

CORONAVIRUS RESOURCE CENTER

# COVID-19: Practical Considerations in Respect of Russian M&A Transactions

21 April 2020

The spread of the new coronavirus infection COVID-19 (“COVID-19”) in Russia and globally and unprecedented restrictive measures taken by the governments to combat COVID-19 continue to have a significant impact on all aspects of business activity, including mergers and acquisitions (M&A) transactions.

We have issued a client update earlier addressing the general impact of the spread of COVID-19 on Russian contracts.<sup>1</sup> In this client update, we focus on practical tips that are most relevant for signed or potential Russian M&A transactions. You can also find [here](#) a brief client update in English regarding the allocation of the evolving risks of COVID-19 in M&A transactions prepared by our New York office.

On the *Debevoise Coronavirus Resource Center* webpage available [here](#), you will also find regularly updated guidance on various aspects of and situations related to the COVID-19 outbreak in Russia and various foreign jurisdictions, including the United Kingdom<sup>2</sup>, the State of New York and France.

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## Practical Considerations for Signed M&A Transactions

- **Representations, indemnities and pre-completion covenants:** The parties need to consider to what extent the COVID-19 outbreak can affect their compliance with representations, indemnities and pre-completion covenants, primarily, in respect of the target company:

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<sup>1</sup> See our [client update](#) dated 27 March 2020.

<sup>2</sup> You can also find [here](#) our client update in respect of the impact of COVID-19 on English law contracts.

- Generally, compliance with these provisions constitutes a condition precedent, therefore, if those are breached in respect of the target company, the buyer will be able not to proceed with closing or terminate the agreement after the long stop date. For example, one of the seller's representations, compliance with which constitutes a condition precedent, is often that there are no material breaches of key contracts of the target company. However, the restrictive measures that have been imposed may prevent the target company from proper performance of its obligations under such contracts (e.g., under supply agreements) resulting in their breach or termination;
- The seller should consider whether any changes in the operations of the target company require disclosure to the buyer, including in the form of a disclosure letter, to reduce its risks;
- M&A agreements often provide that the seller is not liable for the failure to comply with its representations and certain covenants if such failure is caused by changes in applicable law. The parties should consider whether such carve-outs are applicable to the consequences of the restrictive measures imposed by the authorities;
- As a rule, the buyer has the right to request additional information in respect of the target company between signing and closing and it can exercise such right to have a better understanding of the extent of any negative changes in the company.
- **Conditions precedent:** The parties should consider whether the agreed conditions precedent can still be satisfied in the current circumstances. If the parties intend to proceed with the transaction, they can agree to waive certain conditions precedent or extend the deadline for their satisfaction (long stop date).
- **Communication with third parties and closing logistics:** When planning the closing, the parties should take into account various mandatory or voluntary restrictive measures imposed by the authorities and certain entities:
  - Though the Russian Federal Antimonopoly Service generally continues to consider filings, antimonopoly authorities of various countries (e.g., Austria, the United States, France) have encouraged applicants to postpone filing of any non-urgent applications or advised that their consideration might be delayed;
  - Notaries and registrars continue to provide services, including during the so-called "non-working days" from 4 to 30 April 2020 declared by the Decree of the

President of the Russian Federation.<sup>3</sup> A number of registrars work remotely. As recommended by the Federal Notary Chamber, notary chambers of the constituent entities of the Russian Federation now prepare lists of “notaries on duty” who can perform notarial deeds during this period.<sup>4</sup> However, notarial deeds or registrations may require original documents issued by Russian or foreign authorities (also properly legalised in the latter case), the provision of which may be delayed, including due to potential suspension of apostilling services in various jurisdictions (e.g., in Hong Kong). Certain delays may also take place if the notary whom the parties intended to engage for the performance of notarial deeds is not a “notary on duty”;

- In some instances, a general meeting of shareholders/members of the target company or the parties to the transaction is required for closing of the transaction or in preparation for it. On 18 March 2020, a federal law came into force which permits holding all general shareholders’ meetings of Russian joint stock companies, including those that must take place with the shareholders physically present, in the form of absentee voting in 2020.<sup>5</sup> However, any possible delays with holding such meetings should be considered;
- Russia imposed various restrictions on the operations of organisations and movement of people. E.g., law firms are prohibited from receiving any visitors in Moscow and the movement of people in the city was also significantly restricted.<sup>6</sup>

Given these circumstances, the parties should consider postponing any scheduled transaction closing dates and making relevant amendments to the documentation.

- **Acquisition of shares in Russian public companies:** If the transaction can trigger a mandatory tender offer under Russian law and the transaction closing can fall during the period of “non-working days” imposed by the Decree of the Russian President (including if such period is extended), the parties, especially the buyer, should also monitor the guidance issued by the Bank of Russia regarding this matter:
  - For example, the current position of the Bank of Russia<sup>7</sup> is that the 15-day period for consideration of the mandatory tender offer by the Bank of Russia (upon the

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<sup>3</sup> Decree of the President of the Russian Federation No. 239 on Measures Ensuring the Sanitary and Epidemiological Safety of People in the Russian Federation in Connection with the Spread of the New Coronavirus Infection (COVID-19) dated 2 April 2020 (the “Decree of Russian President”).

