
THE MERGERS & ACQUISITIONS REVIEW

NINTH EDITION

EDITOR
MARK ZERDIN

LAW BUSINESS RESEARCH

THE MERGERS & ACQUISITIONS REVIEW

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THE MERGERS & ACQUISITIONS REVIEW

Ninth Edition

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EDITOR'S PREFACE

By a number of measures, it could be argued that it has been some time since the outlook for the M&A market looked healthier. The past year has seen a boom in deal making, with many markets seeing post-crisis peaks and some recording all-time highs. Looking behind the headline figures, however, a number of factors suggest deal making may not continue to grow as rapidly as it has done recently.

One key driver affecting global figures is the widely expected rise of US interest rates. Cheap debt has played a significant part in the surge of US deal making in the first few months of 2015, and the prospects of a rate rise may have some dampening effects. However, the most recent indications from the Federal Reserve have suggested that any rise will be gradual and some market participants have pushed back predictions for the first rate rise to December 2015. Meanwhile, eurozone and UK interest rates look likely to remain low for some time further.

The eurozone returned to the headlines in June as the prospect of a Greek exit looked increasingly real. Even assuming Greece remains in the euro (as now seems likely), the crisis has severely damaged the relationship between Greece and its creditors. The brinkmanship exhibited by all parties means that meaningful progress cannot occur except at the conclusion of a crisis: the idea that reform will benefit Greece has been lost and each measure extracted by creditors is couched as a concession. However, while the political debate has become ever more fractious, the market's response to the crisis has been relatively sanguine. This is largely a result of the fact that the volume of Greek debt is no longer in the market, but in the hands of institutions. But it is also a sign of the general market recovery and expectations that major economies will continue to grow.

Perhaps one of the more interesting emerging trends in the last year is the interplay between growth and productivity. Some commentators have suggested that the recent rise in deal making is a symptom of a climate in which businesses remain reluctant to invest in capital and productivity. Pessimistic about the opportunities for organic growth, companies instead seek to grow profits through cost savings on mergers. It is difficult to generalise about such matters: inevitably, deal drivers will vary from industry to industry, from market to market. However, if synergies have been the principal motivation in

much of the year's deal making (it certainly has been in a number of large-cap deals) then it may be that the market is a little farther from sustainable growth than some would like to think.

I would like to thank the contributors for their support in producing the ninth edition of *The Mergers & Acquisitions Review*. I hope that the commentary in the following chapters will provide a richer understanding of the shape of the global markets, together with the challenges and opportunities facing market participants.

Mark Zerdin

Slaughter and May

London

August 2015

Chapter 18

CYPRUS

*Nancy Ch Erotocritou*¹

I GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

Since Cyprus's accession to the EU, the legislation regulating M&A activity in Cyprus has been closely aligned with Europe-wide practices.

Prior to Cyprus's EU membership, the ability of Cyprus companies to merge was limited to domestic mergers and was governed by the general provisions of the Company Law on arrangements and reconstructions. In 2007 Cyprus enacted legislation harmonising its existing laws with Directive 2005/56 on cross-border mergers of limited liability companies opening the route for cross-border mergers between companies incorporated in Cyprus and companies in the EU.

A cross-border merger may take place by acquisition whereby one or more limited liability companies are wound up without going into liquidation and transfer all their assets and liabilities to an existing company or a newly established company. In exchange, the shareholders of the acquired company are issued shares and a settlement amount in cash payment not exceeding 10 per cent of the nominal value of shares or when the shares have no nominal value of the accounting par value.

What is envisaged is a cross-border merger of companies that have been incorporated in accordance to the laws of a Member State and have their registered office, central administration or main place of establishment within the EU under the condition that at least two of these companies are governed by the law of different Member States.

A cross-border merger may only take place between companies for which merger is permitted in accordance with the provisions of the national law of the Member State in which they are incorporated. In Cyprus any company may take part in a cross-border merger, except companies with limited liability by guarantee (that is to say, without

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share capital) and companies under liquidation. Most structures involve either a merger between private limited liability companies by shares or in cases where the intended result of the merger is the formation of a European company, public limited liability companies by shares.

Notably the legislation provides for simplified procedures in the case of intra-group cross-border mergers, dispensing with requirements for expert reports, general meetings at dissolving company level and the need to include information on share exchange ratio and related issues in the cross-border merger plan; providing significant savings of both time and cost. Such simplification procedures have provided a stepping stone to international groups of companies, which have sought to restructure or consolidate their activities in the financial crisis taking full advantage of the Cypriot tax regime.

