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TO: Clients and Friends of the Firm

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RE: M&A Made In Ukraine

I. Introduction

For a while, it seemed like all M&A transactions in Ukraine have ceased to exist. Only recently did the M&A activities finally pick up, mostly due to Russian companies coming into Ukrainian market through Cyprus. And yet, there is still much undeveloped potential in Ukraine for the right investor. The rules for acquiring Ukrainian companies, and/or their components, are clearly set forth in the Law "On Joint Stock Companies".

In general, M&A transactions under Ukrainian law include mergers ("zlittya"), accessions ("priednannya"), separations ("podil"), extractions ("vydil") and transformations ("peretvoryennya"). In effect, mergers, accessions, separations and transformations will result in the termination of a legal entity. This means that a winding down procedure will be required for one or more of the parties to the transaction, which will include time necessary for receiving the consent of the Antimonopoly Committee of Ukraine, if applicable, and liquidation in all registration authorities (the Pension and three social insurance funds, the State Statistics Committee, and the State Administration, including an audit by the tax authorities).

In all of the above cases, such transactions are initiated by the general assembly of shareholders of a joint stock company or, in specific cases provided by law, pursuant to a court decision or decision of a government body. Separations and extractions are only carried out pursuant to a court or government body decision. In some cases the law may also require the consent of a government body for terminating a joint stock company via a merger or accession. Importantly, joint stock companies may not partake in simultaneous mergers, accessions, separations, extractions and/or transformations and, therefore, complex M&A transactions require careful

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planning, timing and concerted efforts of the companies involved with their legal advisors and registration departments.

With the above background in mind, immediately below we provide an overview of the various types of transactions in the Ukrainian M&A realm.

II. Types of M&A Transactions

A. Mergers

A merger of two or more joint stock companies results in the birth of a new joint stock company, known as the legal successor, which receives all of the rights and obligations of the merging companies. Simply put, Company A and Company B merge whereby both companies disappear and a new Company C is created.

Merger participants are subject to two restrictions. First, as a result of the merger, the merging companies must terminate their activities simultaneously upon the transfer of their rights and obligations to the legal successor. Thus, a Ukrainian "merger" sounds more like a consolidation under Western M&A concepts. Second, a joint stock company may participate in a merger only with other joint stock companies (i.e., a joint stock company cannot merge with or be merged into a limited liability company).

Once a decision has been made to undertake a merger of joint stock companies, the supervisory council of the participating companies must submit to their general assemblies an agenda of issues for approval, including the termination of each company by way of merger, the terms and conditions of the merger agreement, the charter (articles of association) for the resulting new company, and the text of the transfer act. The merging companies must then hold a joint general assembly of the companies to decide on the creation of the new company's governing bodies. The voting procedure may be determined in the merger agreement.

Upon completion of a merger, all rights and obligations of each participant is transferred to the newly created company – legal successor on the basis of a transfer act. The shares of the

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participating companies' shareholders are subject to conversion into shares of the legal successor or annulment in the established procedure if bought out by the companies. Thus, in the end, the participating companies are terminated and a new company is established in their place.

In a nutshell, the merger procedure can be broken down into the following steps:

1) the participating companies must decide on winding up their activities, creating a termination commission and electing members of the termination commission;

2) the participating companies must satisfy their creditors' claims pursuant to the established priority;

3) the shareholders of the participating companies must exercise their right to the mandatory buyout of their shares by the companies, if they so desire;

4) the termination commission must draw up a transfer act, reflecting the transfer of all rights and obligations of the participating companies to the newly formed legal successor;

5) the supervisory council of each participating company must take a series of decisions, including approval of the draft charter of the legal successor, the explanations and draft of the merger agreement, the transfer act prepared by the termination commissions, and the terms and conditions of share conversions;

6) the supervisory council must order an independent conclusion regarding the terms and conditions of the merger agreement;

7) the general assembly of each participating company must approve the transfer act, the merger agreement, the charter of the legal successor, the election of officers charged with winding up the company's affairs;

8) an application must be submitted to the securities commission, along with all required documents, to register the issuance of shares of the legal successor;

