The pursuit of a company's interest over the life of a company

Corporate Acquisition and Joint Ventures Commission

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National Report of Republic of Cyprus

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Introduction

The typical lifecycle of a company consists of various phases, as for example, startup, growth phase, maturity (mid- to large-size privately held company), IPO and listed phase, and finally the acquisition by another company.

The various stakeholders in a company – understood in a very broad sense including equity holders, debt holders, management, employees, advisors and public – have expectations in the company. According to the stakeholder-value-theory all these expectations of the stakeholders form the company's interest.

Undoubtedly, the expectations of the various stakeholders and, therefore, the company's interest change and develop over the life cycle of the company.

The general report and the working session focus on these changes and developments, how they are reflected resp. influenced by the rules of the various jurisdictions and what the consequences are for us, the legal advisors. For efficiency reasons, the general report is limited to the developments of certain stakeholders' expectations (see A to D in the below matrix)

The following matrix provides an overview of the stakeholders (A to D) and the phases (1 to 5) that are covered by this general report. At the same time it provides an overview of the structure of this questionnaire (chapters A to D, each having sub-chapters 1 to 5). Our goal is to shed light on one or several aspects of a specific stakeholder's interests in each phase so that, as a result, the entire questionnaire provides an overview of the development of the interests of the various stakeholders over the life cycle of the company and, thus, shows the development of the company's interest as such.

	1. Startup	2. Growth	3. Maturity	4. IPO / Listed	5. Acquisition
A. Equity holders	A.1	A.2	A.3	A.4	A.5
B. Debt holders	B.1	B.2	B.3	B.4	B.5

C. Management / Employees	C.1	C.2	C.3	C.4	C.5
D. Lawyers	D.1	D.2	D.3	D.4	D.5

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Interest of equity holders

Start-up phase

In the start-up phase, an entrepreneur or third parties may wish to invest in a business idea as equity holders in a business association. In this context:

In your opinion, what is an entrepreneur's typical reasoning for setting up a specific business association? Attract investments by third parties? Avoidance of personal liability? Tax reasons? Protect IP rights and technology?

Avoidance of personal liability would be the most typical reasoning. Tax reasons would be an important factor usually considered by entrepreneurs given that the corporate tax rate is significantly lower than income tax rates imposed on individuals. Tax planning considerations would also be relevant where the entrepreneur intends to engage in business in other jurisdictions. It should be noted that for certain activities it might be a legal requirement that they are carried out by a legal entity so an entrepreneur might have no choice but setting up a certain type of business association.

What kind of business association structures does your jurisdiction offer to equity holders (e.g., partnerships, corporation, LLC, etc.)? What are the most crucial differences between these business association structures from an equity holder's perspective?

The business association structures typically employed at the start-up phase of a business are the private limited liability company and the partnership. The most crucial difference between them is the liability of members. All members of a company enjoy limited liability. This is not the case in partnerships. In a general partnership all partners have unlimited liability. In a limited partnership one or more general partners have unlimited liability and limited partners are only liable for liabilities up to the amount contributed as capital. Also important is the different tax treatment: companies are subject to income tax at the rate of 12.5% whereas partnerships are deemed as transparent entities and their income is taxed after being allocated to the partners (individuals or legal entities) at the applicable income tax rates.

If statistics on the use of business association structures are available in your jurisdiction: which are the most commonly used business association structures for start-ups? Do you see a particular reason for the dominance of one specific structure?

There are no official statistics on the use of business association structures available. In practice the private limited liability company seems to be the most popular vehicle for the reasons mentioned above.

In case of a corporation or LLC (in the following we simply refer to the "company"): are there any equity instruments other than common shares that are typically used for equity investments? Non-voting shares? Other forms of participation rights?

Ordinary shares are the most commonly used equity instruments at the start-up phase. Non-voting shares or shares carrying qualified voting powers may be used in some cases depending on the circumstances.

Can equity investors remain anonymous (for example by the use of bearer shares)? Anonymous towards the company, other investors, the public? In the event equity investors cannot remain anonymous when holding shares, is there any alternative scheme that can be implemented to participate on an anonymous basis (for example, silent partnership schemes)?

The Companies Law, Cap. 113, as amended (hereinafter Cap.113) requires registration of shareholders (i.e. the equity investors) in the register of members of the company and does not permit the issue of bearer shares. The registered shareholders of a private limited liability company are notified to the Registrar of Companies and Official Receiver and their names are publicly available. The same applies for any transfers of shares whereby the details of the transferee are notified to the Registrar of Companies. Anonymity towards the company, the public and other investors may be achieved by the use of nominee or trust arrangements whereby the registered owner holds the shares in the company for the benefit of a beneficiary and, depending on the provisions of the trust deed or instrument, may act on such persons' instructions.

Once the entrepreneur has set up a company: what could be a typical focus of third party equity investors when they invest in a company in this phase?

A third party making an equity investment in a start-up company would typically focus on return on investment and the non-dilution of interest in a future equity injection. Third parties being business associates might have particular interest in the establishment of a long term relationship and long-term return on investment.

What could typically be the friends', family's and fools' ("FFF") focus? Helping the entrepreneur to get his/her business going?

The focus of FFF would most likely be helping the entrepreneur to get his/her business going. However, the activities and potential they see in the business could differentiate their focus and the interests they might want to protect.

What could typically be the professional investor's focus?

The professional investor would focus primarily on return on investment at a latest stage of the company's life (possibly long-term return on investment). Also one would expect professional investors to have concerns relevant to the control of the company. They are likely to aim in securing power or control on certain matters e.g. investments or expenditure above a certain amount, certain decisions on the business direction of the company etc. through veto powers, qualified voting etc..

If there is a difference in focus among the various equity investors, how is this typically reflected in the legal relationship (be it corporate or contract law)? Are there legal instruments that are only used by certain investors (e.g., only by professional investors)?

The interests of investors are likely to be reflected in a shareholders' agreement the terms of which are regularly incorporated into the constitutional documents of the company. Professional investors are more likely to require the adoption of more complicated and detailed provisions or arrangements to be included in such documents. In the case of start-ups with non-professional investors the relationship will often be governed by the typical provisions employed in constitutional documents of private limited liability companies. The use of shareholders' agreements and tailored constitutional documents is not usual yet in such cases the degree of complexity and the detail employed is not the same as in the case of professional investors. No single type of legal instruments is used exclusively by certain types of investors. Yet instruments such as redeemable preference shares are typically used by investors with experience.

Growth phase

In the start-up phase a business idea comes into existence: the idea is put into a business plan, a company is set up, first steps relating to production, service, distribution, sales etc. are made. The growth phase allows potential new investors to better assess not only the viability of business idea, but also the commitment of the people involved. In this phase, the new investors are usually not FFF, but professional investors. As a result, the FFF who invested in the start-up phase are faced with more demanding and skilled potential new co-investors. Against this background:

In your opinion, does the focus of the equity holders (e.g., the FFF or professional investors) shift in the growth phase (as compared to the start-up phase)?

They are more likely to wish to obtain or maintain involvement in the management of the company.

If so, what could be a particular focus for equity holders in the growth phase? Protection from dilution?

Ensuring capable management of the company and the right to participate in the decision making would be the focus of equity holders in the growth phase. Added to this protection from dilution would become a major concern for equity holders.

In your experience, do the equity investors from the start-up phase participate in further capital rounds in the growth phase? Do they usually accept dilution? Do they usually cash out at this point in time?

The participation of equity investors from the start-up phase in further capital rounds in the growth phase depends on the circumstances and in particular the performance of the company. Professional investors are less likely to accept dilution at this stage if the company's performance is good and they have started experiencing some return on their investment.

In your jurisdiction, does the company law provide existing equity holders protection from being diluted in further financing rounds in the growth phase? If so, how are they protected? Is there a need for equity holders to seek protection on a contractual basis?

Company law does not protect by statute against dilution of existing equity holders except in the case of public limited liability companies. In those cases respect of pre-emption rights on allotment of new shares is mandatory. The public company is not a vehicle usually used at this phase of the company lifecycle. Protection against dilution is achieved by the adoption of relevant pre-emption right provisions in the constitutional documents (deemed as the "statutory contract"). Moreover pre-emption rights would often be secured contractually in shareholders' agreements.

When new potential investors offer to come on board during the growth phase, the existing equity holders may be reluctant to provide the information required to satisfy the potential new investor's need for valuation. The reason for the existing shareholders' reluctance may be, for example, that the required information contains (still) unprotected intellectual concepts, knowledge or ideas. In your experience, which legal instruments are used to find a balance between the potential new investor's need for information and the existing equity holders' wish to keep such information confidential? Do existing equity holders have legal means to prevent management from disclosing such information?

Confidentiality and non-disclosure agreements are the main instruments used to govern the disclosure of information to potential investors. The provisions of such agreements aim to strike a balance between the need of the potential investor to receive information for purposes of evaluation and the need of the company (and existing equity holders) to keep information confidential. Existing equity holders do not have the legal means to prevent management from disclosing such information, except if the constitutional documents of the company do not permit such disclosures by the management without a relevant prior decision or the consent of the general meeting. It should be noted however that the employment contracts of the management might prohibit such disclosures or subject them to prior decision of the board of directors.

Maturity

During the various capital rounds in the growth phase, the circle of equity investors in a company typically becomes larger and the atmosphere may become less familiar. Also, in the maturity phase the management of the company may become more professional in the sense that there is a management in place which is not, or not significantly, invested in the company (i.e., intensification of the principal-agent-conflict). As a consequence, legal concepts that govern the relationship between equity holders (such as fiduciary duties of majority equity holders) as well as legal concepts that govern the relationship between management and equity holders (such as fiduciary duties of the members of the board of directors e.g. duty of loyalty, principle of equal treatment) may become more important. In other words, corporate governance may become more important. Against this background:

In your opinion, how does the equity holder base change between the start-up phase, the growth phase and the maturity phase? How does the focus of the equity holders change? Focus on fair distributions of earnings?

Focus on fair distributions of earnings would be the main aim of equity holders entering during this phase. It would be anticipated that such investors would be less interested in exercising control except if they enter the company with a noteworthy participation percentage. In such case it would be expected that they would also focus on control of the body that appoints the management (board of directors of the company).

In your jurisdiction, does the law provide for stricter corporate governance rules for large (privately-held) companies as compared to small companies? If so, what exactly triggers the application of the stricter corporate governance rules? In which sense are the corporate governance rules different / stricter?

There is no distinction on corporate governance rules between large (privately-held) companies and small companies.

In your jurisdiction, do (certain) equity holders (e.g., majority shareholders) have obligations towards (certain) other shareholders or the company (e.g., duty of loyalty)? Please explain such obligations.

Cap. 113 does not set-out specific obligations or duties owned by majority shareholders towards other shareholders. Obligations and duties may, however, derive from the articles of association if relevant provisions were adopted.

Minority shareholders may choose to make use of what is known as the "alternative remedy" in cases where the behaviour of the controlling majority is oppressive to them. A member of a company who complains that the affairs of the company are conducted in a manner oppressive to some part of the members (including itself) may apply to Court for an order. If the Court is of the opinion that the company's affairs are being conducted as aforesaid and that to wind up the company would unfairly prejudice that part of the members, but otherwise the facts would justify the making of a winding-up order on the ground that it was just and equitable that the company should be wound up, the Court may, with a view to bringing to an end the matters complained of, make such order as it thinks fit[1]. The order may be for regulating the conduct of the company's affairs in the future or for the purchase of the shares of any members of the company by other members of the company or by the company and, in the case of a purchase by the company, for the reduction accordingly of the company's capital, or otherwise.

