

financial & private sector development

The Regulation of Related Party Transactions: Review of the European Union and Greek Practices

A presentation by Jean Michel Lobet, Senior Financial Markets Specialist
World Bank Corporate Governance Group
Athens, March 28, 2014



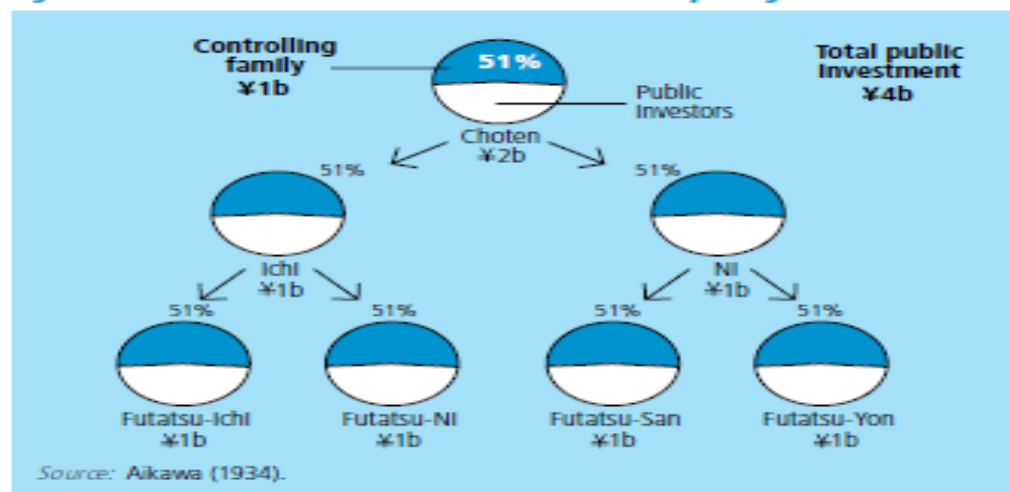
THE WORLD BANK



Why related-party transactions?

- Related-party transactions are prevalent in emerging markets.
- Related-party transactions are common, especially in markets with weak law enforcement.
- Beyond self-dealing, other methods of expropriation, such as insider trading and dilution of share value, can also harm minority shareholders.

Pyramid structures can mask related-party transactions



Solutions for this problem? Good Corporate Governance provisions in the law

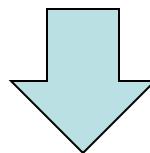
- Do nothing, and count on market forces to sort out the problem?

*Not really an option...
the temptation to “take
the money and run” in an
unregulated environment
is just too great.*

OR

- All dealings between a corporation and its controllers be banned by law?

*Not really an option...
in many instances,
related-party
transactions actually
make economic sense.*



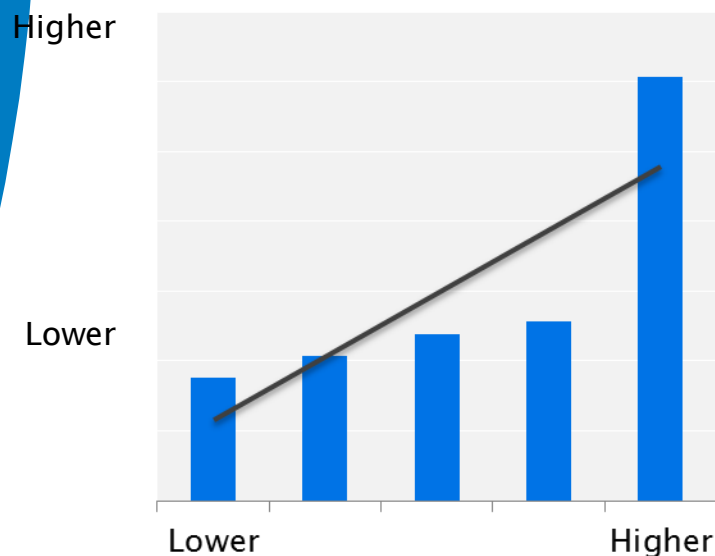
**STRICTLY REGULATE RELATED-PARTY TRANSACTIONS THROUGH
SOUND CORPORATE GOVERNANCE REFORM**



Why does protecting investors matter?

