Implementation of the SRD II Provisions on Related Party Transactions

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Abstract

In 2017 the European Union adopted amendments to the Shareholder Rights Directive enacted a decade earlier. Among the changes was a new Article 9c dealing with the topic of related party transactions (RPT). This paper analyses how that new provision has been implemented in a range of Member States and assesses its impact on the prior laws of those states.

Compared with the initial proposals of the European Commission, Article 9c as adopted was considerably watered down. Allegedly inspired by the related party provisions of the UK Listing Rules, those proposals mandated disclosure at the 1% level of significance (measured typically by the value of the company's assets), accompanied by a fairness opinion, and approval by the independent shareholders (majority-of-the-minority (MOM)) at the 5% level). As enacted, MSS were given a choice of MOM or board approval and freedom to set the criterion for triggering the approval requirement. The same freedom as to trigger was accorded to the MSS in relation to disclosure and the requirement for a fairness opinion was dropped.

In consequence, MSS had a wide range of choices to make at the transposition stage. A major focus of this piece is an analysis of the choices actually made by the MSS (Part 3). This provides a basis for the assessment in Part 4 of the impact of Article 9c in moving the laws of the MSS towards a more demanding orientation. There are three main conclusions. First, the requirements of Article 9c for approval of RPT had limited impact. No MS which did not already have MOM adopted it in the transposition process. As for board approval, which was already widespread in the laws of the MSS, it is doubtful whether the transposition of the Article ensured the independence of the board members called upon to approve the transaction. Second, it is likely that the most important change required by the Article was public disclosure, even if shorn of the fairness opinion. The adverse impact of disclosure on the company's share price is potentially capable of reducing the levels of wholly one-sided RPT. Public disclosure, although already required by the laws of some MSS, was not widespread.

Third, and more optimistic, there is evidence that the process of transposing Article 9c caused MSS to review their laws on RPT more generally and, in some MSS, this provided an opportunity for reformers to secure changes beyond those required by the Article itself. This might be termed the "catalysing" effect of transposition. The outcome in any particular MS turns on the balance of power between reformers and conservatives, but transposition gives reformers the opportunity to make a case which might otherwise not have been available to them.

Keywords: related party, approval, majority-of-the-minority, disclosure, materiality, Shareholder Rights Directive, harmonisation.

JEL Classifications: H73, K22, Z18

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ABSTRACT

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Compared with the initial proposals of the European Commission, Article 9c as adopted was considerably watered down. Allegedly inspired by the related party provisions of the UK Listing Rules, those proposals mandated disclosure at the 1% level of significance (measured typically by the value of the company's assets), accompanied by a fairness opinion, and approval by the independent shareholders (majority-of-the-minority (MOM)) at the 5% level). As enacted, MSS were given a choice of MOM or board approval and freedom to set the criterion for triggering the approval requirement. The same freedom as to trigger was accorded to the MSS in relation to disclosure and the requirement for a fairness opinion was dropped.

In consequence, MSS had a wide range of choices to make at the transposition stage. A major focus of this piece is an analysis of the choices actually made by the MSS (Part 3). This provides a basis for the assessment in Part 4 of the impact of Article 9c in moving the laws of the MSS towards a more demanding orientation. There are three main conclusions. First, the requirements of Article 9c for approval of RPT had limited impact. No MS which did not already have MOM adopted it in the transposition process. As for board approval, which was already widespread in the laws of the MSS, it is doubtful whether the transposition of the Article ensured the independence of the board members called upon to approve the transaction. Second, it is likely that the most important change required by the Article was public disclosure, even if shorn of the fairness opinion. The adverse impact of disclosure on the company's share price is potentially capable of reducing the levels of wholly one-sided RPT. Public disclosure, although already required by the laws of some MSS, was not widespread.

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1. Introduction

This paper reports on the implementation in selected Member States of the provisions on related party transactions (RPT) inserted by Directive 2017/828 into Directive 2007/36/EC through its new Article 9c ("Transparency and approval of related party transactions"). The paper covers the following countries: Austria, Belgium, France, Germany, Italy, the Netherlands, Poland, Spain, Sweden and the United Kingdom. While not covering all the EU Member States (MSS), the analysis does include all the major economies, nearly all the founding MSS, some countries which have joined more recently and one country no longer a member of the EU, including countries whose corporate governance institutions have to deal with different shareholding structures, and countries from different "legal families" (French, Germanic, Nordic, common law).

In this paper, the 2017 Directive is referred to as the Shareholder Rights Directive II (SRD II) and the original 2007 Directive as the Shareholder Rights Directive (SRD). The date set for transposition was 10 June, 2019. Overall, it requires that all MSS implement special approval and disclosure rules addressing RPT in companies incorporated in their jurisdiction the shares of which are admitted to trading on a regulated market ("listed companies.").

This paper is divided into five principal parts. Following this introduction, **Part 2** describes the background to the Directive and the issues left open for the MSS at the point of implementation. **Part 3** presents the MSS' implementation decisions against the provisions of Article 9c, in particular, how the MSS have exercised the choices left open to them by the Article. **Part 4** assesses Article 9c against the laws of the MSS. It discusses whether the MSS laws on related party transactions (RPT) have become more robust as a result of the transposition process or have only been slightly affected, either because they were substantially in compliance with the Directive's requirements before its adoption or because of the changes made at MS level were of little practical impact. The Directive is a minimum harmonisation provision, which means that MSS must meet the standards it lays down but they are in principle free to exceed them.[1] Thus, a further question concerns the extent to which the laws of the MSS have been harmonised as a result of the transposition of Article 9c. **Part 5** concludes.

There is one terminological point that needs to be made at the outset. There is probably no corporate law system in the EU which has not, from an early stage, regulated transactions between a company and its directors as a matter of potential conflict of interest. The significance of the term "related party" is that it goes beyond directors to include non-directors who are in a potentially conflicted position, notably *substantial shareholders*. Regulation of related party transactions thus has particular resonance in jurisdictions where controlling shareholders are commonly found in listed companies. However, it may also be salient in dispersed shareholding jurisdictions, where director tunnelling is more common, if regulation specific to RPT involves the use of techniques, such as ex ante disclosure to the market, which do not feature in standard corporate law.[2] In what follows, unless the context makes it clear otherwise, we exclude from consideration rules applying only to directors and not more broadly. Directors are, of course, included within the wider category of related parties.

[1] Preamble, paragraph 55, SRD II.
[2] This may explain the early adoption of RPT regulation in the UK, the location of the reforms in the listing rules and the setting of the disclosure threshold at the apparently low level of 0.25% of the company's assets etc.

2. Purport of the Directive

2.1 The Regulatory Issues

It is well recognised that the regulation of RPT involves numerous trade-offs which the rule-maker must address.[3] At the core of the problem there is, on the one hand, the risk that a corporate controller will extract for itself value which ought to be shared with all the shareholders in the company. There are numerous ways of extracting value in a non pro rata way, but a transaction between the controller and the company is a commonly employed method. This is because the opportunity to use it arises frequently in the normal course of the company's activities and because the fairness of the transaction is often difficult for outsiders to assess. The term "related party transaction" (as opposed, say, to "controller transaction") captures indirect as well as direct transactions, for example, a transaction between the company and another entity in which the controller of the first company holds a bigger economic interest than in the controlled company or between the company and a relative of a controlling shareholder or director. Such transactions are clearly unfair to the non-controlling shareholders and might call for regulation on that ground alone. Moreover, a jurisdiction in which unfair related party transactions are rife is likely to attract less in the way of minority equity investment – or attract it only on less favourable terms – than one in which they are rare. So, there is a capital markets argument for regulation as well as a corporate governance one.

The regulatory trade-off arises from the fact that, on the other hand, RPT may be value-enhancing from the company's point of view. The related party may be prepared to provide a good or service on better terms than are available from a non-controller. For example, a controller with good inside knowledge of the company may be willing to invest in the company's debt or equity on terms more favourable to the company than a third-party. In extreme cases, the controller, perhaps for reputational reasons, will be prepared to "prop up" a company in circumstances where an outsider would not be prepared to invest at all. The trade-off, then, is that strict regulation of RPT to eliminate unfair transactions may also inhibit value-enhancing ones, and lax regulation to facilitate value-enhancing transactions may permit the extraction of private benefits by the controller. Or, to put the matter another way, the aim of the regulation should be to place the decision on approval of RPT in the hands of the body which

[3] For an incisive summary see L. Enriques and T. Tröger, "The Law and (Some) Finance of Related Party Transactions: An Introduction" in L. Enriques and T. Tröger (eds), *The Law and Finance of Related Party Transactions* (2019).

can be expected to show the lowest total of false positive (allowing RPT which are unfair to the company) and false negative (disallowing RPT which are value-enhancing) decisions. The trade-off presents the rule-maker with a difficult judgement to make, particularly when the rule-maker sits at a "federal" level and has to deal with countries in which the issue of RPT presents itself in different ways and with different levels of intensity.

Linked to the issue of the intensity of the regulation of RPT is the choice of regulatory techniques, of which there are several. The trade-off noted above means that simple prohibition of RPT is unlikely to be a widely used technique, though it can be found in some limited cases, for example, the prohibition of loans by companies to their directors. As to the more widely used techniques, they also embody trade-offs. The core questions are about who is to discharge the task of distinguishing unfair from fair transactions and whether this assessment is to be carried out as a pre-condition for the conclusion of the transaction (ex ante) or only after it has been adopted by the company (ex post). The strongest form of regulation is ex ante approval by the non-controlling shareholders (majority-of-the-minority (MOM) approval), because it goes furthest in injecting the non-controlling shareholders into the decision whether to proceed with the transaction. However, the quality of the decisions achieved in the MOM process depends heavily on the sophistication and expertise of the non-controlling shareholders. Non-controlling shareholders are not normally animated by the prospect of private benefits,[4] but this does not necessarily mean that they are good at identifying transactions which are value-enhancing for the company. This may explain why RPT regulation in many jurisdictions has been associated with the growth of institutional shareholding in listed companies. Institutional shareholders (at least some of them) have not only the incentive to seek such regulation to protect their minority investments but also the expertise to exercise the influence they seek, which in turn makes rule-makers more likely to enact RPT rules. MOM is also a potentially expensive and time-consuming regulatory technique and is not likely to be used across the board. Approval by the "independent" members of the board ("independence" being capable of being defined more or less rigorously) is quicker and cheaper than MOM and potentially more expert, but may allow the controller to exercise excessive influence over the decision-makers,

[4] Occasionally, a non-controlling shareholder may "hold up" a value-enhancing transaction with the aim of extracting a private benefit for itself. For differing analyses of the quality of minority shareholder approval and the likelihood of hold-ups see Z. Goshen "The Efficiency of Controlling Corporate Self-Dealing: Theory Meets Reality" 91 Cal. L. Rev. 393 (2003); E. Rock, "Majority of the Minority Approval in a World of Active Shareholders" in L. Enriques and T. Tröger (eds), above n 2.

even if formally excluded from the approval process, for example, where a controlling shareholder in fact chooses all the board members.

Ex post disclosure of RPT, usually in the company's annual or semi-annual financial statements, is now widely required in accounting standards, whether national or international, but is thought to be the weakest regulatory technique. This is because the information is provided too late to influence the particular decision, though adverse shareholder or market reaction may induce caution on the part of the controller over future RPT. Ex ante or, more likely, contemporaneous disclosure is a more powerful regulatory technique, at least in efficient capital markets. The adverse impact of an unfair RPT on the company's share price (and adverse governance reactions by investors) are likely to be greater when a discrete transaction is reported than when reporting accompanies a range of disclosures about the company's position, as with the release of financial statements. So, although contemporaneous disclosure may not stop an unfair transaction the controller is determined to proceed with, it is likely to reduce the probability of an unfair RPT being put forward, because of the potential cost-of-capital, reputational and corporate governance consequences of transparency.

