The Mergers & Acquisitions Review

Seventh Edition

Editors
Simon Robinson and Mark Zerdin

Law Business Research

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PUBLISHER'S NOTE

In presenting this seventh annual edition of *The Mergers & Acquisitions Review*, the publisher would like to extend warm and heartfelt thanks to editor Simon Robinson, who has recently retired from Slaughter and May. Simon has held the position of editor of *The Mergers & Acquisitions Review* since its inauguration seven years ago, and Simon and his partners at Slaughter and May have been instrumental in the success of The Law Reviews series. Thank you Simon.

The publisher would like to welcome Mark Zerdin, also a partner at Slaughter and May, as current and future editor of *The Mergers & Acquisitions Review*. We are delighted to have Mark on board, and we look forward to future editions in Mark's very capable editorial hands.

Gideon Roberton
Publisher, The Law Reviews
August 2013

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EDITOR'S PREFACE

This past year has seen some surprising twists and turns, not only in the mergers and acquisitions markets but also in the economic and political environments. November saw the re-election of Barack Obama, although this had less of an impact on the markets than an announcement by Ben Bernanke in May that the US Federal Reserve would consider a slowdown in its programme of quantitative easing. On the other side of the Pacific, Xi Jinping has outlined a new communist doctrine – the 'Chinese dream'. The doctrine reflects the changing economic outlook in China where growth will be increasingly consumer rather than investment-led. A new political rhetoric has also emerged in Japan as Shinzo Abe, elected in a landslide December victory, seeks to reinvigorate the Japanese economy. Both rebrandings flirt with nationalist sentiment and the attitude of these two countries towards one another will continue to bear on the region's business environment.

In Europe, despite an awkward Cypriot bailout, the sovereign debt crisis showed signs of stability and government bond yields are falling. Europe also improved its attractiveness in the eyes of investors and remains the largest destination for foreign direct investment. However, there has yet to be a return to growth. Investors seem split fairly evenly between those who believe Europe will emerge from the crisis in the next three years, and those who believe it will take five years or more. In any event, a return to the boom years is unlikely in the near future, particularly as the emerging markets see a relative slowdown. The IMF data for 2012 shows that the combined growth rate of India and China is at its lowest in over 20 years while global growth fell below 2.5 per cent in the second half of 2012. This global slowdown continues to pull M&A figures down making 2012 the fifth consecutive year in which deal values fell globally.

There are reasons for optimism though, particularly in the US market which has seen some substantial deals (the acquisitions of Heinz and Virgin Media being particular highlights). These deals have been made possible by the return of debt financing where the right deal can attract very favourable terms. Equities have also performed much more strongly over the past year. In May 2013 both the Dow Jones and the FTSE 100 hit record highs – validating to some extent the aggressive monetary policies pursued in the US and the UK. Whether political will can start to lift the markets more broadly still remains to be seen.

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

Mark Zerdin
Slaughter and May
London
August 2013

Chapter 23

EGYPT

Omar S Bassiouny and Mohamed Oweis[1]

I OVERVIEW OF M&A ACTIVITY

The Egyptian economy in 2012 has been in a critical condition across the board as a result of political turmoil that led to a severe fall in foreign investment and foreign currency cash reserves, combined with a substantial increase in the budget deficit and domestic and external debts. Meanwhile, merger and acquisition (M&A) activities showed an improvement led by strategic and private equity activities. Egypt represents an especially fertile ground for M&A activity in light of its diversified economy and businesses that have been struggling, strong demographics, strategic geographical position and transition to a democratically elected government.

II GENERAL INTRODUCTION TO THE LEGAL FRAMEWORK FOR M&A

The Egyptian legal system, with its strong civil law influence, is based upon a philosophy of legal codification. Mergers and acquisitions are regulated in Egypt by diverse legislation, which include the Civil Code No. 131 of 1948 (the Civil Code) regulating *inter alia* the legal framework of any sale and purchaser transaction and the rights and obligations arising therefrom, the Egyptian Companies Law No. 159 of 1981 (the Companies Law) regulating *inter alia* corporate governance issues and the Capital Markets Law No. 95 for 1992 (the Capital Markets Law), which regulates capital markets' transactions.