It is not easy to prove that the affairs of the company are conducted in a manner oppressive on the minority. Certain behaviour that in one context might not constitute oppression in another it might indeed be deemed as the ground for a finding of oppression. Orders under this remedy were issued in cases such as dilution of minority shareholders, dismissals of minority shareholders from the board of directors, misappropriation of company's assets for the benefit of a majority shareholder etc.

Does the company have any means to control the circle of its equity holders (i.e., can the articles of incorporation prevent competitors from holding shares in the company?) or have such restrictions to be agreed among the other equity holders (e.g., shareholders' agreement)?

As a general observation it should be noted that in private companies there are restrictions in the transferability of shares. The effect of such restrictions pause some limits on the circle of equity holders. Further restrictions relating to the circle of equity holders may be adopted in shareholders' agreements. It is rare that provisions are included in articles of association that would prevent or prohibit the acceptance of a competitor as shareholder. It is more likely that such provisions would be encountered in shareholders' agreements. It is noted however that it is typical that articles of association provide that the board of directors has the power to refuse to register a transfer of shares if it deems (at its discretion) that such transfer would not be in the best interests of the company. Such

[1] Section 203 of Cap. 113.

provision could arguably be employed to prevent certain persons from holding shares in the company. The enforceability of such provisions does not seem to have been judicially tested as regards competitors.

IPO / Listed phase

Following the IPO, a company enters into a new phase of being listed. The listing has potentially a great influence on the equity holder: the sale of their interest becomes easier. Against this background:

How does the focus of the shareholders change through the going public as compared to the maturity phase? Does the fact that a shareholder may at any time sell the residual value in its share (ideally) at a fair price in your opinion soften the focus on distribution of earnings? Does the focus shift from long term to short term?

In reality the change of focus would depend on the liquidity of the market and the demand. At times at which there is a liquid market the focus on distribution of earnings is softened and less long-term objectives might be pursued. However, where there is little demand for the shares and there is considerable deviation between the net asset value of the share and the market value then the focus of equity shareholders is expected to remain on the distribution of earnings. This has been experienced by a number of listed companies in the Republic of Cyprus over the current economic crisis.

In your jurisdiction, are there publicly available records on the identity of (certain of) the shareholders in a listed company? If so, does this in your opinion influence the shareholders' focus?

Listed companies (like private companies) are obliged to submit to the Registrar of Companies and Official Receiver an annual return with a list of all of their shareholders as at the last day of the period to which the said return relates to. Such return is available for public inspection.

The identity of shareholders holding certain percentage of the total voting rights of the issuer is to be disclosed by the listed company ("the issuer") pursuant to the Transparency Requirements (Securities Admitted to Trading on a regulated Market) Law of 2007, Law

N.190(I)/2007, as amended (hereinafter Law N.190(I)/2007)[2] if the shares to which voting rights are attached to are admitted to trading in a regulated market. Pursuant to section 28 a shareholder is obliged to notify the issuer and the Cyprus and Securities and Exchange Commission (hereinafter CySEC) of the percentage of voting rights held where as a result of an acquisition or a disposal the percentage, in the case of acquisition reaches or exceeds or in the case of disposal reaches or falls below the thresholds of five percent (5%), or ten percent (10%), or fifteen percent (15%), or twenty percent (20%), or twenty five percent (25%), or thirty percent (30%), or fifty percent (50%) or seventy five percent (75%) of the total voting rights of the issuer[3]. The issuer is obliged to disclose all information contained in such notification as soon as possible and not before the next working day following the receipt. Such information must be published on the regulated market and on the website of the issuer.

The public availability of information as to the identity shareholders and the changes in the holdings of shareholders may influence the shareholders' focus. For example they might choose to follow the example of an institutional shareholder and dispose shares. The importance of availability of information as to the identity of shareholders should be understood against the background that this jurisdiction is a small one and a stock exchange boom followed by a crash was experienced between the years 1999-2003. This has contributed in reputation becoming an important element for consideration when people make investment decisions.

An efficient allocation of resources requires a most accurate pricing of the shares.

In this regard, are companies that are listed in your jurisdiction under an obligation to publish price-relevant information (ad hoc publicity)? If so, please provide a short overview of the respective rules including the exemptions from such obligation.

Law N.190(I)/2007 requires listed companies to disclose the following potentially price-sensitive facts or events:

[2] The said legislation transposed the Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC and Articles 2, 5, 9 and 11 of the act of the European Community titled "Commission Directive 2007/14/EC of 8 March 2007 laying down detailed rules for the implementation of certain provisions of Directive 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market.

[3] This general rule is not applicable in certain special cases set out in section 29 of Law N.190(I)/2007.

a. the acquisition or disposal of its own share either by itself or through a person acting in its own name but on the issuer's behalf where that reaches or exceeds the thresholds of five percent (5%) or ten percent (10 %) of the total voting rights, in the case of an acquisition or reaches or falls below the thresholds of five percent (5%) or ten percent (10%) of the total voting rights, in the case of a disposal[4],

b. the total number of voting rights and capital at the end of each calendar month during which an increase or decrease of such total number has occurred[5],

c. every draft proposal for the amendment of its memorandum of association or articles of association and the date of a general meeting convened to examine any such proposal[6],

d. any change in the rights attaching to the various classes of shares, including changes in the rights attaching to derivative securities issued by the issuer and giving access to the shares of that issuer[7],

e. any new loan issues, with reference to terms and any guarantee or security in respect thereof[8],

f. the notification received by a significant shareholder of acquisitions or disposals of shares (to which voting rights are attached) that due to acquisitions or due to disposals the thresholds of 5%, 10%, 15%, 20%, 25%, 30%, 50% or 75% have been exceeded or fallen below (see below for applicable exceptions)[9].

The general rule on disclosure of acquisitions or disposals of shares to which voting rights are attached to above or below the specified thresholds does not apply in the following cases:

a. shares acquired for the sole purpose of clearing and settling of transactions at the latest of three working days following the transaction,

[4] Section 17 of Law N.190(I)/2007.
[5] Section 18 of Law N.190(I)/2007.
[6] Section 20 of Law N.190(I)/2007.
[7] Section 21 of Law N.190(I)/2007.
[8] Section 22 of Law N.190(I)/2007.
[9] Sections 19 and 28 of Law N.190(I)/2007.

b. a custodian holding shares in its custodian capacity, provided that the custodian can only exercise the voting rights attached to such shares under instructions given in writing or by electronic means by the beneficiary of the shares,

c. an acquisition or disposal of voting rights by a market maker, that reaches or crosses the 5% threshold of the total voting rights of the issuer, provided that the market maker acts in its capacity as a market maker and in accordance with the provisions of applicable legislation and neither intervenes in the management of the issuer concerned nor exerts any influence on the issuer to buy such shares or back the share price,

d. shares of an issuer, which are held in the trading book of a credit institution or an investment firm, in accordance with applicable legislation,

e. shares provided to or by the members of the European System of Central Banks in carrying out their functions as monetary authorities, including shares provided to or by members of the European System of Central Banks under a pledge or repurchase or similar agreement for liquidity granted for monetary policy purposes or within a payment system, provided that the transactions last for a short period and that the voting rights attaching to such shares are not exercised.

It can be assumed that no jurisdiction requires listed companies to publish all price sensitive information. If this is correct in your jurisdiction, how does the law protect the market and its participants (including, the equity holders in the company) from market abuse? Are there insider trading and market manipulation prohibitions? If so, please provide a short overview and, if you can, provide certain peculiarities about them?

The market and its participants are given protection through insider dealing and market manipulation prohibitions applicable pursuant to the Insider Dealing and Market Manipulation (Market Abuse) Law of 2005, Law N.116(I)/2005, as amended (hereinafter Law N.116(I)/2005)[10].

[10] This legislation transposed Directive 2003/6/EC of the European Parliament and of the Council of 28 January 2003 on insider dealing and market manipulation (market abuse), Commission Directive 2003/124/EC of 22 December 2003 implementing Directive 2003/6/EC of the European Parliament and of the Council as regards the definition and public disclosure of inside information and the definition of market manipulation", Commission Directive 2003/125/EC of 22 December 2003 implementing Directive 2003/6/EC of the European Parliament and of the Council as regards the fair presentation of investment recommendations and the disclosure of conflicts of interest", Commission Directive 2004/72/EC of 29 April 2004 implementing Directive 2003/6/EC of the European Parliament and of the Council as regards accepted market practices, the definition of inside information in relation to derivatives on commodities, the drawing up of lists of insiders, the notification of managers' transactions and the notification of suspicious transactions

The said law prohibits certain acts by the possessor of inside information. These are as follows:

a. the use of inside information by acquiring or disposing of, or by trying to acquire or dispose of, for their own account or for the account of third parties, or through persons closely associated to them, either directly or indirectly, financial instruments to which that information relates to,

b. the disclosure of inside information to any other person, unless such disclosure is made in the normal course of the exercise of their employment, profession or duties,

c. the recommendation to or inducement of another person, on the basis of inside information, to acquire or dispose of financial instruments to which that information relates, irrespective of whether or not the other person knew that information.

Administrative and criminal sanctions are provided for violations of the above prohibition.

Further Law N.116(I)/2005 imposes certain obligations on issuers whose financial instruments are admitted to trading on a regulated market or for which request admission to trading on a regulated market. These include:

a. publication as soon as possible of inside information which directly concerns them and posting and maintaining it on their website (if any) for 5 years,

b. the non-combination of insider information with commercial promotion of their activities in a misleading way,

c. publication of confidential information which either they or a person acting on their account or on their behalf, disclose to a third party in the normal course of their professional or duties,

d. publication of any significant changes concerning already publicly disclosed inside information after these changes occur, through the same channel as the one used for the public disclosure of the original information,

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and issued for the purposes of application of the action of the European Community titled Commission Regulation (EC) No 2273/2003 of 22 December 2003 implementing Directive 2003/6/EC of the European Parliament and of the Council as regards exemptions for buy-back programmes and stabilisation of financial instruments.

e. synchronisation as closely as possible of publications in the Republic of Cyprus between all categories of investors.

Law N.116(I)/2005 imposes obligations for publication of transactions of persons discharging managerial responsibilities and persons closely related to them that relate to financial instruments of the issuer. In addition publication requirements are imposed on a shareholder who owns directly or indirectly, a percentage of more than five per cent (5%) of the share capital or the voting rights of the issuer who must publicize a transaction where, as a result of the said transaction, his holding's percentage in case of an acquisition, reaches or exceeds, or in case of a disposal, reaches or falls below, the threshold of 6%, 7%, 8%, 9%, 10% and every one per cent (1%) following that until a hundred per cent (100%) of the share capital or the voting rights of the issuer. This obligation is differentiated from the obligation under Law N.190(I)/2007 mentioned above as to (i) the person obliged to make the publication (in this case it is the shareholder not the issuer), (ii) the subject matter (in this case it is not just voting rights but also the capital) and (iii) the levels of the thresholds.