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9) the securities commission will issue a temporary certificate of registration of new shares;

10) the new shares will be assigned an international identification number by the securities commission;

11) the legal successor must conclude a depository agreement with a custodian to service the new shares;

12) the shares of the participating companies will be exchanged for shares of the legal successor;

13) the results of the placement (exchange) of new shares must be approved by the participating companies;

14) the charter of the newly formed legal successor must be registered;

15) the report on the results of the placement (exchange) of new shares must be submitted to the securities commission;

16) the securities commission will register the report on the results of the placement (exchange) of new shares and cancel the share issuances of the terminated merger participants;

17) the participating companies must register the termination of their activities;

18) a new certificate of state registration of a share issuance will be issued to the legal successor.

A merger is deemed final from the date of the introduction of an entry into the Unified State Register of Enterprises and Organizations of Ukraine (Unified State Register) regarding the termination of the merger participants and the registration of the newly created legal successor.

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B. Accession

This amalgamation, which can directly be translated as “unification” or “joining,” is more like the classic merger whereby one or more joint stock companies transfer all of their rights and obligations to another joint stock company which survives the transaction. In simple terms, Company A unifies with Company B and Company B survives while Company A disappears. For purposes of this discussion, we divide the parties into (i) the acceding participant(s) and (ii) the surviving company. As with mergers above, a joint stock company may only accede into another joint stock company.

The accession procedure is analogous to the steps required for the merger procedure as described above. Briefly, the supervisory council of the participating companies must submit the issue of accession and the accession agreement to their general assembly of shareholders, along with the transfer act. A joint general assembly is convened to approve the said issues, the charter of the surviving company and, if necessary, any other issues.

In cases when the surviving company owns more than 90 percent of the ordinary shares of the acceding participant(s), the resulting accession will not require amendments to the charter of the surviving company connected with its shareholder rights. Instead, the supervisory council of the surviving company may take the decisions on behalf of the company to approve the accession, the transfer act and the accession agreement. In addition, the explanation of the terms and conditions of the accession agreement (see Step 5 above) and the receipt of an independent expert conclusion regarding the agreement (see Step 6 above) will not be required.

As a result of the accession, the acceding participant(s) will be subject to termination and their shares will be converted into shares of the surviving participant and allocated amongst the shareholders. Any shares of the surviving company, which were owned by the acceding participant(s), will not be subject to conversion and, instead, will be subject to annulment.

The accession of a joint stock company into another joint stock company will be deemed final from the date of the introduction of an entry into the Unified State Register regarding the termination of the acceding participant(s).

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C. Separation

The separation of a joint stock company entails the termination of the original joint stock company with the transfer of all of its rights and obligations to more than one new joint stock company/legal successor. For sake of simplicity, Company A (the separation target) is separated into Companies B and C (the newly formed companies) with the disappearance of Company A. A separation is not based upon a transfer act, rather it is based upon a so-called "separation balance sheet". A joint stock company may only be separated into joint stock companies. In the West, such transactions are also known as subdivisions or split-offs.

Once again, the separation procedure is carried out in an analogous manner to the merger procedure described in Section A above. The supervisory council of the separation target must submit the separation issue for approval of its general assembly of shareholders. These issues include termination of the separation target, the procedure and conditions of the separation, the creation of the legal successors, the share conversion procedure into shares of the newly created companies, and the approval of the separation balance sheet.

The general assembly of shareholders of the separation target will need to approve all of the above issues and approve the charter and composition of the newly created companies. With respect to share conversion, the shares of the separation target must be converted into shares of the newly formed companies and allocated amongst the corresponding shareholders. Upon placement of the new shares, the joint relations of the shareholders in the charter capital of the separation target must be maintained. As a result of the termination of the separation target, each shareholder of the separation target will receive shares of each of the newly formed companies.

If the separation target is required to buyout its own shares from shareholders before the separation transaction is completed, then such shares will not be subject to conversion and, instead, will be subject to annulment pursuant to the procedure established by the securities commission. In the end, each newly formed company will jointly bear subsidiary liability for the obligations of the separation target which arose prior to separation but were transferred under the separation transaction.