Finally, there is the technique of ex post liability, where a court or regulator reviews RPT by reference to a standard in order to distinguish unfair from value-enhancing RPT. The law of Delaware is often thought to be the prime example of this approach, with its doctrine of "entire fairness" review by the courts of suspected unfair RPT. As its law has developed, however, Delaware has become a jurisdiction which places significant emphasis on ex ante independent board and MOM approval. If these procedural steps are followed, the standard for ex post review is substantially reduced, almost to a vanishing point when it becomes a business judgement test.[5] There is thus a big incentive for controllers to follow the recommended ex ante procedural steps. A jurisdiction more committed to ex post review is Germany. Through a variety of ex post review possibilities, drawn from both civil and criminal law, notably its law on corporate groups but also the disguised distribution rules, duties of loyalty for directors and controlling shareholders and criminal liability for breach of trust (*Untreue*), German law generates ex ante incentives for controllers to avoid unfair RPT.

As we recount in the next sub-section, the European Commission appears to have started from the position that unfair RPT were a significant issue across the EU, consequently discouraging equity investment from institutional shareholders. It also proposed to implement the most

[5] *Kahn v M & F Worldwide Corp* 88 A3d 635 (2014).

demanding of regulatory techniques: MOM for larger RPT, independent board approval for smaller ones accompanied by contemporaneous disclosure. It appears to have been heavily influenced in its approach by its understanding of the operation of the Listing Rules for the London Stock Exchange, as promulgated by the UK's Financial Conduct Authority (FCA). There was opposition from other MSS, notably Germany, for which strong ex ante rules appeared unnecessary in the light of its ex post liability rules and the involvement of shareholders seemed to undermine its traditional reliance on the supervisory board (with its codetermination requirements) to perform the function of monitoring management.[6]

2.2 The requirements of the Directive for an RPT regime

2.2.1 Background

The EU requirement for an RPT regime in the Member States is a component in the effort to improve corporate governance in European listed companies. The first step in this process was taken by virtue of the EU recommendations regarding remuneration for directors in 2004[7] and independent directors in 2005,[8] as well as by virtue of the SRD in 2007.[9] The SRD was intended to buttress the position of shareholders in companies primarily in anticipation of, and in conjunction with, general meetings of the shareholders. It contained, among other things, basic norms regarding the timing of notices to attend general meetings and the contents of such notices, the right to participate at general meetings by proxy or electronic means, shareholders' right to vote by mail, and the counting of votes.

Still, the discussion involving corporate governance in European listed companies continued and gained new impetus in response to the financial crisis in the latter half of the decade. The crisis inspired new EU initiatives. Initially, these specifically focused on companies within the financial sector. However, in March 2011 the European Corporate Governance Forum, which was a body set up to advise the Commission on corporate governance matters, issued a statement recommending that consideration be given to introducing common principles on RPT across Europe. Only a month later, the Commission presented the idea in the 2011 Green Paper

[6] For a sceptical analysis of the functionality of the German ex post liability regime, given recent changes in German industrial structure, see T. Tröger, "Germany's Reluctance to Regulate Related Party Transactions: An Industrial Organisation Perspective" in L. Enriques and T. Tröger (eds), above n 2, Ch. 15.
[7] Commission Recommendation 2004/913/EC.
[8] Commission Recommendation 2005/162/EC.
[9] Directive 2007/36/EC of the European Parliament and of the Council of 11 July 2007.

on corporate governance.[10] Based on the response the topic was included in the Company Law Action Plan 2012 which signalled that a proposal was to be presented shortly.[11]

In 2014, the Commission presented its original proposal for the SRD II which, like the SRD, had in view corporate governance in listed companies in general. Related party transactions were not the only, probably not even the central, concern of SRD II. It addressed a number of other topics, including the investment objectives of institutional shareholders and their alignment with the goals of the ultimate beneficiaries. A central concept in the SRD II - as in the mainstream global corporate governance discussion - is to boost the long-term engagement of shareholders and guarantee to them greater influence over certain specific corporate decisions. The requirement of an RPT regime is an expression of the latter.

The proposal was negotiated between the MSS in the Council for about a year before a Council agreement was reached. The Commission's original proposal of 2014 on RPT was rather short and drew heavily upon the statement by the European Corporate Governance Forum. Due to strong objections from several MSS, notably Germany and other large MSS, the proposal was changed in several ways during the negotiations in the Council. The end result was, by necessity, a compromise. Some might say a watered-down compromise.

However, due to an EP initiative to include in the Directive a requirement on so-called "country-by-country reporting" (a topic unrelated to RPT) it took almost another two years before the Directive was issued in June 2017 (with no such requirement). The negotiations with the EP had limited impact on the RPT provisions.

2.2.2 Area of application

In the same way as other EU measures in the area of corporate governance, the SRD II focuses on companies the shares of which are admitted to trading on a regulated market. Indeed, as an amendment to SRD, which had this scope of application, it is likely that those drafting and negotiating SRD II assumed that this issue was effectively decided for them. While an RPT regime must be implemented for these companies, it is up to the MSS to decide whether to introduce comparable RPT regimes for companies the shares of which are traded on other market places or for limited companies in general.

[10] The EU Corporate Governance framework, Green Paper, COM(2011) 164 final, 5.4.2011.
[11] Action Plan: European company law and corporate governance - a modern legal framework for more engaged shareholders and sustainable companies, Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, COM/2012/0740 final.

2.2.3 Decision-making process for, and public disclosure of, RPT

The overall purpose of requiring an RPT regime is to ensure that companies and non-controlling shareholders are protected against transactions which are detrimental to their economic interests. In the recitals of the SRD II, it is stated that "transactions with related parties may cause prejudice to companies and their shareholders, as they may give the related party the opportunity to appropriate value belonging to the company".[12] Against this background, the Directive prescribes that the MSS implement a special decision-making process for certain transactions between companies and related parties as well as rules regarding the public disclosure of such transactions.[13] These were the "corner stones" already in the Commission's original proposal, but the rigour of the proposals changed a lot during the negotiations. Basically, the initial proposal required two things. First, Member States should ensure that companies, in case of transactions representing more than 1% of their assets, publicly announced such transactions at the time of the conclusion of the transaction, and accompanied the announcement with a fairness opinion from an independent third party. Thus, the focus was on disclosure contemporaneous with the transaction, significantly supplementing the ex post disclosure in the financial statements already required by International Accounting Standards. Second, Member States should ensure that transactions with related parties representing more than 5% of the companies' assets or transactions which could have a significant impact on profits or turnover were submitted to a vote by the shareholders in a general meeting, with the interested shareholder excluded from voting. The final version of Article 9 moved away significantly from these initial proposals.

2.2.4 Transactions to be covered by the regime

While the Commission proposal for the Directive stipulated that related party transactions representing specified percentages of the company's assets should be covered by the RPT regime, the adopted Directive requires that the regime be applied to "material transactions". What constitutes a "transaction" is not expressly defined in the Directive. While the term readily leads to thoughts of transfers or acquisitions of assets, and it also appears that these types of transaction were what the Commission originally had in mind with the regime, nonetheless – in order to avoid a discussion regarding the scope of the concept of "assets" – the phrase "material transactions" was introduced during the negotiations. The term "transaction" was left,

[12] Preamble, paragraph 42.
[13] Art. 9c.

however, without any further discussion of its meaning. In particular, the Directive does not make a reference here to IAS 24.9, which was used by the drafters for the definition of a "related party"[14] but not for the definition of the term "transaction", even though IAS 24 contains one. Naturally, there are many conceivable "transactions" between companies and related parties other than transfers and acquisitions of assets. Such transactions may involve service agreements, guarantees of related parties' obligations or contracts for the use of corporate assets, the property in which remains with the company, and much more. Does the Directive require that the RPT regime, including the special decision-making process, apply to every conceivable type of transaction? If the transaction can be ascribed a value, the answer to this question may be assumed to be in the affirmative.

More significant was the adoption of the term "material" to define the transactions falling within the Article. As we noted above, the Commission's proposal contained precise criteria to determine the circumstances in which the specified procedures were to be followed. In a major watering down of the proposal, in the adopted Directive this issue was explicitly left to the MSS. The MSS are to define "material" transactions by establishing "one or more quantitative ratios based on the impact of the transaction on the financial position, revenues, assets, capitalisation, including equity, or turnover of the company or take into account the nature of the transaction and the position of the related party."[15] When selecting these ratios, MSS are directed to have regard to (a) the potential impact on shareholders' economic decisions of knowledge of the transaction and (b) the risks of the transaction for the company and its non-related party shareholders. Despite this general guidance, the MSS understood the Article to give them a wide freedom in relation to the choice of an appropriate ratio and thus considerable scope to soften or harden the rules governing RPT, as we see in Section 3.2.2.

2.2.5 Exempted transactions

In keeping with the purpose of ensuring that companies and minority shareholders are protected against transactions which prejudice their economic interests, the RPT regime need not be applied to transactions entered into in the ordinary course of business and concluded on market terms.[16] While the practical argument for this exemption is strong, since in some situations there are likely to be repeated transactions of this type between the company and a related party

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[14] See below 2.2.3.
[15] Art. 9c.(1).
[16] Art. 9c.(5).

which it would be highly burdensome to subject individually to the RPT regime, the exemption was not to be found in the Commission's original proposal. It was introduced as a response to strong opinions from certain MSS during the negotiations. As was also pointed out during the negotiations, the exemption gives companies some leeway to avoid the RPT regime, by taking a broad view of the ordinary course of business or market terms. The Directive's response to this point is to require the company's administrative or supervisory body to set up a procedure to assess periodically whether these conditions are fulfilled, thus pushing the issue further up the company's decision-making hierarchy than it might otherwise fall.

In addition, the Directive allows MSS to exempt some further categories of transactions from the RPT regime. There are five such categories and MSS are free to take all, some, or none of them out of the regime. They are:

> "(a) transactions entered into between the company and its subsidiaries provided that they are wholly owned or that no other related party of the company has an interest in the subsidiary undertaking or that national law provides for adequate protection of interests of the company, of the subsidiary and of their shareholders who are not a related party, including minority shareholders in such transactions;
>
> (b) clearly defined types of transactions for which national law requires approval by the general meeting, provided that fair treatment of all shareholders and the interests of the company and of the shareholders who are not a related party, including minority shareholders, are specifically addressed and adequately protected in such provisions of law;
>
> (c) transactions regarding remuneration of directors, or certain elements of remuneration of directors, awarded or due in accordance with Article 9a;
>
> (d) transactions entered into by credit institutions on the basis of measures, aiming at safeguarding their stability, adopted by the competent authority in charge of the prudential supervision within the meaning of Union law;
>
> (e) transactions offered to all shareholders on the same terms where equal treatment of all shareholders and protection of the interests of the company is ensured.".[17]

2.2.6 The concept of "related party"

Who or what, then, is a party related to a company? In light of the right of the MSS to themselves define what is deemed to be a material transaction, one might expect that the MSS would also be able to determine the purport of the concept, "related". However, this is not the case. According to the Directive, and already in the Commission's proposal of 2014, the term,

[17] Art. 9c.(6).

"related party", has the same meaning as in the international accounting standards adopted pursuant to the IAS Regulation.[18]

The definition of a "related party" in IAS 24 is wide in many respects. As a consequence, the following legal and natural persons will be deemed to be parties related to companies within the purview of the regime:

> a legal person which is part of the same corporate group as the company, irrespectively of whether it is the company's parent, its subsidiary or another subsidiary of the company's parent;
>
> an associated company or joint venture of the company, i.e. an undertaking in which the company holds at least 20 per cent of the voting capital;
>
> an undertaking with which the company is associated;
>
> a natural person (alone or together with a third party) who holds not less than 20 per cent of the voting capital in the company;
>
> a board member or managing director of the company.

Notwithstanding the fact that the Directive states that the term related party "has the same meaning" as in the international accounting standards, the fact that the Directive is a minimum harmonisation Directive, means that MSS can introduce an even wider definition. By setting significant voting influence at 20 per cent, the IAS definition is in this particular respect less demanding than that used in a number of MSS' rules on RPTs. Consequently, a number of MSS lowered this figure to 10 per cent on transposition, as we see below. During the negotiations there were MSS arguing in favour of the RPT regime covering not only a related party to the company but also a related party to the related party. The concept was introduced but finally taken out again as being too far-reaching.

