COVID-19 PRESSURE POINTS: INFRASTRUCTURE AND PPP (RUSSIA)

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Legal Briefings – By **Olga Revzina, Roman Churakov, Grigory Smirnov, Yana Ivanova, Lola Shamirzayeva and Olga Polkovnikova**

The spread of COVID-19 and the restrictive measures taken by the state to curb it is undoubtedly making a heavy impact on the economy, including the infrastructure and public private partnership (PPP) market. In this bulletin, we have analysed the key legal implications of the above circumstances for infrastructure projects and have summarised some of the steps taken by the state to mitigate the consequences of COVID-19.

Subject to the parameters and special aspects of a particular project, COVID-19 and the relevant restrictive measures may qualify as a force majeure event, adverse change of law, special event, grounds for termination of the respective obligations in accordance with Articles 416 and 417 of the Russian Civil Code, grounds for amendment or termination of the agreement by the decision of the court as a result of a "material change of circumstances" further to Article 451 of the Russian Civil Code. Nonetheless, the coronavirus does not afford ground for non-payment by the concession grantor (public partner) under a concession agreement (PPP agreement) or the concessionaire (private partner) under a facility agreement or other financial instruments. In this bulletin, when we hereafter say "concession agreement", "concessionaire" and "concession grantor" we also imply "PPP agreement", "private partner" and "public partner", respectively.

Among the state measures aimed at supporting the infrastructure market there are, *inter alia*, the prolongation of the term of certain licences and authorisations, right of a tenant to demand a reduction of the rental charges, possibility for the parties to a state contract to amend the term or the price of such contract in 2020 in case it has become impossible to perform the contract due to COVID-19, and the simplified procedure for entering into contracts whose subject matter comprises design and construction works of a capital construction facility.

KEY IMPLICATIONS OF COVID-19 AND MEASURES UNDERTAKEN BY THE STATE FOR THE INFRASTRUCTURE PROJECTS

- The prospects of performance of concession agreements (the "**CA(s)**") depend on the acts of the authorities in the constituent entities of the Russian Federation. Notwithstanding the strict lockdown in place in most of the Russian Federation, generally, the operations in the construction sector are not suspended. Similarly, the "organisations which cannot suspend their operations due to the production and technical conditions" carry on with their work. Housing and public utilities sector organisations would be, in almost all cases, among such enterprises (which opens up a window of opportunity for carrying on with performance under the CAs in this sector). In some regions, such as the Republic of Bashkortostan, the list of the running enterprises is made by reference to both the "authorised" sectors (e.g., housing and utilities), and to the particular companies authorised to continue operations. You would need to confirm the legal mode of operations in the context of the pandemic in your region specifically.

- COVID-19 might be considered as a force majeure event. Such qualification has been given by the public agencies in relation to the state procurement and has been confirmed by the Mayor of Moscow in relation to the obligations due for performance in Moscow. At the moment of publication, 44 constituent entities of the Russian Federation have acknowledged COVID-19 as a force majeure event. Even if there are still no current practices established throughout all of Russia, it should be assumed that in regions with the strict lockdown imposed and/or operations of the organisations suspended and/or certain operations banned, the court would confirm the fact of the force majeure event in relation to the relevant organisation directly affected by such event. It should be emphasised that in most CAs, epidemics are listed among force majeure events, which should make proving easier. On the other hand, to this day there is still no clarity as to how the courts would react to: (a) a lack of funds and/or goods needed to perform an obligation, to the extent the operations of the enterprise are not prohibited, (b) non-working days introduced in late March to continue in April, (c) the economic crisis (hopefully, short-lived), which is to follow the pandemic. If history could be of any guidance on this point, looking back to 1998 and 2008 we note that the courts did not see crisis as a force majeure event. There are good reasons to believe that the courts might take a similar stance on the point of COVID-19. In addition, it should be noted that the civil laws proceed on the premise that a lack of funds or goods available on the market does not represent grounds for release from liability. Nevertheless, there is already a case pending before a court, where the debtor alleges that COVID-19 is a force majeure event and seeks a court order on deferral of the obligations discharge. Given that now the proceedings in courts have been basically put to a halt, pending termination of the emergency measures undertaken by the state, there is no way of establishing how the proceedings in that case would end. Finally, it is important to take into account the fact that, to be granted a release from liability as a result of the force majeure event, the party affected by such force majeure would need to show the interrelation between the default under the obligation and such force majeure.