Market manipulation in the form of the following acts is prohibited:

a. transactions or orders to trade which give, or are likely to give, false or misleading signals as to the supply of, the demand for or the price of financial instruments, or which secure, by a person, or persons acting in collaboration, the price of one or several financial instruments at an abnormal or artificial level except if its proved that they were entered into for legitimate reasons and that these transactions or orders to trade conform to accepted market practices on the regulated market concerned,

b. transactions or orders to trade which employ fictitious devices or any other form of deception or contrivance,

c. dissemination of information through the media, including the internet or any other electronic means, or the dissemination of information in any other manner which gives or is intended to give false or misleading signals as to financial instruments, including the dissemination of rumours and false or misleading news, where the person who made the dissemination knew, or ought to have known, that the information was false or misleading.

Administrative and criminal sanctions are provided for violations of the above prohibition. Additionally civil liability for compensation to anyone who suffers damage or loss of profit or both which arose as a result of an act or omission in violation of the obligations imposed by Law N.116(I)/2005 may arise.

Acquisition

In its life cycle, the company may itself become the object of an acquisition and integration into the acquirer's structure. At this point the life cycle of the company ends. For the purpose of the remainder of this questionnaire, we assume the acquirer proceeds via a public tender offer. Against this background:

In case a listed company (target) is approached by another company (bidder), the board of the target will have to decide whether it supports the offer (friendly offer) or not (unfriendly offer). What are the interests that the board of directors needs to take into consideration for this decision? Shareholders' interests only (e.g., offer price only)? The interests of other stakeholders (employees, community etc.)?

One of the general principles governing every bid that falls within the scope of the Takeover Bids Law of 2007, Law N.41(I)/2007, as amended (hereinafter Law N.41(I)/2007)[11] is that the board of directors of the target must act in the interests of the company as a whole. Further it must not deny the holders of securities the opportunity to decide on the merits of the bid and it must not act in a manner that frustrates the successful outcome of the bid[12]. These principles focus on the interests of the shareholders.

The said law imposes an obligation on the board of directors to draw up and make public a document setting out its opinion on the bid (or the revised or competing bid if any) and the reasons on which such opinion is based. This must include the views of the board of directors on the effects of implementation of the bid on all of the company's interests and specifically on employment, as well as on the bidder's strategic plans for the target (as they are set out on the offer documents) and the possible repercussions of such plans on employment and the locations of the company's places of business[13].

The said law does not impose a positive obligation on the board of directors to consider any interests of stakeholders (other than the shareholders). However the fact that there is

[11] This legislation transposed Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids.

[12] Section 5(d) of Law N.41(I)/2007.

[13] Section 33(2) of Law N.41(I)/2007.

an obligation that the document setting out the opinion of the board of directors includes also the views of the board of directors on employment and the consequences of the bidder's strategic plans on employment implies that the interests of employees and the place of business of the target are also to be taken into consideration.

In case of an acquisition of the listed company (target) by another company (bidder), the shareholders' are at a disadvantage as they cannot communicate efficiently or act in concert (for example, regarding the rejection of a low offer). A rational bidder should try to use this disadvantage of the shareholders to his benefit. In your jurisdiction, how does the law protect shareholders of the target in case of public tender offers? (for example, is there a specific process for public takeover offers which provides protection? Does the bidder need to treat target shareholders equally? Are there, for example, minimum price rules and/or best price rules?)

Generally the possibility of and opportunity for communication between shareholders and/or the concerted actions by shareholders in listed companies depends very much on the level of dispersion of ownership and the percentages of the holdings. One may observe that in most listed companies in this jurisdiction there are shareholders with shareholdings of more than 5%. These conditions may potentially facilitate the above practices. Notably communication and concerted actions in times of bids have been witnessed in the past. The small size of the Republic of Cyprus and the fact that shareholders or players in the market often have connections with each other are conceivable explanations for these practices.

Several provisions of Law N.41(I)/2007 offer protection of the shareholders. The mechanisms employed thereunder are diverse. There is a set of statutorily imposed general principles to which the bidder and the target must abide to. These are as follows:

a. all holders of securities of a target which are of the same class must be afforded equal treatment; moreover, if a person acquires control of a company, the other holders of securities must be protected,

b. the holders of securities of a target must have sufficient time and information to reach a properly informed decision on the bid,

c. where it advises the holders of securities, the board of directors of the target must give its views on the effects of implementation of the bid on employment, conditions of employment and the locations of the company's places of business,

d. the board directors of a target must act in the interests of the company as a whole and must not deny the holders of securities the opportunity to decide on the merits of the bid and must not act in a manner that frustrates the successful outcome of a bid,

e. false markets in the securities of the target, of the bidder company or of any other company concerned by the bid must not be created in such a manner that the rise or fall of the prices of the securities becomes artificial and the normal functioning of the markets is distorted,

f. before announcing the bid, the bidder must ensure that he/she can fulfil in full any cash consideration, if such is offered, and secure the approval of the general meeting of its shareholders for the issuing or allotment of securities, if such are to be offered as consideration,

g. the conduct of the business of the target must not be hindered by the bid for longer than it is reasonable,

h. where the target has different classes of shares and/or has issued transferable securities that can be converted into shares, the bidder must make separate bids, one for every class of shares, which must be comparably identical, and separate bids, one for every class of transferable securities that can be converted into shares, which again must be comparably identical with the bid or bids expressed for the securities.

Most of the above general principles are substantiated and elaborated in further provisions that address specific matters. Further protection than the general principle set out in paragraph f. above is given by the obligation of the bidder to support the offer with a confirmation by one or more credit institutions or other organizations having the necessary solvency that the cash which the bidder will be called to pay to the recipients at the expiration of the bid is available and will remain available in such credit institution or organization until the day of its payment. An analogous confirmation must in addition be issued by the board of directors[14]. These confirmations should be submitted together with the offer document (that is subject to approval) to the competent authority i.e. CySEC.

Protection to shareholders (as a whole) is also given by virtue of certain prohibitions applicable to trading and other actions[15]. As regards persons who possess information

[14] Section 17 of Law N.41(I)/2007.

[15] Section 25 of Law N.41(I)/2007.

concerning the bid or a potential bid the prohibitions of Law N.116(I)/2005 are made applicable mutatis mutandis. The sale of securities in the target during the period of acceptance of the takeover offer by the bidder and the persons acting in concert with him/her is prohibited. The acquisition of securities subject to the bid by the bidder, other persons acting in their own name but on behalf of the bidder, controlled undertakings and persons acting in concert with him/her is prohibited during the period of a partial bid. When a bid is contemplated, including the period prior to the announcement until the expiration of the period for acceptance, the bidder and persons acting in concert with the bidder may not:

a. make any arrangements with shareholders of the target,

b. enter into arrangements with persons who although not shareholders of the target, nevertheless acquire voting rights in the target,

c. deal or enter into arrangements which involve the trading in securities of the target,

d. enter into arrangements which involve acceptance of a bid, if there are favourable conditions attached which are not being extended to all the shareholders of the target,

if there are favourable conditions attached to such arrangements which are not being extended to all the shareholders of the target, except if the bidder revises the bid.

The obligation of publication of trading, the procurement of an irrevocable commitment or letter of intent[16] or the non-compliance with the terms of such commitment or letter is an indirect form of protection as it allows the shareholders to make a properly informed decision taking into consideration such facts[17]. The bidder, any other person holding a percentage of five per cent (5%) or more of the voting rights of the target or the bidder, must announce immediately every acquisition of securities of these companies by themselves, persons acting in their own name but on their behalf or in concert with them, by controlled undertakings, as well as the acquisition price and any voting rights already held in that company. Also any person acquiring a percentage equal to half per cent (0,5%) or greater of the voting rights of the target or the bidder must make an announcement for such acquisition, as well as every subsequent acquisition of securities in such companies, by

[16] I.e. a written or oral commitment to accept the takeover bid or vote in favour of a resolution in the context of the bid.
[17] Section 26 of Law N.41(I)/2007.

himself, persons acting in their own name on his behalf or in concert with him or by his controlled undertakings, as well as the acquisition price and any voting rights already held in that company. An announcement of a procurement of an irrevocable commitment or letter of intent by the bidder, the target or the persons acting in concert with them must include information on the number of the securities and their percentage on the capital of the company, the identity of the person making the procurement and any conditions to which such irrevocable commitment or letter of intent is subject to. Also there is an obligation to announce the non-compliance with the terms of such commitment or letter and to notify the bidder or the target (depending on the case) as well as CySEC.

The prohibition of revocation or cancellation of the bid once made publicly known - except where specified circumstances apply - is a primary source of protection for the shareholders[18]. The exceptional circumstances are as follows:

a. the making of a competing bid,

b. when the consideration offered to the recipients of the bid consists of securities, the inability to admit these securities on a regulated market,

c. the non-fulfilment of any precondition mentioned in the offer document and approved by CySEC to which the bid is subjected to and in particular the necessary approval by virtue of the relevant legislation in force regulating the protection from competition,

d. not receiving the stated percentages of acceptance,

e. the existence of unforeseen and extraordinary circumstances (other than the economic inability of the bidder), as a result of which the bid may not be materialized, for reasons irrelevant to the will of the parties to the bid, as long as these circumstances are recognised by a decision of CySEC.

Protection of the shareholders relevant to the revision as well as the automatic revision of the bid. A revision of the takeover bid is allowed only with the purpose of improving it[19]. An automatic revision is provided for where during the period of the bid the bidder, other persons acting in their own name on behalf of the bidder, controlled undertakings or

[18] Section 27 of Law N.41(I)/2007.
[19] Section 28 of Law N.41(I)/2007.

persons acting in concert with the bidder acquire securities subject to the bid with terms more favourable than the ones contained in the offer document or in any revision of the bid; the more favourable terms becoming valid for all the recipients of the bid[20].

Further protection is given to shareholders of the target company in the form of a sell-out right that may be exercised within three months from the end of the deadline set for acceptance of the bid. Such right exists only where the bidder holds securities in the target representing not less than ninety per cent (90 %) of the capital carrying voting rights and not less than ninety per cent (90 %) of the voting rights in the target or where the bidder holds or has irrevocably agreed to acquire, following the acceptance of a bid, securities in the target representing not less than ninety per cent (90 %) of the capital carrying voting rights and not less than ninety per cent (90 %) of the voting rights included in the bid.

As regards the price to be offered as consideration for the securities subject to the bid, Law N.41(I)/2007 imposes a minimum offer price rule. Such consideration must be equal at least to the highest price paid or agreed to be paid for the same securities by the bidder or by persons acting in concert with him/her, during the last twelve months prior to the announcement of the bid. Discretion is given to CySEC to allow a lower price in the case of a voluntary bid[21].

The legal obligation of the board of directors to provide the shareholders with their opinion on the bid may also be seen (depending on the circumstances) as a source of protection given that directors being insiders have a better understanding of the affairs and potential of the target company[22]. Added to this the obligation of the board of directors of the target to provide quick and accurate information to its shareholders relating to the content of the bid, any information about material changes in information previously announced or published, any revision or revocation of the bid, any competing bids submitted, the result of the bid, the views of the board of directors as well as those of special experts on the bid or the revised or the competing bid and anything else on the bid and every document or information made public according to the law is a further protection mechanism that contributes to aim of enabling the shareholder to make a properly informed decision on the bid[23].

[20] Section 29 of Law N.41(I)/2007.

[21] Section 18 of Law N.41(I)/2007.

[22] See the previous section for an analysis on this matter.

[23] Section 33(1) of Law N.41(I)/2007.