2.2.7 Choice of approval mechanisms

As we have noted, the Commission proposal of 2014 stipulated MOM for larger RPT. This met with heavy resistance from, among other MSS, Germany and Austria. Hence, the final Directive affords the MSS two ways of obtaining approval. One way is that the general meeting adopts a resolution regarding the transaction, while the other is that the company's administrative or supervisory function takes the decision. As regards both ways, the decision-

[18] Commission Regulation (EU) No. 632/2010 of 19 July 2020 amending Regulation (EC) No 1126/2008 adopting certain international accounting standards in accordance with Regulation (EC) No 1606/2002 of the European Parliament and of the Council as regards International Accounting Standard (IAS) 24 and International Financial Reporting Standard (IFRS) 8, OJEU 20 July 2010, L 186/1.

making process is to be such that it is able to "prevent the related party from taking advantage of its position and provide adequate protection for the interests of the company and of the shareholders who are not a related party".[19] It is also permissible to combine the two procedures, provided the minimum standards for at least one of them are met.

A director or a shareholder involved in the transaction may not, in principle, participate in the approval or the vote. This, too, was the subject of a great deal of discussion during the negotiations. Accordingly, in the final version, a not readily understood exemption was incorporated according to which the MSS may allow a shareholder who is a related party to take part in the vote provided that national law ensures "appropriate safeguards which apply before or during the voting process to protect the interests of the company and of the shareholders who are not a related party, including minority shareholders, by preventing the related party from approving the transaction despite the opposing opinion of the majority of the shareholders who are not a related party or despite the opposing opinion of the majority of the independent directors".[20] This is a highly obscure provision. The preamble to the Directive gives the example of a supermajority requirement for general meeting approval of a RPT.[21] Whether a supermajority requirement is an effective functional substitute for the exclusion of the related party's votes is, however, contingent on the size of the supermajority required and of the related party's shareholding.

2.2.8 The requirements for public disclosure

MSS are to ensure that companies publicly disclose material transactions with related parties not later than the time at which the transaction is concluded. The announcement must contain at a minimum information regarding the nature of the related-party relationship, the name of the related party, the date and value of the transaction, and other information necessary to assess whether or not the transaction is fair and reasonable from the perspective of the company and of the shareholders who are not related parties.[22] There is, however, no requirement for a fairness opinion from a third party or even a report from the directors giving their assessment of the deal. This was a vital requirement of the Commission's original proposal but was gradually watered down during the negotiations. In the adopted Directive MSS are given an

[19] Art. 9c (4), first paragraph.
[20] Art. 9c.(4), third paragraph.
[21] Preamble, paragraph 43.
[22] Art. 9c(2).

arguably unnecessary permission (in a minimum harmonisation directive) to add a requirement for such a report.[23]

Finally, MSS do not have to use the same threshold both for public disclosure and for approval, but can adopt different definitions of materiality for these purposes, especially by differentiating according to the company size. [24]

3. MSS laws measured against the Directive

In this section we consider the choices the MSS have made where a specific decision has been delegated to them by the Directive or where they have made use of their overall freedom to exceed the Directive's provisions under its minimum harmonisation approach, as well as any examples of MSS' failure to reach the Directive's standards.

As of the end of July 2020, the RPT provisions of the SRD II had been transposed in almost all jurisdictions examined. In most instances, transposition was timely or with a brief delay as against the end of the period for transposition on 10 June 2019. The exceptions were Belgium,[25] Italy,[26] and Spain[27]. In these countries, ongoing politically difficult situations hindered timely transposition.

3.1 Scope of application

All MSS considered comply with the requirement to apply the Directive's provisions to companies listed on a regulated market in the EU and incorporated in the MS in question. Only

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23 Art. 9c(3). Conceivably this apparently unnecessary permission was introduced in order to constrain MSS' freedom action in the following way: "Member States shall ensure that the related parties do not take part in the preparation of the report".

24 Art. 9c(1).

25 Implementation in the Law of 28 April, 2020.

26 In Italy the SRD II was implemented with Legislative Decree No. 49/2019 of 10 June 2019. This decree delegated Consob (the Italian Securities Commission) to issue within 180 days the detailed rules required for the transposition of the Directive by way of modification of the existing rules on RPT that were adopted by Consob with Regulation 17221/2010 of 12 March 2010. However, the new Regulation has not yet been published and the 2010 rules are still in force. In the present paper, reference will be made to the draft regulation published by Consob in its consultation paper of 31 October 2019 (downloadable at http://www.consob.it/web/consob/novita/-/asset_publisher/xMXdfdeSuZFj/content/documendo-di-consultazione-del-31-ottobre-2019-recepimento-direttiva-shareholder-rights/10194).

27 For Spain a Draft Bill for a Law to amend the recast text of the Capital Companies Act to adapt it to Directive (EU) 2017/828 of the European Parliament and of the Council has been approved and sent to theParliament: (h http://www.congreso.es/public_oficiales/L14/CONG/BOCG/A/BOCG-14-A-28-1.PDF).

few MSS go further: France applies the RPT regime to all its corporations whether publicly traded or not, and even to LLCs.[28] This reflects its prior domestic law on RPT, which was equally extensive. The Italian RPT regime also applies to companies the shares of which are widely distributed in the public.[29] In addition to this action by MSS it is to be noted that both the London Stock Exchange and Euronext Dublin run markets for smaller companies which are not regulated markets but to which the Exchanges have applied RPT regimes which in some respects go beyond what the Directive requires.[30]

The UK is a partial exception, not to the regulated market requirement but to the incorporation limitation. Its prior rules on RPT applied to companies which had chosen a premium listing on the Main Market of the London Stock Exchange, whether they are incorporated in the UK or not.[31] The Directive required the UK to introduce RPT rules for those companies (the minority) which have chosen a standard listing. These new rules also were applied to standard-listed companies incorporated both in the UK and (with modifications) elsewhere but outside the EEA ("rest of the world" companies).[32] This was done with the aim of ensuring equal treatment of all standard listed companies. This is, therefore, an example of the "spill over" of EU law into areas formally outside its jurisdiction. In the discussion below of the UK the rules for standard-listed companies will be the main focus, but reference will also be made to the more demanding rules for premium listed companies by way of contrast.[33]

3.2 Transaction

3.2.1 The meaning of "transaction"

As noted above, SRD II does not define the term "transaction". Just over half of the surveyed MSS also leave the term open, though they may add the occasional limited piece of clarification. In some cases, this lack of specificity in the transposing legislation may not matter because national law has already developed a serviceable notion of a "transaction" in other commercial

[28] Code de Commerce, Art. L223-19, L225-38, L225-86, L227-10.
[29] See CONSOB Regulation 17,221 Art 2, which remains unchanged according to the proposal for modifications.
[30] See London Stock Exchange, *AIM Rules for Companies*, 2018, Rule 13 and Sched. 4; *Euronext Growth Markets Rule Book*, 2019, Rule 5.18.
[31] These rules were made by the Financial Conduct Authority (FCA) are set out in Chapter 11 of the Listing Rules (LR).
[32] The rules for standard listed companies incorporated in the UK were also made by the FCA and are set out in the Disclosure Guidance and Transparency Rules Sourcebook, Chapter 7.3. Their modified application to standard-listed companies incorporated in the "rest of the world" is set out in LR 14.3.25-26.
[33] With the UK's functional exit from the EU scheduled for the end of 2020, the UK would be free to revert to a RPT regime applying only to premium-listed companies. It is unclear whether there will be pressure to do this.

contexts. France appears to be in this category, although its law refers to the notion of "agreement" rather than "transaction". Elsewhere, the penumbra of uncertainty which surrounds the term as used in SRD II remains at national level. However, in order to make the term more concrete some MSS have referred to the concept of "transaction" contained in IAS 24.9, either explicitly, as in the case of Italy[34] and Spain,[35] or by implication, as can be seen from the similarity of the national and IAS definitions. Thus, in Germany the term is defined as "legal transactions or measures by which an object or another asset is transferred or made available for use against payment or free of charge".[36] This clearly includes non-contractual transfers of property, which sometimes happen within groups of companies.[37] Both are clearly influenced by IAS 24.9. Those MSS which have not adopted a comprehensive definition of the term "transaction" have often added limited clarifications of the term. Belgian law, for example, embraces decisions as well as transactions ("*opérations*"). UK law extends the meaning of a transaction so as to include "arrangements".

A particular issue in this area is whether a failure to act can constitute a transaction, for example, where the company does not move into a particular line of business in order to leave that area free for an important shareholder to exploit or decides not to exercise an option against a related party. Failure to act can be a way of transferring a corporate opportunity to a related party without any formal decision of the company. Most Member States do not mention the issue. In Germany, failures to act are explicitly excluded.[38] In Belgium, it is possible to bring failures to act within the RPT rules, provided the failure results from a "decision" of the board.

3.2.2. The meaning of a "material" transaction

Article 9c states that MSS "shall" define materiality "by reference to one or more quantitative ratios based on the impact of the transaction on the financial position, revenues, assets, capitalisation, including equity, or turnover of the company or take into account the nature of transaction and the position of the related party." This provision gives the MSS significant freedom of action on this point and it is an area in which there is considerable variation in the MSS' approaches, though most make the decision by reference to the company's financial

[34] See the proposed CONSOB Regulation Art 3 (1) a).
[35] See Art 529 vicies Ley de Sociedades de Capital (LSC) as amended by the Draft bill. The IAS are referred for the subjective definition of "related party", but Spanish law does not provide an objective definition of "transaction"
[36] German AktG Art 111a(1).
[37] See T. Florstedt, Der Aktionärsschutz bei Geschäften mit nahestehenden Personen gem. § 107 AktG und §§ 111a-c AktG, Zeitschrift für das gesamte Handels- und Wirtschaftsrecht 184 (2020) 10 at 27.
[38] German AktG Sec. 111(1)(3).

statements. At one end of the spectrum, the French legislator chose not to introduce materiality criteria, but to rely solely on the separate provision in the Article excluding transactions in the ordinary course of business (considered below). It considered this choice to be compliant with the Directive on the basis that it is only a minimum harmonisation directive and therefore that all transactions may be included within the scope of the regime (unless, as is not the case here, the Directive requires exclusion of a particular type of transaction). At the other end, the Netherlands is the only MSS which chose to define materiality by reference to non-quantitative ratios. Its test is whether information about the transaction would be considered inside information under article 7 of the Market Abuse Regulation (MAR). It is controversial whether this particular choice of a non-financial test can be brought within the final words of the extract from Article 9c just quoted. In any event, it is clear that the impact of the Dutch approach is to reduce significantly the impact of the Article in the Netherlands. No transactions additional to those already covered by MAR will be required to be disclosed under the national law transposing Article 9c, though some additional information will need to be given in relation to disclosable transactions, in order to cover fully their related party aspects (see 3.4.1 below).

3.2.3 Valuation

In the other MSS surveyed, where quantitative criteria are deployed, at least three questions arise. The *first* question is how to calculate the value of the transaction, the *second* how to calculate the value of the company (which can be conceived in various ways) and the *third* question is the point at which the ratio between the values is to be considered material. A possible *fourth* issue is whether the same materiality threshold is used for both disclosure of the transaction to the market and for approval of the transaction.

3.2.3.1 Valuing the transaction

Calculating the value of the RPT (the numerator) might be easy when the transaction consists of the transfer of an asset with an easily ascertained market value. By contrast, it might be problematic, for example, where the RPT involves long term service contracts, leasing agreements etc.

The UK simply does not address the issue in relation to standard-listed companies, while for premium listed companies the issuer is obliged to consult its "sponsor" (usually an investment bank) over potentially material RPT, the sponsor being expected to act as a "gatekeeper" on the matter of valuation. Other MSS give only limited help on this issue. Polish law deals only with the special (but important) case of single transactions involving recurring multiple performances, for example under a long-term lease contract, essentially by requiring the value of the individual performances to be summed to determine the value of the transaction, as well as giving guidance on how to value transactions if executed for an indeterminate period (in such a case performances for the first 3-year period of the contract are taken into account).[39] In Austria, as well, via the explanatory notes to the legislation,[40] some guidance is given on particular types of RPT (though not the same as in Poland). With loans, the accumulated interest payments are relevant. If the company provides collateral, the value of the transaction is the fee (and not the value of the goods used as collateral). Germany requires simply an assessment of the "economic" value, Swedish law the "market" value, and Italian law the "fair" value of the transaction, where its value is not obvious from the transaction itself.