The acquisition of shares in private or public companies is governed by the provisions of the Company Law and the companies' articles of association. Where the shares of a public company are listed on the Cyprus Stock Exchange or on a regulated market outside Cyprus, special consideration must be given to the provisions of the Public Takeover for the Acquisition of Shares in a Company and Related Matters Law, which is complemented by directives issued by the Cyprus Securities and Exchange Commission. Other sources of legislation that should be considered are the Cyprus Stock Exchange Law and the Inside Information and Manipulation of Market Law. Special consideration must also be given to the disclosure requirements of the transparency legislation that may be triggered.

II DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

On 29 April 2011 Cyprus enacted legislation amending the Criminal Code, effectively introducing an interest rate ceiling affecting loans granted by persons or entities that are not financial institutions. The interest rate ceiling is calculated using a formula based on half the average bank lending rate of the previous year (including commissions and other charges that banking institutions charge on consumer loans) plus a margin of between 5 and 10 percentage points, which varies according to various risk factors. This interest rate ceiling is calculated and published by the Central Bank of Cyprus quarterly and on 24 April 2015 was set at 10.44 per cent.

The interest rate ceiling applies to lenders that are not financial institutions and catches interest received or charged on granting of the loan, extension of repayment, prepayment and renewal. Breach of the provisions constitutes an offence and on conviction a person may be liable to up to five years' imprisonment or a fine capped at €30,000, or both.

The legislation was intended to target the increasing problem of loan sharking and profiteering but due to its impact on the structuring of intra-group loans, the following arrangements were carved out of the prohibition:

- a* a loan extended to a legal person, where the funds have originated directly or indirectly from sources outside Cyprus, provided that (1) the amount of the loan exceeds €1 million and (2) the minimum disbursement is €500,000;

- b* a loan extended to a legal person, which is disbursed abroad (i.e., outside Cyprus) and provided that (1) the amount of the loan exceeds €1 million and (2) the minimum disbursement is €500,000; and
- c* a loan where the borrower and the lender are legal persons and who are considered to be related or connected parties for the purpose of application of Section 33 of the Cyprus Income Tax Laws.

The carve-outs ensure that the legislation will not have a negative impact on the ability of group companies to enter into intra-group financing arrangements.

The Company Law prohibits a company from directly or indirectly providing financial assistance to a third party for the purpose of a purchase or subscription of its shares or shares in its holding company. A transaction that is considered to be financial assistance is void and therefore gives rise to serious consequences making this a fundamental issue to be considered by parties in structuring an acquisition. In 2009 the prohibition on financial assistance was relaxed so that the prohibition would not apply to private companies provided that the same was not a subsidiary of a public company and provided that the act was approved by a majority of shareholders holding more than 90 per cent of the votes of all the issued share capital of the company. The relaxation has assisted the structuring of the financing of acquisitions in private companies, which has proved another useful tool to groups navigating their way through the financial crisis.

III FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

In previous years Cyprus saw a significant pick-up in restructuring aimed at strengthening financial positions and cleaning up portfolios. Cyprus is frequently used in corporate group structures, either as a means of structuring finance or as a pipeline through which business is conducted. Due to this, late 2011 and 2012 saw inbound investments of international business into Cyprus, whether by means of redomiciliation of head offices, moving of operations to Cyprus through cross-border mergers and other business combinations.

In 2013 Cyprus agreed with the Troika the terms of a €10 billion bailout to restore the viability of the financial sector of Cyprus. To satisfy the criteria imposed by Eurogroup the Resolution of Credit and Other Institutions Law No. 17(I)/2013 was passed, which resulted in resolution measures imposed on Cyprus Popular Bank and Bank of Cyprus (including the controversial 'bail in' provisions). In addition to these, restrictions on capital and exchange controls had been imposed (subject to exceptions) aimed at protecting the financial stability of Cyprus affecting the outflow of funds from Cyprus banks abroad. The restrictive measures were relaxed a number of times since they entered force and in April 2015 Cyprus lifted the last of the capital controls. Currently both businesses and individuals may transfer money abroad with no restrictions and it is expected that the free flow of capital will attract further investment from overseas, with Cyprus expecting to return to a marginal growth this year.

As a result of the banking crisis there has been a significant increase in foreign involvement in the banking sector of Cyprus with Wilbur Ross, a US private equity specialist and the European Bank of Reconstruction and Development participating in

a €1 billion private placement and the former taking 19 per cent of the Bank of Cyprus. The investment is thought to be the biggest single foreign direct investment into Cyprus.