The Income Tax Law No. 91 of the Year 2005 (the Income Tax Law) regulates *inter alia* tax treatment of mergers and acquisitions-related transactions, the Competition Protection Law No. 3 of the Year 2005 (the Competition Protection Law) regulates

1 Omar S Bassiouny is executive partner and Mohamed Oweis is an associate at Matouk Bassiouny.

inter alia mergers and acquisitions transactions that might have an adverse effect on competition in the country and the Central Bank and Banking Sector Law No. 88 of 2003 (the Banking Law) regulating *inter alia* mergers and acquisitions of banks in Egypt.

Mergers and acquisitions of listed companies are comprehensively regulated under Chapter 12 of the Executive Regulations of the Capital Market Law, promulgated by Ministerial Decree No. 135 of 1993 (the Capital Market Executive Regulations).

Judicial Egyptian court precedents do not serve to provide a legal framework of mergers and acquisitions in Egypt for two reasons. Firstly, judicial precedents do not have a *de jure* legally binding effect in Egypt (although they may have a *de facto* persuasive moral effect). Secondly, and most importantly, the overwhelming majority of mergers and acquisitions agreements refer any disputes arising therefrom to settlement by arbitration leaving state courts with very limited sources for precedents.

III DEVELOPMENTS IN CORPORATE AND TAKEOVER LAW AND THEIR IMPACT

The last six months – fuelled by political volatility and economic difficulty – witnessed major new legislative and executive developments that directly affected M&A in Egypt. The most significant developments related to the taxation of M&A transactions. While profits achieved by non-residents through selling their shares or quotas in Egyptian companies used to be exempt from taxes, the Income Tax Law was amended in December 2012 to limit this long-standing tax exemption. In relation to this, Article 56(2) was added to the Income Tax Law through Law No. 101 of 2012 stipulating that a tax rate of 10 per cent shall be imposed on initial transactions of any security in the secondary market following the initial public offering thereof; and on the profits achieved by both residents and non-residents (whether individuals or legal persons) if such profits are achieved through selling shares or quotas including all kinds of share sale and share swap transactions as long as the acquisition concerns a portion exceeding 33 per cent of the capital or voting rights of the acquired company and whether the acquisition takes place through a single transaction or various transactions. In this regard, the taxable profits will be based on the difference between the price upon which the acquisition took place and the price on which the shares or quotas were obtained (or the nominal value of the shares or quotas in case of incorporation).

Notwithstanding the above, after the promulgation of the above-mentioned tax amendment the Presidency announced that the application of said tax amendments will be temporarily suspended. However, there has been no official published law or decree suspending the application of said law, a matter that caused major confusion in the mergers and acquisition market in Egypt. A new law was issued in May 2013 providing that the tax treatment for mergers and acquisitions in Egypt will be reversed to its original status whereby profits achieved by non-residents through selling their shares or quotas in Egyptian companies shall be exempt from taxes.

Another important development related to a law issued in early 2013 instituting the need for acquirers to secure a regulatory approval from a newly established authority called the Sinai Development Authority prior to acquiring any shares in any Egyptian company with headquarters or branches in the Sinai Peninsula. This new requirement considerably lengthened the process for closing mergers and acquisitions transactions in Egypt. For example, in a bank acquisition that recently closed the process took over two months.

The most significant legal development in recent years is represented by the promulgation of Chapter 12 of the Capital Market Executive. Chapter 12 regulates takeovers of companies listed in the Egyptian Exchange; and Egyptian companies whose shares were available for public subscription (target companies).

