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INTERNATIONAL

MERGERS AND ACQUISITIONS

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LEGAL ALERT: legal regulation on mergers and acquisitions in mongolia

Mergers and Acquisitions refer to establishment of a new company by consolidation of companies (Merger), or uniting another company by purchasing it (Acquisition) through financial transactions between those companies.

Mergers & Acquisitions is carried out by companies for the purpose of covering their operational capital gaps and expanding their operations. The primary goal of this method is to buy time, because of the priority of speed and time in business than anything else, so using this business solution is a very optimal, time-efficient choice.

In this alert, you will find information on how issues related to mergers and acquisitions are regulated in Mongolia.

I. REGULATION UNDER THE COMPANY LAW

Mergers and acquisitions are defined as “consolidation of companies” /Merger/ and “uniting companies” /Acquisition/, and regulated as one of the ways to reorganize a company in the Company Law of Mongolia.

A. Consolidation of companies is defined as “termination of activities of two or more companies and the transfer of the rights, obligations and liabilities of such companies to a newly established company”. In other words, it is Merger of more than two companies.

The resolution/decision on consolidation and the consolidation agreement must be adopted by an overwhelming majority of the votes of shareholders eligible to vote who attend the meetings of each company and the draft resolution and the agreement defining the conditions and procedures for reorganization, charter of the newly created company, and the proposal defining the procedure for converting the securities of each company must be submitted to the shareholders' meeting. As a result, the shareholders of the old companies have the right to own the shares of the new company. The voting rights of shareholders participating in the shareholders' meeting are equal to the converted voting rights set forth in the company's reorganization agreement

B. Uniting companies is defined as “termination of the activities of one company and transfer of the rights, obligations and liabilities of such company to another company” which in other words is acquisition of a company by another company. The acquisition of the company will be carried out in the same process as the merger of companies. The board of directors /in the absence, the executive management/ shall prepare the draft decision/resolution on acquisition of the company, an acquisition agreement, and proposal for the procedure for converting the securities of the target company into securities and other assets of the acquiring company, and submit to the meeting of shareholders of each company. The decision/resolution on reorganization of a company through acquisition shall be adopted by an overwhelming majority of votes of shareholders eligible to vote who attend the meetings set forth. If, prior to a proposed acquisition, the acquiring (surviving) company owns more than seventy-five percent (75%) of the common shares of the target company and it is deemed unnecessary to amend the charter of the acquiring

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(surviving) company, the Board of Directors (in its absence, the shareholders meeting) of the acquiring company may adopt a resolution on the acquisition and determine the procedures to be followed in giving effect to the acquisition.

2.1. Rights of shareholders During a Reorganization¹

Reorganization of a company can have a significant impact on the position and interests of shareholders. If the company is reorganized by means of reorganization /merger, acquisition, separation, division, transformation/, the shareholder who voted against the decision has the right to demand for buyback of his shares from the company. On the other hand, the shareholder loses all rights other than the preceding right. The shares of the shareholder who has not exercised this right, his/her shares will be converted according to the reorganization decision/resolution and the shareholders of the reorganized company will enjoy the above rights. Within 15 working days after the decision to reorganize the company, the reorganized company shall notify the creditors and other clients in writing of the reorganization. In the case of a joint-stock company, it must notify the Financial Regulatory Commission of Mongolia and a securities trading organization of the decision/resolution within 3 business days. The reorganization of the joint-stock company shall be registered to the State Registration Authority on the basis of permission by the Financial Regulatory Commission.

2.2. Company Reorganization Case (Acquisition of a company)

For the purpose of integrating the assets and resources of APU JSC and Evergreen Investments LLC in the most optimal way to create a new value in the liquid food industry, the Board of Directors of APU JSC, upon its resolution No.17/22, dated July 6, 2017, decided to acquire Evergreen Investments LLC by issuing 321,304,553 ordinary shares with a nominal value of 10 mongo to the ownership of shareholders of Evergreen Investments LLC in a closed market, and submitted such proposal to an extraordinary meeting of shareholders for final decision. Accordingly, the shareholders meeting adopted the proposal for reorganization of APU JSC through acquisition of Evergreen Investments LLC and the activities of Evergreen Investments LLC was terminated and its rights, obligations, and responsibilities were transferred to APU JSC².

II. STAGES OF MERGER AND ACQUISITION OF COMPANY

To simply put, company acquisition is the sale of activities between companies. Unlike other acquisitions, the activity or the object of the transaction includes tangible assets such as real estate and buildings, savings, securities, intellectual property, debt and liabilities, and relations with interdependent economic values, thus, it is complicated to determine the amount directly and requires an elaborate process, such as selecting multiple types of trade. Therefore, the company goes through several stages until the target company is acquired. Therefore, the company goes through several stages until it is acquired.