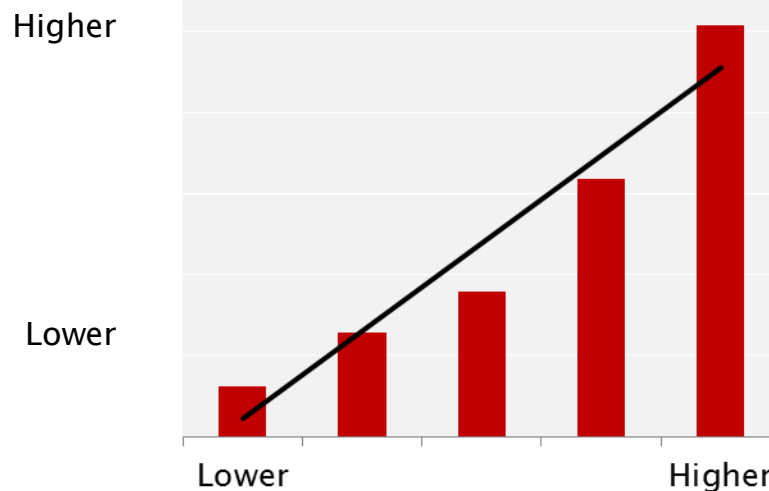
Higher market capitalization

Market capitalization to GDP



Higher entry level to capital markets

Number of listed firms



Note: Relationships remain significant when controlling for income per capita. Higher values on the strength of investor protection index indicate greater protection.

Source: Doing Business database, World Bank (2010).



Where are investors most protected – and how?

-  1. New Zealand
-  2. Singapore
-  3. Hong Kong, China
-  4. Malaysia
-  5. Canada
-  6. Colombia
-  7. Ireland
-  8. Israel
-  9. United States
-  10. United Kingdom

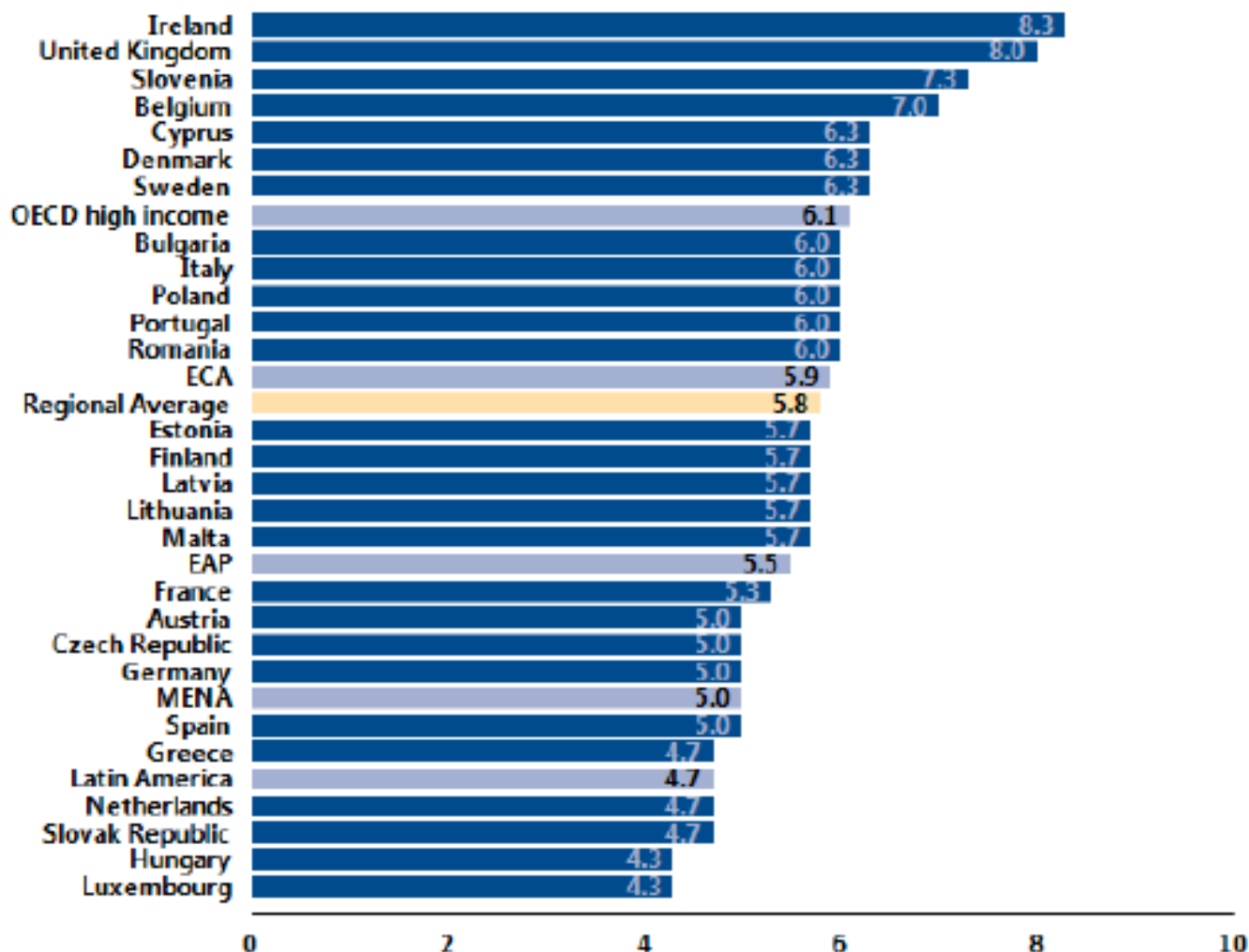
Good Practices:

- Regulated approval of RPTs
- Detailed disclosure requirements
- Clear director duties
- Easy access to corporate information
- Experienced and vigilant boards
- Well-defined shareholder rights
- Robust control environment



Investor protections in the EU

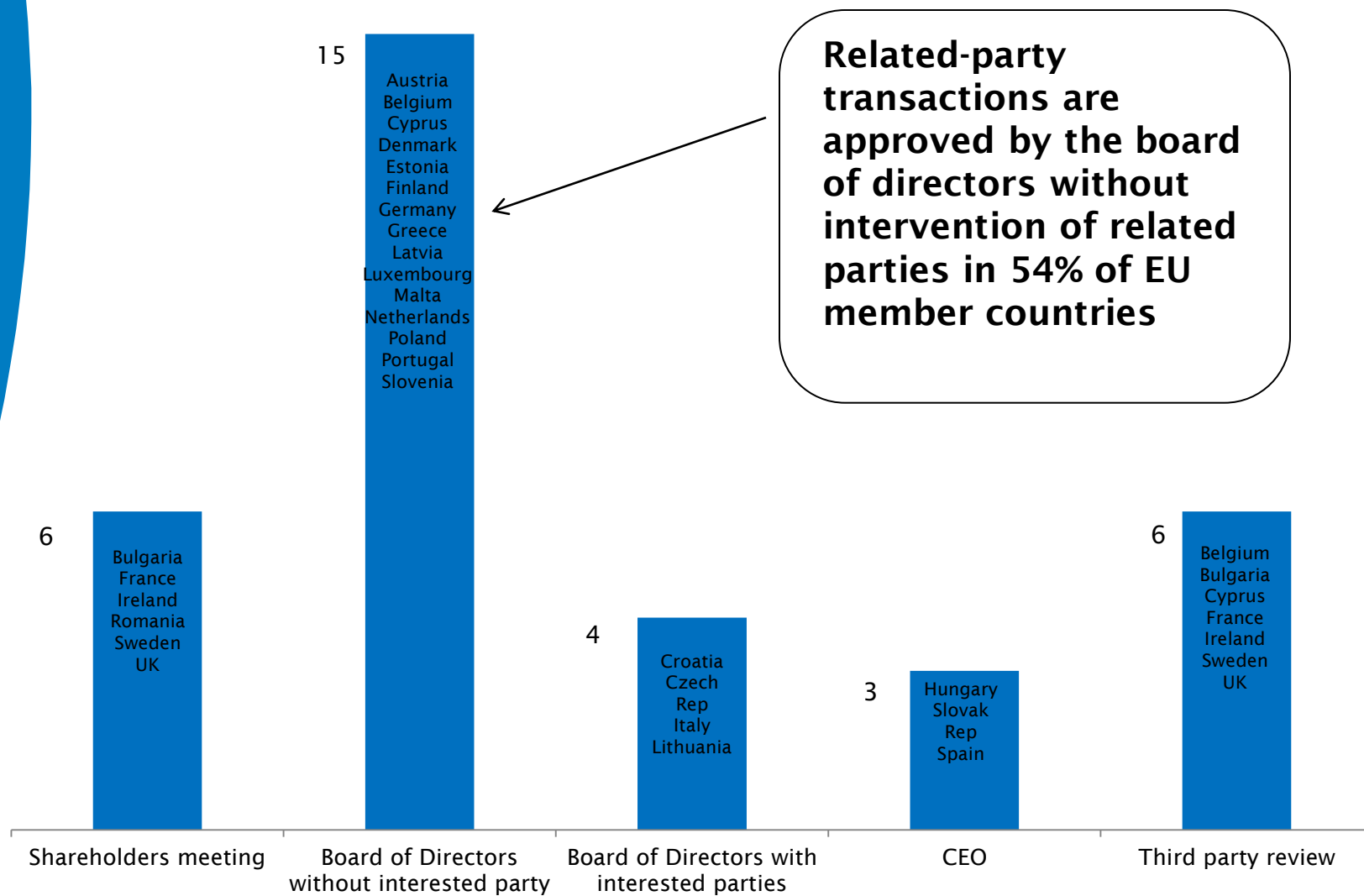
Strength of investor protection index (0–10)