- The restrictive measures implemented by the state might be deemed as an adverse change of law, and as such:

    - might trigger the provision of part 1 Art. 20 of Federal Law No. 115-FZ dated 21 July 2005 “On concession agreements” (the “**Concession Agreements Law**”) (and, equally, the relevant provision in Federal Law No. 224-FZ dated 13 July 2015 “On public private partnership, municipal private partnership in the Russian Federation and on making amendments to certain enactments of the Russian Federation” (the “**PPP Law**”)), whereby, should a regulation issued by the Russian Federation, a constituent entity of the Russian Federation or a municipality result in worsening of the concessionaire's condition, such that it substantially loses what it would have been entitled to in the event of the CA execution, the grantor shall undertake steps aimed at procuring the return on concessionaire’s investments and ensuring gross revenues yield for the concessionaire, namely, increase the grantor's fee, extend the period of the CA, increase the amount of the capital grant, and ensure provision of additional state-backed or municipality-backed guarantees to the concessionaire. Meanwhile, it should be borne in mind that a change of material terms of the CAs in regional and municipal concessions would require a consent from the Federal Antimonopoly Service (FAS). Further, the parties may envisage a different operating procedure in the CA in the event of change of law, and in such case, it is likely that the above rule of law might not be fully available (in accordance with the law, the “procedure for undertaking such steps and making relevant amendments is to be set forth by the CA”);

    - might qualify as a special event. In this context, the practice of structuring the change of law as a special event would be different, subject to the specific concession project. In some concessions, there is no such event whatsoever, in others only a discriminatory change of law would be recognised as such (e.g., applicable to one specific company only, or to concessionaires working in the project-specific sector), yet in others any negative change of law is deemed as such. In any event, the concessionaire would still need to prove the interrelation between the change of law and losses (frustration of the CA to the extent of performance when due), and the fact of exceeding the threshold (cap) of losses oftentimes set forth in the text of the CA. The concessionaire would be in a position to claim reimbursement of extra costs and/or extension of the period for performance of obligations only once all the relevant steps have been exhausted;

    - might qualify as grounds for full or partial termination of the obligations by virtue of Article 417 of the Russian Civil Code. Most of the obligations of the concessionaire,

by their nature, are continuing and cannot be terminated. For instance, such obligations might include regular reports to be provided by an independent engineer – if the engineer cannot get to the construction site during the period of quarantine, the obligation to provide the report might be terminated, and the next report would have to be submitted following the next reporting period only. We recommend reviewing the list of obligations carefully and identifying which of the obligations might be terminated as a result of the restrictive measures put in place by the state.

- In addition, the pandemic might be grounds for amendment or termination of the agreement by the decision of the court, if the latter holds it as a “material change of circumstances”. You will recall that a change is recognised as material if a party to the agreement proves that, should the parties have been able to reasonably anticipate it, they would not have entered into the agreement in the first place, or would have executed such agreement on substantially different terms and conditions. For now, relevant qualification remains a possibility admitted by the expert community only and has not yet been tested in courts. In any event, it should be kept in mind that the civil laws are based on the premise of priority granted to the termination of the agreement over an amendment thereof, and on the premise that amendment would only be allowed where termination is not appropriate.