It seems correct to conclude that, just as the Directive does not set out how the transaction is to be valued, so also most of the MSS have not addressed comprehensively the issue of how to calculate its value and have handed it down the chain to the companies covered by the rules.[41] In the light of the wide range of transactions potentially caught by the RPT rules, this is perhaps to be expected, but the approach does expose companies to considerable legal uncertainty. Whether the resulting incentive for companies is to take a broad or a narrow approach to valuation will depend, presumably, on how constraining the domestic rules are and the rigour with which they are enforced. For example, if the rules are strongly enforced but easy to comply with, the incentive generated by the uncertainty is to bring the transaction within the procedure, and vice versa.

3.2.3.2 Valuing the company

The next question is how to calculate the value of the denominator – normally taken as the value of the company's net assets as revealed in the balance sheet. Sweden, however, adopts the market value of the company's shares as the denominator in the calculation,[42] whilst the UK[43]

[39] See Polish Act on Public Offering, the Conditions Governing the Introduction of Financial Instruments to Organised Trading, and on Public Companies 90h(2)-(3).
[40] 910/A XXVI. GP, p. 16.
[41] Dutch law does not address this issue, consistently with its non-quantitative definition of the materiality criterion, nor does the issue arise in French law in line with its decision not to set a materiality threshold.
[42] See Chapter 16a Section 2 The Swedish Companies Act (2005:551). The Swedish approach has the merit of approaching both the nominator and the denominator of the calculation on the same basis, i.e. by reference to market values.
[43] Profits, assets, market capitalisation or gross capital (with extensive guidance being provided on how to calculate these items). This reflects the approach previously adopted for premium-listed companies.

and Italy use multiple tests, some based on the balance sheet and some based on capitalisation. Satisfying any one of the tests will trigger the procedure. Those MSS which use the book value of the assets as the denominator nevertheless, and arguably inconsistently, often use market values to assess the value of the enumerator (the transaction), as we saw above.

3.2.3.3 Setting the ratio for materiality

The third and final task is the choice of the percentage trigger for the RPT to be considered material. The typical choice is 5%, but a few MSS are lower (Belgium and Sweden 1%; Germany 1.5%; Spain 2.5% of turnover as an alternative to the 5% of the assets test) and Austria is higher for disclosure purposes (see below). Comparisons of the choices made are very difficult and sometimes irrelevant, partly because, as already indicated, the percentages refer to different items. The Swedish 1% market to market ratio is most likely not comparable to the Belgium 1% where the ratio is calculated as market value to book value.

Another reason for caution is the fact that much depends on the size of publicly traded companies in different jurisdictions. It has been estimated that in Germany a 5% level for approval would require between 7% and 12% of listed companies to seek approval of a RPT at least once a year, whilst lowering that figure to 1.5% (as was done in the final version of the transposing German law) raised the percentages to between 13% and 28%.[44] By contrast, a limited empirical investigation in the UK revealed that in a three-month period in 2007 (when RPT rules applying only to premium-listed companies were in operation for companies on the Main Market of the London Stock Exchange), the 5% rule for shareholder approval was triggered in only four cases out of a population of some 600 companies. None of these cases involved a FTSE 100 company (i.e. the largest companies trading on the Main Market of the LSE). Equally startling, the 5% test for disclosure by smaller companies on the Alternative Investment Market (not in fact within the Directive) produced more disclosures than the apparently more demanding 0.25% test for disclosure by companies on the Main Market.[45]

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[44] A. Engert and T. Florstedt, "Which related party transactions should be subject to ex ante review? Evidence from Germany" *Journal of Corporate Law Studies* (forthcoming); T. Florstedt, "Die wesentlichen Änderungen des ARUG II nach den Empfehlungen des Rechtsausschusses" (2020) 41 Zeitschrift für Wirtschaftsrecht 1,6.

[45] See P. Davies, "Related Party Transactions: the UK Model" in L. Enriques and T. Tröger (eds), *Law and Finance of Related Party Transactions* (Cambridge UP, 2019) 390.

3.2.3.4 The same ratio for disclosure and approval?

A further issue is whether the same materiality threshold is used for both disclosure of the transaction to the market as for approval of the transaction.[46] In the original Commission proposal, a lower threshold was set for disclosure (1%) than for approval (5%), but this distinction was lost when the decision on materiality was shifted to the MSS. In fact, all the MSS which have set materiality thresholds in response to the Directive used the same level for both purposes, with the exception of Austria. Significantly, Austria sets a higher (10%) level for disclosure as compared with 5% for board approval.[47] This suggests that mandatory disclosure was a more constraining change for companies than mandatory board approval, contrary to what one might initially expect. This is presumably because disclosure potentially has a significant impact upon the share price, whereas the board typically knows about important RPT because of its constitutional position within the company, irrespective of the requirements of the Directive, and quietly approves of them where they are in favour of a controlling shareholder. In 2018, no transaction in a listed company in Austria would have passed the higher threshold.[48]

Overall, it can be seen that giving the MSS a wide freedom to set materiality thresholds allowed them to control very significantly the practical impact of the new RPT rules in their jurisdictions. Of course, there is an argument for not subjecting insignificant RPT to the Directive's procedures, even if they do not arise in the ordinary course of business and are not conducted on market terms, but the Directive does not require the materiality criteria to be chosen with this object alone in view. When setting the criteria MSS are simply required to take into account only two rather general criteria: "(a) the influence that the information about the transaction may have on the economic decisions of shareholders of the company; (b) the risk that the transaction creates for the company and its shareholders who are not a related party, including minority shareholders."[49] Only France, following its pre-Directive policy, seems to embrace whole-heartedly the proposition that most RPT should be subject to the Directive's procedures. Significantly, this outcome is achieved by *not* making use of the freedom given to

[46] If the national rules require shareholder approval of the RPT, then disclosure will necessarily occur at that point, as is the case in Sweden, but it would be compliant with the Article to set a *lower* threshold for disclosure. As we saw in the previous paragraph, the UK adopted this approach for premium-listed companies: shareholder approval at the 5% level and disclosure at 0.25%.
[47] See Austrian AktG Art 95a(3) and (5).
[48] J. W. Flume, Transaktionstransparenz und Vermögensbindung in der AG, GesRZ 2019, 230, 234. U. Torggler, Auf halben Wegen und zu halber Tat: AktRÄG 2019 beschlossen!, Recht der Wirtschaft 2019, p. 431.
[49] Art 9c(1).

MSS by Article 9c (1) to set materiality criteria and by using the separate exemption for RPT reflecting the "ordinary course of business" to avoid the unnecessary triggering of the procedure for trivial RPT.

3.2.4 Aggregation of transactions

In order to close an obvious way of escaping the materiality thresholds, Article 9c(8) requires transactions with the same related party to be aggregated if they did not by themselves meet the materiality threshold and the threshold test then to be applied to the aggregated amount. The aggregation period is defined as "any 12-month period or in the same financial year". The "or" seems to be understood in all MSS as an option for the legislator, which makes sense as in most cases transactions in the same financial year also take place within a 12-month period.[50] The surveyed MSS divide more-or-less equally between the two options of a rolling twelve-month period and a fixed financial year. However, the two choices do not have the same implications for the practical impact of the rules. The former appears better adapted to discouraging opportunistic conduct. Thus, for example, in Austria, which has chosen the financial year and adopted a 10% threshold for disclosure,[51] transactions at the 9% level at the end of one financial year would not have to be aggregated with a transaction at the same level at the beginning of the following financial year for the purposes of disclosure to the market.

There is also a highly technical issue about how the aggregation requirement applies to the earlier transactions, which by definition will have been carried out without compliance with the Directive's procedures. It is possible to require disclosure of the earlier transactions at the point at which the aggregation threshold is crossed, though this necessarily means that the requirement for disclosure at the time of the conclusion of the transaction is not applied to the earlier ones. The only practical way of implementing the approval requirement is to apply it only to the transaction which carries the aggregate over the threshold. It also follows that non-compliance with the approval requirements in relation to the last transaction in the sequence should not involve any adverse legal consequences in respect of the earlier transactions. German law adopts this approach.[52]

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[50] Only exceptionally, a financial year can be shorter than 12 months.

[51] See Austrian AktG Art 95a(3) and (5).

[52] See German AktG sec 111(b)(1) - requiring approval only of the transaction which takes the aggregate over the threshold and 111(c)(1) requiring disclosure of the earlier transactions only at the point the threshold is crossed. The UK rules bizarrely state that when the threshold is crossed the company must comply with both the disclosure and approval requirements in relation to *each* of the aggregated transactions (unless an earlier transaction was independently subject to those requirements): DTR 7.3.13.

3.3 Related party

3.3.1 The definition of related party

As noted above, the Directive adopts itself a definition of related party, by reference to IAS 24. The dominant form of transposition is simply to refer to that definition in the national law. Since the Directive is a minimum harmonisation measure, it appears to be open to MSS to add to (though not to subtract from) the IAS categories. Spanish law takes advantage of this freedom by adding shareholders holding 10%[53] or more of voting rights or shareholders "represented on the board by directors" to the list of related parties.[54] French law did not adopt the approach of referring to the IAS definition, taking the view that its domestic definition did not need amendment. Consequently, the perimeter of the French RPT regime appears sometimes wider than the European one (in particular through the inclusion of "indirect interests" and of agreements entered into by a corporation with shareholders owning at least 10% of voting rights or with the parent company of such a shareholder[55]) and sometimes narrower, especially in a group context. Where the domestic definition is broader than that deployed in the Directive, the result is not problematic; where it appears to be narrower, this is an example of partial non-compliance. The list of persons specifically identified as "related parties" under French law is much shorter than that provided for in IAS 24. It does not encompass family members, all entities that belong to the same group or having a significant influence, associate or joint venture entities.[56] Contrary to what some have claimed, the French reference to the notion of "indirect interest" appears insufficient to fill the gap since, according to case law, it requires that the interested person has benefitted from the transaction.[57]

[53] For premium listed companies, the UK also includes a 10% shareholder. See LR 11.1.4 and 4A. However, for standard-listed companies the UK has adopted the IAS definition without amendment.

[54] This automatic application of the abstention rule to proprietary directors has been controversial in the literature. See LATORRE, N., *El control de las operaciones vinculadas en la sociedad cotizada*, 2020, 156; and LEÓN, F., "Las operaciones con partes vinculadas en la Directiva 2017/828", RDM, 312, 2019, V. In favour of the rule PAZ-ARES, C.,"Identidad y diferencia del consejero dominical", *Estudios sobre órganos de las sociedades de capital. Liber Amicorum Fernando Rodríguez Artigas y Gaudencio Esteban Velasco,* Juste y C. Espín eds), vol. II, 2017, pp. 39ff.

[55] In French joint stock companies, the Act of 15 May 2001 for New Economic Regulations ("*nouvelles regulations économiques*" or "NRE") further expanded the scope of the RPT regime, requiring approval for transactions between companies and shareholders owning at least 5% of voting rights or with a company controlling such a shareholder. The threshold was increased to 10% by an Act of 1 August 2003.

[56] The UK faced a similar problem. Its definition of a "related party" for premium listed companies was in some respects narrower than IAS 24. It solved the problem by applying the (lower) approval requirements for RPT within standard listed companies to premium listed companies in those cases where the premium listed rules did not apply because of the narrower domestic definition of related party. See DTR 7.3.11.

[57] Note, however, that the French securities regulator, by way of recommendations, extends the notion of "indirect interest" in order to ensure an independent approval of the transaction, see *infra* § 3.5.

3.3.2 The parties to the transaction

Having defined a related party, it would seem to follow that the Directive applies simply to transactions between the listed company and the related party as defined. As with aggregation, however, it can be argued that extensions are required to avoid circumvention of the core obligations of the Directive. There are two versions of this point. First, it can be argued that some transactions between the company and someone other than the related party need to be included because there is a risk that a related party will benefit nevertheless from the transaction or arrangement. The UK rule-maker has accepted this argument in two cases. One is the case of joint financing of an asset or undertaking by the company and the related party, where there is not necessarily any transaction between the company and the related party. The risk is that the terms of the financing unfairly benefit the related party. The other is a general anti-avoidance provision: "any other similar transaction or arrangement . . . between an issuer and *any other person* the purpose and effect of which is to benefit a related party."[58] The latter is also the case in French law, which includes within the scope of the RPT regime any agreement entered into either directly or through an intermediary ("*personne interposée*") and agreements in which a concerned party is indirectly interested.