As mentioned above, a listing provides (ideally) liquidity for the company's shares and ensures a high level of information for a potential new investor. In fact, equity investors may invest in listed companies exactly for these reasons. In your jurisdiction, how is an equity investor protected from a delisting? Does the delisting require (qualified) shareholder consent? What are the deadlines for the delisting? Do issuers need to provide for an off-exchange trading for a certain period following delisting?

Currently the delisting of the securities of a company from the Cyprus Stock Exchange (hereinafter CSE) may occur only in specific circumstances. These are as follows:

a. The delisting of securities may be decided by the Council of CSE where due to special circumstances, the conditions for the smooth operation of the stock market as regards the securities of the issuer no longer exist and in particular where material listing conditions cease to exist or where significant ongoing or periodical obligations are not observed, placing at risk the interests of investors or the proper operation of the market[24]. Such decision must be approved by CySEC. In such scenario the involvement of CySEC and the Council of CSE offer some assurance as regards investor protection.

b. Further to the above situation securities listed on regulated/organised markets may be delisted from CSE upon a decision of the Council of CSE, which is taken at its own initiative or upon the issuer's application, provided it is approved by CySEC. The powers of the Council of CSE in this case are wider than in the case set-out in paragraph a. above. Yet in any event the approval of CySEC is required. It must be observed that on this ground the issuer may request the delisting, but it is at the discretion of the Council of CSE whether it will proceed with a relevant decision to be taken to CySEC for approval. This ground does not give a right to the issuer to effect or conclude the delisting but only to request it.

c. Securities listed on a non-regulated/non-organised markets of CSE may be delisted upon a decision of the Council of CSE where it is observed that the issuer does not fulfil the listing requirements or violates any of its obligations such as the suspension of trading remains for a period longer than six months, the issuer presents a negative net worth for the last three years without measures being taken to reinforce its capital or it has no nominated advisor for a period longer than six months.

[24] Section 178(1) of the Cyprus Securities and Stock Exchange Law of 1993 as amended.

d. Securities listed in non-regulated/non-organised markets of CSE may be delisted upon the request of the issuer following a special resolution of the general meeting of the shareholders which has been approved by 90% of the capital represented in the meeting and after the lapse of a time period of six months or any other greater time period which the Council of CSE shall specify after the publication of the relevant application. The imposition of a high yardstick set at 90% is a protection mechanism for investors. Added to this the six month minimum period before the delisting is actually effected provides some added protection as the decision does not have an immediate effect.

It is important to highlight that it does not seem to be possible at the moment that an issuer whose securities are listed in a regulated market requests delisting following a decision of its general meeting without a prerequisite decision of the Council of CSE and approval of such decision by CySEC. The Cyprus Securities and Stock Exchange Law of 1993, Law N.14(I)/1993, as amended (hereinafter Law N.14(I)/1993) provides that CySEC may regulate the circumstances under which this may occur, the procedure as well as the conditions to be met in directives (i.e. pieces of subsidiary legislation). At the time of writing this report no such directive was in place[25]. However, CySEC was working on drafting relevant subsidiary legislation that would regulate, amongst others, delisting and relevant matters.

Currently neither Law N.14(I)/1993 nor any relevant subsidiary legislation provides for off-exchange trading for any period following delisting. Off exchange trading provisions might be considered in the context of the subsidiary legislation mentioned above that is under preparation.

Interest of debt holders

Start-up phase

[25] Section 181 of Law N.14(I)/1993.

In the start-up phase, the entrepreneur may ask the so called "FFF" (friends, family and fools) for a loan. In other words the entrepreneur asks them to invest in a business idea as debt holders. In this context:

In your experience, what could be the typical focus of the FFF in this phase? Helping the entrepreneur to get his/her business going? How is this focus reflected in the legal relationship? For example, will such debt holders be likely to refrain from asking for security? Is the agreed interest rate likely to correctly reflect the risks for the debt investor?

The focus of FFF is to help the entrepreneur to get his business going through the means of a loan. Such arrangements are likely to be reflected in loan agreements, promissory notes or bonds of customary form or not. Whether FFF would take security for the loan in the form of a pledge, personal guarantee, fixed or floating charge over assets of the company would depend on the amount of the loan and on the sophistication of the FFF. In most of the cases terms of the loans granted by FFF at this stage do not reflect the risks.

In your experience, is it common for professional investors to act as debt holders in this phase? If so, how is the different focus of professional investors typically reflected in the legal relationship? What are the legal instruments commonly used in your jurisdiction to protect their interests? For example, is it common for the professional investors to request a personal security by the entrepreneur in case the company does not yet have (a lot of) assets to secure a loan?

It is possible that professional investors act as debt holders at the start-up phase in certain though not very common. As a rule such relationship is reflected in contractual and other arrangements which are very likely to be supported by security e.g. personal guarantee or security e.g. mortgages of immovable property of the entrepreneur. Instruments such as debentures secured by floating charges over assets of the company or bonds are employed for the benefit of professional investors. Also pledges of shares or other assets held by the entrepreneur and charges over assets of the company (fixed or floating) are also options employed by professional investors.

Growth phase

In your experience, who provides debt in this phase and what could typically be their focus (e.g., high return on investment)?

Provision of debt in the growth phase is more likely to come from credit institutions or other professional investors who focus on high return on investment.

Are the debt holders and their focus in the growth phase typically different from the ones in the start-up phase? Is it now mostly professional investors (and no FFF)?

Debt holders in the growth phase would more likely be credit institutions or other professional investors. Their focus would be on the ability of the company to make repayment and the relevant timeframe for such repayment. Ultimately they aim to ensure return on their investment i.e. capital and interest.

If there is a difference, how could this be reflected in the contractual relationship? For example, do the interest rates or the security for the debt change?

Where professional investors provide debt in the growth phase the relationship would be reflected in contractual arrangements similar to those they would employ in the start-up phase. The same applies for any security for such debt. Depending on evidence of the performance of the company at the early stages and availability of information enabling the investor to assess the prospects and risks, the interest rates might be set at a lower rate.

What kind of security is commonly requested by debt holders in this phase? For example, rather collateral (pledge, etc.) or personal guarantees by the entrepreneur? What is the reason for the preference of a specific kind of security?

Personal guarantees or mortgage of immovable property belonging to the entrepreneur would still be a security commonly required for debt taken by the company. Pledging of shares and issuing of debentures with a floating charge over assets of the company are other forms of security that might be requested though not as common as personal guarantees.

During the growth phase, the burn rate of the company may be quite high and the company may continuously be at the verge of over-indebtedness. Will investors usually be willing to subordinate their debt?

Usually only the entrepreneur / FFF from the start-up phase or also professional investors?

Professional investors are not likely to accept subordination of debt easily; subordination of the debt owed to FFF or the entrepreneur himself seems to be more probable.

Investors providing debt in this phase may wish to keep the possibility to participate in the potential valuation upside. How could this wish be accommodated in your jurisdiction? For example, are profit-participating loans or convertible loans commonly used instruments?

Convertible bonds are instruments that may be used. Depending on the terms adopted conversion might be made at the option of the investor upon an event of default happening or at any time during which an amount is due to him. Alternatively a contractual arrangement might be made entitling the investor to require the allotment of shares in his name for the set-off of an amount owed by the company. At the same time such arrangements are expected to provide contractual obligations on the company to proceed with the issue of shares.

Maturity

After having reached maturity, the structure of debt holders may change fundamentally. Against this background:

In your jurisdiction, who is usually the debt holder in the maturity phase (e.g., banks)?

Mostly credit institutions and other professional investors.

Are the debt holders and their focus in the maturity phase typically different from the ones in the start-up or growth phase?

The focus seems to be mainly the same as in the growth phase though the terms of the debts might differ (e.g. timeframes and interest rates). For example they may aim in return on investment in a more short term basis.

If there is a difference, how may this be reflected in the contractual relationship?

It would be expected that the provisions governing debts would take predominantly the same form as in the growth phase but the timeframes, interest rates etc. would differ.

Before providing debt to a company, the potential debt holder may require information about the company's financial status to assess the default risk. What financial information is publicly available for potential new investors who wish to invest in a privately-held company? Are financial statements available from public registers? Excerpt from the debt enforcement register? Tax returns? Do companies have means to influence the amount of publicly available financial information?

Audited financial statements should be filed yearly to the Registrar of Companies and Official Receiver together with the annual return of the company to be included in the company's file which can be inspected by the public. This applies to private and public companies.

Public companies whose shares are admitted to trading on regulated markets are obliged to make disclosures of their annual financial report (i.e. annual financial statements, management report and statements by the members of the board of directors, the chief executive officer or a person performing equivalent duties and the chief financial officer), half-yearly financial report, interim management statements (with explanations of material events and transactions that took place during the relevant period and their impact on the financial position of the issuer and a general description of the financial position and performance of the issuer and its controlled undertakings during the relevant period), indicative results and in some cases quarterly reports as part of the on-going listing requirements they have to comply with.

The above constitute legal requirements the object of which is the availability of financial information relevant to a company to investors. Companies may choose should they wish to make publicly available further financial information at their own initiative.

Currently there is no debt enforcement register but information about companies may be obtained at a cost from credit bureaus. Such agencies would gather publicly available information as well as information from market participants (suppliers, associates, competitors etc.). The credit institutions maintain through their association a credit bureau which they use to obtain information.

Tax returns of companies (whether private or public) are not publicly available.

In your jurisdiction, is it common for privately-held companies to issue notes? Could you provide a short overview of the requirements and the procedure relating to the issuance of notes? Is the focus of note-holders any different from other debt holders?

It is not common for private companies to issue notes. Where notes are issued they are usually for rather short-term borrowings compared to borrowings though other forms of debt securities. Provided that borrowing through the issue of notes is permitted by the articles of association, the procedure to be followed would be provided therein usually by a resolution.

Private companies are prohibited from offering their shares or debt securities to the public. Thus the notes may only be addressed to specific persons and in all circumstances the offer must be properly regarded as not being calculated to result, directly or indirectly, in the notes becoming available for subscription or purchase by persons other than those receiving the offer or invitation.

The terms of the notes would be set out or endorsed on the note and/or in the trust deed securing the issue of the notes. A trustee may be appointed for the protection of the interests of the note holders.

IPO / Listed

Once a company is listed, the debt holders have a considerably higher level of information regarding the company's financial situation. One could expect that this reduces the risk for the debt holder. Thus, in your jurisdiction, do listed companies usually have to pay lower interests?

It has not been observed that listed companies pay lower interest rates.

In your jurisdiction, is it possible to list notes? Could you provide a short overview of the requirements and the procedure relating to the listing of notes? In your opinion, is the focus of holders of listed notes any different from the focus of other debt holders?

Listing of notes is possible both in regulated and non-regulated markets of CSE. The listing requirements to be complied with depend on the market in which the notes will be listed.

An issuer of notes to be listed on the regulated Corporate Bonds Market, further to most of the general listing requirements must comply with the following additional requirements:

a. The overall value of the proposed listing should be greater than €200.000.

b. If the bonds are converted or exchanged into shares or options to acquire shares, the shares to which they refer should be listed on CSE or on a recognised stock exchange.

c. A competent person should be appointed as trustee for the protection of the interests and rights of the holders of notes.

d. For at least 2 financial years prior to the application for listing the issuer prepared audited accounts, operated regularly and had relevant activities.

e. An admission document is drawn and published that requires the consent of 75% of all holders for any amendment of the same and which regulates or makes reference to or includes the following:

1. The rights and obligations of the issuer against the beneficiaries or representatives or trustees of the beneficiaries.