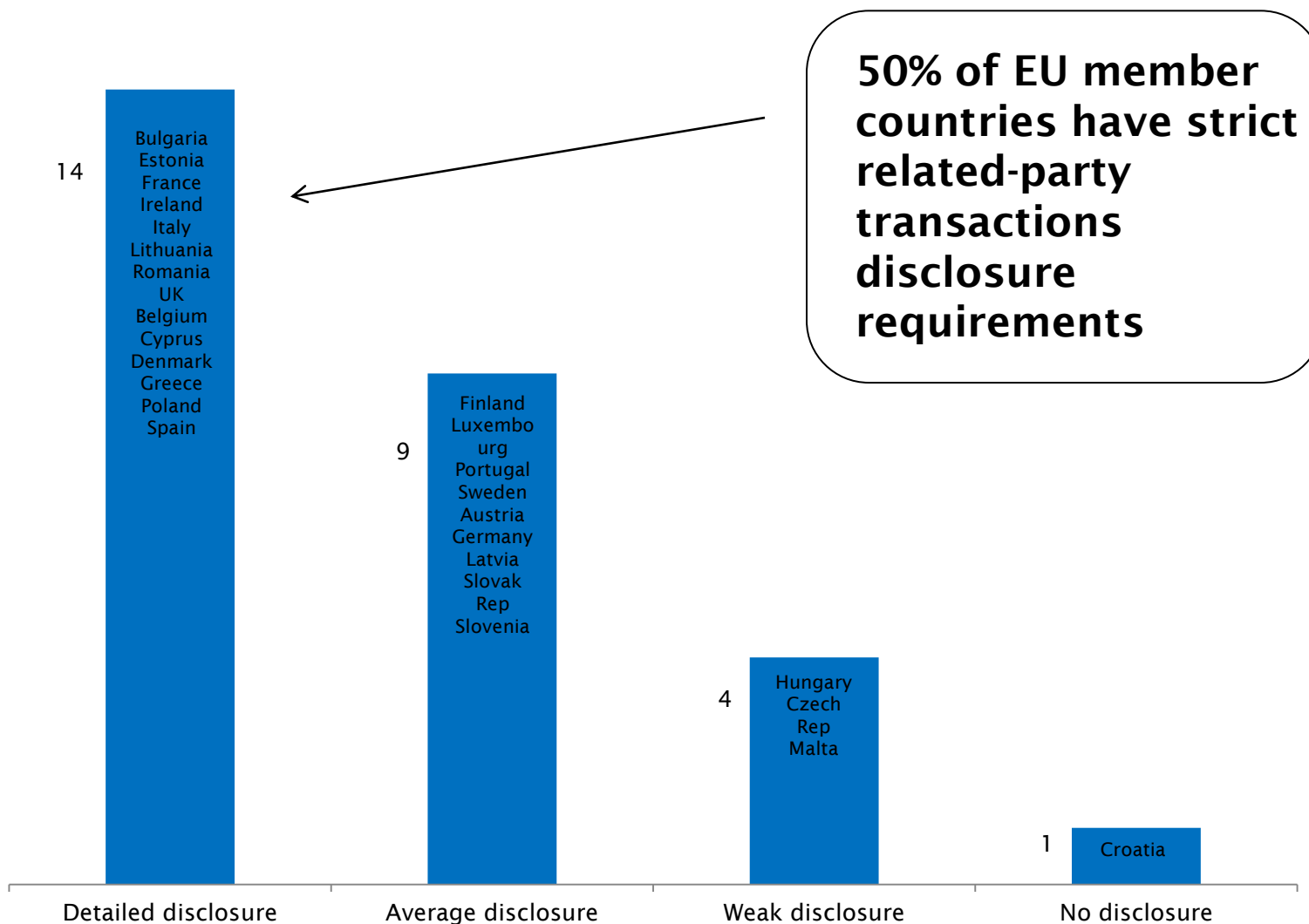
Source: Doing Business database.



