

Cbonds Russian M&A Congress

Dispute Resolution for M&A Deals – what
difference does the new arbitration law
reform make?

Doran Doeh

30 November, 2016

Dispute Resolution clauses for M&A deals need careful consideration – don't leave it till midnight!

- Each side needs to think about how a dispute might arise, what risks are involved and what approach is likely to be best for it in practice – and then reach agreement with the other side. Going into a deal, no one wants to envisage that it might go wrong – so this aspect tends to receive little attention during the negotiations.
- Just using the same provision as last time might not be the right answer, particularly as the law has changed.

The problem explained

There are essentially two alternatives for dispute resolution for most transactions, including M&A

- Courts
- Arbitration

neither of which is unproblematic for M&A transactions relating to Russian companies.

What recourse is each side likely to need?

Seller – payment of the price where the sale is 100%

- Simultaneous signature of purchase agreement (SPA) and completion of sale are rare in Russia
- Simultaneous delivery versus payment can be problematic or expensive, or both
- Deferred consideration? Earn-out? Other terms?

Buyer – delivery of title, recourse if the target company, its business or assets turn out not to be as expected

- DvP also an issue for buyer
- Representations and warranties
- Deferred consideration? Other terms?

What recourse is each side likely to need?

The situation is much more complicated where the sale is of less than 100%, as that there will be an ongoing relationship in what is effectively a form of joint venture

- Shareholders/Corporate Agreement (SHA)
- Charter

In the past, an offshore holding structure was the solution in many cases – this is less possible now, and changes in Russian law have made onshore structuring through an SHA between the shareholders more practical.

Simple solution – Russian arbitrazh courts (assuming Russian governing law for SPA and SHA)

Pros

- Relatively fast
- Low cost
- Readily enforceable in Russia
- Often recommended for small/medium claims
- OK for big but not complex claims?

Cons

- Courts overloaded with claims
- Other side of speed – judge's time is limited
- Judges may not have appropriate commercial expertise
- Approach to evidence – oral testimony and cross-examination rare
- Possible impact of extraneous factors
- International enforceability depends on treaty or reliance on comity of nations

Not so simple solution – foreign court

May be

- Slower, usually
- Often more expensive – possibly much more
- Depending on country, some cons of Russian courts may also apply
- Need to choose appropriate governing law
- Judgment may not be enforceable in Russia – treaty or comity of nations – same problem in reverse

Arbitration – domestic or international - often preferred in Russia for business disputes

Pros and cons

- **Speed**
 - Can be very quick if both sides cooperate – but less so if one side is actively obstructive
 - No appeal on merits – can be two-edged for the loser
 - May still need to go to court for enforcement including interim measures
- **Expertise and neutrality**
 - Parties can select arbitrator(s) – 1 or 3 - may choose someone with particular competence or experience, include non-legal, and language capability
 - Criteria for neutrality of arbitrators can be specified
- **Confidentiality**
 - Confidential information of the parties
 - Confidentiality of the arbitration and the award

Arbitration – often preferred in Russia for business disputes but problematic for M&A

- **Costs**

- Can be cost-efficient where the parties are cooperative in achieving this – keeping processes simple and speedy, avoiding unnecessary steps
- But can also be very expensive, sometimes more so than litigation in the courts, not least because the arbitrator(s) need(s) to be paid

- **Enforceability**

- Awards internationally enforceable under New York Convention – Russian awards enforceable in other member states, foreign awards enforceable in Russia
- **BUT** Russian courts developed a policy that “corporate disputes” (title to shares, corporate governance and other issues) are within the exclusive jurisdiction of the Russian courts, i.e. **non-arbitrable** - *NLMK v Nikolay Maximov* (key dispute initiated in 2011, decisions in 2012 and following years) – applies to SPAs and SHAs, including purely private ones to which the company is not a party, and applies to claims for damages under representations and warranties

How does the new arbitration regime improve the situation?

With effect from February 2017, corporate disputes are arbitrable provided

- Russia is the seat of the arbitration (i.e. Russian arbitration laws apply to the process)
- The arbitration is supervised by a licensed arbitration institution - either one of the two established institutions named in the legislation or has been licensed by the Ministry of Justice and has special approved rules for corporate disputes, which should help to organize multi-party disputes – German approach is model
- Recognized foreign institutions can apply

How does the new arbitration regime improve the situation – and what are the drawbacks?

- Arbitration of disputes can be written into the company's charter
- But there are limits, e.g.
 - Does not apply to disputes relating to the calling of a general meeting
 - Does not apply to ownership of stocks or shares in strategic entities
 - Does not apply to public joint stock companies or companies with over 1000 shareholders
- Technicalities on establishment of arbitral institutions may limit availability of arbitrators of the kind which commercial parties really want to use for their disputes – not yet clear how this will work
- Foreign-seated arbitral awards in corporate disputes may not be enforceable in Russia – treated as *ad hoc*

Dilemmas

- Russian courts?
- Russian arbitration? If so, which institution?
- International arbitration?

Consult your lawyers and consider their advice carefully

Thank you for your attention!

Doran Doeh
Dentons – Moscow
doran.doeh@dentons.com
+7 495 644 0500