

B2B: M&A Trends in Russia

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Using Russian law as governing law for M&A transactions as a recent trend in M&A activity has been discussed widely in the context of the state's proclaimed policy to this effect. This trend could have been set in motion in the context of the government's de-offshorization policy, in conjunction with plans to privatize state-owned assets. The prospective privatization plan includes quite a long list of major companies that will be sold entirely or see the state's stake reduced. The privatization methods will be set individually for each of the companies.

Moreover, assets being transferred by Russian public officials to the Russian state may also play a role in resolving the tension between English law and Russian law in governing M&A transactions, and in strengthening the trend of opting for Russian law.

However, it is another widely discussed factor that may prove decisive in turning the balance to Russian law: the reform of Russia's Civil Code. Among other things, the new amendments introduce some concepts that are well known in terms of English law.

English law is traditionally chosen for major transactions, whereas Russian law prevails in transactions by medium-sized business where Russian business is reluctant to deal with the large volume of documents used under English law. Another complication is the need to resolve disputes abroad.

Nevertheless, it is doubtful whether a strong trend to enter into M&A deals under Russian law will develop in the near future. The amendments may reinforce the tendency to choose Russian law in medium-sized transactions but will hardly create a preference for Russian law in major transactions.

First of all, cautious players will be waiting for the courts' view on how the suggested

mechanics are used. But more importantly, the suggested amendments have been criticized because of potential problems with their implementation.

An English-law
transaction
allows
the purchaser
to claim
damages from a
breach
of warranties,
while
a Russian-law
deal does not.

For example, a purchaser under an English-law transaction may claim damages incurred as a result of a breach of warranties given by the seller or misrepresentation, or may claim an indemnity; if the agreement is governed by Russian law, these mechanisms are not usually available. The draft amendments to the Russian legislation attempt to transfer the above concepts into Russia's legal framework. For example, the amendments provide for representations as to facts, although the concept may not be regarded as mirroring a representation under English law. Under the amendments, for a seller to be liable: a representation must be given in relation to a fact that is important for execution and performance of the agreement, a purchaser must rely on the representation and a seller must believe or have reasonable grounds to believe that a purchaser relied on it. In other words, it is not sufficient merely to include a representation in the agreement. The current amendments do not clarify whether the purchaser's knowledge that a representation is untrue will influence its ability to sue the seller. There is also no obligation to stipulate representations in the agreement.

The amendments also introduce a concept that is closest to the idea of an indemnity under English law. However, the wording of the amendment gives rise to certain questions. Among other things, it follows from the suggested amendment that unless the contract provides for the amount of the indemnity to be paid such amount must be determined according to the mechanism for compensating damages. Under English law, an indemnity is a promise by one party to the other to hold that other party harmless against a particular cost or liability, which means that an indemnity is in essence a separate obligation. There being no obligation on the purchaser to prove damages gives a high level of comfort to the purchaser claiming the indemnity. The current amendments contrast with this, referring to damages and thus potentially nullifying the effect of the entire amendment. The current amendments also do not allow any third party to give an indemnity, whereas in English-law-governed transactions, an indemnity may be given by a group company of the seller.

The amendments to Russian civil legislation may represent the start of a move towards the use of Russian law. However, for this to gather momentum, not only do the amendments need to be refined, there must also be increased trust in Russia's judicial system.

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