, as part of that larger effort of economic recovery of the country.

It is likely too soon to tell, but are you concerned about potential LPs defaulting on their current commitments? Based on your discussions with clients, have LPs been increasingly reaching out with capital call funding concerns (even if just prospectively)? Do they expect any pressure on fees typically earned by funds?

Pérez-Llorca's Response: Yes, we are concerned about potential LPs defaults on their commitments. The lack of exits also does not help in alleviating the liquidity pressures faced by LPs.

We do not expect to see additional COVID-19-related pressure on fees typically earned by PE sponsors. Prior to the outbreak of COVID-19, this was already an area subject to increasing pressure by LPs that such fees be reduced.

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7. Availability of Debt Financing

As we have seen to date, PE funds and their portfolio companies have taken various measures to secure debt financing from commercial banks to stabilize cash flows in light of the uncertainty of the current financial climate. In the past and of relevance now, non-bank lenders in the private credit industry have shown more willingness to provide financing, albeit on more expensive terms and likely with more scrutiny from the lending party.

Based on your discussions with clients and contacts in the industry, are they seeing, or do they expect to see, significant liquidity concerns within their portfolio companies? Have you advised portfolio companies to draw down on credit facilities? If so, are they seeing any resistance from their lenders at this stage? Please also comment on the extent to which you anticipate commercial banks taking a more conservative approach to lending during and after the pandemic, as well as the best strategies, including

alternative sources of financing, available to PE sponsors and their portfolio companies as they seek alternative cash flows to weather the downturn.

Pérez-Llorca's Response: At this time, PE sponsors have been focused on liquidity concerns with their portfolio companies. So far, we have not identified any extraordinary lender resistance to allowing maximum drawdown by portfolio companies of their credit lines, even in respect of companies operating in sectors such as tourism that have been heavily hit by the COVID-19 crisis.

We do not anticipate banks taking a more conservative approach to lending to companies that are financially sound during and after the pandemic, although we see opportunities in two areas: an increase in direct lending activities and also in debt-buy-back transactions by PE sponsors for subsequent recapitalization purposes in view of ultimately entering into new financing with more favorable terms for the portfolio companies.

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8. ESG Initiatives

Leading up to COVID-19, environmental, social and governance-related ("ESG") initiatives were becoming a strong area of focus for investors as part of the criteria used to assess the long-term quality and sustainability of potential investments. The growing view was that a strong ESG proposition can create long-term value for companies, their employees, stakeholders and ultimately communities. As an example of the various recognitions given acknowledging the value of ESG in recent years, the U.S. Business Roundtable had released a new statement in August 2019 affirming businesses' commitments to ESG. This statement was signed by CEOs of a number of Fortune 100 companies, including a number of companies that have since received significant attention in light of COVID-19, such as Amazon, American Airlines, 3M, Boeing, Marriott, Target and Walmart. Given the public perceptions and expectations of a corporation's role at this time, we would anticipate that ESG commitments will continue to remain highly relevant across all sectors.

In consideration of the current business concerns and priorities around preserving cash flow and stabilizing operations, as well as the social consequences of the disruption caused by COVID-19, to what extent do you anticipate that ESG principles remain relevant in guiding new investment opportunities and management of existing investments at this time?

Pérez-Llorca's Response: Yes, absolutely. PE sponsors in the post-COVID-19 world will undoubtedly focus on and favor companies with strong ESG attributes.

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9. <u>“Key Person” Focus</u>

Even for established funds with close, long-term relationships with their investors, the nature of COVID-19 has been so unprecedented that we are seeing investors focus closely on obtaining the clarity needed and further insights on measures taken by PE sponsors to protect their investments. We have seen significant focus on ensuring that business continuity plans are updated in a manner that takes into consideration the possibility of further operational changes imposed by applicable government requirements and recommendations such that appropriate risk management protocols are in place, including as to key persons whether at the business or involved with any number of a given business's vendors. Given the unpredictability of COVID-19, which has already impacted leaders at the highest levels of government and business (UK Prime Minister Boris Johnson and Morgan Stanley CEO James Gorman being two notable examples), understanding “key person” triggers at the portfolio company level for insurance coverage and/or commercial contracts will be of heightened importance. Similarly, in more extreme cases at the fund level, the “key person” triggers in fund documents may become relevant in the case of extended unavailability (e.g., what constitutes “incapacitation”), including which investor rights may vest upon a “key person event” (such as redemption rights or other protections). In either case, parties may seek to broaden key person clauses going forward to address relevant commercial considerations due to these experiences to date with COVID-19.

As it relates to business continuity, are you seeing, or do you expect to see, additional succession or contingency plans that provide assurances if certain key people are unable to meet their obligations for an extended period of time? At the fund level, what would generally be needed to trigger a “key person event” and what are the rights in favor of the investors should such an event occur? Based on your discussions with clients and contacts in the industry, what are the measures you would advise clients to take regarding how best to prepare for and manage the risk surrounding any key person changes caused by COVID-19?