In relation thereto, the Capital Market Executive Regulations provide for various obligations on the acquirer depending on the percentage of the stake to be acquired from the issued and share capital of the target company. Any person who wishes to acquire – whether directly or through related parties – one-third or more of the issued share capital or voting rights of the target company must undertake such acquisition through a mandatory tender offer addressed to all shareholders of the target company. In addition, if a person holding (independently or in conjunction with related parties) more than one-third of the ownership or voting rights of the target company but not exceeding 50 per cent of such ownership or voting rights shall be obliged to submit a mandatory tender offer addressed to all shareholders of the target company if its aggregate shareholding in the target company is increased by more than 2 per cent of the ownership or voting rights of the target company within 12 consecutive months; or its aggregate shareholding in the company exceeds 50 per cent of the ownership or voting rights of the target company. The aforementioned obligation to submit the mandatory tender offer applies *mutatis mutandis* to any person holding more than 50 per cent (but less than 75 per cent) of the ownership or voting rights of the target company if such person's shareholding in the target company is increased by more than 2 per cent of the ownership or voting rights of the target company within 12 consecutive months or exceeds 75 per cent of the ownership or voting rights of the target company.

IV FOREIGN INVOLVEMENT IN M&A TRANSACTIONS

As outlined above, despite continued anti-government protests, Egypt has seen significant M&A activity throughout 2012. The significant players in transactions in Egypt were Qatar, the United Arab Emirates, the EU and the Far East.

The impact of the EU financial crisis was clearly felt in Egypt where two major French banks, namely Sociétė Général and BNP Paribas, divested their Egyptian subsidiaries to QNB of Qatar and Emirates NBD of the United Arab Emirates respectively. Meanwhile, European manufacturers concerned about growth potential in the European Union have tried to acquire companies in Egypt, noting the opportunities for growth as a result of its large population.

V SIGNIFICANT TRANSACTIONS, KEY TRENDS AND HOT INDUSTRIES

In recent years, M&A trends have been focused around sectors that are affected by the large population, consisting mainly of fast-moving consumer goods, financial services, health care and education.

Stimulated by the low valuation of the equity markets as a result of the current political unrest, public-to-private transactions are starting to appear as a new trend in Egyptian M&A, whereby a number of companies have expressed their intention to delist their securities from the EGX followed sometimes by a relisting abroad. The process typically requires the launch of a public tender offer to buy out the minority shareholders through either a cash offer or a cash or shares offer, followed by a delisting of the EGX. The most recent examples include the recently announced offer by Orascom Construction to buy out the minority shareholders and then undertake a new listing in the Amsterdam Stock Exchange.

The $3 billion acquisition by France Telecom of the shares it did not already own in MobiNil (one of Egypt's largest mobile phone companies) is a particular highlight. The recent acquisition by QNB's of a majority stake in NSGB for $2.6 billion and the most recent acquisition by Emirates NBD's of BNP Paribas' Egyptian banking business for $500 million indicates renewed confidence in Egypt's future, both politically and economically, and 2013 may see more of the same.

VI FINANCING OF M&A: MAIN SOURCES AND DEVELOPMENTS

Private equity has played a significant role in recent Egyptian M&A taking advantage of attractive valuation. Private equity has encompassed health care and pharma, education, fast-moving consumer goods and manufacturing. The main players include Abraaj Capital, Gulf Capital, Citadel Capital and Al Ahly Capital.

In the past few months the Egyptian legal system has witnessed the introduction of a new financing mechanism compliant with shariah law: *sukuk*. *Sukuk* is the Arabic name for financial certificates, but commonly refers to the Islamic equivalent of bonds. However, the main difference between conventional bonds and *sukuk* is that *sukuk*, as trust certificates, are not debt instruments and instead convey a beneficial ownership interest in one or more underlying assets. *Sukuk* has been introduced to the Egyptian legal system by virtue of Law No. 10 of 2013 (the Sukuk Law).

Although *sukuk* are mainly intended to be used as a project finance vehicle, there is nothing in the Sukuk Law that precludes financing acquisitions through *sukuk* as long as the financing structure is compliant with the requirements of the Sukuk Law. In relation thereto, Article 9 of the Sukuk Law requires that a project that may be funded through *sukuk* must:

a entail legitimate activities;
b operate under a competent management;
c operate in Egypt;
d has independent accounts;
e be profitable (as evidenced by feasibility studies); and
f satisfy any other conditions listed in the subscription prospectus.

However, and considering that *sukuk* is too much of a recent development and, generally, a project finance strategy, it is unlikely that *sukuk* will be used to finance traditional acquisitions (i.e., acquisition of the share of the target company) but it might be used for financing acquisition of assets.