- COVID-19 is no ground for non-payment under a facility agreement and other financial instruments. In this regard, the recommendations of the Central Bank of Russia to the banks are as follows:

    - when score-based models are used for identifying a default, to disregard the events occurring during the period of high-alert regime enactment. This does not mean that non-payments are excluded from the events of default during the period of the pandemic outbreak, but merely suggests that, if the facility is restructured during such period, the credit reference agencies and other banks are advised against using it as grounds for worsening the credit prospects for the borrower;

    - not to worsen the debt service quality and financial standing of the borrowers from the transportation sector and a number of other economy sectors for purposes of creating provisions for losses. This relief provides a greater comfort for the banks in dealing with bad debts and serves as an incentive to refrain from declaring a default.

- COVID-19 might be qualified as grounds for termination of the obligations in accordance

with Article 416 of the Russian Civil Code as a result of frustration thereof resulting from an event beyond the control of any of the parties. These grounds could be efficiently used, for instance, when the project is at the very initial stage, and, against the backdrop of the quarantine, its further implementation is no longer commercially viable.

SOME OTHER ASPECTS OF THE PUBLIC POLICY PERTAINING TO COVID-19

- The “anti-crisis” Federal Law No. 98-FZ “On making amendments to certain enactments of the Russian Federation on matters of emergency prevention and recovery”, which took effect on 1 April 2020, stipulates a right of any tenants to demand a reduction of the rental charges from the real estate landlords if such real estate cannot be used due to the high-alert regime's enactment. At the same time, the procedure for exercising such right and the reduction ratio for the rental charges are not specified. Nevertheless, in its Decree No. 439 dated 3 April 2020, the Government treats such reduction as a recommendation only. We believe that the tenants are entitled to claim reduction of charges, including through court, in reliance upon the legal effect of the law prevailing over the act of the Government.

- Pursuant to Federal Law No. 223-FZ dated 18 July 2011 "On procurement of goods, works and services by certain categories of legal entities” (the “**Procurement Law**”), the customers are entitled to cancel procurement at any time before the execution of the contract with reference to COVID-19.

- For organisations engaged in PPP facilities construction we note that, if necessary, goods may be imported from abroad through goods haulage vehicles not otherwise precluded from cross-border movements.

- A 12-month extension is granted for the effective period of:

    - subsoil licences (pertinent for construction of underground structures, including tunnels) and a number of medical permits and authorisations (a licence for production of and dealings in ethanol, state registration of drugs/medicines);

    - construction permits and a number of town-planning documents necessary for construction to be carried out.

- Power receipt in the course of technological utilities connection and in the course of heat

supply facilities technological connection is allowed without the authorisation from Rostechnadzor (Federal Service for Environmental, Technical and Nuclear Supervision).

- A possibility of procurement without tender (from a single supplier) is envisaged in respect of any goods, works and services for healthcare delivery in an emergency or first-aid time-critical situation as a result of force majeure events, and further as a result of high-alert regime enactment for prevention of any emergencies. Requirements for pre-selection and request for fee proposals (quotes) in the course of procurement from a single supplier for the emergency response have been cancelled.

- The timeline for state procurement is not extended, given that under Governmental Decree No. 443 dated 3 April 2020 the periods to be calculated in business days are to be calculated in calendar days. However, the Procurement Law now leaves a possibility for the parties to change the contract performance period or its price in 2020 to the extent, in the context of performance thereunder, any events beyond the control of the parties have occurred due to COVID-19 outbreak giving rise to a frustration of the contract.

- The procedure for execution of contracts whose subject matter comprises both design and construction works of a capital construction facility has been adjusted:

    - the condition of implementation of a national project, as grounds for approval of lists of relevant capital construction facilities by the authorised bodies (which now include local administrations too), has been withdrawn;

    - alongside procurement of engineering survey works and construction and mounting works, supply of any equipment (rather than medical equipment only, as before the amendments) is now possible.

- On 27 March 2020, the Russian Federation Chamber of Commerce and Industry circulated a letter on matters of force majeure confirmations stipulating, without limitation, the following:

- opinions may be issued, *inter alia*, by regional trade chambers;
- it is important to note that, among the documents, should be enclosed the "documents from competent authorities evidencing the events referred to by the applicant in the application, as force majeure events";
- the opinion is to be issued during 10 business days from the date of the request.

More on COVID-19

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