<sup>4</sup> For example, the list of the “notaries on duty” of the Moscow Notary Chamber (in Russian) is available [here](#).

<sup>5</sup> We have discussed this novelty provision in detail in our client update of 19 March 2020 available [here](#).

<sup>6</sup> Decree of the Mayor of Moscow No. 44-UM, on Amendment of Decree of the Mayor of Moscow No. 12-UM dated 5 March 2020, dated 18 April 2020.

<sup>7</sup> See press release of the Bank of Russia (in Russian) available [here](#).

expiration of which such mandatory tender offer can be sent to the public joint stock company) will be calculated by the Bank of Russia as usual, taking into account business days, weekends and public holidays, without regard to the regime of non-working days from 4 to 30 April 2020;

- The Bank of Russia also recommends that inquiries be made in respect of whether the target public joint stock company, proposed guarantor bank, appraiser and registrar of such public joint stock company would be available to perform the acts required pursuant to Chapter XI.1 of Federal Law No. 208-FZ on Joint Stock Companies dated 26 December 1995.
- **Possible suspension or termination of the deal:** Consequences of COVID-19 may cause one of the parties to the transaction to lose interest in the performance of such transaction in full or for a certain period of time (for example, the buyer in the event of a material adverse change in the business of the target company). If so, the respective party should consider what options are available to it under the agreement or applicable law to terminate or suspend the transaction, for example:
  - Failure to satisfy conditions precedent which may allow for postponing closing or terminating the deal;
    - In particular, it is sometimes a special condition precedent that there is no material adverse change. Such contractual arrangement is more common for M&A transactions governed by English law and sometimes varies to a significant extent from transaction to transaction. The parties often agree that the definition of material adverse change would not include any general adverse changes in the economy (*i.e.*, those that affect the economy as a whole rather than the target company only), therefore, the COVID-19 outbreak may not fall within the definition of the material adverse change;
    - The material adverse change as a contractual arrangement should be distinguished from the concept of “material change of circumstances” envisaged by Article 451 of the Russian Civil Code. In M&A transactions governed by Russian law, parties often exclude the possibility of terminating their agreement pursuant to Article 451 of the Russian Civil Code; however, if there is no such provision in the agreement, the parties may be able to demand its termination or modification (*e.g.*, price adjustment). In practice, the concept of “material change of circumstances” is one of the most difficult to rely upon due to the high standards of proof and court practice;<sup>8</sup>

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<sup>8</sup> See our [client update](#) dated 27 March 2020.

- Force majeure – force majeure provisions are not commonly included in M&A transaction documentation. However, in M&A transactions governed by Russian law, it is important to check whether the parties excluded the application of the force majeure provisions because, if not, those can apply by virtue of Article 401(3) of the Russian Civil Code. Importantly, the recognition of the onset of force majeure due to the COVID-19 outbreak<sup>9</sup> by the governmental bodies does not, by itself, release the parties from the proper performance of their obligations or liability for the failure to perform or to duly perform their obligations. The parties need to consider the impact of force majeure on their ability to perform their obligations: *e.g.*, the buyer's obligation to pay the purchase price can be performed as long as the banks are open for operation, *i.e.*, essentially, it is not affected by force majeure, unlike non-monetary obligations of the buyer (*e.g.*, to open an account with a depository, to provide extensive documentation in the proper form at closing, to make antimonopoly filings by a certain date, etc.);
- Suspension of reciprocal performance of obligations – the parties to the contracts governed by Russian law should review their documentation for any reciprocal obligations (*i.e.*, those conditional upon the performance of the obligations by the other party). Subject to the particular factual circumstances, a party may suspend or repudiate the performance of an obligation which is not affected by a force majeure event (*e.g.*, a monetary obligation) but is reciprocal in relation to the obligation so affected by such a force majeure event;
- Other special grounds for termination provided by contract or applicable law.

In any event, the party intending to terminate the contract must avoid unreasonable delays in making such decision or otherwise perform any acts that may be construed as its intention to proceed with the deal. Otherwise, the right to terminate may be forfeited. For example, as regards transactions governed by Russian law, Articles 450.1(4) and (5) of the Russian Civil Code provide that the party entitled to terminate a contract must act reasonably and in good faith in exercising such right and may not terminate a contract if it has affirmed the effect of such contract, including by accepting the performance of obligations by the other party.

To reduce the risk of disputes arising out of the termination of the deal and properly address its consequences, the parties may consider signing a separate termination agreement.

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<sup>9</sup> See, *e.g.*, Article 20.1 of Decree of the Mayor of Moscow No. 44-UM, on Amendment of Decree of the Mayor of Moscow No. 12-UM dated 5 March 2020, dated 18 April 2020.