First of all, the acquiring and the target company enter into a memorandum of understanding that

¹ Г.Давааням, Хувьцаат компанийн эрх зүйн үндсэн ойлголт, УБ., 2021 он, 223 дахь тал

² Resolution of the Extraordinary Meeting of Shareholders of APU JSC No. 2, 18.08.2017, file:///C:/Users/Grata-08/Documents/LEGAL%20ALERT/A5_brochureok.pdf

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sets out the general terms and conditions after considering the offers of each company and exchanging information. Following this, the two companies conclude a contract on the agreed general terms and conditions. The final agreement is concluded based **on due diligence analysis**³ by the buyer, and the sale is closed. However, the above-mentioned actions will not be carried out in the case of a hostile acquisition of a company whose shares are traded on the stock exchange. So let's take a look at the legal due diligence with respect to friendly takeover.

2.1 Negotiation on General Terms and Conditions

The first step in acquisition of a company is the negotiation through financial advisors and law firms. When negotiations for the acquisition of a company begins, the seller must provide the buyer with basic information related to the object of the transaction which is the activity. Despite less importance of this information compare to the data as a result of the due diligence analysis, it is an opportunity to obtain critical closed and insider information, thus, it is required to enter into a non-disclosure /confidentiality/ agreement. After signing the confidentiality agreement, the parties to the contract come to mutual will and agree on the general terms and conditions such as the object of the transaction or the assets, structure of the acquisition, and the purchase price. As previously mentioned, until the final contract for the acquisition of the company is concluded, the buyer must conduct a due diligence analysis to check the activity or the object of the transaction, as well as select the most favorable form of acquisition of the company, and determine the specific terms and conditions.

In the main agreement:⁴

1. The breakdown of the economic conditions and structure of the purchase price of the asset that is the object of the acquisition;
2. Important conditions related to the purpose of the acquisition;
3. Conditions related to the due diligence analysis;
4. Confidentiality clause with respect to the information obtained from the due diligence analysis;
5. Conditions related to conclusion of a transaction with the right to conclude monopoly or dominant transactions;
6. Obligation to negotiate in good faith;
7. Conditions related to the obligation to inform the public.

The seller and the buyer will determine the main terms of the contract until then.

2.2 Legal due diligence

a) Necessity of due diligence⁵

The due diligence shall be conducted to investigate all information and facts about the parties to the contract, their legal status, activities, assets, finances, subject of the agreement, and the

³ Eng. Due diligence is the concept of due diligence related to the company to be purchased. There are several types of due diligence, including asset due diligence, legal due diligence, and operational due diligence. The probability analysis is carried out by experts in each case.

⁴ S.Batbayar, National Institute of Law, "Main methods of company acquisition and reorganization: Experience of foreign countries", 2013, page 23, <https://legaldata.mn/b/229>

⁵ T. Mendsaikhan, Contract Law, First Edition, UB., 2021, page 180

factors affecting them, and to determine the actual situation. For example, extensive due diligence before purchasing a company can provide more detailed information about the company and identify its strengths and weaknesses. Market, financial, and legal due diligence are usually carried out in the course of the negotiation process or before the contract is signed. Financial research is primarily done by certified public accountants, while market research is done by specialized professionals such as economists and professional business investment advisors. As for lawyers, they are responsible for conducting the legal due diligence.

b) Scope of legal due diligence

Legal due diligence usually conducted in the following three areas: ⁶

- Determining the legal status of the parties to the agreement;
- Verifying the legal basis of the agreement, the subject of the agreement or the property and rights to be acquired under the contract, works and services to be performed, and the joint activities, the validity of relevant documents, and the accuracy of the relevant facts;
- Identifying the risks and other obstacles that may affect the validity and implementation of the contract.

Additionally, in order to identify the personal status⁷ and legal status of the person/legal entity that is going to conclude the contract, the legal capacity and competence, the full right of representation, and the full right to conclude the contract may be checked. Risks related to the conclusion of the contract and other factors that may affect or hinder the performance of the contract shall be determined during the legal due diligence. The scope and type of work in this third area will be determined specifically depending on the purpose and characteristics of the contract. For example, in the case of negotiation for the purpose of investing in and cooperation with a company, the law firm shall examine, in accordance with relevant laws and regulations, various information and compliance of documents related to the company's shareholders, assets, immovable property rights, operations, special licenses, major transactions, conflict-of-interest transactions, debit, credit, solvency, intellectual property rights, litigation, labour issues, etc., and prepare a report.

