

Practical tips to prepare your loss claim resulting from the COVID-19 pandemic

The COVID-19 outbreak is causing uncertainty around the world. Organisations are facing or have faced various challenges in terms of health and safety of employees, infrastructure of working from home, supply chain disruption and liquidity to name a few.

As organisations navigate through this latest crisis it is important to consider mechanisms to recover losses incurred. The legal mechanism may not be clear currently – but what is important to know are the steps to undertake now to support possible future loss claims; and at the same time to prepare for claims anticipated against your organisation.





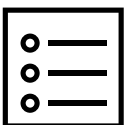
Why you should start collecting evidence of losses sooner rather than later

Organisations are currently suffering losses in connection with the COVID-19 pandemic. Losses could be pursued under various mechanisms including against business partners, under insurance policies or as losses claimed from governments in response to decrees and / or measures or under bilateral investment treaties. The mechanism to be pursued is something that would need to be assessed with legal advisers. Irrespective of the mechanism, the process to quantify the losses is similar – and this is something that should be done sooner rather than later.

From the point of view of mechanisms aimed at compensating for losses, whether actual (*damnum emergens*) or lost profit (*lucrum cessans*), there is generally an obligation of the injured party to prove the losses incurred – specifically, the occurrence and the amount of losses, as well as the causal link

between the loss and the loss event or breach of duty (e.g. what losses were caused as a result of the government measures in the case of a claim against the government). The injured party would also need to prove that it had taken reasonable steps to mitigate the losses incurred and disclose whether these losses have already been fully or partially compensated in other ways.

Whilst cash flow management is currently crucial for organisations to keep running, they should also be preparing for the remediation process in due course. It is important to act now and start collecting evidence in relation to potential losses as later it may be difficult to go back and recreate and capture all of the information retrospectively; plus later on it is possible you may miss documents and information that may have supported your position.



5 Steps To quantify losses effectively

1. Review any contracts that may give rise to a claim for compensation for actual loss or lost profit, or an obligation to reimburse a counterparty. It is also important to examine the terms of the contracts which relate to the current situation and which could lead to a limitation or cancellation of the right to compensation.

2. Identify the documents required to substantiate the loss and the deadlines by which the claim, including the documentation, is to be submitted. If the required information is not entirely clear, communicate it with your insurance company, an insurance broker, or contact a lawyer.

3. Set up internal processes so that the information you need to prove the loss is stored in one place, and you do not have to search for it when you need it. It is better to have more data and documents than less, but all of them should be relevant.

4. If the compensation includes lost profit or consequential type losses, it is appropriate to obtain the services of an expert ahead of time and to discuss with him/her the documents he/she will need to calculate the loss. The necessary supporting documents may vary depending on the calculation method applied, which will be dependent upon the given situation. Consideration will also need to be given to the period that the losses will be incurred and whether permanent losses need to be assessed.

5. Make a request for compensation in a timely manner, within the time limit specified under the applicable contract, policy or regulation, and ensure it is as thorough as possible. This needs to be done in conjunction with your legal advisers.



Tips:

- In addition to evidence about the losses incurred, it is important to clearly document the decisions made by the organisation in reaction to the crisis that were implemented to mitigate any losses including governmental anti-crisis measures.
- Whereas it would be preferred for the claim to be robust, the submission of the application within the deadline is more important, as in many cases it will be possible to supplement the application during the process.
- If you are a multi-country business, it is important to precisely monitor restrictions in all countries in which your organisation is operating, as restrictions impacting them may have different timescales.



Case study – What evidence to collect

A Company operates a luxury hotel and restaurant, which targets mainly foreign affluent clientele. In addition to hotel guests, the hotel restaurant is also open to the public, which accounts for about 50% of sales.

As a result of the extraordinary measures imposed due to the outbreak of COVID-19, the Company has suffered significant financial losses:

1. The hotel was closed until further notice and all booked reservations were cancelled.
2. The restaurant had to close its premises to the public, resulting in a decrease in sales; in addition, the restaurant had to discard or donate part of the inventory which it could not use.
3. In order to mitigate the decrease in sales, the restaurant has begun to offer its customers take-away food.
4. The average spend of customers on take-away food is only around 30% of the pre-crisis level, mainly due to a lack of the hotel clients from abroad.
5. The Company has a contract with its key food supplier that sets a minimum value of goods which it is obligated to purchase each month. If it fails to do so, the supplier has the right to demand the payment of a penalty.