Article 8 of the Sukuk Law presents different types of *sukuk* depending on the structure of the relationship between the owner of the *sukuk* and the beneficiary therefrom including *inter alia* financing *sukuk* (used to finance the purchase or manufacturing of assets), *sukuk* of Igara (used to finance purchase and subsequent lease of assets or services), investment *sukuk* (used to finance diverse patterns of investments), production *sukuk* and funds *sukuk*.

Pursuant to the Sukuk Law, *sukuk* might be issued by the government, public entities, banks subject to the supervision of the Central Bank of Egypt, commercial companies, and international and regional financing institutions approved by EFSA and the Central Bank of Egypt. The amount of *sukuk* issued by any of the above-mentioned entities may not be less than 100 million Egyptian pounds (or its equivalent in foreign currencies) except for the *sukuk* issued by commercial companies the amount of which must not be less than 50 million Egyptian pounds (or its equivalent in foreign currencies).

Apart from *sukuk* financing, mergers and acquisitions may be financed through various other tactics including the incorporation of an acquisition vehicle that borrows funds to acquire the target company in Egypt (the acquisition loan) with the intention of debt pushdown post-closing. Ideally, the acquisition vehicle and the target company merge following the acquisition whereby the operating cash flow of the target company may be used for paying off the acquisition loan. Otherwise, and in the event that the acquisition vehicle acquires the target company in Egypt, the acquisition loan may be repaid through the dividends distributed from the target company to the acquisition vehicle. While the financial means needed for repayment of the acquisition loan must be generated by the target company, which – contrary to the acquisition vehicle – conducts an operating business, such repayment means may raise questions under Egyptian law as to the corporate interest of the target company in guaranteeing or repaying the acquisition loan. Moreover, and pursuant to Article 96 of the Companies Law, the target company may not legally guarantee the acquisition loan if the acquisition vehicle is represented in the target company's board. Accordingly, the prohibition would only be circumvented in the event that all the board members of the target company are independent and none is even nominated to the board by the acquisition vehicle.

Finally, and as to the pricing of credit, it is to be noted that the Stamp Duty Law No. 111 of the Year 1980 (the Stamp Duty Law) has been amended by virtue of Law No. 9 of 2013 whereby a stamp duty shall be imposed – on a quarterly basis – on any credits or loans granted from banks to clients. The price of the stamp duty shall be one per mille for the utilisation of credits or the granting of loans on each quarter and shall be equally borne by the bank and the client.

VII EMPLOYMENT LAW

While stock or securities-based transactions do not present major employment law complications, employment law issues become quite substantial in connection with mergers and acquisitions that are related to asset-based transactions.

For example, while pursuant to the Labour Law No. 12 of 2003 (the Labour Law) in context of a transfer of assets, employees are to be automatically transferred to the new employer (i.e., the acquirer), the actual transfer of the employees from one company to another with the Labour Office and the Social Insurance authorities remains procedurally bureaucratic. As an illustration, in many cases, the National Organization for Social Insurance does not recognise the acquisition as a means of transferring employees from one employer to another and hence requires the employees of the target establishment to sign a resignation from their previous employment and to accept their employment with the acquirer, which renders the legislative instrument of automatic transfer *de facto* inoperative.

It is also worth noting in such context, the seller and the purchaser remain jointly liable for all employees' rights, prejudicing the concept of a 'clean break' by any seller.

The concept of clean break is important for any seller in a divestment and simply means that – unless otherwise explicitly assumed by the seller in the transaction documents – the seller shall not be liable but rather indemnified against any actual or contingent residual liability arising out of the company or asset subject of divestment, which becomes the responsibility of the purchaser.

VIII TAX LAW

As highlighted above, taxation issues related to M&A have witnessed volatile changes over the past few months so that the ultimate position of Egyptian law is that profits achieved be either natural or legal persons through selling their shares in companies listed in the Egyptian exchange are exempt from income tax (although they are now subject to stamp duties as indicated below). On the other hand, profits accomplished by juristic persons or natural persons who are undertaking the sale and purchase of shares on a regular professional basis through selling their shares or quotas in unlisted companies shall be taxable.