2. The relation between the rights of beneficiaries and the rights of beneficiaries of other securities and bonds of the same issuer or other issuer on whom the issuer or its capital depends.

3. The reserves, the procedure of repayment or other provisions relating to the amortization of the debt.

4. For debt securities whose repayment or partial repayment is guaranteed by a third party, a copy of the decision or of the document providing the guarantee.

5. The name or names of the representatives or trustee for the representation and protection of the interests of the beneficiaries, any terms relevant to the responsibilities and replacement of such persons.

With the exception of the content of paragraph d. above, the above requirements apply also to an issuer of notes to be listed on the unregulated Emerging Companies Bonds Market.

The procedure for listing of notes requires the submission of a listing application together with several documents[26].

The focus of holders of listed notes is different in that they can sell the notes in the secondary market and thereby cash their investment without being forced to wait until repayment provided of course that the economic situation permits this and there is demand for such notes.

Acquisition

In your jurisdiction, what is commonly the effect of a public tender offer on listed notes. Do they have to be redeemed? Can holders of listed notes interfere in the process of a public tender offer? If so, by which means?

Except if the terms of issue of notes provide for redemption upon a takeover bid or a takeover being successful, no particular effect would be anticipated as regards listed notes. The holders of listed notes are not given any legal ground to interfere with a takeover bid.

In your jurisdiction, what is the typical influence of a public tender offer on existing credit facilities?

A takeover bid would not normally affect existing credit facilities and the terms of such facilities would be expected to remain in force. In general a takeover bid would not trigger differentiation of the terms of facilities.

[26] If the notes shall be listed in a regulated market the documents would be: a declaration of the members of management bodies of the issuer in a specified form, the approval of CySEC for the publication of a prospectus or proof that the prospectus approved by another competent authority of a member state of the EU was submitted to CySEC, copy of the prospectus, copy of the trustee agreement/deed, copy of the memorandum and articles of association, copy of a relevant resolution for the issue of notes, copy of the shareholders register in electronic and paper form and other relevant documentation that may be required by CSE. If the notes shall be listed in a non-regulated market the documents would be: a declaration of the members of management bodies of the issuer in a specified form, an admission document, copy of the trustee agreement/deed, copy of memorandum and articles of association, copy of a relevant resolution for the issue of notes, a declaration of the nominated advisor, irrevocable declarations of the persons that have agreed to receive the securities to be allocated (if applicable), the approval of CySEC for the publication of a prospectus or proof that the prospectus approved by another competent authority of a member state of the EU was submitted to CySEC (if applicable), copy of the prospectus (if applicable), copy of the shareholders register in electronic and paper form and other relevant documentation that may be required by CSE.

Interest of management / employees

Start-up phase

In the start-up phase, it is essential that the key management is committed towards the development of the business idea or project. In this context:

Which are the most commonly used means to ensure that the management/key employees will not leave the company until the company reaches the growth or maturity phase? Are warrants or similar incentives granted during this stage?

It is not common for companies to provide incentive schemes to management or key employees at the early start-up phase. If an incentive would be given at this early stage with the aim of commitment of the management/key employees most probably this would be in the form of share options.

It is likely that at this stage, there are not sufficient funds for remuneration of management/key employees. Is it common to grant warrant or stock incentive schemes in your jurisdiction? Is there any other scheme to liaise with this issue?

Warrants and share option incentive schemes are not common at this stage of the life of the company. Financial participation of employees is not well developed practice in this jurisdiction, especially at the early stages in the life of the company.

Growth phase

The management plays a crucial part in order that a company achieves going from a start-up phase to a growth phase and tend to assumes considerable risks by devoting to such project. Therefore, it would seem reasonable to protect the management in further financing rounds during the growth phase.

In case new investors come on board in the growth phase and such investors request replacement of the current management: in such replacement, does the current management usually lose rights granted under an incentive plan? How broad are "bad leaver" provisions usually formulated?

Any rights granted under an incentive plan would be expected to be subject to the employment continuing at the time of exercise, thus upon termination of the employment rights will most probably be lost. Where shares were allotted pursuant to such an incentive scheme prior to termination of employment they are unlikely to be transferable. On the contrary the company may retain a right for the shares to be transferred to it or to be transferred by the employee as per the directions of the company. It is not a rare practice that a company maintains irrevocable powers of attorney from the employees who hold shares in favour of the company or its officers or a specified party and/or blank instruments of transfer in order to secure compliance with the obligation of the ex-employee and enforcement of the right of the company.

"Bad leaver" provisions would usually provide for a discounted or nominal compensation to be paid to the bad leaver. The mechanism for determining the value of the compensation or the discount would be prescribed. The circumstances in which a person would be deemed a "bad leaver" would normally be specified in a shareholders' agreement and/or some other contractual arrangement that relates to the incentive scheme and/or the articles of association e.g. dismissal due to gross misconduct, fraud, dishonesty, breach of restrictive covenants e.g. non-compete, non-disclosure obligations and confidentiality etc.

Upon implementation of an incentive plan, the rights related to the shares that the management will be entitled to receive are usually subject to vesting. Is there any specific vesting period that is applied in your jurisdiction or is the vesting period usually linked to a liquidation event (such as an IPO)?

Incentive plans relating to shares are not regulated and thus there are no mandatory rules as to vesting of such rights. In most cases where incentives plans exist (which are not frequent), these are unilaterally introduced by the company. Any relevant rights are likely to be subject to vesting over a period of 1-3 years. Such rights would be expected to be subject to a condition of continuation of employment at the time of exercise and to a prohibition or restrictions on transferability. Also it is possible that the rights would relate to employee shares or some class of shares which would carry special rights but are less likely to carry voting rights or, if they do, such voting rights would be rather restricted or diminished compared to those carried by ordinary shares. Shares subject to incentive schemes put in place at this stage are not likely to be transferable. It is not rare that an ex-employee would be obliged to sell the said shares as the company requires or directs or to transfer them to the company or that the company retains a right to sell the shares on behalf of the ex-employee on the basis of a calculation mechanism that is pre-determined or on the basis of a valuation of the price e.g. fair value or value on the basis of net assets as determined by the auditor of the company or an independent auditor. Where the company is a private one such shares are unlikely to carry pre-emption rights. During the period of the boom of CSE public companies aiming to go public would link the vesting period with the IPO. However this is not the case at this period, as there is little desire on the part of companies to become listed in CSE.

In certain jurisdictions the management may fall out of labor relationship since it is developing executive duties for the company and/or may hold certain stock of the company (it might fall in a special labor relationship or corporate relationship). Is this the case in your jurisdiction? If so, is the loss of labor rights compensated by special laws or by contractual means?

The rights that derive from the employment relationship are not in any way prejudiced by the fact that such person may perform executive duties or the fact that such person may hold equity or other securities or rights. Yet it is often the case that further protection will be secured under the employment contract.

Maturity

After having reached maturity, the business activity and the relationship between the shareholders and the management / key employees tend to become more complex (in particular, intensification of the principal-agent-conflict). The increasing complexity triggers certain hindrances or deterrents for the ongoing activity of the company. In this context:

In your jurisdiction, do the various corporate bodies (e.g., board of directors, directors, management) have an obligation to "act in the best interest of the company"? If so, how is the "interest of the company" defined? Is it the interest of all stakeholders (including the interests of all equity holders (e.g., holder of non-voting shares), debt holders, management, employees and public) or just the shareholders? Are only long term interests taken into account or also short term interests?

Generally the director's duties are owed to the company; this means that directors should have regard to the interests of the shareholders as a whole and not to the interests of individual shareholders.

The duty to act bona fide in the interest of the company was seen as an obligation to act in the interests of the shareholders. It is the directors' subjective opinion as to the interests of the company as a general body - balancing the short-term interests of the present members against the long-term interests of future members - which counts. The approach taken by the courts of this jurisdiction is to consider whether any intelligent and honest man in the position of the directors of the company concerned could, in the whole of the existing circumstances, have reasonably believed that the transaction was for the benefit of the company.

Though the orthodox approach was that directors did not owe a fiduciary duty to the present or future creditors, in recent English and commonwealth case law - which has persuasive effect and is often followed by the courts of this jurisdiction - there is support that regard must be given to the creditors as well[27]. Whether it shall be considered that a duty is owed to the creditors shall depend on the circumstances e.g. whether a company is insolvent or near-insolvent or of doubtful solvency or if a contemplated payment or other course of action would jeopardise its solvency. Cap. 113 makes specific provisions for the assessment of the directors' conduct on a company going into insolvency in light of the effect of the transaction, act or conduct on the creditors' of the company.

The success of other stakeholders in proceedings against the directors of a company on the basis of a breach of the duty to act bona fide in the interest of the company is very doubtful under company law rules. Duties towards other stakeholders e.g. employees might exist under other pieces of legislation e.g. labour law but are based on different premises.

A company can bring an action against a director for breach of duty or for negligence in the performance of such duty as director. A company remains liable for actions authorised or committed by a director, but it may be entitled to make a claim for contribution against the director in question. In exceptional cases shareholders may bring derivative actions on behalf of the company so as to enforce the company's rights against the wrongdoing directors who have control and prevent the company from suing itself. The shareholders would need to establish fraud on the minority and that the behaviour was ratifiable by majority.

[27] For example see Walker v. Wimborne (1976) 50 ALJR 446.

"fiduciary duties" or a duty to treat equity holders equally? How are these defined?

Fiduciary duties of directors have been the product of case law and have been based on rules and principles developed in English and commonwealth case law. These may be categorized on two main groups:

a. The duty to act bona fide in the interests of the company: This is deemed as the most fundamental duty. The directors are under a duty to act bona fide in what they consider (and not what a court may consider) is in the interest of the company and not for any collateral purpose[28]. This is a subjective test. The court will not interfere in the management of a company unless it is satisfied that no reasonable director could have come to the conclusion that the director's actions were in the best interests of the company. Courts do not interfere where it is a question of bad judgment exercised by a director. However, a director acting in bad faith cannot benefit from this.

   Breaches of this duty has been found in situations where:

   1. there was use of powers for an improper purpose,

   2. the directors exceeded powers e.g. a director caused unlawful acts or acts outside the company's powers or the powers conferred to him by the company's constitutional documents,

   3. there was fettering of discretion of directors; a director must exercise his full discretion when carrying out his duties as a director and no factors or influences must limit his discretion as this would be deemed as being in conflict with his duty to be able to act always in the best interests of the company,

   4. there was a conflict duty and interest; having fiduciary duties to discharge, a director shall not be allowed to enter into engagements in which he has or may have a personal interest in conflict or that may possibly conflict with the interests of the company,

[28] Re Smith & Fawcett [1942] Ch 304

5. a director profits by virtue of the office he holds e.g. profit making by director who dealt with property or assets of the company, took personal advantage of information or corporate opportunities presented to the company or to him by virtue of the position he held as director; this would apply to situations of secret profits,

6. directors did not act or deal fairly as between different groups of shareholders; subject to the provisions of the company's memorandum and articles of association, a director must treat all shareholders equally and fairly, irrespective of the class of shares which they hold.

b. The duty of care and skill: A director is obliged to exercise a reasonable degree of skill and care in carrying out his duties. The director is required to exercise that degree of skill which might be expected from someone having both: (a) his own particular knowledge and experience; and (b) the general knowledge and experience which might be expected of a person carrying out the same functions as those carried out by that particular director. The test involves both an objective element as well as a subjective one. The nature and extent of the duty of a director depends on the nature of the business carried out and the particular knowledge and experience of the individual director. On the other hand the standard of care is determined objectively, the care required is such as the ordinary man might be expected to take in the same circumstances. A director is not expected to exercise a skill which he does not possess nor is he bound to bring any special qualification to his office[29]. But where a director does possess a qualification he must give the company the advantage of his knowledge when carrying out the company's business. However, it must be noted that a director shall not be liable for damages occasioned by errors of judgement of such director.

