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M&A in Cyprus

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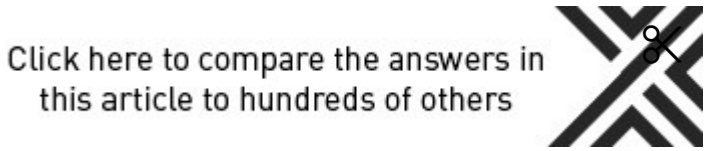

Country snapshot

Trends and climate

What is the current state of the M&A market in your jurisdiction?

Cyprus is undergoing an increase in M&A activity. The country's return to economic growth has seen a renewed interest in foreign investment into the local market, with mergers, acquisitions and joint ventures on the rise.

Have any significant economic or political developments affected the M&A market in your jurisdiction over the past 12 months?

Increased economic activity in the dominant sectors within the economy has led to a gross domestic product growth close to 4% in real terms throughout 2018, which has both resulted in and been affected by increased M&A activity.

Are any sectors experiencing significant M&A activity?

Regulatory restructuring in the banking sector in recent years has encouraged a number of transactions in the sector. Tourism and leisure industries have also attracted significant investment in the form of both new ventures and M&A activity.

Are there any proposals for legal reform in your jurisdiction?

There are no proposals for legal reform. The legal certainty afforded by the coherent statutory framework and the extensive judicial precedent are facilitators in M&A activity.

Legal framework

Legislation

What legislation governs M&A in your jurisdiction?

The following laws govern M&A in Cyprus:

- The Companies Law, Cap 113 governs the merger and restructure of private domestic companies as well as the merger and division of public companies. The Companies Law also governs cross-border mergers and acquisitions. These provisions transpose the EU Cross-Border Mergers of Limited Liability Companies Directive (2005/56/EC) into Cyprus Law. The EU Company Law Directive (2017/1132) codifies existing legislation which has been transposed into Cyprus law.

- The Public Takeover Bids for the Acquisition of Securities of Companies and Related Matters Law (41(I)/2007), as amended, transposes the EU Takeover Bids Directive (2004/25/EC) into Cyprus law. The Public Takeovers Law regulates public company takeover bids and gives the Cyprus Securities and Exchange Commission (CySEC) authority to issue subsidiary legislation further regulating such bids.
- The Cyprus Securities and Stock Exchange Law (14(I)/1993), as amended, is also relevant in relation to public mergers and acquisitions and so is the Transparency Requirements (Securities Admitted to Trading on a Regulated Market) Law (190(I)/2007), as amended.
- The EU Market Abuse Regulation (Regulation (EU) 596/2014) is fully applicable and Cyprus has enacted implementing legislation in the form of the Market Abuse Law (102(I)/2016).
- The Control of Concentrations between Undertakings Law (83(I)/2014) regulates concentrations between undertakings, and notification to and clearance by the Commission for the Protection of Competition (CPC).
- The Preservation and Safeguarding of Employees' Rights on the Transfer of Business, Facilities or Parts of Business or Facilities Law (104(I)/2000), as amended protects, employee rights on transfer of a business.

Regulation

How is the M&A market regulated?

The Cyprus Registrar of Companies (RoC) is the competent authority for recording changes in the shareholding and management of Cyprus public and private companies and partnerships.

The CySEC regulates public takeover bids pursuant to Section 4 of the Public Takeovers Law. The following categories of public bid are caught:

- where the target's registered office is in Cyprus and its securities are traded on a Cyprus regulated market; and
- where the target's securities are not admitted to trading on a regulated market in the EU member state in which the target has its registered office, when certain conditions are met.

The CySEC has the power to approve partial bids, provide exemptions to obligatory public bids and impose administrative fines.

The CPC is the national competition authority to which mergers, acquisitions and joint ventures which meet the jurisdictional thresholds are notified. Implementation of transactions is prohibited prior to clearance by the CPC.

Are there specific rules for particular sectors?

Additional regulatory approval from competent authorities are required for transactions in certain sectors, including the banking, insurance, financial services and investment funds and media sectors.

In particular, the banking sector, any proposed acquiring party of a qualifying holding (indirectly or directly) in an authorised credit institution incorporated in Cyprus must notify such intention to the Central Bank of Cyprus (CBC) and provide all requested information. The CBC will perform its assessment and communicate all relevant information to the European Central Bank (EBA), which is exclusively competent to decide whether to oppose an acquisition of a qualifying holding in a credit institution incorporated in Cyprus, within the framework of the Single Supervisory Mechanism.