IV SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

In recent years Cyprus has taken great strides in its attempt to develop its hydrocarbon resources. In particular it has concluded a number of bilateral agreements with Egypt, Lebanon and Israel in order to delimit its exclusive economic zone (EEZ). The Ministry of Commerce, Industry and Tourism of Cyprus held its first hydrocarbon licensing round in 2007, with Noble Energy International Ltd receiving an exploration licence for block 12 (there are 13 blocks in the Cyprus EEZ, but only 11 of the 13 blocks were contested in the first licensing round). In December 2011, Noble Energy announced the discovery of 5 trillion cubic feet of natural gas with additional appraisal drilling to follow prior to development. In 2012, Cyprus commenced a second licensing round. On 24 January 2013 Cyprus signed an agreement with ENI/KOGAS (Italian/Korean) for an estimated €150 million to grant authorisation for the exploration of blocks 2, 3 and 9. On 7 February 2013 Cyprus signed an agreement with TOTAL E&P Activities Petrolieres (France) for an estimated €24 million to grant authorisation for the exploration of blocks 10 and 11. ENI-KOGAS began exploratory drilling in September 2014 and plans to drill several exploratory wells within 2015 and 2016. There has also been a recent declaration of commerciality for the Aphrodite gas field by Noble, Energy Delek Drilling Limited Partnership and Avner Oil Exploration Limited, confirming the existence of substantial recoverable natural gas reserves in Block 12 of Cyprus EEZ.

Foreign investors have already invested in the exploration of natural gas in Cyprus and it is hoped that joint venture activity for exploitation of natural resources will provide Cyprus with the means to move past the problems caused by the global financial crisis and the Cyprus banking crisis. The energy industry also provides huge potential for investment in the provision of oil and gas ancillary services and agreements are in the pipeline between the Cyprus government, local and foreign companies who wish to provide oil and gas related services to the region. The announcement of the commerciality of the Aphrodite field is very significant for Cyprus transition into a net natural gas producer. The government of Cyprus has been engaged in talks to export natural gas to Jordan and Egypt via undersea pipelines, both in desperate need for natural gas. Exporting the gas to Egypt would also provide Cyprus with the opportunity to use Egypt's unused export terminals to reach far-reaching markets.

In addition to exploitation of natural gas, Cyprus has seen tourism increase by 9.6 per cent for the period January – May 2015, in comparison to the corresponding period in 2014. There has also been greater British investment in hotel stock in Paphos, with hope for similar agreements to be made with German and Scandinavian tour operators. A recent agreement has been reached with Qatar Airways for use of Larnaca airport as the 13th destination of the airline. This development improves connectivity of Cyprus and the EU by extension, with the Middle East and Asia and is expected to boost tourism and investments from the Arab world. Emirates and Etihad Airways have also announced that they will be increasing the frequency of flights to and from the island.

German commercial carrier Germania also plans to operate seven new flights a week from 2015 connecting Paphos with Dusseldorf, Berlin, Hamburg, Bremen and Erfurt, with Austrian airline NIKI commencing flights from Paphos to Vienna.

Finally, the government has announced plans to implement legislation for the licensing of casino operations in 2015, which is also expected to have a positive impact on the tourism industry. The plans include the development of a casino resort including other leisure services such as hotels, spas and conference centres. A recent deal with the Buena Vista Hospitality Group to construct Europe's largest integrated sports, health and wellness resort on the outskirts of the village of Kalavassos also evidences interest from foreign investors in the tourism and hotel industry of Cyprus.

In respect of immigration matters, the incentives that were published by the government for the issue of residence permits (fast track procedure) and the provision of citizenship through direct investment has triggered interest from individuals from China, Russia, Ukraine and the Middle East contributing to investment activity.

V FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

The financing of M&A varies depending on the structure of the proposed transaction and the ultimate objective. In recent years intra-group cross-border merger activity has increased with a view to restructuring group activities, the financing of which is mainly internal. On the acquisition side, projects have been structured as joint ventures, splitting the funding between two independent groups through a combination of debt and equity injections and coupled with a comprehensive exit strategy. Financing has also recently been raised through debt issuances of bonds and notes on capital markets. The Cypriot legal and tax system gives Cypriot special purpose vehicles a significantly positive platform for the issues of debt instruments and Cypriot issuers have been involved in sizeable issuances of a variety of debt instruments, mostly on foreign markets.

The impact of the provisions on financial assistance and interest rate ceilings for intra-group loans discussed above is a consideration in the structuring of financing for M&A activity. As regards developments in Cyprus with respect to the financial crisis discussed above, these have not affected the advantages of structuring transactions through Cyprus and it is expected that Cyprus will continue to attract foreign investment.

VI EMPLOYMENT LAW

Compared with 2014 with unemployment levels as high as 16.1 per cent, unemployment has seen a steady decrease this year to 15.6 per cent, according to Eurostat statistics, whilst employee protection continues to be of the utmost importance in the route to recovery from the financial crisis. Employee protection in Cyprus was strengthened by the implementation of European legislation since Cyprus' accession to the EU. Specifically with respect to cross-border mergers and acquisitions or transfer of undertakings, legislation such as the preservation of employees' rights during the transfer of a business (Law 104(I)/2002), legislation regulating the requirement to consult with employees and provide information, the setting up of European council works and special negotiating bodies and provisions requiring the board of directors of a target company to consult

with its employees immediately after an offer to buy it out has been announced and has provided an increasing role to employees in the process of mergers and acquisitions involving Cypriot companies.