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A separation transaction is deemed final from the date of the introduction of an entry into the Unified State Register of Enterprises and Organizations of Ukraine (Unified State Register) regarding the termination of the separation target and the registration of the newly formed companies.

D. Extraction

The extraction of a joint stock company involves the creation of one or more joint stock companies out of an existing joint stock company without the termination of the existing joint stock company. Under an extraction transaction, a portion of the rights and obligations of the existing joint stock company are transferred to the newly created joint stock company (companies) pursuant to a separation balance sheet (see separation above).

As an example, Company A (the extraction target) transfers a portion of its rights and obligations to Companies B and C (the newly formed companies) but Company A survives the extraction transaction. Similar to the aforementioned M&A transactions, only joint stock companies may be extracted from a joint stock company. In Western jargon, such transactions are commonly known as spin-offs or sometimes split-offs depending on the country.

Analogous to the other M&A procedures, the supervisory council of the extraction target must submit the following extraction issues to its general assembly of shareholders for approval: (i) the approval of the procedure, terms and conditions of extraction; (ii) the creation of a new company (companies) and their governing bodies; (iii) the conversion procedure of a portion of the target's shares; and (iv) approval of the separation balance sheet. With respect to the share conversion, there are two options: (i) distribution of the shares of the newly created company (companies) amongst the shareholders of the extraction target or (ii) the acquisition of shares of the newly created company (companies) by the extraction target. Thereafter, the general assembly of shareholder of each of the newly formed companies must approve their company charters and their governing bodies.

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The share placement(s) of the newly formed company (companies) must maintain the joint relations which existed between the shareholders in the charter capital of the extraction target. In addition, any shares of the extraction target, which were bought out from shareholders by the company during the extraction procedure, may not be transferred to the assets of the legal successor(s), are not subject to conversion, and are subject to annulment.

As a result of an extraction transaction, the extraction target will bear subsidiary liability for the obligations transferred to the newly formed company (companies) pursuant to the separation balance sheet. The newly formed or extracted company or companies will bear subsidiary liability for the obligations which arose in the extraction target prior to the extraction but did not transfer to the newly formed company (companies). If two or more companies were extracted, then such companies will jointly bear subsidiary liability for the obligations together with the extraction target.

An extraction transaction will be deemed final from the date of the introduction into the Unified State Register of an entry on the establishment of the newly formed company (companies) which were extracted from the extraction target.

E. Transformation

A transformation, otherwise known as a "conversion", means the change of a joint stock company's legal or business form with the termination and transfer of all of its rights and obligations to the legal successor pursuant to a transfer act. For example, a joint stock company may be transformed or converted into a limited liability company or any other company form under the Law of Ukraine "On Economic Associations". Like in many other countries, this type of M&A transaction is not very common due to the public nature of many joint stock companies.

Procedurally, the supervisory council of the joint stock company must submit the required issues for approval by its general assembly. Firstly, the general assembly must decide whether it wishes to transform the company into a different business form. Secondly, it must decide upon the transformation procedure and conditions. Finally, the general assembly has the task of

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approving the procedure for exchanging its shares of stock for participatory interests in the legal successor's share capital.

Upon transformation, the shareholders of the newly created business entity become known as "participants", as most other business forms in Ukraine do not issue shares of stock. Rather, the shareholdings of the participants are represented by participatory interests in the authorized capital of the newly created business entity (for example, a limited liability company). Thus, the general assembly of participants will need to approve the new founding documents of the legal entity, including the charter, and the election and appointment of the management body pursuant to the requirements of legislation.

In distributing the participatory interests in the new business entity to the participants (former shareholders), the joint relations between shares of stock of the shareholders in the original joint stock company in the authorized capital of the company must be maintained for purposes of initial registration. If the company bought out shares from shareholders during the transformation procedure and did not sell and/or extinguish them pursuant to law, then such shares will not be subject to transformation into participatory interests and will be annulled.

A transformation is deemed final from the date of the introduction of an entry into the Unified State Register of Enterprises and Organizations of Ukraine (Unified State Register) regarding the termination of the initially registered joint stock company and the registration of the newly converted legal successor/business entity.