A participation in a bank can be described as a 'qualifying holding' when it represents 10% or more of the shares or voting rights in the bank or crosses the other relevant thresholds (20%, 30% or 50%). In addition, obtaining rights to appoint the (majority of) the management board or other means of providing significant influence over the management of the bank also falls within the scope of a qualifying holding.

Acquisitions in the banking sector are subject to the Business of Credit Institutions Law (66(I)/1997), as amended, and subsidiary legislation issued by the CBC. Guidance on the assessment of acquisitions of qualified holdings is available in the Joint Guidelines on the prudential assessment of acquisitions and increases of qualifying holdings in the Financial Sector issued by the Joint Committee of the three European Supervisory Authorities (the EBA, the European Insurance and Occupational Pensions Authority and European Securities and Markets Authority) in December 2016.

The CBC is exclusively competent to regulate acquisitions of qualified holdings in relation to credit acquiring companies.

Types of acquisition

What are the different ways to acquire a company in your jurisdiction?

An acquisition of a company normally occurs through:

- a share sale between the existing owner and the purchaser; or
- absorbing a company in the context of a merger.

Alternatively, it is also possible to carry out an acquisition of a business as a going concern (or part thereof), which is implemented though an asset purchase agreement between the purchaser and the company owning the business.

In the case of public listed companies, acquisitions occur by way of takeover in accordance with the Public Takeovers Law. Where a public company is not listed, shares can be acquired without making a public offer. Special provisions of the Companies Law further regulate mergers of public companies.

Preparation

Due diligence requirements

What due diligence is necessary for buyers?

Before negotiation of transaction documents on an acquisition, it is standard practice for a buyer to conduct legal, commercial, financial and tax due diligence.

Legal due diligence can entail corporate aspects relating to:

- ownership and management;
- security charges registered against the company;
- validity of titles to assets;
- IP rights; and
- employment issues (including collective agreements).

Depending on the nature of the target's activities, a regulatory due diligence may also be required in terms of the validity and other aspects of the target's licences and authorisations to conduct its business. A buyer and the seller may also want to assess competition law aspects of a proposed transaction to ascertain whether, for example, merger control thresholds may be triggered and whether there are other competition law implications.

Information

What information is available to buyers?

Normally a request for information will be sent by a buyer to the target's management, who will supply copies of the documents requested and responses to queries raised.

Public records maintained by the Cyprus Registrar of Companies (RoC) can be accessed on payment of a fee. These records include:

- the memorandum and articles of association of a company;
- the details of past and present directors and secretaries of a company;
- information on current and past shareholdings in a company; and
- charges registered against a company;
- annual report filings.

The Cyprus Stock Exchange (CSE) may also provide a register of a public listed company's members on application by an interested party.

With respect to labour matters, certain collective employment agreements are publicly available.

What information can and cannot be disclosed when dealing with a public company?

In a hostile takeover bid, the bidder will have access only to publicly available information. Where the target's board decides to recommend a takeover bid, it must treat all bidders equally under the Takeover Bids Law and disclose equal levels of information.

Stakebuilding

How is stakebuilding regulated?

Stakebuilding is largely regulated through the process of disclosure. Disclosure requirements are triggered in relation to securities listed in the CSE at thresholds of 5%, 10%, 15%, 20%, 25%, 30%, 50% and 75%. In certain circumstances, a party may need to disclose acquisitions or disposals to the issuer of the securities concerned, the Cyprus Securities and Exchange Commission or the CSE.

Documentation

Preliminary agreements

What preliminary agreements are commonly drafted?

It is common for heads of terms or memoranda of understanding to be signed as preliminary agreements in proposed M&A transactions. The parties also commonly enter into exclusivity and non-disclosure agreements before beginning negotiations on an M&A transaction.

Principal documentation

What documents are required?

In the case of an acquisition of a private company by way of share purchase, the following are typical transaction documents:

- the asset or share purchase agreement (the acquisition agreement);
- a letter of disclosure by the seller addressing the warranties in the acquisition agreement;

- the target's board minutes in relation to the change of director, bank signatories, change of auditors and approval of share transfers on completion; and
- instruments of transfer and share certificates for the shares being sold.

In the case of a public takeover bid, the following are required:

- an announcement of the intent to make a public offer or confirming the decision to make a public offer;
- the offer document must include confirmation by a credit institution or other organisation that sufficient funds are available to satisfy full acceptance of the offer;
- an acceptance and transfer form, issued by the offeror and sent to all of the target's shareholders;
- the reasoned opinion by the target's board of directors sent to the target's security holders accompanied by an independent expert report;
- a revised offer document, where applicable; and
- the final result of the offer announced and published in two daily national newspapers.