Moreover, pursuant to the latest tax amendment, profits arising from the company's re-evaluation (including through changing the company's legal form) shall be taxable. In particular, taxes shall be levied on any profits accomplished through the merger of two or more resident companies, the split of a resident company into two or more resident companies, transforming a partnership into a corporation, transforming a corporation into another form of corporation, the acquisition of at least 33 per cent of the ownership, voting rights or assets of a resident company or transforming a juristic person into a corporation.

Furthermore, it is to be noted that Stamp Duty Law No. 111 of 1980 has been amended by Law No. 9 of 2013, whereby a stamp duty tax shall be levied on all trading of securities in the Egyptian Exchange, whether such securities are issued by Egyptian or foreign companies and whether or not such securities are listed in the Egyptian Exchange. The value of the stamp duty is two per mille to be borne equally between the purchaser and the seller.

IX COMPETITION LAW

The Competition Law provides wide discretionary powers to the Competition Protection Authority, whereby the latter maintains visibility over mergers and acquisitions that have appreciable effect in the Egyptian market. According to Article 19 of the Competition

Protection Law, all persons whose annual turnover exceeds 100 million Egyptian pounds (as evidenced by the most recent budget) must notify the Competition Protection Authority of their acquisition of any assets, ownership rights, usufructs or shares or their engagement in any partnership, merger or acquisition or when they combine between the management of two or more persons as per terms and provisions of the Executive Regulations of Competition Protection Law.

In connection thereof, Article 44 of the Executive Regulations of the Competition Protection Law issued by the Ministerial Decree No. 1316 of the Year 2005 (the Competition Executive Regulations) stipulates that the notification referred to above must be sent to the Competition Protection Authority within 30 days as of the date of the effectiveness of the relevant transaction.

Considering the above, the filing requirement regulated by the Egyptian Competition Law is characterised by the following features:

The filing requirement is triggered if the annual turnover of the acquiring company and the target company along with their related parties, combined, exceeds 100 million Egyptian pounds.

The filing requirement applies to any kind of acquisition (i.e., through sale of shares, sale of assets or any other kind of partnership or transfer of business).

The filing is due within 30 days as of the date of the financial closing of the transaction.

While the Egyptian Competition Law dictates the notification of any transaction that satisfies the above-mentioned threshold to the Egyptian Competition Authority, it neither bestows the latter with any authority to block the transaction nor requires the approval of the Egyptian Competition Authority for the completion of the transaction.

According to Article 22(2) of the Competition Law, a fine of between 10,000 and 100,000 Egyptian pounds shall be inflicted on whoever breaches the above-mentioned filing requirement. Notwithstanding the above, and without prejudice to any stricter penalty, a fine of between 20,000 and 200,000 Egyptian pounds shall be inflicted on the concerned party if it deliberately provides the Competition Protection Authority with incorrect data or documents.

On a different note, the Merger Control Provisions of the COMESA Competition Regulations (the COMESA Regulations) have raised increasing concerns regarding its application in the COMESA member states.[2] The COMESA Regulations provide for the mandatory notification of direct or indirect acquisition by one or more persons of the whole or part of a business, in the event that: both the acquiring firm and the target firm operate in two or more COMESA member states; or either the acquiring firm or

2 COMESA (the Common Market for Eastern and Southern Africa) is a regional body of 19 African countries (Burundi, Comoros, the Democratic Republic of Congo, Djibouti, Eritrea, Ethiopia, Kenya, Libya, Madagascar, Mauritius, Rwanda, Seychelles, Sudan, Swaziland, Uganda, Zambia, Zimbabwe, Egypt and Malawi). The Regulations entered into force in December 2004 upon their publication in the COMESA Official Gazette. Thereafter, the COMESA Competition Commission was established under Article 6 of the Regulations and hence the merger control provision therein became operational on 14 January 2013.

the target firm operate in two or more COMESA member states. In relation thereto, the notification obligation applies to all mergers and acquisitions, irrespective of the size of the parties or of the transaction. However, it is important to note that the application of the COMESA Regulations is restricted to activities that have an appreciable effect on trade between COMESA member states and that restrict competition in the region.