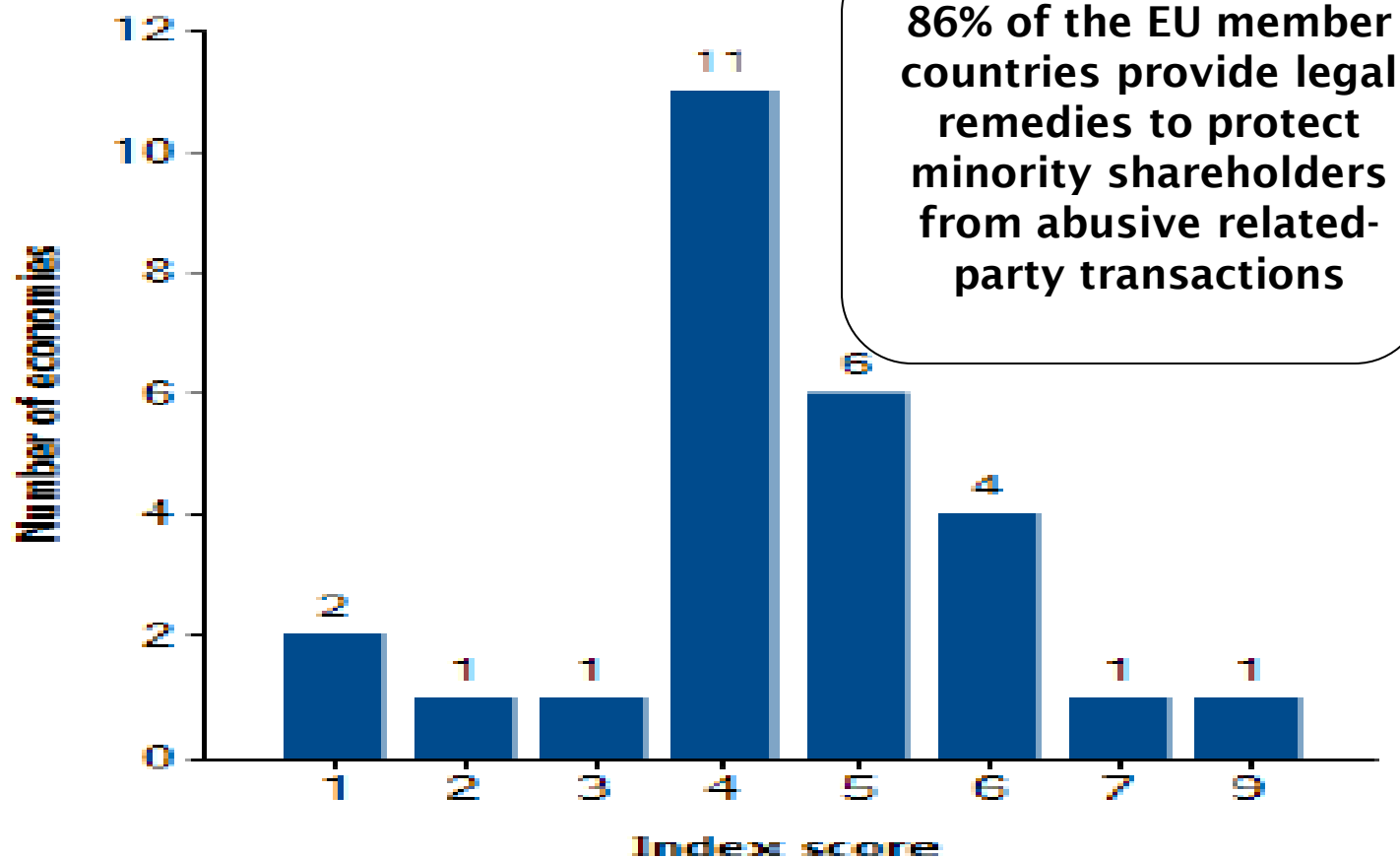
How are RPTs approved in the EU?