Which side normally prepares the first drafts?

In relation to the acquisition of private companies, in the context of an auction process, the first drafts are usually prepared by the seller (and commented on by the bidder as part of the offer process). In other cases, the first drafts are sometimes produced by the buyer.

In a takeover offer, the bidder prepares the offer document.

What are the substantive clauses that comprise an acquisition agreement?

A standard acquisition agreement typically contains the following substantive clauses:

- conditions precedent to the transaction;
- an obligation to sell and purchase the shares;
- closing requirements;
- representations and warranties;
- limitations on the seller's liabilities with respect to the sale;
- specific indemnities and guarantees;
- specific provisions regulating tax and allocation of burden between the parties;
- confidentiality restrictions;
- boilerplate clauses relating to costs, notices, assignment, entire agreement and severance; and
- governing law and jurisdiction clauses.

What provisions are made for deal protection?

Cyprus law can accommodate exclusivity and confidentiality provisions, as well as non-solicitation clauses. It is not unusual for acquisition agreements to contain clauses to the effect that the target's (majority) shareholders will not sell or transfer to a third party other than the prospective buyer.

Closing documentation

What documents are normally executed at signing and closing?

On transactions where there is a period between signing and closing typically the following documents are signed:

- the acquisition agreement;
- the disclosure letter; and
- relevant corporate authorisations of the target approving the documentation being entered into and the transaction overall.

In a share acquisition, the following are executed on closing:

- instrument of transfer;
- waivers of pre-emption rights and any requisite consents;
- resignation letters from officers and appointment letters for new officers;
- updated disclosure letter;
- new bank mandate forms; and
- closing board minutes to record the closing of the transaction, the transfer of shares and closing actions.

Are there formalities for the execution of documents by foreign companies?

No specific formalities for the execution of documents by foreign companies exist in Cyprus.

Are digital signatures binding and enforceable?

Digital signatures are binding and enforceable in Cyprus under the Legal Framework for Electronic Signatures and Associated Matters Law (188(I)/2004), which transposes Directive 1999/93/EC on electronic signatures. Digital signatures are not widely used on M&A transactions.

It is standard practice in local M&A for fully conformed original documents to be exchanged at signing and completion. Scanned counterparts are often exchanged initially in cross-border transactions, with original documents subsequently being sent to the parties.

Foreign law and ownership

Foreign law

Can agreements provide for a foreign governing law?

Yes, agreements can provide for a foreign governing law. The overall legal environment in Cyprus is particularly accommodating to English law-governed agreements, given that Cyprus is a common law jurisdiction and its corporate statutory framework is modelled on the English Companies Act of 1948 (updated to reflect the latest developments in corporate law and to transpose EU law into the national legal order).

Foreign ownership

What provisions and/or restrictions are there for foreign ownership?

No provisions or restrictions on foreign ownership of shares generally exist, except in the case of certain regulated sectors where consents must be obtained in advance.

Valuation and consideration

Valuation

How are companies valued?

Companies are normally valued by auditors. The basis of a valuation may vary depending on the nature of the business and the types of asset in question.

Consideration

What types of consideration can be offered?

In private acquisitions there is no restriction on the type consideration which may be freely agreed between the parties. Typically, consideration will be cash, loan notes or payment in kind.

In public takeover bids, consideration must be equal to at least the highest price paid (or agreed to be paid) for the same securities by the bidder or by persons acting in concert with the bidder during the 12 months preceding the announcement of the bid.

In the case of a voluntary bid, the Cyprus Securities and Exchange Commission may allow for a lower bid price at its discretion. The consideration for public takeover bids may take the form of securities, cash or a combination of the two, except in the following circumstances, where a full cash alternative must be offered:

- where the consideration offered by the offeror does not consist of securities admitted to trading on a regulated market;
- where the offeror or persons acting in concert with it have purchased cash securities carrying 5% or more of the voting rights in the offeree company (over a period of 12 months preceding the announcement of the bid up to and including the date when the offer acceptance period closes);
- in the case of a squeeze-out or sell-out; or
- in the case of a mandatory bid being triggered.

<u>Strategy</u>

General tips

What issues must be considered when preparing a company for sale?

From the seller's perspective, the following should be considered when preparing the company for sale:

- retaining valuation experts to conduct a valuation;
- reviewing statutory books and registers of the company to ensure all records are up to date;
- reviewing all corporate governance processes;
- considering regulatory consents that may need to be obtained/planned for in advance;
- confidentiality issues and preparing confidentiality agreements for advisers and other parties involved in the planning;
- data protection issues; and
- (if an asset sale) considering and planning for any transfer of undertakings issues.