According to COMESA Regulations, failure to notify the COMESA Competition Committee of a notifiable transaction (as per the parameters highlighted above) may result in having the transaction ruled unenforceable in the COMESA region in addition to imposing a penalty of up to 10 per cent of either or both of the merging parties' annual turnover in the COMESA Market as reflected in the accounts of any party concerned for the preceding financial year.

However, the enforceability of the above-mentioned Regulation under the Egyptian legal system is still questionable as the COMESA Regulations have never been published in the Egyptian Official Gazette. According to Article 145 of the Egyptian Constitution (which replaces Article 151 of the 1971 Constitution but provides for similar terms), treaties shall have the force of law after ratification and publication in the Official Gazette. Nevertheless, the enforceability of the COMESA Regulations may be based on the fact that the accession agreement whereby Egypt joined COMESA was published in the Official Gazette on 28 January 1999 (the COMESA Accession Agreement) and that the latter stipulates in Article 2 that Egypt will abide by any regulations issued by any of the COMESA organs including the COMESA Council of Ministers. Seeing that the COMESA Regulations have been issued by the COMESA Council of Ministers in December 2004, it may be considered as duly incorporated into the Egyptian legal system as per the above-mentioned Article 2 of the COMESA Accession Agreement.

Notwithstanding the above, the Egyptian legislator has not yet introduced any machinery that would give effect to the COMESA Regulations and there is no legal mechanism that would allow Egyptian authorities to label a transaction ineffective if it fails to comply with the above-mentioned filing regulations or to impose a penalty on the party that fails to abide with the filing requirement. There is also uncertainty as to how the filing requirement as stipulated under Article 19 of the Egyptian Competition Law would be reconciled with the filing requirement embedded under the COMESA Regulations while both regulations provide for significantly different rules. Hence, and in order to fulfil its obligations under the COMESA Concession Agreement, the Egyptian legislator may consider amending the filing requirements under the Competition Protection Law to make them compatible with the requirements of the COMESA Regulations.

X OUTLOOK

Looking ahead, private equity and strategic acquisitions are likely to continue to foster growth in the M&A scene in Egypt. Any relative political stability is likely lead to an improvement of the equity markets, which is typically associated with a surge of M&A activity.

Appendix 1

ABOUT THE AUTHORS

OMAR S BASSIOUNY

Matouk Bassiouny

Omar S Bassiouny is the co-founder and executive partner of Matouk Bassiouny. Omar heads the firm's corporate and M&A practice and has been consistently ranked in band 1 by Chambers & Partners and IFLR in the areas of corporate law and mergers and acquisitions. He has earned special recognition in mergers and acquisitions for his in-depth focus on private equity and venture capital and cross-border transactions.

Recognised for his negotiations skills and business sense, Omar also has considerable expertise in setting-up joint ventures and new projects in Egypt, as well as ensuring compliance with local laws and corporate governance.

Omar focuses on all corporate matters including M&A, public takeovers, restructuring and cross-border transactions. In addition to corporate law, Omar has significant experience on all aspects of investing and doing business in Egypt.

His experience includes advising Emirates NBD on the acquisition of BNP Paribas Egypt as part of Emirates NBD's strategic regional expansion and market entry into Egypt (transaction value: $500 million); and Abraaj Capital on the merger of Al Borg Laboratories with Al Mokhtabar Laboratories, creating the largest private medical diagnostics business in the Middle East and South Asia. Transaction value: $434 million.

MOHAMED OWEIS

Matouk Bassiouny

Mohamed Oweis has graduated from the English Department of the Cairo University Law School in 2011 as the highest-ranking LLB candidate in Cairo university. Afterwards, Mohamed obtained his diploma in Public Law from Cairo University as the highest-ranking public law diploma candidate in 2012. Mohamed joined Matouk Bassiouny in August 2011 and has been engaged in many high-profile M&A transactions in addition to handling many international arbitrations. Mohamed is also a member of the academic staff of the Public Law Department in Cairo University Law School.

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