3.3.2.1 Transactions between subsidiaries and parties related to the parent

The second version of the point is that comprehensive regulation points to the inclusion of some transactions between related parties of the company and persons other than the company. In particular, it can be argued that non-listed subsidiaries of the listed company should be included within the rules when they transact with a related party of the parent. (If listed, the subsidiary will be subject to the RPT rules in its own right.) If transactions between non-listed subsidiaries and parties related to the parent are outside the scope of the RPT rules, then it would seem possible to avoid the application of the Directive's rules at the parent level by transferring assets to the subsidiary and then (but perhaps not immediately) to the related party of the parent. On this matter the Directive is ambiguous. Article 9c(2) and (4), dealing with public disclosure and approval respectively, refer to transactions "with related parties", without expressly identifying the other party to the transaction. By contrast Article 9c(7) requires companies to "publicly announce material transactions concluded between the related party of the company and that company's subsidiary." This suggests that the approval rules do not apply to transactions

[58] DTR 7.3.3. This provision simply tracks that previously applied to transactions by premium-listed companies. See LR 11.1.5.

between a subsidiary and a related party of the parent. If approval were required for such transactions under Article 9c(4), it would be unclear why Article 9c(7) was needed for disclosure, since Art. 9c(2) could do the job.

The Directive has been interpreted in this sense by Germany, i.e. as requiring only public announcement of transactions between a subsidiary and a related party of the parent and not approval of them.[59] The same is true of Austria,[60] France,[61] the Netherlands[62] and Poland.[63] By contrast, Italy,[64] Spain,[65] Sweden and the UK[66] apply both approval and disclosure requirements to transactions between the company's subsidiary and a related party of the parent. Belgian law is ambiguous.[67]

Where approval is required for a transaction between the subsidiary and a related party of the parent, that approval is a matter for the board or shareholders of the parent company, since the approval required is imposed on the company which is listed. Given that the approval rule governs a decision of the parent, it is arguable that it does not matter in which jurisdiction the subsidiary is incorporated. The UK follows this logic but Swedish law confines the approval requirement to transactions between Swedish subsidiaries and the related party.[68]

Whether transactions by subsidiaries with related parties of the parent are regulated only for the purposes of disclosure or also for approval, in most jurisdictions the aggregation provisions include transactions by parties related to the parent with both parents and subsidiaries. An exception is Poland, where there is no aggregation.[69] This seems to be the consequence of a

[59] German AktG 111c(4), contrasted with 111b(1) and 111c(1).
[60] Austrian AktG Art 95a(8).
[61] According to the preparatory work of the "PACTE" Act, the implementation of the Directive requirement was deemed unnecessary because transactions concluded with subsidiaries are already included in the corporate governance report pursuant to Article L. 225-37-4 of the Commercial Code, which must be published on the company's website for listed companies.
[62] Art. 2:170 DCC.
[63] See Polish Act on Public Offering 90k.
[64] Article 2391-bis, 2nd alinea provides that CONSOB rules shall apply to the approval of transactions executed by an issuer either directly or through subsidiaries. Article 5 of the proposed regulation, which includes the rules on disclosure, applies also to the RPTs executed by an issuer through a subsidiary.
[65] Article 529s.1 The Draft Bill includes among RPTs those carried out by non-listed "subsidiaries" of the company with related parties.
[66] DTR 7.3.1(1): "a reference to a transaction or arrangement by an issuer includes a transaction or arrangement by its subsidiary company." France too addresses the issue since it does not start from the proposition that the RPT regime is confined to listed companies. See n 21 above.
[67]Loi introduisant le Code des sociétés et des associations et portant des dispositions diverses, 23 March, 2019, Art 7.97.
[68] See Chapter 16a Sec. 9 Swedish Companies Act. The rational given for confining the approval requirement to transactions between Swedish subsidiaries and the related party is that Swedish law cannot regulate the decision-making procedure in a company in another jurisdiction.
[69] See Polish Act on Public Offering 90k.

decision to treat transactions with subsidiaries as a separate class of RPT from those with the parent company, the former seemingly not being covered by the scope of application of Article 9(c)(8). Consequently, the materiality test (5%) is applied separately to related party transactions with parents and with subsidiaries.

3.4 Procedural requirements for RPT

As we noted in section 2.2.2 Article 9c imposes two procedural requirements on RPT which fall within its scope. The first is a disclosure requirement and the second an approval mechanism.

3.4.1 Announcement of the related party transaction and a fairness opinion

All MSS follow closely the provisions of Article 9c on the timing and content of the announcement. As to timing, the Directive requires disclosure of the transaction at the latest upon its "conclusion".[70] There is some uncertainty here whether this provision means that the transaction has to be announced before it is approved. If so, the market and non-controlling shareholders will have a little time to react, potentially adversely, before the approval decision. If approval and announcement are coterminous, that opportunity will not exist. Where the approval mechanism is via the shareholder meeting, as in Sweden,[71] this opportunity will necessarily be the available, since established national law will require that the shareholders be told in good time the facts relevant to the decision they are to take. In the case of board approval, some German commentators take the view that disclosure is required before supervisory board approval.[72] A two-tier board structure facilitates this approach, on the basis that the managing board "concludes" the transaction subject to "approval" by the supervisory board. However, a similar approach is possible within a one-tier board, on the analysis that the management concludes the transaction whilst the board approves it, even if there is some overlap in the membership of the two groups. [73] In other jurisdictions the position is unclear. [74] will require an announcement before the transaction is concluded, for example, an announcement of an intended placing of shares which has not yet been carried out, though a MAR

[70] Art 9c(7).
[71] See Chapter 16a Sec. 7 Swedish Companies Act.
[72] Hüffer/Koch, *AktG*, 14th ed, 2020, 111C, comment 2.
73 DTR 7.3.8: disclosure required "when the terms of the transaction are agreed"; approval of the board before the transaction "is entered into". The LR avoid this problem because they do not require board approval: small RPT are to be disclosed and large RPT are to be approved by the shareholders. There is no third procedural requirement.
74 Regulation (EU) No 596/2014 on market abuse.

announcement will not necessarily carry all the information needed to understand its related party aspects. A clear outlier in relation to the timing of the announcement is Italy where the announcement has to be made within seven days of the conclusion of the transaction rather than at the latest at the time of its conclusion. It appears that Italy takes the view that the market abuse rules deal sufficiently with contemporaneous disclosure, though it is difficult to square this view with the wording of the Article 9c(2).

There is scope for debate about how extensive is the disclosure required by the Directive's catch-all requirement that, in addition to the specific information required, the announcement should contain "other information necessary to assess whether or not the transaction is fair and reasonable from the perspective of the company and of the shareholders who are not a related party . . ." Most States pass the problem on by copying out the Directive's requirement into the national legislation, without amplifying it, though the French rules specify some relevant additional information[75] and the Italian rules require a detailed information document for all major RPTs.[76] Polish law requires that the announcement contains also information necessary to assess whether the transaction has been made on market terms.[77] The Directive requires a public announcement, which most MSS interpret as an announcement on the company's web site.[78] The UK mandates use of the mechanism for making announcements to the market (the "regulatory information service"), though those announcements also appear on the relevant company's web site.

The credibility of the announcement might be enhanced by a fairness opinion. In the end, the Directive did not require this, but it permits MSS to require one and specifies the permissible sources of the opinion: the board (with the related party excluded), a committee of the board consisting of a majority of independent directors[79] (most obviously the audit committee) and, likely to be most helpful, an independent third party. A minority of the MSS surveyed require a fairness opinion: Belgium (committee of independent directors), Italy (ditto), Spain (audit committee/independent third party) and the UK (the company's investment bank sponsor - for premium listed companies only). However, the absence of a formal fairness opinion in the

75 See C. com., Art. R.225-30-1 (also R.225-88-2), introduced by governmental decree n° 2019-1235 of 27 Nov. 2019: the additional required disclosure concerns in particular the purpose of the agreement and the relationship between its price for the company and the company's most recent annual profit.
76 See CONSOB proposed Regulation, Art. 5 and Annex 4.
77 See Polish Act on Public Offering 90i(2) item 4.
78 Similarly, German AktG Art 111c (2) and - at least for the most basic information - Austrian AktG Art 95a(5).
79 Independence here appears to mean independence as defined in corporate governance codes (i.e. independence from the management of the company or a substantial shareholder). It is thus a much wider exclusion that simply not being the related party in a particular transaction.

transposing national regulation must be placed in the context that the board issuing the announcement is usually obliged to opine on the merits of the transaction and may decide, or be encouraged, to supplement its opinion with external support in order to give it more credibility with shareholders and investors or to protect themselves against liability. Thus, the French securities regulator recommends for companies listed on a regulated market the appointment of independent experts in order to assess the most significant RPT.[80] In those MSS where shareholder approval of the RPT is required (see below), rules and practice surrounding the holding of general meetings are likely to produce similar result.

3.4.2 Choice of approval mechanism

This was one of the most hotly debated issues during the negotiations for the Directive, the Commission having originally proposed that shareholder approval should be the only available approval mechanism. As adopted, Article 9c permits MSS to choose between board and shareholder approval and to add a shareholder vote (ex post) where the board approval is the chosen approval mechanism. Not surprisingly, only those States which previously required shareholder approval have adopted this mechanism and the remainder have chosen board approval (except in relation to certain specific RPT where shareholder approval was already required by corporate law). Where board approval has been chosen, only Germany permits the decision to be taken by a committee of the (supervisory) board.[81]

The principal MSS requiring shareholder approval across the board are France, Sweden and Spain. France retains its two-stage procedure: the principal approval mechanism is the board but a transaction approved by the board requires in addition ex post shareholder approval, typically at the next annual general meeting. If the transaction fails to obtain shareholder approval, it remains valid but the related party and the directors have a potential liability in damages to the company. The incentives generated by this procedure are thus for the board not to approve transactions it thinks its shareholders will not support in due course. Spain requires shareholder approval in the case of "large" RPT – transactions[82]. The UK rules implementing

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[80] AMF Recommendation, n° 2012-05, Les assemblées générales d'actionnaires de sociétés cotées, mod. 5 Oct. 2018, Proposition n° 4.6: "Encourage the Board of Directors to appoint an independent expert when the conclusion of a [RPT] is likely to have a very significant impact on the balance sheet or the results of the company and/or the group."

[81] German AktG 107(3).

[82] In Spain the RPT must be approved by the general meeting, if the value of the RPT is equal to or greater than 10% of the total asset items according to the last annual balance sheet approved by the company. The competence to approve other RPT shall correspond to the board of directors, which may not delegate it into the CEO or a managing subcommittee of the board, except in two cases: intra-group transactions carried out in the field of

the Directive require only board approval (i.e. in standard listed companies) but the existing rules for premium-listed companies require shareholder approval at the 5% level.

3.4.3 Independent voting and approval requirements

Article 9c excludes an "involved" director or shareholder from taking part in "the approval or the vote". This leaves a number of unanswered questions. Looking at board approval, all MSS expressly exclude the related party from voting on the approval resolution. All but Austria,[83] Germany[84] and Italy[85] also exclude that person from participation in the board's deliberations leading up to the vote. If one considers that related parties can influence the result of the approval process without casting a vote by simply participating in the deliberations, Austria, Germany and Italy are arguably in breach of Article 9c(4). This point turns on what is meant by the word "approval" in the Article. The Article does not expressly rule out participation in discussions. If the term "approval" is intended to capture some decision-making process other than voting,[86] then the Austrian, German and Italian provisions are permissible. On the other hand, this interpretation means the Directive has failed to address the problem that in small groups which meet frequently, influence can be asserted by dominant persons without themselves having to exercise a vote simply through what they say. Perhaps this is an insoluble problem since a prohibition on speaking or even exclusion from the meeting on the relevant matter would not provide a comprehensive answer to it. As we noted in section 2.1, this conundrum is one of the strongest arguments in favour of taking the decision out of the hands of the board entirely and adopting majority-of-the-minority shareholder approval instead.

It is important to note that the Directive excludes from approval not only directors and shareholders who are parties to the transaction in question, but also directors and shareholders who are "involved" in the transaction with the related party, without being parties to it themselves. This is a formula necessary to take account of the broad definition of "related party"

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ordinary business and under market condition and transactions made under standard commercial conditions, applied generally or collectively and not exceeding 0.5 % of the annual turnover) (art 529 duovicies Draft Bill).