What tips would you give when negotiating a deal?

The following are useful tips when negotiating a deal:

- Fully prepare before starting negotiations. Having full visibility of due diligence findings can be pivotal to negotiating key terms in transaction documents.
- Use specialist advisers, particularly in regulated industries or where an investor is entering a new market where cultural complexities can impact commercial realities.

Hostile takeovers

Are hostile takeovers permitted and what are the possible strategies for the target?

Yes, a takeover bid may proceed even where the target's board of directors does not recommend the bid. Hostile takeover bids must take into account the fact that the target's board of directors is under an obligation to:

- communicate information to its shareholders and employees promptly and accurately;
- give its views on the effects of implementation of the bid; and
- make recommendations to shareholders.

Warranties and indemnities

Scope of warranties

What do warranties and indemnities typically cover and how should they be negotiated?

Typical warranties and indemnities cover the following matters in respect of the target:

- the target's share capital;
- the seller's capacity to enter into the transaction;
- the company's financial and statutory records;
- any warranties relating to specific assets (eg, where real estate or where there are other specific business assets);
- IP rights;
- data protection considerations;
- regulatory licences;
- employees;
- material contracts;
- pending or future litigation, disputes and investigations;
- compliance with laws; and
- anti-money laundering and know-your-customer compliance.

Normally a buyer will want to obtain as much comfort as possible by requesting extensive warranties, coupled with indemnities for specific matters preparing the ground to claim damages for breach of warranty and indemnification in respect of specific indemnities negotiated. A seller will resist extensive warranties and seek to have these qualified by the buyer's own knowledge and reasonable investigation.

Limitations and remedies

Are there limitations on warranties?

Warranties are usually qualified by way of disclosure of specific matters by the seller in a disclosure letter. The parties may also negotiate certain matters in the transaction document restricting the warranties proposed – for example:

- a cap on liability;
- a *de minimis* threshold below which claims cannot be made (individual and aggregate);
- specific time periods when a claim can be made;
- provisions regulating the mechanism for a dispute that may arise for a breach of warranty and a third-party claim;
- a general obligation to mitigate loss suffered;
- qualifying warranties known by the buyer;
- a requirement that the buyer exhaust all rights against insurers and other relevant third parties; and
- limits on the seller's liability for actual claims.

What are the remedies for a breach of warranty?

A breach of warranty gives rise to a claim for damages in contract by the aggrieved party. Depending on the nature of the breach, a claim in tort for misrepresentation may also arise.

Are there time limits or restrictions for bringing claims under warranties?

Statutory limitation periods apply; claims arising out of contract are subject to a six-year limitation period.

Tax and fees

Considerations and rates

What are the tax considerations (including any applicable rates)?

The sale of securities is exempt from taxation. The term 'securities' is defined as shares, bonds, debentures, founders' shares and other securities of companies or other legal persons, incorporated in Cyprus or abroad and options thereon.

Although there is no capital gains tax on sales of shares or business assets, capital gains applies on the sale of immovable property in Cyprus and shares in companies the assets of which, directly or indirectly, consist of immovable property in Cyprus.

Stamp duty at banded rates is payable on certain transaction documents.

Exemptions and mitigation

Are any tax exemptions or reliefs available?

Tax treatment varies greatly depending on the nature of the acquisition (shares or assets) and the particular factual circumstances of the transaction.

Where shares are acquired, accumulated or carried forward, Cyprus tax losses generated by the target are transferred along with the company. A company's carried forward loss cannot be set off against the profits of other companies through group relief, but can be set off against the company's own future profits.

Trading losses can be carried forward for up to five years from the year to which the profits relate. Where a Cyprus target with trading losses is acquired by a company, it may use the losses against its own future trading profits, provided that there has been no major change in the nature or conduct of its trade three years prior to the acquisition and three years after that date. If the purchaser intends to substantially change the nature of the target's business, it may be advisable to wait until at least three years have elapsed from the date of acquisition.

What are the common methods used to mitigate tax liability?

A fact-specific tax assessment should be carried out to determine any tax liability mitigation.

Fees

What fees are likely to be involved?

Legal, financial and tax advisory fees are likely to form the bulk of fees involved in a merger or acquisition. These vary depending on the size of the deal.

In addition, on a public takeover, Cyprus Securities and Exchange Commission fees may apply.

If merger control clearance is required, a €1,000 filing fee must also be paid to the Commission for the Protection of Competition (CPC). In the case of a full CPC investigation (Phase II), the fee is €6,000.

Filings with the registrar of companies will also carry disbursements which vary depending on the type of submission.