The nature of the company's business and the manner in which the work and affairs of the company are in fact distributed between directors and other officials or bodies of the company (provided that such distribution is reasonable and not inconsistent with any express provisions of the articles of association or the law) are important in order to ascertain the above duties and their application.

[29] Re Brazilian Rubber Plantations & Estates Ltd [1911] 1 Ch. 425, Re City Equitable Fire Insurance Co [1925] Ch 407, see also Schmitthoff, Clive M., Thompson James H., *Palmer's Company Law*, 21st ed. London, Stevens & Sons Limited, 1968, page 583.

In your jurisdiction, how are conflicts of interest addressed by the law? Are the rules on conflicts of interests for listed companies applied to non-listed companies? Have the rules on conflicts of interests become more rigid in recent years?

Conflicts of interest are addressed in provisions of different laws or rules which apply in different situations.

There is a general statutory duty on a director who is in any way interested (whether directly or indirectly) in a contract or proposed contract with the company to declare the nature of his interest at a meeting of the board of directors[30]. The procedure to be followed in such event is also provided in the law. Any director who fails to comply with the provisions of this section shall be liable to a fine. The above obligation exists whether the company is private, public or listed company.

Customarily the articles of association of companies (private and public) also make provisions as to the conflicts of interests of directors and relevant disclosures.

Further provisions that regulate conflicts of interest are applicable to listed companies exist pursuant to Law N.14(I)/1993 and relevant subsidiary legislation. These rules do not apply to non-listed companies but they may choose to comply with them voluntarily[31].

As regards transaction which could potentially involve conflicts of interest special disclosure requirements are provided by law and subsidiary legislation. The conclusion of contracts or transactions between an issuer and management bodies or specified persons[32] must be made on the basis of the practice widely adopted at the time and relevant notification or announcement to CySEC and CSE must be made by the issuer who must also publish details of such contracts or transactions within 7 days where the total value is more than €170.860. Such contracts or transactions should also be announced in the

[30] Section 191 of Cap. 113.

[31] In such case compliance and the manner in which the non-listed company will seek to achieve the requirements of the Code are not overseen by CSE.

[32] The specified persons are indicated as the chairman and the members of the board of directors, the chief executive officer, the chief financial officer, the head of the accounting department, the secretary, the auditors, pension funds of employees of the issuer and any shareholder who, on his own or with other person (i.e. persons who hold securities in their name on behalf of another, undertakings controlled by the said shareholder, persons acting in concert with the said shareholder or with persons who hold securities in their name on behalf of another), holds 5% or more of the shares carrying voting rights.

annual general meeting of the issuer.[33] Analogous obligations exist as regards issuers of bonds with the only difference being that the threshold is higher than €341.720[34].

For the above contracts or transactions the member of the board of directors or the person which is determined as having any interest must state such interest in the meeting of the board of directors or of the general meeting of the holders of securities of the issuer (as the case may be) before a relevant decision is taken. Such person cannot vote in the meeting of the board of directors in relation to any such agreement or transaction and in case he does his vote should not counted nor his presence be not taken into account for the quorum of the board of director's meeting. The announcement must contain a statement that the board of directors or the persons present in the general meeting were fully informed and that the person having an interest abstained from the decision making. Further in the relevant announcement the issuer shall state the procedure which was followed for the calculation of the value of the transaction and that an independent valuation was obtained[35].

The Corporate Governance Code (the "Code") issued by the Council of CSE and applicable to listed companies addresses the issue of conflicts of interest in several provisions[36]. Firstly the Code expressly states that material transactions of the company and/or its subsidiaries and associated companies, of any form, in which any director, chief executive officer, senior executive, secretary, auditor or major shareholder of the company (who directly or indirectly holds more than 5% of the company's issued share capital or voting rights) has directly or indirectly any material interest to the matters must be reserved for decision by the board of directors[37]. The transaction must be reported as such in the formal schedule of the board of directors. Secondly, the Code makes the board of directors responsible as regards the monitoring and settlement of any matters of conflict of interest between executive directors, the members of the board of directors and shareholders including cases of mismanagement of assets or transactions with associated parties[38].

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[33] Section 137 of Law N.14(I)/1993.

[34] Section 157 of Law N.14(I)/1993.

[35] Paragraph 5.2.2. of the Regulatory Decision of the Council of CSE on the Stock Exchange Markets, Administrative Regulatory Act 326/2009, as amended.

[36] It should be noted that companies listed in the parallel market of CSE are not obliged to follow the Code other than Part C.3. of the Code that relates to the audit committee, the auditor and matters relating to financial reporting, corporate governance and internal control.

[37] Paragraph A.1.2.(g) of the Code.

[38] Paragraph A.1.4. of the Code.

An area of potential conflicts of interests regulated in the Code is that of the directors' remuneration. The establishment of a remuneration committee of the board of directors is provided for consisting of exclusively of non-executive directors. This committee makes recommendations to the board of directors (within agreed terms of reference) on the level and context of the executive directors' remuneration and determines packages for each of the executive directors, including pension rights and any compensation payments[39]. As regards performance based remuneration of executive directors the Code provides that this part of their remuneration should be designed so as to align the interests of such directors with those of shareholders and to give them keen incentives to perform at the highest levels. However, according to the Code the performance criteria should be based on the long-term viability of the company and should include non-financial criteria that relate to the creation of long term value of the company as is compliance with applicable rules and procedures[40].

As regards the disclosure of any conflicts of interest to the shareholders, the Code states that the members of the board of directors and the executive directors should be obliged to immediately communicate to the board of directors and the shareholders (through the annual report of the company and accounts) any information pertaining to any own material interest which might arise from company transactions which fall within their duties as well as to any other conflict of own interests with those of the company or companies related thereto, which arises from the exercise of their duties subject to the continuous obligations for immediate communication of information[41].

Lastly, Law N.190(I)/2007 requires disclosure of interests and conflicts of interest. In particular persons who produce or disseminate research concerning financial instruments or issuers of financial instruments (admitted to trading on a regulated market or for which a request for admission to trading in the a regulated market is made) and persons who produce or disseminate other information recommending or suggesting an investment strategy, intended for distribution channels or for the public are obliged to take reasonable care to ensure that such information is fairly presented and disclose their interests or indicate conflicts of interest concerning the financial instruments to which that information relates[42]. A relevant person i.e. a natural or legal person producing or disseminating

[39] Paragraph B.1.1. of the Code.

[40] Paragraph B.2.4. of the Code.

[41] Paragraph D.2.2. of the Code.

[42] Section 28 of Law N.190(I)/2007.

recommendations in the exercise of his profession or the conduct of his business has an obligation to disclose all relationships and any circumstances that may reasonably be expected to impair the objectivity of the recommendation, in particular where the relevant persons have a significant financial interest in one or more of the financial instruments which are the subject of the recommendation, or a significant conflict of interest with respect to an issuer to which the recommendation relates. This would apply where such person is a director of the issuer.

Conflicts of interest of the management is an area that has seen more regulation (in terms of reporting etc.), often rigid and bureaucratic, in the past two decades but only as regards listed companies.

In your jurisdiction, is it common to put in place incentive plans for key management and employees or are they only entitled to receive a cash bonus (usually based on individual and overall performance)? Do incentive plans provide tax advantage for the company?

Cash bonus on individual and overall performance is the simplest and most common means of incentive for the key management and employees of the company. Provident funds and insurance/pensions schemes are also frequently provided though usually such schemes are applicable for all employees (not just key management and employees). More long-term incentives such as share option schemes are sometimes utilised by companies but not as frequently as the above mentioned incentives. Where long-term incentives schemes are put in place these are expected to be addressed to top executives, managers and some key employees (they are not likely to be addressed to all employees). Long-term incentive schemes may sometimes run in parallel with cash bonus or other profit sharing schemes.

Companies do not enjoy any tax advantage from such schemes except in the form of deductible expenditure for approved pension funds and provident funds.

IPO/ Listed phase

Reaching an IPO is often the pinnacle of private companies which have reached certain growth and have an attractive equity interest. Obviously, the management and employees play a significant role in the IPO / listing process. In this context:

It is our understanding that when a company goes from a private to a public setting it implies considerable changes for management and employees. In your experience and within this framework, what is the most significant change for management and employees? Does going public usually increase the total amount of the compensation and/or does it usually change the structure of the compensation (cash, shares, warrants, etc.)?

The most important change for existing management and employees of the company entering the IPO/listed phase is that a new dimension i.e. the share price and its maintenance or increase complements or replaces the main previous focus which was the financial results of the company. The fact that ownership does not remain fixed also contributes to this pressure. The dispersed ownership may, under certain circumstances, intensify this pressure as the management and employees have significantly less (direct) interaction with the shareholders.

It would normally be expected that going public would have a positive impact on the total amount of compensation for management and employees especially if the IPO is very successful. It has been observed that the compensation structure does more often than not change with incentive schemes such are share options, warrants and bonus shares being put in place for the benefit of employees yet this would not always be the case.

Following the IPO the management is constantly assessed by the performance of the share price. Also the management's pay may to large extent depend on the share price performance. One could expect that management may abstain from taking any steps that are likely to weaken the share price – even if such steps are beneficial to the company in long term. In your jurisdiction, are there any measures that are commonly taken to address this conflict (i.e., incentives for long term strategies)? Is, for example, by law or by agreement a part of the pay paid in mid- to long term options?

The Code addresses several of aspects of this issue however its provisions relate solely to directors' remuneration. The relevant general principle is that the level of remuneration should be sufficient to attract and retain the directors needed to run the company successfully, but companies should avoid paying more than it is necessary for this purpose. The Code recommends a proportion of executive directors' remuneration be structured so as to link rewards to corporate and individual performance[43].

[43] Paragraph B.2 of the Code.

The Code makes several provisions[44]:

a. In the case where part of the remuneration of executive directors is related to performance, this part should be designed in a manner that aligns the interests of such directors with those of shareholders and that gives executive directors keen incentives to perform at the highest levels. Performance criteria should be based on the long-term viability of the company and should include non-financial factors relating to long term value creation of the company e.g. the compliance with applicable rules and procedures.

b. Where the remuneration policy includes variable compensation, companies should set limits on the variable component(s). The non-variable component of remuneration should be sufficient to allow the company to retain variable remuneration when performance criteria are not met.

c. Executive director's share options should not be granted at a price lower than the average closing price of the last 30 trading days prior to the granting date. Schemes under which share options are granted should only be adopted following the approval of an extraordinary general meeting of the company's shareholders. Share options should not be exercised indicatively for at least 3 years after their allocation. Additionally shares should not be sold indicatively for at least 3 years after their allocation.

d. The remuneration of non-executive directors should be in accordance to the time they devote to the meetings and the decision-making process. Remuneration of non-executive directors should not be linked to the company's profitability and should not include share options. Additionally, the remuneration of non-executive directors should not be in the form of participation in the company's insurance/pension schemes.

e. Where remuneration with a variable component is awarded, a large part of the variable component should be deferred for a minimum period. The part of the variable component subject to deferred payment should be determined in relation to the relative weight of the variable component, compared to the non-variable component of remuneration.