[83] Austrian AktG Art 95a(4) only prohibits participating in the vote, but does not restrict participation in the preceding deliberations.

[84] German AktG 111(b)(2). Contrast 107(3), which excludes the related party from membership when the approval decision is delegated to a committee of the board.

[85] Article 7 and 8 of CONSOB proposed Regulation.

[86] This is perhaps quite strongly suggested by the German text of the Directive which states that the interested person "nicht an der Zustimmung oder der Abstimmung teilnehmen." Suppose the board adopts the policy of approving RPT (or perhaps RPT below a certain level of significance) without discussion and voting, unless one third of the members of the board wish to initiate a discussion and vote. Article 9c(4) would then operate to exclude the interested directors when calculating whether the one third threshold had been crossed in any particular case.

discussed in 3.3.1. It is also arguable, although it is unclear whether the Directive requires it, that shareholders and directors should be excluded who have a relationship with the related party which renders their independence suspect, even if the transaction is not a related one as far as they are concerned. The UK excludes from consideration of the transaction a director who is an "associate" of the related party. The term includes, for example, a close family member of the director or shareholder. That person cannot vote or participate in discussion even where the relationship is not relevant to the characterisation of the transaction as a RPT.[87] German law seems to aim at a similar goal but via a high-level provision which excludes those for whom there is a concern about a conflict of interest.[88] French law excludes any board members "directly or indirectly" interested in the transaction, which is likely to capture at least some persons in the category of associates in the UK.[89] Moreover, the French securities regulator has expressed the opinion that the phrase "a person indirectly interested in an agreement to which he is not a party" should include someone "who, by virtue of his relationship with the parties and the powers he possesses to influence their conduct, derives or is likely to derive a benefit from it".[90] Thus, a corporate shareholder controlled by the shareholder ultimately benefiting from the agreement should not influence the vote on the agreement, nor should the shareholder controlling the company benefiting from the agreement. Poland excludes a member of the supervisory board from voting if the transaction "relates to his or her interests"[91] which seems to be broader than the member just being a party to the transaction, and additionally repeats the decision-making criteria set out in Article 9c(4) first subparagraph.[92] Finally, shareholders acting in concert, in particular where the concert provides for a common voting policy, should not influence the voting on an agreement entered into with one of the concert party.[93]

No MS excludes a director simply on the grounds that, but for the votes of the related party, that director would not have been elected to the board, even though a director aware of that support might be expected to favour the related party's interests. This is an example of the

[87] DTR 7.3.8. For example, the company may contract with a partnership of which one of its directors is a member; the spouse is not a member of the partnership but is a director of the company. Both the director and the spouse would be excluded from consideration of the transaction.
[88] German AktG 111b(2) but not in the case where the decision is taken by a committee of the board where only a majority of its members need to be free from concerns about conflicts of interest: German AktG 107(3).
[89] See also under article 7:96 of the Belgian code, referring to a director who has a direct or indirect financial interest which is contrary to the interest of the company.
[90] Recommendation n° 2012-05, n° 4.2. The relationship between the recommendations of the AMF and the requirements of the law is a matter of some uncertainty.
[91] See Polish Act on Public Offering 90i(4).
[92] See Polish Act on Public Offering 90i(3)-(4).
[93] See Polish Act on Public Offering 90i(3)-(4).

Directive's failure to address the central problem in the board approval mechanism, ie, that a controlling shareholder or even a dominant director does not need to participate in the decision-making in order to have its wishes respected. The other directors will know for themselves what is expected and will act accordingly. However, in Spain the exclusion does apply in the case of a "proprietary" director, i.e. a director who represents a particular shareholder (except within a corporate group).[94] In other countries, some of the general formula mentioned in the previous paragraph might catch the situation of the "nominee" director.

For shareholder meetings, exclusion of involved shareholders from voting is routine[95] but they are normally entitled to participate in the discussion. See Sweden (where shareholder voting is the main approval mechanism),[96] Germany (where it is exceptional)[97] and the UK (where it is required for premium listed companies at the 5% level).[98] It is arguable here that the small-group dynamics which operate in board meetings where there are frequent interactions among the members do not apply to shareholder meetings where the group is normally large and meets only episodically.

None of the MSS included in our survey has made use of the obscure exemption in Article 9c (4) according to which the MSS may allow a shareholder who is a related party to take part in the vote provided that safeguards apply to protect the interests of the company and of the shareholders who are not a related party.

3.5 Exemptions

Article 9c(5) excludes from the approval requirement transactions in the ordinary course of business and on normal market terms unless MSS choose to include them. None of the MSS has chosen to do so, though German and Italian law have delegated the option to companies.[99]

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[94] The duty to abstain from participating to the meeting and voting in the full board meeting applies to the affected directors and to those who represent shareholders affected by the transaction (proprietary directors) (art. 529 duovicies.2 Draft Bill). For the controversial nature of this provision see n 53.

[95] When competence is attributed to shareholders' meeting, Spain excludes involved shareholders from voting only when the majority of independent directors have not given their approval to the transaction. The general rule is that shareholders can vote, but the decision is ex post reviewed by judicial fairness control, with a reversal of the burden of proof when the vote of the concerned shareholder has been decisive for the approval of the agreement. Since the Directive permits MSS to opt for board approval alone, this provision on shareholder voting probably does not infringe it.

[96] See Chapter 16a Sec. 7 Swedish Companies Act.

[97] German AktG 111b(4)(2). Shareholder approval is an available mechanism under German law where the supervisory board does not give its approval and the management board requests the shareholders to consider it.

[98] LR 11.1.7.

[99] German AktG Sec. 111(2)(3); Art 13 (3) (c) of Consob proposed Regulation.

However, as noted in 2.2.4, Article 9c requires the board to set up a procedure to monitor the operation of this exclusion. All MSS have implemented this requirement via a copy-out of the Directive, though Poland's copy-out fails expressly to exclude related parties from this monitoring exercise.[100]

3.5.1 Transactions with subsidiaries

Article 9c(6) permits MSS to exclude a further five types of transactions from the Directive's approval requirements. See 2.2.4. Austria[101] and Germany[102] have taken advantage of all five types of exemption and Belgian law comes close to this position. The first category – transactions between the company and its subsidiary – is used by all MSS. Since all MSS also make use of the exemption for transactions in the ordinary course of business on normal market terms, this exemption is significant for intra-group transactions which do not meet these criteria. This is an important extension, since intra-group transactions are often conducted in the ordinary course of the business of the group but on book values or some other non-market basis. Article 9 envisages that the exemption may be formulated in any one of three, progressively more liberal, ways. The narrowest is where the subsidiary is wholly owned, directly or indirectly, by the company. This is the approach adopted in France and Poland.[103] Here, the rationale for the application of the RPT rules is lacking in functional terms (provided – see 3.3.2 above – transactions between a related party of the parent and the subsidiary are within the RPT rules). The second formulation is where the subsidiary is not wholly owned, but no other related party of the parent has an interest in the subsidiary undertaking. This is the most common form of the exemption adopted in the MSS and it can be argued also to be a situation outside the rationale of the Article. Belgium has taken a narrow view of the notion of "other related party". Transactions between the company and its subsidiaries are brought within the procedure only where a controlling shareholder of the parent holds, directly or indirectly, at least a 25% interest in shares of the subsidiary.

The third possible formulation of the exemption is where national law provides adequate protection for those at risk from the transaction where a related party of the parent does have an interest in the subsidiary. Austria makes some use of this freedom. Thus, for domestic

[100] See Polish Act on Public Offering 90j(2).
[101] See Austrian AktG Art 95a(7).
[102] German AktG Sec. 111a(3).
[103] See Polish Act on Public Offering 90j(1) item 2. The wording used in this provision suggests that the exclusion relates exclusively to direct subsidiaries of the listed company.

subsidiaries, the Austrian legislation contains an exemption for transactions with subsidiaries, even if a related party is one of the subsidiary's shareholders.[104] The legislator justifies this on the grounds that Austrian company law, through various provisions, provides adequate protection in such cases. With non-Austrian subsidiaries, unless the subsidiary is wholly owned or no related party of the parent is a shareholder, the legislator asks for a case-by-case analysis whether the protection of the interests of the company, the subsidiary and the minority shareholders is adequate and thus delegates the decision to the company. Spain makes use of this exemption in a more limited and concrete situation in order to disapply the procedure, even though the subsidiary is not wholly owned, when assets are transferred under a statutory restructuring procedure which provides its own minority protections rules.

3.5.2 Shareholder approval under national law

The second exemption - transactions requiring shareholder approval under other provisions of national law - is widely used, mainly by specifying in the transposing law a list of the transactions which are so exempted. This may appear to be an exemption which eliminates redundancy and overlapping. It is unclear how important the second category of exemption is in practice. In those instances (the minority) where MSS implementing the Article 9c require shareholder approval for RPT, the national rules for shareholder approval for specific transactions may be laxer than the requirements of Article 9c, for example, by permitting a significant shareholder to vote. Whether national approval is permitted to replace approval under the Article in such a case turns on the (unclear) meaning of the proviso to Article 9c.6(b). This makes the permission to use national shareholder approval available "provided that fair treatment of all shareholders and the interests of the company and of the shareholders who are not a related party, including minority shareholders, are specifically addressed and adequately protected in such provisions of law."

By contrast, if the standard method chosen to implement the Directive in a MS is board approval, little will be gained by removing from the board the need to give that approval if at the same time it is promoting under national requirements a resolution to the shareholders on the same topic. This it can hardly do if it does not approve of the substance of the resolution. The same is broadly true of the obligation to make a public announcement about the transaction, since a shareholder resolution in a listed company will be in the public domain. Indeed, not making use of Article 9c's second permission has the advantage that the MS which has chosen

[104] Austrian AktG Art 95a(7) no. 1.

board approval does not need to assess the adequacy of its national rules on shareholder approval against the Article's "fair treatment" standard, and possibly amend them.

3.5.3 "Say on Pay"

Possibly for these reasons, a number of MSS do not make use of the second exemption, even though their national corporate laws require shareholder approval for various corporate transactions.[105] Nevertheless, these MSS may avail themselves of the narrower third category, which concerns shareholders' 'say-on-pay' decisions. Into this category fall the UK,[106] the Netherlands, Spain[107] and Poland[108], while those MSS which make use of the second exemption also use the third, perhaps not surprisingly. The question that arises is why the remuneration exemption has been more broadly used than the general shareholder approval exemption.

It is important to note in this regard that the exemption in Article 9c.6(c) is tied to remuneration approved under the provisions of Article 9a. Art 9a gives MSS two options for implementing "say-on-pay". One is a binding shareholder vote, taken at least every four years, which determines the company's remuneration policy during that period. A remuneration policy is not the same as an agreement reached with a particular director about his or her remuneration. The agreement must reflect the policy but is separate from it. The third exemption thus permits the company to implement the approved pay policy without being required to follow the Article 9c approval process in respect of each implementing decision.

Where the MS has chosen the alternative for the implementation of the "say on pay" rules, i.e. an advisory vote, the exemption permits a MS which has chosen shareholder approval to implement Article 9c to continue with an advisory vote under Article 9a in the particular area of remuneration. Where board approval has been chosen under Article 9c, as in the majority of MSS, the need for the third exemption is less clear, since decisions on remuneration of senior executives are presumably taken by the board or a committee of it. Probably, the main advantage of the exemption is that a public announcement is not required each time the board makes a remuneration decision. Even so, one wonders how many remuneration decisions reach the "materiality" thresholds set in the MSS.

[105] The UK seems to have chosen not to make use of the second exemption precisely because it was uncertain about what the fair treatment standard entailed and whether UK company law met its requirements: FCA, *Consultation on proposals to improve shareholder engagement*, CP 19/7, 2019, para 4.23.
[106] DTR 7.3.5(2).
[107] Art. 529 vicies.2.b Draft Bill.
[108] See Polish Act on Public Offering 90j(1) item 3.