How are RPTs disclosed in the EU?



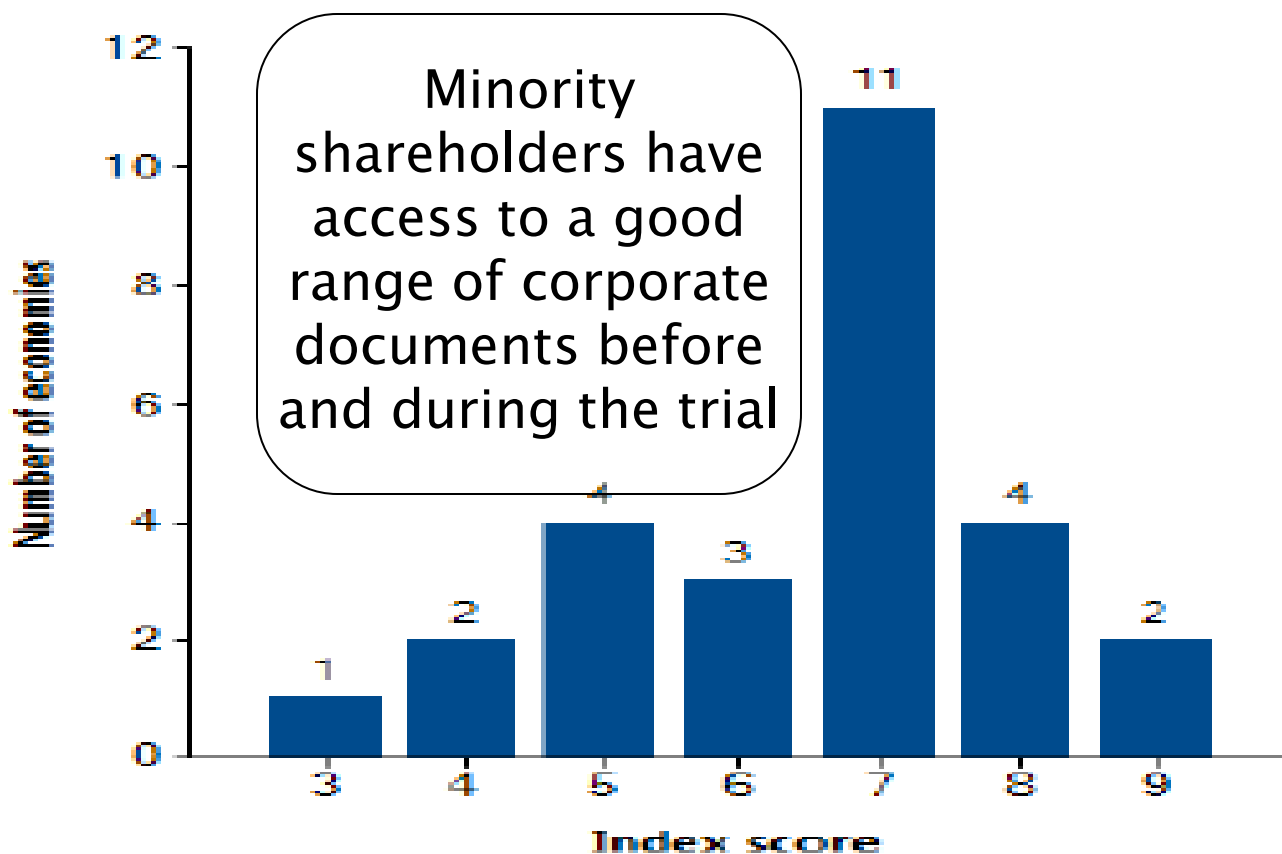
Director liability in case of prejudicial RPTs in the EU