[44] Paragraphs B.2.4 - B.2.10, B.3.1, B.3.5 of the Code

f. The allocation of shares and the exercise of options (share options or any other stock options) should be subject to predetermined and measurable performance criteria.

g. After the allotment, the directors should retain part of the shares until the end of their term as members of the board of directors, subject to the need to finance any costs associated with the purchase of the shares. The number of shares to be retained should be determined. Indicatively they should be double the total annual remuneration (variable and non-variable components).

h. Disclosure of remuneration of each director including detailed disclosures as regards the variable income such as shares, share option etc.[45] is required in the company's report on corporate governance so that the shareholders become aware of potential incentives of directors.

i. In the cases of directors who receive shares, warrants, rights, etc. as remuneration or whose remuneration is related to the price of shares, such remuneration must be subject to shareholders' approval prior to the adoption of the relevant schemes. Approval thereof pertains to the scheme as a whole and not to every director individually[46]. The exact content of the resolution and the cases in which it should be submitted are described in Annex 3 of the Code.

Is the management and/or employees bound by a mandatory lock up period upon the IPO? In the event the lock up period is not mandatory, please explain the common standards in your jurisdiction towards implementing a lock up period.

There is no mandatory lock up provision for management and/or employees. Lock up periods could only be put in place contractually.

Acquisition

In the scenario of the acquisition, it is frequent that the management is essential towards the subsequent development of the company. In this context:

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45 Paragraph B.3.1, and for further details on the issues to be reported see Annex 2 "Disclosures of the director's remuneration".

46 See Annex 3 of the Code on Share-based remuneration and shareholder approval to such schemes.

The focus of the board of directors of a listed company may be set to a large extent on the share price performance. Usually, this should be in line with the corporate interest. However, in case a listed company is being approached by a potential bidder, the board of directors and the management of the potential target may face a conflict of interest: an acquisition that may be beneficial to the shareholders of the potential target, may at the same time require replacement or adjustment of the target's board of directors and management. In your jurisdiction, how is this conflict of interest addressed? For example, are there limits to the defense measures that the board of directors of the target may take?

Several provisions of Law N.41(I)/2007 aim to deal with potential conflicts between the interests of the shareholders and those of the board of directors. The focus is the benefit of the shareholders.

Certain limitations are imposed on the powers of the board of directors of the target company from the moment the board of directors becomes aware that a bid is imminent up to the expiration of the period allowed for acceptance of the bid by the shareholders or the revocation or cancellation of the bid. With the exception of seeking alternative bids, the board of directors is prohibited from taking any action which may result in the frustration of the bid without the prior authorization of the general meeting of shareholders. Any decisions of the board of directors of the target taken before such period and not yet been implemented that do not fall within the normal course of the company's business and the implementation of which may result in the frustration of the bid must be approved or confirmed by the general meeting of the shareholders.

Prior authorization from the general meeting of shareholders is required before the board of directors decides any of the following:

a. the issue of shares, which may result in a lasting impediment to the bidder's acquiring control of the target,

b. any lawful acts entailing substantial differentiation of the assets or obligations of the company or the entering into ex gratia acts, unless CySEC approved such acts where satisfied that they do not result in frustration of the bid;

c. the buy-back of own shares, unless CySEC approved such buy-backs where satisfied that it does not result in frustration of the bid.

Which are the common alternatives in order to keep management / key employees focused and keen to continue in the company?

Some kind of employee participation scheme or profit sharing scheme is likely to be offered but it is likely that it would apply only to a very limited number of key management and/or employees. It has been observed in some cases that benefits may even be negotiated between the company and such employees (often individually) rather than unilaterally decided.

In parallel, is it common to reinforce non-competition and confidentiality undertakings of the management / key employees upon acquisition? Is it common to regulate a non-solicitation by the Seller and that it is enforceable (for which period)?

Non-competition and confidentiality undertakings by the management/key employees are likely to be included in the initial employment contracts of such employees. Following the acquisition of a company an attempt may be made to enter into news contracts with the management/key employees. Such new contracts may, among others, seek to include or strengthen any non-competition and confidentiality undertakings. Such contracts would be expected to provide for further term s or deviate from the initial ones e.g. changes in positions, duties and responsibilities, higher salaries etc. Attempts to reinforce non-competition and confidentiality undertakings of the management/key employees are common.

The adoption of non-solicitation provisions that would bind the seller is almost a rule in the case of acquisitions of non-listed companies where there is a binding contractual relationship between the seller and the purchaser of the company. The duration of non-solicitation obligations as regards employees would depend to a great extent on the industry and may range depending on the position or expertise of employees. In most cases they would be expected to last from 1 to 3 years but longer periods have also been observed.

Interest of advisors / lawyers

Start-up

During the start-up phase, it is one of the most difficult stages to advice companies and/or projects since the company does not have the resources (funds) to implement an appropriate legal scheme and the management/equity holders tend to think in the short term rather than the long term.

Which are the common difficulties you liaise with during this stage? How do you tend to structure your fees (for example, do you go below your standard rates and agree to have this difference compensated at a later stage when the company has become more successful)?

The adoption of a fixed fee, part of which payable in advance, would be the most common fee structure at the start-up phase. Alternatively hourly fees would be adopted. It is not unusual that fees are kept below standard rates at this stage especially if potential is seen for the establishment of a long-term relationship over which the difference would be expected to be compensated. Even where the fees set are below the standard rates adopted by the law firm, they could not be lower than the minimum legal costs and expenses set for out of court cases[47].

As regards court cases it is most likely that fees would be charged as per the civil procedure or other applicable rules. Higher fees may be charged provided that there is relevant agreement with the client and these are declared in court. However, it is unlikely that companies in the start-up phase would choose this option.

In case you accept warrants / rights to shares as compensation for professional services rendered: how do you set the amount or the value of such warrants and rights? Do you rely on valuations of the company? If so, whose valuations? Is it common for an advisor in this situation to request that the company has previously successfully completed a minimum viable product ("MVP") stage which reduces the risk of failure (i.e., as part of the lean start-up methodology it is advisable to diminish uncertainty for the project by means of developing an MVP to validate the project)?

It is not a common practice for lawyers to accept warrants or rights as compensation for professional services.

Growth

Commonly, it is important to provide appropriate legal advice when the company intends to achieve going from the start-up phase to a growth phase. The role of lawyers and

[47] These are included in regulations were issued pursuant to the Advocates' Law, Cap. 2, as amended.

advisors would likely enhance the possibilities to effectively reach a solid growth phase. In this context:

How do you tend to structure your fees during this stage (in particular, is there a difference in the fee structure as compared to the start-up phase)?

Retainers or combinations of retainers for specified services together with hourly fee pricing for services not falling within such retainer would start at this phase. Some clients might prefer not to have a retainer with lawyers and require assistance if and when needed on the basis of hourly fees or a fixed fee depending on the project at hand. The rates to be charged would depend on the circumstances such as the frequency and complexity of the services required but in special cases they could be marginally lower than the standard rate. This is likely to be observed in cases of hourly fees for specific projects where the client maintains a retainer (that does not cover such projects) which has already been paid in full. The potential for a long-term relationship would also be taken into consideration when determining the rates for any of the above fee structures.

Again, as regards court cases that would relate to matters arising in ordinary course of business of the client e.g. debt collection, labour disputes etc. it is most likely that fees will be charged on the basis of the civil procedure rules. Higher fees may be charged provided there is agreement with the client and these are declared in court. Companies in the growth phase choose this option rarely for important and special cases e.g. a technology company might make this choice for litigation relating to protection of its intellectual property rights.

Is it common for advisors (in particular, lawyers) to take board positions during this phase? If so, how is such board member compensated? In cash? Or with exclusivity for providing legal services to the company?

Whether advisors would take office in the board of directors during this phase would depend on the activities of the company. For example advisors, including lawyers, are more likely to take positions in boards of regulated companies (e.g. investment firms) or listed companies where the composition of the board of directors is relevant for regulatory compliance purposes or examined by authorities at some stage.

In most cases where lawyers hold an office in a board of directors, the compensation for holding such position would be paid in cash.

It is not very likely that advisors would take positions in the board of directors of a company during this phase.

As the lawyer you may be asked by the entrepreneur to render advice on the division of equity (in particular to FFF)? What is the basis for your advice regarding the division of equity?

The basis of a lawyer's advice would depend on the circumstances. As the entrepreneur is the client the focus would be the entrepreneur's interests. It would be expected that a lawyer would guide the entrepreneur into the different options of structuring the company and the possible mechanisms governing relationships. The activities of the company would also be an aspect that would influence the advice. The basis of advice relating to the division of equity would depend on the objectives of the parties involved, the intended timeframes, the degree of intended participation and involvement in the management etc.

In certain jurisdictions corporate law is rigid and does not allow to regulate certain rights of the shareholders in the by-laws of the company (such as, preferential pre-emptive rights, drag along or tag along rights). Please explain (succinctly) which is corporate legal scheme that applies in your jurisdiction. Is the shareholders agreement enforceable against third parties in your jurisdiction or is only binding between the relevant shareholders?

Cap. 113 does not generally prohibit the adoption of provisions in the articles of association that would govern the relationship of the shareholders in the future and would provide for relevant arrangements. Provision for pre-emption rights in the articles of association of a private company is in fact very common[48]. There is no prohibition in providing for drag along and tag along rights in the articles of association and it is not rare that they are included.

Provisions of shareholders' agreements are usually reflected in the articles of association. There are several reasons for this practice. Firstly, the fact that the shareholders' agreement is not binding or enforceable against third parties. Thus a person who became a shareholder but who did not adhere to the shareholders' agreement when becoming shareholder would not be bound by its terms. Adoption of the analogous provisions in the

[48] In the case of public companies pre-emptive rights are provided by statute and apply whether or not included in the articles of association of the company. Nevertheless more often than not they are expressly included in the articles of association.

articles of association would bind all shareholders (whether they are subscribers or they acquired the shares at a latest stage through transfers) regardless the effect and enforceability of a shareholders' agreement. Secondly, the remedies available for infringements of the articles of association would be different to those available for breach of the shareholders' agreement. Remedies for infringement of the articles of association would lay in company law and would include specific performance, injunctions (interim, prohibitory etc.), declaratory and other court orders as well as damages. In the case of breach of the shareholders' agreement the remedies would be limited to damages.

Maturity

After having reached maturity, the business activity is much more complex and the interests of the company become more intricate. In this context:

How do you tend to structure your fees during this stage (in particular, is there a difference in the fee structure as compared to the start-up or growth phase)?

If there is a long established relationship then combinations of a retainer for specified services together with hourly fee pricing for services not falling within the retainer would most likely be employed. It is very common though that clients would negotiate a fixed fee for particular projects not falling within the retainer or where no retainer exists. As regards court cases companies are more likely to adopt a similar approach to the one described above for the growth phase.

Are you able to become member of the board of directors of the companies? Do you tend to render more unique advice to companies (while the corporate counsel provides the typical ongoing corporate advice)?