Due to the restriction of business activities, the Company reduced its purchases of goods and services, as well as labour costs, by combining layoffs and forced holidays.

Examples of documents relevant to the case study

Actual losses

- costs of spoiled / expired goods / products that are no longer usable due to limitation / closure of business activities, including proof of disposal / donation;

- cancelled reservations of clients requesting to return deposits, including communication with them and the bank account statements confirming the refunds;
- sanctions from trading partners relating to / caused by the crisis;
- additional costs that would not have been incurred if the crisis had not occurred (increased cleaning requirements, disinfection needs, purchase of protective equipment); and
- documentation of penalties, sanctions, late payment interest including consequences of non-compliance with bank covenants and other financing terms.

Lost profit

- the business and marketing plans of the company and pre- and post-crisis budgets and their changes in relation to the evolution of the situation reflecting expected sales and the number of hotel and restaurant guests during normal operations and during the crisis, including post-crisis prospects; and
- documentation of savings due to limitation / closure of business activities, documentation of the "usual" costs and revenues vs. an overview of actual expenditures and revenues.

Mitigation measures

- documentation of the steps taken to mitigate the effects of the crisis and their evolution as the crisis develops, such as: seeking to reduce wages and other fixed costs, finding alternative suppliers, changing the distribution channels (take-away), changing assortment, negotiating deferrals of contractual obligations and loan repayments, transfer of employees to another job; and
- the impact of the state measures on limiting the losses caused by the crisis.



Checklist



Types of potentially relevant documents

Financial

- Accounting documentation including managerial accounting, financial statements (consolidated as well as for individual divisions), general ledger;
- Business plans, budgets, comparison with the actual figures;
- Financial restructuring and communication with banks;
- Periodic or ad-hoc financial and budgetary reports for management;
- Minutes from management and shareholder meetings;
- Long-term and short-term profit and cash flow plans;
- Information on wages, including supporting documents to identify the impact of the state of emergency;
- Investment plans and programs;
- Break-even point analysis;
- Planned and actual R&D expenditure;

- Key performance indicators (inventory turnover, rate of return on investment, working capital, analysis on ageing of receivables);
- Review of costs drivers and change in cost allocation policies;
- Sales and revenue analysis, profitability studies of individual products;
- Internal audit reports;
- Tax returns.

Marketing

- Long-term and short-term marketing objectives;
- Estimation of the market size and market share per product;
- Sales trends and forecasts, sales budget and sales plans;
- Advertising and promotion plans and budgets;
- Order intake and backlog;
- Order history;
- Records of complaints, returns and lost customer orders;
- Development of new products, analysis of competitiveness of existing products.

Production related

- Production capacity, production plans and schedules;
- Inventory records and obsolescence;
- Work efficiency information;
- Scrap and rework costs;
- Records of orders of production inputs and their fulfilment by suppliers;
- Cost of changing suppliers;
- Maintenance problems and associated costs;
- Quality control reports;
- Purchase budgets;
- Make-or-buy study results;
- Staff turnover, availability / shortage / absenteeism, time sheets, overtime costs;
- Industrial relations reports.

Other

- Invoices, receipts, delivery notes;
- Bank account statements;
- Contracts (including insurance policies), termination of contracts / cancellation of orders, payment notices, instructions, etc.;
- Discounts granted, e.g. for perishable goods;
- Documentation of fines, penalty payments, late payment interest in causal connection with crisis development – including evidence of their payment;
- Internal communication – e.g. emails, newsletters;
- Confirmation from the doctor, decision of the hygiene station;
- Photo-documentation;
- Overview of material seized by the State without adequate compensation.



Tips:

- For periodically prepared documents, such as cash flow reports, save versions for individual periods during the crisis, as well as shortly before and shortly after the crisis. Continue to capture the impact as and when restrictions are lifted and when businesses return to normal – as there may be longer lasting effects.
- Set up cost centres internally so that management can charge / allocate time to dealing with the crisis.
- Empower a person / team to drive the data collection and define data collection rules and procedures. It is of great importance, particularly in the remote working environment.

Please call us if you wish to discuss further.



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