III. REGISTRATION REQUIREMENTS RELATED TO MERGER & ACQUISITION

A new company established as a result of merger of companies becomes legitimate upon registration with the state registration authority.

While, if a company has acquired another company, it shall become valid upon deregistration of the target company and registration of the amended charter of the acquiring company /if any/.

The following documents are required for registration with the state registration authority⁸:

No	REQUIRED MATERIALS	RECOMMENDATION

⁶ T. Mendsaikhan, Contract Law, First Edition, UB., 2021, page 181

⁷ Personality includes a person's name, age, gender, marital status, citizenship, residential address, registration number, and occupation. Depending on the content and importance of the contract, some of these information may be clarified.

⁸ General Authority for State Registration, <http://burtgel.gov.mn/service/index.php/les-newlist/les-new>
<https://gratanet.com/regions/mongolia>

1	Application UB-03, UB-12 forms	Download from http://burtgel.gov.mn/service/index.php/lesnewlist/download
2	Verification sheet for the name of the legal entity	A person authorized to apply for the name of a legal entity may visit in person at the state registration office or submit a request electronically.
3	Receipt of payment of state stamp duty and service fee	<ul style="list-style-type: none"> • The fee for name verification service is 10,000 MNT • State stamp duty 44,000 MNT • Service fee for issuing control number of stamps is 10,000 MNT
4	Certificate of state registration /original/	The changes in the information of the legal entity shall be registered and indicated in the state registration certificate.
5	Decision/Resolution/ Minutes of the meeting /1 copy/	The decision/resolution/ on reorganization shall be made separately by all participating legal entities. /if there are 2 or more shareholders, the minutes of the meeting shall be made and signed by the chairman of the meeting/
6	Charter /2 copies/	Shareholders of the acquiring legal entity and newly reorganized legal entities shall approve their revised charter. /conclude a shareholder agreement, if applicable/
7	Copy of passport of foreigners	If the founder, executive director or authorized person is a foreign citizen, a copy of the passport of that citizen
8	Proof of address of the legal entity	Certificate of immovable property /copy/, lease agreement. /the residence address of the founder is acceptable/
9	Certified Financial Statements	The financial statements during and after the re-organization shall have been certified by the finance and treasury department of the respective district
10	The acquisition agreement /1 percent/	It shall be signed and certified by the shareholders of the acquiring and the target companies.
11	The opinion of the Authority for Fair Competition and Consumer Protection of Mongolia /merger, acquisition/	In the event of a merger or amalgamation of a dominant legal entity, an opinion shall be obtained from the Authority for Fair Competition and Consumer Protection in accordance with Sections 8.1 and 8.2 of the Law on Competition.
12	Permission of the competent authority	If you are engaged in activities such as banking, insurance, auditing, etc., you will need a written permission issued by relevant authorities such as the Ministry of Finance and the Financial Regulatory

		Commission of Mongolia.
13	Reference from the tax office	Section 10.6 of the Law on the State Registration of Legal Entities (in the case of merger, acquisition, and division of legal entities, the taxpayer's deduction card/form /TB-03/ must be submitted)
<ul style="list-style-type: none"> • <u>In case of reorganization of a legal entity with foreign investment:</u> <ol style="list-style-type: none"> 1. The decision of the competent authority to permit foreign investment in accordance with Article 21.1 of the Investment Law. 2. If the document is executed in a foreign language, it must be translated into Mongolian by certified translator. If it is executed in a foreign country, it must be certified by an "Apostille" certificate, and a notary or a consul. 3. Executive management, founders, officials authorized to represent without power of attorney, and other persons authorized by power of attorney have the right to apply 		

References:

1. Law on Company (2011), Retrieved from <https://legalinfo.mn/mn/detail/310>
2. The Law on the Securities Market (2013), Retrieved from <https://legalinfo.mn/mn/detail/9243>
3. General Authority for State Registration, <http://burtgel.gov.mn/service/index.php/les-newlist/les-new>
4. S. Batbayar, National Institute of Law, "Main methods of company acquisition and reorganization: Experience of foreign countries", 2013, <https://legaldata.mn/b/229>
5. T. Mendsaikhan, Contract Law, First Edition, UB., 2021
6. G. Davaanyam, Basic concepts of joint-stock company law, UB., 2021
7. Resolution of the Extraordinary Meeting of Shareholders of APU JSC No. 2, 18.08.2017, file:///C:/Users/Grata-08/Documents/LEGAL%20ALERT/A5_brochureok.pdf
8. FRC, "Procedures for making offers to purchase shares of joint-stock companies on a mandatory and voluntary basis" Annex to Resolution No. 163 dated 5.28.2010

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