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## Practical Tips for Potential M&A Transactions

- **Due diligence:** In addition to standard legal due diligence exercise, the buyer should separately evaluate the risks related to the COVID-19 outbreak, including the risks of the failure to perform or termination of key agreements of the target company, insurance coverage, whether the target business can be effectively carried on subject to disease prevention and control orders and restrictive measures, etc.
- **Issues related to evaluation of the business and shares/interests:** The COVID-19 outbreak has significantly impacted the value of companies and volatility of capital markets. These factors should be borne in mind by the parties when negotiating transaction terms, specifically:
  - The price adjustment may require rethinking in light of the changes in the business of the target company. The price adjustment using the “*completion accounts*” mechanism (*i.e.*, price adjustment based on the financial position of the target company at closing) may become even more attractive for the buyer as it permits it to assess the company’s standing as of the closing date rather than as of the most recent reporting date (“locked box” mechanism) which may not reflect all adverse consequences of COVID-19 for the business. The “locked box” mechanism, in its turn, secures the receipt by the seller of the purchase price for the target company without regard to the impact of COVID-19;
  - If the transaction can trigger a mandatory tender offer by the buyer or shareholders’ right to claim statutory redemption of their shares, the buyer should keep in mind that the price for the shares of a public joint stock company for these purposes cannot be lower than a six-month volume weighted average market price. This may result in a higher price compared to the current price levels.
  - The correct period and date for the valuation of shares/participation interests in limited liability companies will also be of importance for swap deals and other transactions where shares/participation interests are intended as the means of payment.
- **Moratorium on bankruptcy**<sup>10</sup>: On 6 April 2020, the Russian government imposed a six-month moratorium on commencement of bankruptcy proceedings by creditors

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<sup>10</sup> On 1 April 2020, amendments to Federal Law No. 127-FZ on Insolvency (Bankruptcy) dated 26 October 2002 (the “Bankruptcy Law”) came into force. New Article 9.1 was added to the Bankruptcy Law which permits the Russian government to impose a moratorium in certain circumstances on commencement of bankruptcy proceedings by creditors and to determine its duration.

in respect of a wide variety of debtors, including debtors in the sectors most affected by the spread of COVID-19 and core business entities of the Russian economy.<sup>11</sup> Consequences of the moratorium for such debtors include, among other things:

- If bankruptcy proceedings are commenced in respect of a debtor during a three-month period after the cessation of the moratorium, many transactions consummated by it for the transfer of assets or assumption of obligations or duties during the moratorium will be deemed void.<sup>12</sup> All M&A transactions of such debtor will most likely fall into this category;
- Discharge of the debtor's monetary obligations by way of set-off are not allowed;
- No late payment/default and other financial penalties will accrue for the failure to perform or to duly perform its monetary obligations by the debtor.

Given the wide range of debtors subject to the moratorium and potential financial problems faced by the companies at present, the above risks should be taken into account in respect of both the target company (during due diligence) and the respective party to the M&A transaction.

- **Termination of negotiations:** If a party decides to withdraw from negotiations that may be subject to Russian law, such party should avoid behaviour that may be deemed to be bad faith conduct of negotiations.<sup>13</sup> In particular, it should avoid continuing negotiations without the intention to contract and should inform the other party as early as practicable about the termination of negotiations providing reasons, etc.
- **Allocation of adverse consequences between the parties:** The parties should also consider allocating any adverse consequences of the COVID-19 outbreak between the buyer and the seller, including by way of indemnity, *i.e.*, by providing in the transaction documents which losses caused by the spread of COVID-19 should be indemnified by the buyer to the seller and vice versa. As one of potential ways to allocate such risk, the buyer may be entitled to exit the transaction in the event of

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<sup>11</sup> The most affected sectors include air transport, hotel business, catering, etc. These measures also apply to entities included in the list of (i) core business entities; (ii) strategic enterprises and strategic joint stock companies; (iii) strategic institutions and federal executive bodies providing for the implementation of the national government policy in industries where such entities operate (see Resolution of the Government of the Russian Federation No. 428 dated 3 April 2020).

<sup>12</sup> Article 9.1(4) of the Bankruptcy Law. As of the date of this client update, the Federation Council of the Federal Assembly of the Russian Federation passed a Bill abolishing this provision.

<sup>13</sup> Article 434.1 of the Russian Civil Code.

further deterioration of the situation caused by the COVID-19 outbreak, but subject to the payment of a break-up fee to the seller.

- **Other recommendations:** When drafting M&A transaction documentation, the actual impact of COVID-19 and new legal regulations adopted to combat COVID-19 should also be taken into consideration, for example:
  - Timing provisions should be drafted taking into account the new concept of “non-working days” introduced by the Decree of the Russian President because the legal status of such “non-working days” under the applicable law is still unclear. Given that many companies continue their operations during such “non-working days”, the parties may provide that those are deemed to be business days;
  - When drafting representations, conditions precedent and termination triggers, the parties should consider whether appropriate carve-outs and limitations of liability are required which may be worded in either broad (as including any consequences of COVID-19 and any other pandemics not known yet) or narrow terms (as applicable to already known adverse effects only). In addition, the seller should consider incorporating special carve-outs in the pre-completion covenants to be able to take actions outside the ordinary course of business if required for urgent response to the COVID-19 outbreak.

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For more information regarding the coronavirus, please visit our [Coronavirus Resource Center](#).

Please do not hesitate to contact us with any questions.



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