

Introductory Speech on Related Party Transaction
of Mr. Xavier Tessier, Head of International Affairs,
Autorité des marchés financiers, French Securities Regulator
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I would like first thank the OECD for the organisation of this roundtable. OECD plays a great and unique role in term of corporate governance, in establishing standards and promoting these standards around the world.

It is indeed a very valuable exercise to share views and experience about corporate governance, in particular, because corporate governance is of course rules and principle, but it success depends heavily, and more than in other field of financial regulation of an ethical behaviour that goes beyond the rule.

The spirit in which corporate rule are applied is even more important than the legal process. Corporate governance is not an exercise of ticking the box, as it was said this morning, it is important that the rule applied have been well identified by the players as useful rule developed to protect the integrity of the market, and the interest of shareholders.

Before going more specifically about the French regulation, let me first mention the report IOSCO has issued some years ago after the corporate scandals of Enron and Parmalat. I would like just to recall because we are in Hong Kong that this report was drafted by the Technical Committee of the Organisation chaired at that time by Andrew Sheng, the former Chairman of the Hong Kong Securities Commission. The report, I quote, underlined that : several recent financial scandals have involved transaction where corporate funds were used to purchase assets from entities controlled by managers or controlling shareholders at what now appear to be considerably inflated prices, or else caused the issuer to sell assets to managers or controlling shareholders at a considerable discount. In many case; these related party transaction have been described as corporate looting to benefit a small number of individuals at the expense of the company's investor

In analysing the various aspects of these scandals and in order to improve the situation, IOSCO's work highlighted in particular seven areas, four are linked with today's topic:

- the first was : Corporate governance, including the role of independent directors on an issuer's corporate board, the protection of minority shareholders, the importance of independent

auditor oversight committees and mechanism to protect against conflicts of interest presented by related party transactions ;

- and associated to that Issuer disclosure requirement including management's discussion and analysis of material events and factor likely to have an impact on the issuer;
- and also, auditor and audit standards including auditor independence, the effectiveness of audit standards and auditor oversight committees;
- and finally, the use of complex corporate structures and special purpose entities, and the circumstances where they may pose particular regulatory issues.

Then the report has clearly underlined that Related party transaction is an issue which is at the cross road of corporate governance, disclosure and transparency and market integrity rules.

Indeed corporate governance is the system of overlapping legal, regulatory, organisational and contractual mechanism designed to protect the interest of a company's owner and limit opportunistic

behaviour by corporate manager who control the company's operation. Generally corporate governance rule protect investors against corporate managers whose interest may not necessarily coincide with those of the company's shareholders. This is a fundamental point to understand, I mean, the differences between the manager and the owner in modern corporate structure. It is probably a challenge in emerging market, when brilliant entrepreneurs decide to make their company listed in order to raise capital. They have then to take into account the interest of all their shareholders. In that case the fear is not that shareholders and management interest diverge but that the controlling shareholders may direct the company in ways that exploit minority shareholders.

IOSCO report on financial fraud underlined three specific measures:

- the independence of members of the issuer's board of director to help protect the interest of shareholders, who own the issuer, against the management who control day to day operation;
- controls to protect against the abusive related party transactions, where issuer assets might be used to benefit senior managers or controlling shareholders and

- legal protection for shareholders, in particular minority shareholders (measures to be reported to general assembly, organisation of general assembly and participation of minority shareholders).

Corporate governance, control mechanism and disclosure, indeed all are closely interrelated. Corporate governance ensures the quality of the internal control and of the information disclose to the public. Internal control and external auditor play a key role in assessing the quality of the various processes and at the end the accuracy of the information published.

The European legislation has clearly recognised this interrelation in its roadmap for company law. After the Corporate scandals, the European commission has taken two series of measures, more directly some work where undertaken in the field of corporate governance in order to strengthen the current regulation and add the missing element. Secondly, in the field of its action plan for financial services, the Commission has take into account the problem raised by this scandals in the drafting of the transparency directive.