VII TAX LAW

Cyprus continues to attract foreign investment through its favourable tax regime. Companies incorporated in Cyprus are often used in international tax structures as holding companies, trading companies and financing companies. Cyprus imposes a 12.5 per cent corporate tax rate and has a number of other beneficial tax treatments. Cyprus does not levy any withholding taxes on dividends and interest paid to non-Cypriot entities. Dividends received are fully exempt from tax unless such dividends derive from passive activities. In addition to this, group loss relief for a loss incurred in an income year is allowed between resident group companies that meet certain conditions and losses can be carried forward indefinitely.

Tax considerations ultimately depend on the structure of the business acquisition. There is no capital gains tax payable in Cyprus except on gains accruing from the disposal of immovable property or the disposal of shares in companies whose property consists of immovable property held in Cyprus. There is no income tax payable on profits realised from the disposal of securities, irrespective of the holding period, the number of shares held or trading nature of the gain. The term 'securities' has been classified to include, among other instruments, shares, bonds, debentures and founder shares.

Reorganisations such as mergers, share-for-share exchanges, contribution of assets in exchange for shares and divisions are exempt from income tax, capital gains tax and stamp duty, although tax clearance should be applied for from the Inland Revenue Department during the restructuring.

VIII COMPETITION LAW

Joint ventures and mergers and acquisitions involving Cypriot companies are types of business operations that may be caught under the Control of Concentrations Between Enterprises Law, which regulates merger control issues in Cyprus. The ultimate objective of the legislation is to prevent business restructurings that could negatively affect competition and harm or distort the internal structure of the market. In order to be caught by the legislation there must be a concentration of enterprises and the concentration must be of major importance.

A concentration exists in any of the following circumstances: (1) the merger of two or more previously independent undertakings; (2) the acquisition of direct or indirect control (whether by the share capital or assets, or by contract or other arrangements) of the whole or parts of one or more other undertakings; or (3) the establishment of a joint venture fulfilling all the functions of an autonomous economic entity on a permanent basis.

A concentration is considered to be of major importance when: (1) the aggregate turnover achieved by at least two of the enterprises exceeds, in relation to each one of them, €3.5 million; and two of those enterprises engages in commercial activities within

the Republic of Cyprus; and (2) at least €3.5 million of the aggregate turnover of all the participating enterprises concerns the disposal of goods or the supply of services within the Republic of Cyprus, or (3) it is declared as being of major importance by the Minister of Energy, Trade, Industry and Tourism.

If the participating undertakings meet these thresholds a notification must be made to the Commission for the Protection of Competition (CPC). The notification may be followed by a number of proceedings after which the CPC submits its decision on the same. The CPC will grant either a conditional or an unconditional clearance of the notified concentration or declare that it is prohibited. If the concentration has a community dimension, the CPC has an obligation to refer it to the European Commission for examination at EU level.

IX OUTLOOK

Despite a painful economic reform process resulting from the 2013 banking crisis, the recent predictions of the IMF indicate an expected growth of 0.2 per cent in 2015. The lifting of the capital controls in combination with a series of incentives put in place by the government in the aftermath of the crisis have created international interest and investment opportunities in various sectors. Cyprus continues to constitute an ideal jurisdiction for the purpose of structuring M&A deals and it is hoped that the coming years will see a return to the peak level of M&A activity experienced some years ago.

Appendix 1

ABOUT THE AUTHORS

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Nancy Ch Erotocritou joined the Cyprus office in 2007 and became a partner in 2011. She practises in international banking and finance law, mergers and acquisitions and corporate law and advises multinational companies and leading international banking institutions on cross-border transactions.

Ms Erotocritou received her LLB with honours from Sheffield University, her LLM from University College London and her LPC from BPP London. She was admitted to the Cyprus Bar Association in 2007 and became partner in 2011.

Ms Erotocritou has been recognised as a leading lawyer by the legal directories *Legal 500*, *Chambers Global*, *IFLR* and *Best Lawyers International*. She is a member of the Cyprus Bar Association, the Women's International Shipping and Trading Association and is the exclusive banking and finance representative of the Women's Law Network in Cyprus.

Ms Erotocritou has contributed articles to a number of publications including the *Comparative Law Yearbook of International Business*, Volume 32a; *Getting the Deal Through: Mergers and Acquisitions* 2010, 2011, 2012 and 2013; Neate and Godfrey: *Bank Confidentiality* (6th Edition), Cyprus chapter; and International Law Office's banking newsletter. She has also written a number of articles on cross-border mergers, *societas europaea* and banking law developments.

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