3.5.4 Transactions on same terms

The fourth exception is specific to banks and we do not discuss it here. The fifth exception - transaction on same terms for all shareholders - appears to be one again where the rationale for the application of Article 9c is absent. The exemption refers to what may be termed "sharing rules" which, by definition, very substantially reduce the risk of a special advantage being made available to a particular shareholder. However, a sharing rule does not entirely eliminate the risk. For example, a high dividend may be paid to all shareholders which is motivated by a controlling shareholder's need for cash and which leaves the company less well positioned to invest in its business. How far this risk is ameliorated by the requirement in Article 9c.6(e) that there be not only equal treatment of shareholders but also protection of the interests of the non-controlling shareholders and the company will be a matter for interpretation. The exemption has been taken up in Austria, Germany, the Netherlands and the UK. However, in the Netherlands the proviso just mentioned is expressly included in the domestic legislation and is expected to carry weight in the courts.

Where the MS has chosen board approval to implement Article 9c, the national rules in the obvious cases (dividends, share issues) are likely to require board approval and a public announcement in any event. So, the exemption may appear to be beside the point. The relevance of the exemption may be in those cases where the MS implementing Article 9c has added a requirement for a fairness opinion which the national rules on the particular transaction do not require, precisely because the national regulation is based on a sharing rule.

Where the approval mechanism under Article 9c is shareholder approval, as in Sweden and the UK for premium-listed companies, the exemption may also have some limited value in those cases where the national rules governing the transaction permit approval to be given in advance, for example, in relation to share issues. By contrast, Article 9c requires approval of the "transaction". Without the exemption, the company might have to go back to the shareholders for a second approval under Article 9c when it needed the capital, potentially slowing down the capital raising process.

3.6 Sanctions

Following the standard pattern, the Directive does not lay down sanctions for breach of Article 9c. This is left to the Member States, subject to the requirements that MSS must ensure the sanctions are applied and that they are "effective, proportionate and dissuasive" (Article 14b).

Since in no MSS is the regulation of transactions between a company and a conflicted director a new topic, there exists in all MSS a set of sanctions which can be extended to RPT more widely. The same seems to be true where there has been only a failure to disclose, since disclosure requirements for listed companies, with a sanctioning regime, are now extensive in the EU.

Thus, there are two sets of national sanctions which are potentially available: those laid down in corporate law relating mainly to the validity of the transaction and the liability of directors and others to the company; and those laid down in securities law, usually by way of administrative sanctions on issuers and directors for non-compliance with the rules. The balance between these sanctions varies from jurisdiction to jurisdiction. At one end of the spectrum stand Italy and the UK which have implemented Article 9c via amendments to their securities laws, no doubt because their prior regulation was embodied in their securities laws, and so rely heavily on the sanctions attached to that category of rules. In these jurisdictions the continuing rigour of enforcement by the public authorities is central to the impact of the RPT rules.[109] In Italy the major impact of Article 9c was that it led to a strengthening of the sanctions available to CONSOB for breaches of the RPT rules. The new administrative sanctions for breaches of the RPT rules can be applied by CONSB both to the company and to its directors.[110] Even in those two countries, however, a transaction with a related party who is a director could well amount to a breach of corporate law as well and so trigger corporate law sanctions. The administrative sanctions are typically civil penalties, payable to the regulator or to the State, though other penalties, such as public censure, may also be available. The penalties are typically applied to the company and its directors, rather than the related party, since the obligations under Art. 9c are imposed on the company.

[109] For an analysis of the initially pro-active stance of the securities regulator in Italy but then its apparent falling away see M. Bianchi, L. Enriques and M. Milic. "Enforcement of Related Party Transactions in Italy: One Securities Regulator's Challenge" in L. Enriques and T. Tröger (eds), above n ??, ch 17.

[110] See new Art. 192-quinquies (1) and (2) of the Consolidated Financial Markets Act, which foresees pecuniary sanctions from euro 10,000 to euro 10,000,000 for the company breaching the RPT rules, and from euro 5,000 to euro 1,500,000 for each of the company's directors and auditors. The maximum sanctions had been fixed in euro 150,000 by Legislative Decree 49/2019 implementing the SDR II in Italy, but have been elevated to 10 million and 1,5 million respectively by Art. 2 of Legislative Decree No. 84/2020 of 14 July 2020. This change has been criticised by Assonime (the Italian Association of stock corporations) as being too harsh and possibly exceeding the parliamentary delegation to the Italian Government, considering the maximum amount of the penalties and the fact that the sanctionable breaches have been loosely defined. See News Legislative, 6/8/2020, http://www.assonime.it/attivita-editoriale/news/Pagine/News06082020.aspx. Similar comments have been made by the 14th Permanent Commission of the Italian Senate which, in its opinion on the draft legislative decree, had expressed doubts particularly on the fact that the relevant regime does not distinguish between directors concerning the role performed by each of them in the approval and execution of RPT: see News Legislative, 22/4/2020, http://www.assonime.it/attivita-editoriale/news/Pagine/News220420.aspx.

By contrast, most MSS transposed the Directive by amending their corporate laws, thus triggering corporate law sanctions relating to breaches. These are normally private law sanctions, but in some countries, such as France, criminal sanctions[111] may play a significant role. Moreover, even in countries which make little or no use of the criminal law, a failure to disclose which causes no harm to the company may need to be sanctioned by securities law, as the Spanish[112] rules recognise.

It is clearly a major limitation on the impact of the Directive that it deals effectively with neither sanctions nor enforcement. However, this is a limitation of many EU Directives in the corporate law area.

4. The Directive measured against MSS laws

In this section we seek to assess the impact of Article 9c of the Directive on MSS laws. One question which might be asked is whether the Article has produced a high degree of harmonisation among the laws of the MSS on RPT. However, SRD II was avowedly a minimum harmonisation directive. As stated in its Recital 55: "This Directive does not prevent Member States from adopting or maintaining in force more stringent provisions in the field covered by this Directive . . . to protect the interests of minority shareholders . . ." It follows that a uniform system of regulation of RPT across the MSS was never the objective of the Directive. Subject to the MSS meeting the standards set out in Article 9c (the issue discussed in Section 3), the Directive had no further harmonisation ambitions.

4.1 Shaping of transposing rules by the MSS

Although it is hardly useful to criticise a minimum harmonisation Directive by reference to continuing divergences among the laws of the MSS on the topic in question, nevertheless it is

[111] Through general corporate criminal liability, notably *abus de biens sociaux*, where action may be initiated by both minority shareholders (ut singuli) and the public prosecutors, who seem willing on occasion to initiate high profile cases.

[112] In Spain breach of disclosure duties is sanctioned by penalties included in the securities regulation. Authority to levy the sanctions is attributed to the National Capital Markets Commission (CNMV). Responsibility for complying with the obligation extends both to the company and to the directors, who *may* likewise be subject to the penalty. But there are corporate law sanctions as well in appropriate cases. See art. 232 LSC) and PORTELLANO, "El deber de evitar situaciones de conflicto de interés: entre la imperatividad y la dispensa [arts. 229, 230 y 529 ter.1.h) LSC]", en Roncero, coord., *Junta general y consejo de administración en la sociedad cotizada*, 2016, t. II, pp. 459 y ss.).

relevant to interrogate the level and appropriateness of the minimum standards contained in it. If the impact of Article 9c on the laws of the MSS was marginal or even retrograde, then it can be criticised as representing a waste of EU legislative effort, which could have been deployed elsewhere. If, on the other hand, it moved MSS laws towards a greater focus on RPT, then in our view it is to be welcomed.

As compared with the Commission's original proposals, the minimum standards embodied in the resulting Directive must be judged disappointing. Those proposals required MOM approval at the 5% level and public disclosure at the 1% level, coupled with a fairness opinion. This was fatally undermined by two changes which put crucial decisions in the hands of the MSS at the implementation stage. First, the triggers for the approval and disclosure requirements were left to be set by the MSS themselves through their definitions of what counted as a "material" RPT. Second, MSS were given a choice between MOM approval and approval by the independent members of the board. On a lesser, but still significant scale, the disclosure requirement, which remained mandatory, lost its mandatory accompanying fairness opinion.[113]

These changes have enabled MSS to shape very substantially the Directive's impact in their jurisdictions. The definition of materiality plays a central role in the structure of the Article, since a non-material transaction is excluded entirely from the scope of the Article. As we have seen above, MSS have taken different approaches to this issue, ranging from France, which did not take up the option at all, through Belgium, Sweden and Germany (which adopted low percentage thresholds for materiality – 1%, 1 % and 1,5% respectively) to the common choice of 5% - although, as noted above, these percentage figures do not necessarily measure the same values. Some MSS were arguably able to deprive the Article of significant impact in their jurisdiction in this way, for example, Austria in relation to the disclosure requirement or the Netherlands in relation to RPT not already falling within the ambit of MAR. Even in a minimum harmonisation Directive this degree of flexibility for the MSS is hard to justify. Although it may well be true that different percentage thresholds have similar results in different markets, the failure of the Article to identify a common basis for choosing the relevant percentage in each market meant that MSS essentially had a free hand.

[113] In 2006 Luca Enriques identified optionality at the transposition stage as a major weakness in the company law directives adopted up to that time. See "EC Company Law Directives and Regulations: How Trivial Are They?" (2006) 27 *University of Pennsylvania Journal of International Economic Law* 1.

The second important optional provision in the Article relates to the choice of the approval mechanism: board alone, shareholders alone, board followed by the shareholders. Within that choice was a further option to require or not a fairness opinion from an independent person. Although it is possible to take a sceptical view of fairness opinions, they have considerable value where the body that produces them has no incentive to favour corporate controllers. Overall, in relation to approval, the Article provides a limited "menu" of choices for MSS. But those choices relate to a central element of the RPT rules. It is the conventional (and probably correct) view that board approval is an incomplete protection for minority shareholders in respect of RPT with controlling shareholders, unless very extensive steps are taken, as in Delaware, to exclude the influence of controllers, or unless there is significant influence of non-controlling shareholders upon the composition of the board, whether through stakeholder influence on board composition or appointment rights for minority shareholders. Absent these, it is conventionally thought, further, that majority-of-the-minority approval by shareholders is more effective, provided the minority consists of sophisticated shareholders.

On this basis, giving to MSS the option to choose board approval, without a fairness opinion and with only a general reference to the requirement that the approving directors must be "independent", weakened the impact of the Directive. It is significant that, with the partial exception of Spain (in relation to "large" RPT) the only countries which, when transposing Article 9c, involved shareholders in the approval mechanism on a routine basis (France, Sweden) had adopted that approach before the Directive was proposed.[114] As to the MSS requiring board approval, there is only very limited evidence of MSS improving their prior rules when transposing the Article, so as to provide credible fairness opinions or stronger guarantees of director independence. Thus, the Article did not succeed in mandating an effective mechanism for the protection of minority shareholders, whether by way of MOM or a reliable system of board approval.

4.2 Role of mandatory disclosure

However, shareholder influence may be exercised through mechanisms other than approval. The requirement for the disclosure of material RPT at the time of the conclusion of the transaction may have an important impact on the behaviour of controlling shareholders, as we

[114] The UK is partly in this category. It made use in its prior law of shareholder approval in relation to premium-listed companies and still does so, but it did not extend it to standard listed companies when transposing the Article.

discussed in Section 2.1, and disclosure remained a mandatory element in the Article, albeit shorn of the fairness opinion. In a back-handed way, the Austrian legislator acknowledged the importance of disclosure when providing a higher threshold for disclosure than for board approval. However, no other MS pursued this policy of emasculating the disclosure requirement through a high materiality threshold. It may be that the long-term impact of the Article will lie with the disclosure obligation rather than with pursuit of the Holy Grail of a truly independent board for RPT purposes.

This prediction turns on how it is expected disclosure will impact upon the behaviour of related parties. Disclosure might operate by shaming the controller, particularly where the behaviour is contrary to generally accepted business practices, so that the reputational harm to the related party arising out of continuing with the proposed action is high.[115] Or it may be effective when it imposes costs on the controller, through a higher cost of capital, for example, which outweigh the benefits to it of RPT. Neither mechanism is fool-proof. The first depends of the scope of a jurisdiction's social norms in relation to tunnelling. On the second, a controller who extracts private benefits of control may continue in this course, even in the face of higher costs, because the costs of disclosure (lower share price, higher capital costs) are borne by all the shareholders in the company, whereas the benefits extracted go wholly to the controller. The point at which the private benefits exceed the controller's share of the costs obviously depends upon the slope of the curves which plot these amounts.