III. Merger (Accession) Agreement or Separation (Extraction, Transformation) Plan

The supervisory council of each joint stock company participating in an M&A transaction is charged with drafting the terms and conditions of either the merger (accession) agreement or separation (extraction, transformation) plan. Regardless of the type of transaction in question, the agreement or plan must contain, at a minimum, the following:

1) the full name and requisites of each participating company;

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2) the procedure and coefficients of the conversion of shares and other securities, as well as the amount of possible cash payouts to shareholders;

3) information on the rights to be provided by the legal successor(s) to the securities owners (other than the rights attached to their shares of stock) of the terminated participant(s) or, in the case of an extraction, the extraction target and/or the list of steps to be taken with respect to such securities;

4) information on the proposed parties, who will become officers in the legal successor(s) after finalization of the transaction and the proposed remuneration or compensation for such officers.

The supervisory council of each participant must also prepare for its shareholders an explanation of the terms and conditions of the merger (accession) agreement or separation (extraction, transformation) plan. The explanation must contain an economic substantiation of the feasibility of the transaction, including the appraisal value of the company's assets and a calculation of the coefficient of the conversion of shares of stock and other securities.

If a participating company has over 100 ordinary shareholders, then the supervisory council must obtain a conclusion of an independent expert (auditor, appraiser) regarding the terms and conditions of the proposed transaction. The independent conclusion must contain an evaluation of the substantiality and adequateness of the methods applied to the appraisal of property and share conversion calculation.

Once the supervisory council is prepared to approach the shareholders with its proposed transaction, it must send to the shareholders its findings in order to provide them with the opportunity to familiarize themselves with the transaction and prepare for voting at the general assembly of shareholders. These materials must include the draft merger (accession) agreement or separation (extraction, transformation) plan, an explanation of the terms and conditions of the agreement or plan, the conclusion of the independent expert, if necessary, and, in case of a merger or accession, the annual financial report of the other participating companies for the past three years.

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When the general assembly of shareholders of each participating company convenes, it must resolve the issues related to termination as a result of the transaction (where applicable), approval of the terms and conditions of the agreement or plan, and the transfer act or separation balance sheet. Of course, the material terms and conditions of a merger or accession agreement approved by the general assembly of each participating company must be identical.

IV. Miscellaneous Issues

This article presents only a brief overview of the painstaking process called an M&A transaction in Ukraine. Significantly, shareholders always have the right to refuse to participate in an M&A transaction and exercise the right of mandatory buyout of their shares by their companies. In all such cases, the shares bought out by the company will not be subject to a conversion procedure. In conversion cases, the participating companies may elect to receive cash payments in lieu of shares of stock, provided that their charter allows for the receipt of cash and a clear cut procedure is provided by either the merger (accession) agreement or the separation (extraction) plan.

In case of issuance securities other than shares of stock, the relevant company must provide the owners of such securities with the same volume of rights that was provided to them prior to undertaking the underlying transaction. Once the M&A transaction is finalized, each shareholder (participant) will possess the same number of votes it had under their previous shares of stock or participatory interests prior to the transaction.

During the course of any M&A transaction, the parties will need to also take into consideration the protection of their creditors' rights by publishing an official notice of the transaction prior to its finalization. Each creditor must have the opportunity to either secure their rights or demand premature termination or performance of obligations prior to finalization of the transaction in question.

Other issues such as notice to the securities commission, re-registration of shares or the relevant share conversion procedure may also be time consuming and are beyond the scope of this article.

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Finally, those participating companies which will be terminated as a result of an M&A transaction must also keep in mind the lengthy, complex and cumbersome liquidation procedure established by Ukrainian law. Thus, it is vital to all participants in an M&A transaction to do careful due diligence, plan ahead and ensure quality professional assistance at all stages of the transaction.

V. Conclusion

Although the number of M&A transactions has declined significantly in the last couple of years, in Ukraine they continue to be governed by the legislation described in this rather lengthy memorandum. And since Ukrainian legislative acts (and, in particular, those pesky, detailed instructions that support the primary legislation) often change, please feel free to contact us if you have any follow-up questions.