BANKRUPTCY & RESTRUCTURING

CorporateLiveWire

EXPERT GUIDE 2023

www.corporatelivewire.com

SINGULARIS HOLDINGS:
10 YEARS' LATER - P8

REVERSE VESTING ORDERS
IN CANADIAN INSOLVENCY PROCEEDINGS HIGHLIGHT THE FLEXIBILITY OF THE CANADIAN PROCESS - P20

THE JUDICIAL IMPACT
OF THE COVID-19 PANDEMIC ON BRITISH OVERSEAS TERRITORIES - P24

GERMAN D&O INSURERS
AVOID COVERAGE OF DIRECTORS' LIABILITIES IN INSOLVENCIES - P42

DISTRESSED M&A TRANSACTIONS IN AUSTRIA

By Thomas Trettnak, Christoph Reiter & Philipp Gstrein

Rising interest rates, high inflation and the aftermath of the COVID-19 pandemic and energy crisis in view of the war in Ukraine have had a significant impact on the Austrian distressed M&A market.[1]

On the one hand, both strategic buyers and private equity investors with a certain risk-appetite and cash reserves are looking for opportunities and are eager to acquire companies or parts thereof at a favourable valuation. On the other hand, the sellers may generate much needed cash and liquidity in times of crisis. Finally, as COVID-19 related state subsidies are continuously being cut, there will be more companies facing financial distress in the coming months. In industry terms, we expect to see more distressed deals in the coming year, in particular in retail, real estate & construction and possibly in the hotels & leisure sector.

Austria's legal framework for distressed M&A transactions

Austrian law generally allows for out of court distressed M&A deals that are negotiated and typically closed prior to the opening of formal insolvency proceedings. On the other hand, there are also distressed M&A transactions with an involved party already being subject to formal bankruptcy (i.e. winding up) or restructuring proceedings before the competent courts.

None of these types of deals is governed by a specific legal and regulatory regime only applicable to distressed M&A transactions, though. Rather, a number of general laws and regulations need to be taken into consideration in any relevant case, such as the Insolvency Act, the Restructuring Code, the Equity Substitution Act, and the Company Reorganisation Act. All of these provisions are designed to protect the interests of the involved creditors.

1. The term "distressed M&A transaction or deal" in this article refers to the process of acquiring a financially distressed company or distressed assets pre-insolvency or in the course of an insolvency proceeding.

For pre-insolvency and out-of-court deals, in particular, a customary market standard of transaction documentation has developed over the past years and decades. Usually, the financing banks play the key role in such deals. Further, the transposition of EU-Directive 2019/1023 into the Austrian Restructuring Code has created a new preventive restructuring framework under Austrian law. It also introduced new concepts such as the restructuring of a company against the will of individual creditors (*cram down*), which in the past could have resulted in the failure of a consensual out-of-court restructuring.

For distressed M&A deals in the course of formal insolvency proceedings, the insolvency administrator plays a key role. Although Austrian insolvency courts have specific approval and veto rights with regard to distressed M&A deals, they usually rely on the insolvency administrators' suggestions and follow their respective advice. In small and sometimes even mid-cap deals, direct asset sales initiated by the insolvency administrator are no rarity but rather the norm – such can be effected fairly quickly. In larger transactions, insolvency administrators usually run official auctions, whereby the process is rather straight forward and timing is usually tight.

Specifics of distressed M&A deals

In a typical distressed M&A deal, oftentimes there is a need to find a quick commercial solution among the involved parties, such as banks (or other lenders), suppliers, customers, employees and the management of the insolvent debtor. Overall, the transaction documents and related market standards in a distressed M&A transaction differ quite significantly from a regular M&A transaction in Austria.

MAC (material adverse change) clauses as well as representations and warranties in relation to the debtor's business operations or financials are rather unusual. An insolvency administrator in Austria will typically work with asset and share purchase agreements that are much shorter and simpler than the ones typically used in an ordinary M&A transaction.

> **IT IS ADVISIBLE THAT POTENTIAL BUYERS CAREFULLY ASSESS ALL RISKS RELATED TO THE DISTRESSED BUSINESS BY CONDUCTING A THOROUGH DUE DILIGENCE PRIOR TO ANY ACQUISITION.**

Commercial or investment advisors are usually only engaged by the insolvency administrators in larger deals. Of course, insolvency administrators are also bound by their statutory obligation to protect the debtor's creditors and treat them equally.

The appetite for risk vs. liabilities

Naturally, buyers of distressed entities or assets display larger risk-affinity than ordinary investors. Against this backdrop, it is even more important to avoid exposure to unexpected and incalculable liability. This can be illustrated by the following examples:

- In real estate deals, if the assets to be acquired are polluted, the buyer may be held liable for implementation (at own expense) of appropriate measures to eliminate the relevant contamination.
- If violations of applicable provisions on the protection of employees' rights and interests were committed by the insolvent debtor, the buyer of the distressed assets might also be held liable for such infringements (whereby Austrian law provides for quite strict sanctions in respective scenarios).
- Probably one of the most significant legal risks in distressed M&A transactions is that the purchase price for the business or assets may be set too low (i.e. below the market value). In such event, while purchasers tend to be content with the commercial result of the deal, creditors of the debtor company may (and sometimes do) assert claims against *inter alia* the purchaser to unwind the transaction or to negotiate a settlement with the purchaser. To minimise such risk, a valuation opinion including ballpark figures for the estimated value should be collected by the purchaser prior to the acquisition. This is to later evidence whether the purchase price was indeed appropriate and accurately reflects the true value of the company and/or the acquired assets. Likewise, it is important to ensure that all parties involved have a clear idea of how the purchase price is calculated in order to avoid confusion at a later stage.

In conclusion, it is certainly advisible that potential buyers carefully assess all risks related to the distressed business by conducting a thorough due diligence prior to any acquisition.

Thomas Trettnak is an experienced Corporate M&A partner with CERHA HEMPEL. He is heading the firm-wide CEE M&A and Restructuring PG covering Austria and five CEE countries. He specializes in all aspects of M&A, including VC/PE work and distressed M&A transactions, creditor protection, as well as the reorganization of legal entities in financial distress, and all legal aspects in pre-insolvency and in court insolvency scenarios.

Thomas is particularly renowned for cross-border matters, often for clients based in the US and the UK. He previously worked in-house in M&A for a listed European construction company, and also has transaction and legal project management experience. He is a frequent speaker and writer in his fields of expertise.

Christoph Reiter is an IT/TMT and Corporate M&A partner with CERHA HEMPEL with over 12 years' of professional experience. His practice not only covers corporate & commercial matters, but also (distressed) M&A and insolvency & restructuring cases. Clients speak highly of both his technical and strategic skills.

Christoph is particularly renowned for his cross- border work and his specialist knowledge of how to protect the interests of creditors and business partners of financially distressed or insolvent counterparties, representing them both in and out of court with a high success rate.

Philipp Gstrein is junior associate in the Corporate M&A team focusing on IT/TMT, Venture Capital & Private Equity as well as crypto currencies and smart contracts.
He has assisted in a number of corporate, commercial and insolvency matters as well as distressed M&A deals, with a particular focus on creditor and shareholder protection cases. Phil is a high potential in view of his legal and technical know-how and skills.

CERHA HEMPEL

For more information please contact:
+43 1 514 35 531 | thomas.trettnak@cerhahempel.com
+43 1 514 35 0 | christoph.reiter@cerhahempel.com
+43 1 514 35 0 | philipp.gstrein@cerhahempel.com