Note: Higher scores indicate greater liability of directors. No economy receives a score of 10 on the extent of director liability index.
Source: Doing Business database.



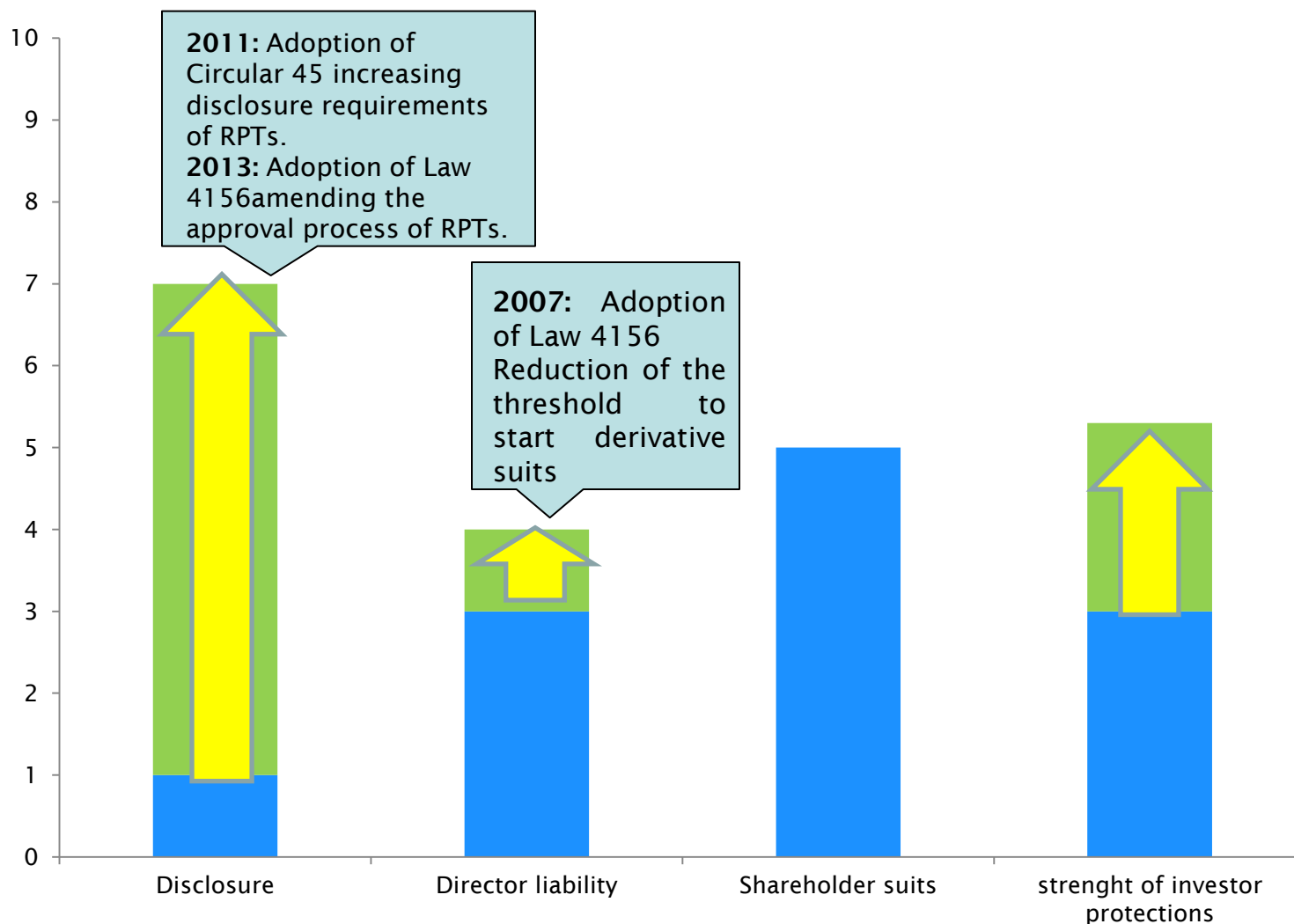
Access to corporate information before and during the trial in the EU



Note: Higher scores indicate greater powers of shareholders to challenge the transaction.
Source: Doing Business database.



