M&A Risk Management Considerations Amid War In Ukraine

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by Snežana Gebauer

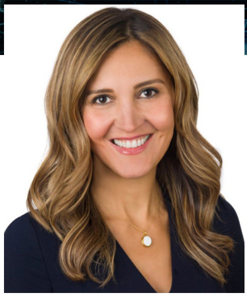
The business implications of the Russian invasion of Ukraine are growing, including economic uncertainty, market volatility, soaring energy and commodity prices, and global trade disruption. And despite coming off **a record year for mergers and acquisitions**, deal making in 2022 has slowed.

This raises a question: What will the long-term impact be for M&A?

The conflict has been devastating for the Ukrainian people, with ripple effects felt around the globe. The U.S., EU, U.K., Canada, Japan and other countries condemned the invasion and imposed the most comprehensive set of sanctions ever levied against a major power. The number and scope of sanctions is likely to expand as Russia continues military operations in Ukraine.

Corporate leaders face critical business continuity decisions, increased risk of cyberattacks, and disruptions in trade partnerships and supply chains. Board meetings are focused on managing risks for existing assets and operations, placing acquisition plans on the back burner. Reporting indicates global deal making **has been down 20% in 2022**, compared with the same period in 2021.

Despite these challenges, there is optimism for robust M&A activity in 2022 and beyond. However, proactive and effective risk management will be more important than ever.



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Through 2020 and 2021, deal makers showed resilience and adaptability to unforeseen challenges presented by the global pandemic and will need to leverage these strengths to navigate through the new reality.

The Russia-Ukraine conflict and the accompanying economic fallout have impacted M&A's future in two important ways: how investments are chosen and how risks are managed.

Deal makers are steering through heightened geopolitical uncertainty and a complex regulatory landscape in addition to the weakened economic conditions. The years ahead will require evaluating all investment decisions through a sharper lens, requiring better intelligence and deeper risk management expertise.

Intelligence-Driven Investment Decisions

Russia's invasion of Ukraine triggered another unprecedented phenomenon: Global business leaders entered the conflict, by suspending or completely terminating business operations in Russia. Over 400 corporations across all industry sectors scaled back operations in Russia, including some of the world's largest companies, often at great expense to bottom lines, effectively self-sanctioning beyond regulatory requirements.

Business leaders brought moral considerations to the forefront of their decision making, defying prior perceptions that corporate commitment to key social issues were superficial. The corporate exodus from Russia raised the moral corporate bar.

It redefined business prosperity in the eyes of stakeholders by meaningfully placing integrity ahead of profits. It also signaled that corporations will be expected to take bolder positions on various environmental, social and governance issues — including equity, diversity, climate change and human rights.

Deal makers will need to reevaluate investment opportunities through the same lens: Decisions about where to invest and from whom to accept investment funding will be more strongly driven by economic, social and corporate governance issues, as well as moral values and shifting geopolitical risks.

Understanding the impact of the evolving global trade relations on the supply chain will be especially critical when evaluating risky investment opportunities where returns seem more promising. Securing actionable intelligence about the investment target, important aspects of its environment and analyzing that information with the assistance of experts will be critical in making the right investment decisions.

Due Diligence, Sanctions and Foreign Direct Investment Reviews

Expanded Scope of Due Diligence

The recently imposed myriad government sanctions have created requirements for more exhaustive due diligence of prospective investments. Given how intertwined the global economy has become, it is critical to ensure that the owners and management of the investment target, its customers, trading partners, providers and distributors are not covered by current sanctions.

The due diligence process would include screening each identified party against current global sanctions. In certain cases, investigation into the beneficial ownership of the investment target and its critical partners will be warranted, especially for those deemed higher risk and where ownership might be opaque.

Further to confirming current ownership, it is important to review historical ownership, particularly recent ownership changes, to account for scenarios where sanctioned individuals or businesses have proxies nominally holding shares on their behalf.

Beyond sanctions risks, the due diligence process will focus on other heightened risk areas: resilience to cyberattacks, supply chain disruptions, business continuity, and the ESG disposition of the investment target.

Suffice to say, due diligence processes will require specialized resources and extended time frames for completion, and deal makers will have to take this into account during negotiations.

Navigating the Evolving Sanctions Landscape

Current sanctions are expected to stay in place not for a few months but likely a few years. Since the conflict started, new sanctions have been introduced on a rolling basis, but with little guidance on implementation, leaving business leaders in unchartered territory.

Deal teams now need to assess carefully whether a proposed transaction is permitted under current global sanctions. The quickly evolving sanctions landscape also requires assessments to be regularly refreshed to account for changes in sanctions.

Foreign Direct Investment Reviews: Staying Ahead of the Regulators

In addition to assessing potential investment targets, deal makers also must ensure their own investors are not exposed to global sanctions lists. When investment is coming from abroad, the **Committee on Foreign Investment in the United States**, or CFIUS, may have to review and approve the transaction. Over a dozen other countries have enacted similar regulations and conduct foreign direct investment reviews.

Businesses or funds with Russian investors might find it challenging to convince these regulatory bodies to proceed with an acquisition. While CFIUS historically focused on deals involving Chinese investors, foreign investment reviews in the U.S. and abroad will likely sharpen their focus on Russian investors.

The determination of whether a business or investor has Russian ties is typically complex and caught in a web of information from multiple jurisdictions and shell corporations. Yet, there is an expectation of deal makers to conduct due diligence to understand beneficial ownership, which will only intensify in times to come.

Heightened geopolitical risks, increased government regulation, supply chain disruptions, and emphasis on ethical investing and ESG all underscore the necessity for actionable intelligence when selecting and evaluating potential investment targets.

They also raise the requirements for better corporate governance and a forward-looking and efficient risk management and compliance framework.

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About the Author

Snežana Gebauer, a partner with StoneTurn, has 20 years of experience in managing complex international investigations for major law firms, Fortune 500 corporations, government agencies and sovereign nations. She frequently advises leaders in business, finance, and government on risk management strategies, investigations, and compliance matters. Snežana is recognized for her deep investigative expertise globally and across every major business sector.