<u>Pérez-Llorca's Response</u>: This question will generally depend on the PE fund. We do not expect to see an increase of succession or contingency plans, particularly in PE sponsors with longer, established track records, although it will ultimately depend on the extent of the unavailability (and circumstances) of the key persons and the rights provided in the fund agreements.

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10. <u>“Material Adverse Effect” and Other Concepts</u>

While the full impact of COVID-19 remains to be seen, it is not surprising that parties are now actively initiating a closer review of material adverse effect (“MAE”) provisions as well as potential issues with pre-closing covenant compliance and closing condition satisfaction for transactions that signed but have not yet closed. Given the disruption to date, buyers may conclude that earlier valuations agreed to pre-COVID-19 need to be revisited. In more severe cases, a buyer may believe that terminating the transaction is the most appropriate path forward, whether on the basis that the target business has suffered an MAE and/or has breached the agreement and is otherwise unable to satisfy its closing conditions. While no quantifiable test exists as to whether an MAE has occurred and courts are generally reluctant to make such a determination, both Delaware and New York law do require that the adverse effects be “durationally significant”. To date, MAE has been invoked successfully only once in Delaware court. In view of the usual practices for defining MAE (which, among other things, generally involve an absence of specific events or dollar thresholds), we see MAE provisions being used as a negotiation tool for buyers who believe that re-negotiation of a deal is appropriate. In the case of COVID-19 in particular, buyers looking to terminate will also need to address common exclusions in the definition of a MAE for industry-wide or “systemic” events such as pandemics, “Acts of God”, changes in law or government actions unless the business was disproportionately impacted. Accordingly, we anticipate that parties, in seeking remedies, will increase their attention on whether closing conditions cannot be satisfied for other reasons, such as in the case where pre-closing interim operating covenants are breached in a manner that would impede closing. Sycamore Partners’ recent termination of its agreement with L Brands, the owner of Victoria’s Secret, is one high-profile example of a decision to terminate based largely on analysis regarding the target’s covenant compliance and ability to satisfy closing conditions.

For existing deals in progress that have been signed but not yet closed, we are seeing an increase in efforts to use material adverse change provisions and other conditions to either unwind or renegotiate transactions. Are you experiencing similar situations with respect to your existing deals, whether on the buy or sell side? What, in your experience, would be the level of change required (and for what duration) in order for a buyer to be well-positioned to prevail on invoking a material adverse change provision? Going forward, do you anticipate any changes to how parties may wish to define MAE in an acquisition agreement as a result of the effects of COVID-19?

<u>Pérez-Llorca’s Response</u>: Yes. In general, buyers are raising questions on the potential termination of agreements as a result of COVID-19 effects, but such arguments are not easy to sustain under Spanish law. The existing Spanish law establishes force majeure provisions both for private contracts and for public procurement contracts that may be applicable under the COVID-19 outbreak. However, the drafting of MAE clauses generally exclude pandemics or situations affecting the Spanish economy as a whole. A specific case-by-case analysis would be required to assess whether an MAE clause applies to the situation caused by the COVID-19 outbreak.

We do not expect to see relevant case law in this regard arising from COVID-19-related MAE clauses until the end of this year, but in the meantime, M&A termination claims in particular sectors such as tourism may offer valuable guidance.

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11. IPO and Exit Prospects

On the eve of the COVID-19 outbreak, market conditions in many regions in Latin America were favorable for PE funds seeking exit opportunities for their most successful investments, with several notable companies planning to launch IPOs or follow-on offerings. As we have seen the pandemic bring on a wave of uncertainty, such exit plans have been put on hold and the extent of the delay and whether other exit opportunities may be pursued are both unclear.

With the outbreak, are you seeing companies delaying or withdrawing their IPO plans or follow-on offerings? Recognizing that this may vary by industry, are companies and investors seeing the IPO window opening back up in the short term and, if so, how do you see the time lag impacting the terms and pricing of offerings? To the extent not, what are the alternatives you are seeing on exit considerations?

Pérez-Llorca's Response: Yes. We are seeing companies delaying or withdrawing their IPO plans or follow-on offerings because of the closure of the public market opportunities due to the COVID-19 outbreak. Although it is too early to tell, some PE sponsors are contemplating other alternatives to achieve their exit given the COVID-19 outbreak, such as disposing of a portion of their equity through minority sales with a combined plan to launch an IPO within 18-24 months for control investments.

LATAM COVID-19 Task Force: Considerations for Private Equity Investors

Willkie has multidisciplinary teams working with clients to address coronavirus-related matters, including, for example, contractual analysis, litigation, restructuring, financing, employee benefits, SEC and other corporate-related matters, and CFTC and bank regulation. Please click here to access our publications addressing issues raised by the coronavirus. For advice regarding the coronavirus, please do not hesitate to reach out to your primary Willkie contacts.

If you have any questions regarding this client alert, please contact the following attorneys or the Willkie attorney with whom you regularly work.

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