Evolution of the regulation of RPTs in Greece 2007-2014: Stricter approval rules, more transparency and more accountability



What are the reform trends

- Increased corporate disclosure requirements in case of RPTs: Greece, Lithuania, Cyprus, Slovenia, Sweden.
- Regulated approval of RPTs: Greece, Sweden, Slovenia
- Stricter director duties: Greece, Slovenia



Areas of opportunity and further progress

	Greece	EU	OECD
Strength of investor protection	3.3	5.7	6.2
- Extent of disclosure index	3	6.2	6.6
- Extent of director liability index	2	4.5	5.3
- Ease of shareholder suits index	5	6.3	6.8

- **Shareholders approval of large related-party transactions: New Zealand, United Kingdom.**
- **Independent review of the terms of RPTs: New Zealand, Australia, Iceland, Norway.**
- **Stricter director liability regime: Canada, Chile.**



Thank you

For questions and comments please contact
Jean Michel Lobet
+1 202 458 0948
jlobet@worldbank.org



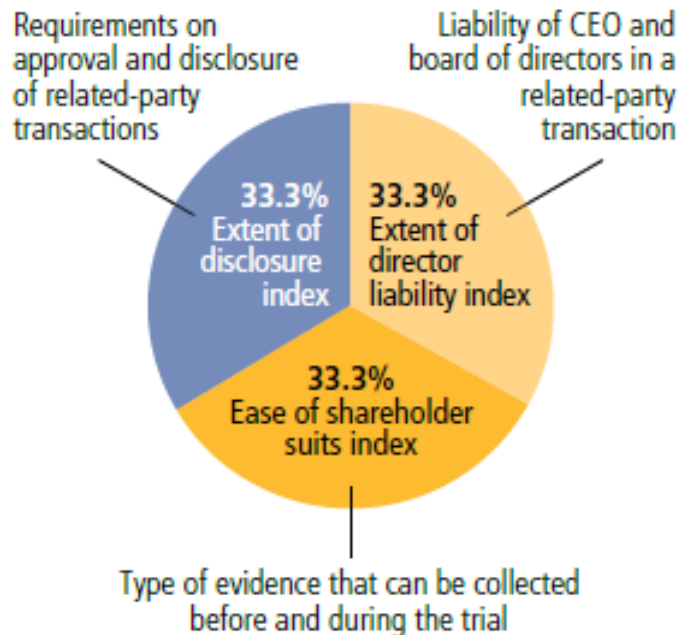
ANNEX



Minority shareholder rights in related-party transactions

FIGURE A.1 Protecting investors: minority shareholder rights in related-party transactions

Rankings are based on 3 indicators



Rankings are based on 3 indices

Extent of Disclosure Index

- Who approves transaction
- What needs to be disclosed, when and to whom

Extent of Director Liability Index

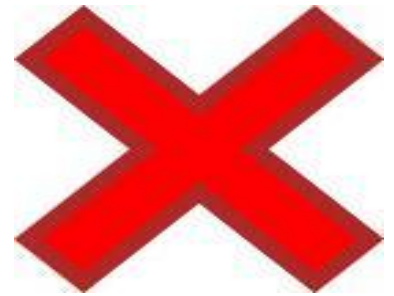
- Available claims against Mr. James and the other directors.
- What needs to be proven for each claim.
- What remedies are available if they are found liable.

Ease of Shareholder Suits index

- Access to company information for proving the investor's case.



WHAT IS NOT BEING MEASURED?



- Not: protections for foreign direct investment (FDI);
- Not: general investor incentives;
- Not: broad frameworks of rights for minority shareholders;
- Not: practical enforcement of laws;
- Not: fraud or violations of law.