The directive 2006/46/CE modifying the 4^{ème} and 7^{ème} directives on company law, not only recalls the collective responsibility of the members of the management board, but also imposes to companies listed in Europe to publish an annual declaration of corporate governance. This declaration should indicate the code to which the company refers to and a description of the principal characteristic of internal system control and risk management within the frame of the process that lead to the elaboration of the financial information. The directive 2006/43/CE which deals with audit of annual account set up the principle of an audit Committee within listed company, one of its roles will be to follow the process of elaboration of financial information.

That is to say that corporate governance rule and a sound system of control and audit both internal and external are important prerequisite to an efficient system of disclosure of financial information as it ensures their reliability and their quality

In term of disclosure, the European regime has been revised by the transparency directive that enters into force last year. It has been implemented in French law though the provision of the so called “Loi Breton” and the general regulation of the AMF. This directive set out the various obligations in term of public disclosure that has to be followed by

company in Europe, in particular it gives the detailed content of the annual financial report, biannual and the quarterly report. The directive has enriched the information to be disclosed, compared to the previous directive and has imposed a quarterly information

Related party transaction is one of the important new elements of this legislation.

Related party transaction should be disclosed in the biannual report when they are not dealt at normal market condition. They should be also reported in the financial part of the annual report. Of course are included in the declaration not only the transaction done by the company but also by all companies that are included in the perimeter of the consolidated account.

Information to be disclosed is in particular:

- the amount of the transaction,
- the nature of the relation with the related party and all information necessary to assess how it impact the financial situation of the company.

What is exactly the definition of a related party: the directive take on board the definition given by the IFRS 24. As you know, Europe has not its own accounting GAAP but implement the international accounting norms such as defined by the IASB. Therefore a related party is a party related to the company directly or indirectly, through one or more intermediaries, control, or is controlled or is under the same control as the company in question

Is also a related party a party which is:

- company associated,
- main managers of the company,
- members of the family or person related to the family of a related party such as defined above,
- a party on which one of the above person has an exclusive control, a specific capacity to influence or holds a significant position in term of voting rights

All listed company is subject to such declaration. Member States may limit this obligation for small company to transaction dealt with its main shareholders and members of its various board.

In the French law that implements the transparency directive, related party transaction, when they are not concluded at a market price shall be approved by the board, then reported to the General Assembly and disclosed in the bi annual and annual report. This means that they are reviewed by auditor. Three levels of controls that show the importance of the good organisation of the general assembly and give rationale to measures that are currently taken to encourage and facilitate shareholders' participation to the general assembly and the exercise of their voting rights

In order to be effective and accurate, provisions on related party transaction are included within a complete set of regulation regarding disclosure and control. Amongst disclosures, it has to be noted in particular the obligation of declaration of personal transactions by managers related to the share of the company, they manage the reporting to the regulator of the person who may be in position to have inside information, all information related to its company and its subsidiaries.

As I said earlier, the efficiency of all this provision depend on the quality of the control. The transparency directive has also strengthened the provision related to the control. Annual financial report and management

report shall be endorsed by identified managers within the company. They are personally responsible for the information contained in it. This provision is within the same spirit as the SOX provision on the managers' responsibility.

It includes the personal responsibility of the main responsible persons involved in the preparation of the financial account.

In addition, the chair of the Board has to release annually a report on corporate governance and internal control, in which is described the various processes put in place to assess the quality of the information disclosed and the quality of the management process.

The report on internal control should refer to the specific norms adopted by the company in terms of internal control. France has released its own term of reference, but also accepts any recognised code such as the Turnbull guidances or the US COSO.

To conclude, I would like to recall that :

- disclosure of related party transactions are useful only if it is clearly exposed, with all information that allow investors and shareholders

to understand its effect on the company in term of financial and strategic consequences;

- the accuracy of the disclosed element has to be controlled both internally and externally, which suppose an effective internal control system, and auditors that fully respect ISA's principles, and are subject to an oversight body;
- finally, the responsibility of the managers and the members of the board shall be clearly stated.

To conclude, I would like also as regulators recall the importance of cooperation within regulators around the world, in particular, when related parties are SPE located off shore.