There is no legal prohibition for a lawyer to hold offices in the board of directors of companies. However, a lawyer would be expected to comply with the provisions of the Advocates' Code of Conduct Regulations of 2002 as amended[49] (hereinafter the Code of Conduct) pursuant to which a lawyer must abstain from actively participating in the conduct of any business of commercial or other economic nature or from being an active member of such business. Though lawyers may hold directorships in companies they

[49] These regulations were issued pursuant to the Advocates' Law, Cap. 2, as amended.

cannot have an employee status nor can they act as managing directors (with the exception of companies being law firms)[50].

The majority of companies would not employ a corporate counsel and requests for advice from such companies would relate to a wide spectrum of issues including very often corporate matters. Corporate counsels would be employed in large companies or sometimes in regulated companies. Requests for advice from companies that employ corporate counsels are likely to be less wide-ranging. Indeed in such companies the standard ongoing corporate advice would be expected to be rendered internally.

From a lawyers' perspective, how is the conflict of interest of the management liaised with (are there any mandatory provisions that apply in your jurisdiction)?

There are no mandatory provisions specific to the conflict of interest of the management that would influence a lawyer's perspective when handling a case where such issues arise. Depending on the case where the client of the lawyer is the company and the facts reveal existing or potential conflicts of interests with those of the management, the lawyer should point out such conflicts of interests, the circumstances under which they may arise and advise the company accordingly on the basis of substantial law e.g. company law, Law N.14(I)/1993, the Code, Law N.190(I)/2007 etc. and the procedures prescribed in the articles of association.

The duties that lawyers owe to their clients under the provisions of the Code of Conduct would apply and compliance with it would be required. These rules are of general application and are not specific to cases involving conflicts of interest involving the management. Also they are not designed to prevent such conflicts from actually coming into existence. Nevertheless they could potentially mitigate their effect.

Subject to the rules of law and the Code of Conduct, lawyers are obliged to always defend their client's interest in the best manner possible, even with regard to their own personal interest, those of their colleagues or the profession in general[51]. They must always act in absolute independence, free of all forms of dependence or pressure as may arise from their

[50] See regulation 18 of the Code of Conduct. These restrictions fall within a more general rule pursuant to which the exercise professions or activities which are incompatible with the legal profession are prohibited in order for lawyers to be in a position to exercise their function with the necessary independence and in a manner conformable to their obligation to participate in the administration of justice

[51] Regulation 16 of the Code of Conduct.

own interests or external influences and must not give advice with the aim of pleasing their client or as a result of external pressure[52]. Given these rules the interests of the management should not influence the lawyer's advice towards the company i.e. the client.

Lawyers have a duty to act on the basis of a trust relationship that may exist if their personal honour, honesty, directness or sincerity is beyond doubt[53]. Consequently when involved in a relevant case lawyers ought to be honest, direct and sincere in both in identifying and in advising on the conflicts of interests.

It should be noted that the Code of Conduct imposes a duty on lawyers not to act or advise more than one client in the same case where there is a conflict of interest or significant risk of such conflict arising among the clients[54].

Does the anti-money laundering provisions in your jurisdiction have changed the form your render advice?

Anti-money laundering provisions have indeed changed the procedures to be followed before rendering advice. Naturally the consequence of such provisions would be that often advice will not or cannot be rendered immediately due to the fact that the obligation for verification of the identity of the client and the performance of relevant due diligence must be fulfilled before the provision of services. One would also note the burden (both in terms of costs and time) that a law firm would have to bear for regulatory compliance purposes as a result of such provisions.

IPO/ Listed phase

Reaching an IPO is often the pinnacle of private companies which have reached certain growth and have an attractive equity interest. It is unlikely that the process of becoming a listed company will be successful without the proper advice. In this context:

How do you structure your fees for an IPO?

Premium pricing (i.e. pricing based on the value of the IPO and depending on the result, a premium or added value being charged) would be the ideal option where expertise has been

[52] Regulation 10 of the Code of Conduct.

[53] Regulation 11 of the Code of Conduct.

[54] Regulation 21 of the Code of Conduct.

developed in the field. A combination of hourly fee pricing and contingent/percentage fee pricing could also be considered as an alternative option by lawyers. Clients would possibly press for a fixed fee for the consultation on IPO matters.

As regards court cases involving matters in the ordinary course of the business of the client e.g. debt collection, labour disputes etc. companies are more likely to adopt an approach similar to that described above for the growth phase. For litigation relevant to the IPO and corporate issues or disputes it is likely that agreement will be made for higher charges than those prescribed by the civil procedure or other applicable rules.

From a lawyers' perspective, which are the main regulatory aspects of offering equity to the public? Is it common that companies reach this stage (in certain jurisdictions becoming a listed company is less rigid)?

The first aspect is the preparation of a prospectus as regards the issue of the securities to be listed in a regulated or not regulated market. Preparation of a prospectus is obligatory for public offers of securities or securities admitted to trading on a regulated market under the Public Offer and Prospectus Law of 2005 as amended. Where the said law does not apply, a prospectus or a statement in lieu of prospectus under the provisions of Cap. 113 is likely to be required. The characteristics and terms of the offering would need to be examined thoroughly to ensure that the offering is done in compliance with applicable rules. Given the current economic climate, it is not common for companies to reach this stage.

Is there any specific secondary market in your jurisdiction that allows early start-up companies to become listed with the aim of obtaining more equity (given the complexity of becoming a public company in certain jurisdictions a start-up company can become listed in a specific market which is less rigid and allow it to obtain other sources of financing, among others)?

Though not specific to start-up companies the Emerging Companies Market and the Emerging Companies Bond Market of CSE could be markets on which securities of such companies could be listed. Both of these markets are non-regulated markets and thus there are less regulatory compliance obligations for the issuer.

Issuers of securities to be listed on the Emerging Companies Market must be public companies. Such companies must have operated regularly and have had activities for at least 2 financial years prior to listing or have satisfied the Council of CSE that they provide satisfactory information so that the investors can evaluate the value of their titles - as this would be initially evaluated with a report by a nominated advisor (advisor appointed for the purposes of compliance with rules of CSE), that their shares shall be held by a satisfactory number of investors and that they obtain and maintain the services of a nominated advisor.

Issuers of corporate bonds listed on the Emerging Companies Bond Market could be private or public companies. The following requirements need to be fulfilled for the listing of bonds:

a. The overall value of the bonds to be listed is greater than €200.000.

b. If the bonds are convertible or exchanged into shares or options to acquire shares, the shares to which they refer should be listed on CSE or on a recognised stock exchange.

c. A competent person was appointed as a trustee for the protection of the interests and rights of the holders of bonds.

d. The publication of a legally binding document (which provides that it may not be amended without the consent of 75% of the beneficiaries of all bonds) which regulates or includes:

    1. the rights and obligations of the issuer against the beneficiaries or representatives or trustees of the beneficiaries,

    2. the relation between the rights of the beneficiaries and the rights of the beneficiaries of other securities and bonds of the same issuer or other issuer on whom the issuer or its capital depends on,

    3. the reserves, the repayment procedure or other provisions relating to the amortisation of the debt,

    4. in the case of bonds whose repayment or partial repayment is guaranteed by a third party, a copy of the decision or of the document providing the guarantee,

    5. the name or names of the representatives or trustee for the representation and protection of the interests of the beneficiaries, the responsibilities and terms of replacement of such person.

Does the fact of becoming a listed company imply that the lawyers and/or advisors adjust rates their rates accordingly?

The rates charged by lawyers and/or advisors are likely to be adjusted where the service provided relates to matters associated with the listing or ongoing obligations of the issuer as a result of the requirements of CSE and/or the rules applicable to the market where its securities are listed and/or other applicable laws[55] or where the lawyer of advisor acts as nominated advisor for the issuer. It has not been observed that adjustments are made for other kind of services for which the fact that the company is listed is irrelevant e.g. legal services for debt collection.

Acquisition

In the scenario of the acquisition, it is frequent that lawyers and advisors are highly involved. In this context:

Which is most frequent scheme of implementing an acquisition (asset deal vs share purchase deal)?

Share purchase deals seem to be more common even though asset deals are not rare. The choice between the two options would depend on the facts at hand including potential tax consequences and possible liabilities of the target.

From a lawyers' perspective, which are the main differences within the process of acquiring a stake in listed companies versus private companies?

In the acquisition of a listed company one would face higher regulatory compliance burden and relevant costs. The behaviour of the bidder as well as of the target company (and its management) is regulated under N.41(I)/2007). In this respect lawyers are often called to advise on the legality of actions and the boundaries of behaviour of the parties involved as well as on compliance of the process with the legal framework in place.

[55] E.g. Law N.190(I)/2007 and Law N.116(I)/2005.

The process for the acquisition of a private company is a very different (compared to that of a listed company) as it is expected that there will be more direct interaction between the acquirer and the sellers (or at least the major shareholder(s)) or their representatives. Lawyers often have a more critical role in the process from the early stages to the post acquisition phase (especially in asset deals). They are likely to consult on the type of scheme for the implementation of the acquisition taking into consideration matters such as the situation of the company and that of the acquirer and the sellers, tax implications, legal implications on the business etc. and would be involved in the actual planning of the acquisition. In most cases lawyers would be called to participate in the negotiations. Evidently lawyers would advise on the agreements and relevant documentation and draft or review them. Given the fact that the framework for the acquisition of private companies is much less regulated, there are fewer boundaries in the actual process. As a consequence one would observe more active involvement and often a rather determinative role for the lawyers involved in the transaction.

From a lawyers' perspective, which are the main steps in your jurisdiction in order that a public entity becomes a private entity as a consequence of an acquisition?

The conversion of a public company into a private one would require an amendment of the name of the company[56] and the articles of association so that the company will fulfil the conditions to qualify as a private company[57]. In particular, the articles of association would need to be amended so as to provide for:

a. The restriction of the right to transfer the shares.

b. The limitation of the number of the shareholders in the company to 50 (not including persons who are in the employment of the company and persons who, having been formerly in the employment of the company, were while in that employment and have continued after the determination of that employment to be shareholders of the company).

[56] Under section 4 of cap.113 the name of the private must include one of the following expressions at the end: "Limited" or "Ltd". Whereas the name of public companies must include one of the following expressions at the end: "Public Company Limited", "Public Company Ltd", "Public Company Limited", or "Public Co. Ltd"," Plc", "Public Limited", " Public Ltd".

[57] Section 29(1) of Cap 113.

c. A prohibition of any invitation to the public to subscribe for any shares or debentures of the company.

How do you tend to structure your fees during this stage (in particular, is there a difference in the fee structure as compared to other phases)?

The fee structure and rates would depend to great extent on the circumstances at hand (friendly v. hostile takeover) as well as on the scheme and the relationship with the client (whether long-term relationship established and expected to continue). Premium pricing would be the optimal option (i.e. pricing based on the value of the transaction, and depending on the result, a premium or added value being charged). Alternatively a combination of an hourly fee and a contingent/percentage fee would be considered. Due to the unpredictability of the time to be consumed at the point when the legal fees are determined, lawyers (whether acting for the acquirer or the seller) often prefer not to propose a fixed rate fee.

As regards court cases involving matters in the ordinary course of business e.g. debt collection, labour disputes etc. companies are more likely to adopt an approach similar to the one described above for the growth phase. For litigation relevant to the acquisition and corporate issues or disputes it is likely that agreement will be made for legal expenses that will be higher than those prescribed by the civil procedure or other applicable rules.

BIBLIOGRAPHY

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