Nevertheless, disclosure as a control mechanism over RPT has greater efficacy than it is often given credit for, and so its promotion by the Article is a significant gain in those MSS which previously lacked general ex ante disclosure requirements before transposition of the Article. Thus, one way of assessing the impact of the Directive on MSS laws is to identify those MSS which fall into this category. In Spain the introduction of a duty to announce a RPT as soon as it is concluded represented a significant improvement from the point of view of transparency and supervision through market mechanisms. Even in France, with strong prior RPT rules, the implementation of Article 9c introduced a general requirement to disclose RPT at the time of their conclusion, thus significantly extending the prior ex post disclosure requirements and the continuing obligation to disclose under the Market Abuse Regulation. Belgium and Poland as well lacked contemporaneous disclosure requirements in their prior laws. Clearly MSS without specific prior RPT legislation fall into this category, ie Germany and Austria (though the latter

[115] See Bianchi et al, above at n ??, for an apparent example of this aspect of disclosure in operation.

escaped from it de facto by setting a high materiality threshold). By contrast, MSS with established prior disclosure rules, such as Italy, Sweden and the UK, were not impacted by this aspect of the Article. Nevertheless, at least at the level of the "law on the books", the introduction of contemporaneous disclosure requirements appears as one of the major gains from Article 9c.

4.3 Article 9c as a catalyst for change outside its formal requirements

Going beyond the disclosure requirement, it is possible to argue that, in assessing the impact of the Article, it may be too crude a measure to focus only to its mandatory elements. It is possible to detect a more subtle impact of any new company law Directive when it is transposed into the national laws of the MSS. The transposing process often triggers off a national debate on the regulation of the area in question which ranges beyond what is necessary to avoid the legal consequences under EU law of non-implementation. The MS may review its experience across the board with its existing law and introduce changes which reflect that prior experience rather than the simply what is necessary to implement the Directive. Sometimes, this may lead the MS to focus in its reforms on matters not covered by the Directive at all. This is what seems to have happened it Italy, where the securities regulator's sanctions were strengthened in the light of deficiencies shown up by prior national experience, even though sanctions are a matter expressly left to the MSS by the Directive.[116] Poland is currently considering to introduce the approval requirement for RPT in closely held joint stock companies which is inspired by the transposition of the rules of the Directive in relation to Polish public companies.[117]

In other cases, national reform may focus on elements of the Directive which are optional or which are set out only at a very general level in the EU text. Spain appears to be a good example of this process in relation to Article 9c. Even though Spain has had an extensive RPT regime since 2014, the reforms introduced consequent upon the transposition of the Article included (i) the adoption of a 10% level to identify a substantial shareholder, (ii) a requirement that the announcement be accompanied by a fairness report from the audit committee, (iii) the exclusion of a "proprietary" director from voting on the authorisation of the transaction, even if the director is not a related person in respect of the transaction, if the appointing shareholder is a related party. None of these changes are required by the Article.

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[116] See Bianchi et al, above n ??
[117] Bill on the amendment of the Commercial Companies Code and other Acts of 20 July 2020 (proposed Art. 384[1] of the Commercial Companies Code), https://legislacja.rcl.gov.pl.

A major area of national debate in relation to Article 9c was about the setting of the materiality threshold. Although the Commission's 5% threshold for approval did not end up in the Article, it clearly influenced the choices of many MSS when setting that threshold, thus acting almost as an example of a Commission Recommendation. Yet Germany opted a more rigorous threshold (1.5%), below the Commission's initial proposal, even though this did not reflect any prior German rule. Further, a number of MSS (Belgium, Sweden) remained with their materiality thresholds well below the 5% level or, in the case of France, did not set one. In other words, they did not treat the Commission's proposal as an invitation to relax the stricter criteria.

There is always a risk with a new EU Directive that MSS with more advanced sets of rules than the Directive requires will reduce those levels to the Directive's minimum, either across the board or in relation to significant elements of the Directive.[118] It is significant that this appears not to have happened in relation to Article 9c. In particular, none of Belgium, France, Sweden and the UK, which had well-developed RPT rules in place beforehand, sought to reduce the prior rules to the minimum required by the Directive, whether in terms of the materiality threshold or the approval mechanism. This presumably reflected the view in those countries that strong RPT rules enhance, rather than detract from, the attractiveness of capital markets. Of course, this is not a positive achievement of the Article, but it is an important avoidance of a negative result.

What these disparate outcomes suggest is that the transposition process ignited or re-ignited a national debate on RPT, in which those favouring a stronger regime than the Directive mandated were able to make some gains as against those who wished to do the minimum necessary to comply with the new EU rules. It is important not to become starry-eyed about the process of national debate triggered by the Directive. Its outcome obviously depended on the balance of forces between reformists and traditionalists within each MSS. It was therefore not a mechanism which was likely to promote overall harmonisation of RPT regimes across the MSS. The national debates were also subject to strong path dependencies, as shown by the fact that only MSS with shareholder approval under their prior law chose it as the mechanism for approval under the Article. Equally, it was not a debate which the reformers were bound to win,

[118] An example is the introduction of the "reciprocity" exception as an option for MSS in the Takeover Directive. This was previously regarded as of doubtful legality but was then widely adopted once the Directive was in place. See P. Davies, E. Schuster and E. van de Walle de Ghelcke, "The Takeover Directive as a Protectionist Tool?" in U. Bernitz and W.-G. Ringe (eds), *Company Law and Economic Protectionism - New Challenges to Economic Integration* (OUP 2010)

as the Austrian and Dutch choices of threshold indicate. Nevertheless, overall, most of the MSS did do more than the minimum required of them.

However, there was one country in our study which can be claimed not to have advanced as a result of Article 9c, because of the EU's traditional difficulty in accepting self-regulation as a way of complying with EU rules. Sweden had strong RPT rules in place prior to the Directive, but these were to be found, initially, in rules made by the Swedish Stock Exchange and then by the Swedish Securities Council. From 2012 the Swedish Securities' Council statement of good practice required listed companies proposing to transfer assets to or acquire assets from a director, senior manager or large shareholder to obtain general meeting approval for the transaction, if it was not insignificant for the company. The general meeting resolution had to be accompanied by an appraisal from an independent expert, which had to be disclosed on the company's website prior to the meeting, and the related party's shares were discounted in the vote. In order to implement the Directive Sweden transferred these rules, with some changes, to the Swedish Companies Act, the self-regulation continuing only in relation to markets not covered by the Directive. Whether this has led to a higher level of compliance with the rules is doubtful, especially as under the new corporate law Sweden relies simply on its standard sanctions for breach of duty by directors. Furthermore, the changes made in the transfer of the rules reduced its impact: shareholders count as related parties only at the 20% level, as suggested by the IAS definition, rather than at the 10% level, as under the Securities Council's practice; and there is formally no requirement for the board's statement accompanying the proposed shareholder resolution to contain an independent appraisal, though it may in fact do so.

5. Conclusion

Our overall assessment of the impact of Article 9c, as adopted, on the laws of the MSS is as follows. That impact was limited by the two optional elements in the Article, namely, the freedom around setting the materiality criteria and the choice between board and shareholder approval, coupled with the removal of the mandatory fairness opinion. Setting a high level for materiality and confining approval to the board enabled MSS very substantially to reduce the protective impact of the Article upon non-controlling shareholders. Consequently, the most important mandatory element in Article 9c turned out to be, possibly contrary to expectations, the requirement for public disclosure of the RPT at the time of the conclusion of the transaction (even without the mandatory fairness opinion). However, the weakness of the Article was to some degree counter-balanced by reforming initiatives which MSS chose to take in the transposition process. These national-level choices did not, perhaps, bring about fundamental changes in the applicable RPT regimes, but they did edge them forward towards better regulation in this area.

Could things have been organised differently? It might be suggested that the Commission would have obtained better results had it proceeded by way of a maximum harmonisation Directive or a Regulation. But this argument is not very convincing. Opposition of the same character would presumably have appeared in the discussions in the Council on a maximum harmonisation Directive or a Regulation as in fact occurred in relation to SRD II - and it might have been more vociferous in the face of a proposal which would constrain national action more tightly than SRD II.[119] In fact, there is an additional risk with a Regulation that the advanced standards in some MSS will be degraded as a result of the need to achieve a compromise which all MSS will sign up to. As a matter of legislative politics Regulations require a high degree of unanimity among the MSS that common rules are required, unanimity flowing perhaps from some transnational crisis, such as the financial crisis of 2007-2010, which led even the UK to accept the benefits of a common rule book for the prudential regulation of financial institutions. In relation to RPT such unanimity was lacking.

Alternatively, the Commission might have anticipated the likely opposition to its proposals and embodied more limited, but precise, targets in its proposals. For example, it might have expended its political capital on achieving more elaborate disclosure rules and better safeguards of independent decision-making, whether at board or shareholder level, and not sought agreement on MOM. However, it is much easier to identify appropriate legislative targets with the benefit of hindsight (when it is too late) than at the proposal stage. In any case, this experience might cause the Commission to reflect upon the functionality of its consultation process, which sometimes seems more part of the process of "selling" the proposed legislation than a genuine exercise in teasing out the difficulties lying in its way. What can be said is that the process of transposing Article 9c served to underline the importance of national decision-making in the development of RPT rules. The best hope of further progress is that the issue will remain on national agendas so that reformists can continue to agitate for legislative changes.

[119] For a discussion of the costs and benefits of minimum and maximum harmonisation within the Single Market and for an example of the push-back against maximum harmonisation proposals from the Commission in the area of consumer law see S. Weatherill "The Fundamental Question of Minimum or Maximum Harmonisation" in S Garben and I Govaere (eds), *The Internal Market 2.0* (2020).

Appendix – National Laws Transposing the Directive

Austria

Bundesgesetz, mit dem das Aktiengesetz, das SE-Gesetz, das Übernahmegesetz und das Unternehmensgesetzbuch geändert werden (Aktienrechts-Änderungsgesetz 2019 – AktRÄG 2019), BGBl I 2019/63 (Federal Act amending the Act on Public Companies, the Act on the Societas Europeae, the Takeover Act and the Enterprise Code)

Belgium

Law of 28 April, 2020, amending the Company Code 2019 (Loi introduisant le Code des sociétés et des associations et portant des dispositions diverses; Wet tot invoering van het Wetboek van vennootschappen en verenigingen en houdende diverse bepalingen), especially Art. 7.97).

France

Loi n° 2019-486 du 22 mai 2019 relative à la croissance et la transformation des entreprises, Journal officiel du 23 mai 2019 (loi "PACTE").

Germany

AktienGesetz (Stock Corporation Act), new Sections 111a-c.

Italy

Legislative Decree No. 49/2019 of 10 May 2019, Gazzetta Ufficiale della Repubblica Italiana, 10 June 2019 (and see n 26).

Poland

Ustawa z 16.10.2019 r. o zmianie ustawy o ofercie publicznej i warunkach wprowadzania instrumentów finansowych do zorganizowanego systemu obrotu oraz o spółkach publicznych oraz niektórych innych ustaw, Dz.U. poz. 2217 (Act of 16 October 2019 amending the Act on Public Offering, the Conditions Governing the Introduction of Financial Instruments to Organised Trading, and on Public Companies, Journal of Laws item 2217)

Spain

Texto Refundido de la Ley de Sociedades de Capital aprobado por el Real Decreto Legislativo 1/2010, as amended by the Ley 31/2014, de 3 de diciembre.

Draft Law, ammending the Ley de Sociedades de Capital and other laws in order to implement Directive (UE) 2017/828, de 17 de mayo de 2017, as regards the encouragement of long-term shareholder engagement:

http://www.congreso.es/public_oficiales/L14/CONG/BOCG/A/BOCG-14-A-28-1.PDF

Sweden

SFS 2019:288, lag om ändring i aktiebolagslagen (2005:551).

United Kingdom

Financial Conduct Authority, *Disclosure Guidance and Transparency Sourcebook* (DTR) Ch. 7.3 - contains the rules introduced specifically to transpose Article 9c.

Financial Conduct Authority, *Listing Rules* (LR) Ch. 11 – contains the prior (and continuing) rules applying to premium-listed companies only.

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