Management and directors

Management buy-outs

What are the rules on management buy-outs?

No special rules apply to management buy-outs.

Directors' duties

What duties do directors have in relation to M&A?

Directors are subject to a number of statutory obligations as well as a range of common law fiduciary duties.

Common law fiduciary duties broadly require that directors:

- act in the best interests of the company at all times;
- are independent;
- avoid conflicts; and
- be fit and proper for their purpose.

For public companies, directors who sign a restructuring plan and any related proposal are liable to the shareholders of the seller for their negligent conduct. A restructuring plan or related proposal signed by a director found to contain false information may give rise to criminal liability on a director.

Directors also owe a common law duty to act with reasonable care and skill in their capacity as directors having regard to whether they have been appointed as directors by virtue of their knowledge and expertise.

Employees

Consultation and transfer

How are employees involved in the process?

In the case of a business sale, the buyer and seller will each need to consider their respective notification or consultation obligations with employees or their representatives under the Preservation and Safeguarding of Employees' Rights in the Transfer of Business, Facilities or Parts thereof Law (104(I)/2000 – the TUPE Law), as amended.

In the case of a share sale, employees will continue to be employed by the same entity despite the change of ownership and there is no obligation to inform them of a change of control in the entity which employs them.

What rules govern the transfer of employees to a buyer?

The rights of employees in both public and private companies are protected under the TUPE Law.

The rights and obligations of the seller emanating from employment relationships automatically transfer to the buyer on completion.

A transfer of all or part of business does not constitute grounds *per se* for dismissal by the buyer or seller, except where a dismissal results from genuine economic, technical or organisational reasons that necessitate reductions in the workforce. Terminated employees are entitled to compensation pursuant to the Termination of Employment Laws of 1967 to 1994 (as amended). Termination for any other reason is unlawful and will give rise to a claim for compensation based on the employee's length of service and employment contract terms under the Termination of Employment Laws of 1967 to 1994.

Pensions

What are the rules in relation to company pension rights in the event of an acquisition?

The precise nature of the scheme and its benefits must be assessed to determine whether it would automatically transfer in the event of a business acquisition. Depending on their precise nature, occupational pension schemes may be transferred.

Other relevant considerations

Competition

What legislation governs competition issues relating to M&A?

The Merger Control Law is the relevant statute which may trigger an obligation to notify a transaction and obtain clearance from the Commission for the Protection of Competition (CPC).

Transactions caught under the Merger Control Law include:

- mergers of two previously independent undertakings or parts thereof;
- acquisitions by one or more persons already controlling at least one undertaking; and
- acquisitions by one or more undertakings, directly or indirectly, whether by purchase of securities or assets, by agreement or otherwise, of control of one or more other undertakings.

Only concentrations of major importance must be notified to the CPC. For the purposes of the Merger Control Law, a concentration of undertakings is deemed to be of major importance and therefore meets the jurisdictional thresholds if:

- the aggregate turnover achieved by at least two of the undertakings concerned exceeds, in relation to each one of them, €3.5 million;
- at least two of the undertakings concerned achieve a turnover in Cyprus; and

- at least €3.5 million of the aggregate turnover of all undertakings concerned is achieved in Cyprus.

Anti-bribery

Are any anti-bribery provisions in force?

There are a number of anti-bribery provisions set out in different statutes that allow effective anti-corruption enforcement – the more significant of which are as follows:

- The Prevention of Corruption Law (Cap 161) makes it an offence, among other things, for an agent (which includes public officials) to receive a gift. Offences are punishable by imprisonment of seven years, a fine of up to €100,000 or both.
- The Penal Code (Cap 154) sets out a number of offences constituting corruption by public officials which include extortion, abuse of office and neglect of official duty. It imposes penalties for both public and private corruption.
- Articles 69 and 70 of the Civil Servants Law address bribery of public officials and makes it an offence to receive or offer 'gifts', broadly defined. Violation results in disciplinary proceedings.

Cyprus has also ratified the Criminal Law Convention on Corruption which was transposed into domestic law. Under this law (23(III)/2000), conduct defined in the convention as 'criminal' is now criminalised in Cyprus and is subject to custodial sentences and fines.

Receivership/bankruptcy

What happens if the company being bought is in receivership or bankrupt?

Any transaction for the acquisition of assets of a company that is under liquidation or receivership would require the cooperation of an appointed liquidator or receiver, respectively.

Any transfer of shares not made with the liquidator's approval and any alteration in the status of a company's members made after the commencement of a voluntary winding up are void.

Antoniou McCollum & Co LLC - Anastasios A. Antoniou and Christina McCollum