

Feedback Statement issued further to Industry Responses to the Listing Authority Consultation Document on Defining Material Related Party Transactions and Disclosure Requirements as required in terms of the Shareholders Rights Directive II

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1 Introduction

On 13 May 2019, the Listing Authority issued a Consultation Document (Ref: 08-2019) on defining Related Party Transactions and Disclosure Requirements as required in terms of the Shareholders Rights Directive II. The Consultation period closed on the 27 May 2019 and the Listing Authority received 3 responses from industry participants and interested parties.

This document summarises the feedback received by the Listing Authority with respect to the Consultation Document and sets out the Authority's response and position thereto.

2 Feedback Statement

2.1 Definition of Material Related Party Transactions

I. Feedback Received

On the basis of feedback received, the use of the 3 tests defined for the purposes of determining whether a related party transaction, is still not clear. Specifically, the Authority has been asked to clarify the following:

- a) Whether the 3 tests are alternative tests;
- b) Whether the profits tests is meant to measure the cost of the related party transaction divided by the company's profit before tax; and
- c) In the case that an issuer reports a loss, if the profits test is used, any related party transaction would automatically qualify as 'material' given that the profits tests would, as a result of the loss, always result in 5% or more.

II. Listing Authority Position

In terms of Listing Rule 5.156, the profits test is defined as follows: "The profits test is calculated by dividing the profits attributable to the assets the subject of the transaction by the profits of the Issuer." This definition is based on the definition adopted for the same purposes, by foreign national competent authorities. The definition of what should be considered as material has been linked to any one of the following three tests, being, the gross assets test, the profits test and the consideration test. Where an Issuer, in any one year, reports a loss, the profits test should, in principle, not be applicable. In such case, the other tests should still be used.

2.2 Exemptions

I. Feedback Received

Respondents have challenged the extent of the exemptions which are being proposed to be transposed in the listing rules, in order to determine those instances where the listing rules applicable to related party transactions shall not apply.

II. Listing Authority Position

The Authority, after taking into consideration the response received, and in terms of Article 9c(6) of Directive (EU) 2017/828 of the European Parliament and of the Council of 17 May 2017 (the new EU Shareholders Rights Directive SRD II) has decided to add the following exemptions:

- a) Transactions regarding remuneration of directors (Article 9c(6)(c));
- b) 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. Article 9c(6)a of the SRD II will be transposed and replacing LR 5.143.1.

As a result, Listing Rule 5.143 – Exemptions shall be amended accordingly.

The Authority will not be applying the following exemptions for the following reasons:

- a) *Entered into between the company and its subsidiaries provided that they wholly or quasi wholly owned.*

The Authority is of the opinion that transparency in such cases is very important, especially when security holders have a claim against one company within the group which may not necessarily be the parent of the group.

- b) *Entered into the ordinary course of business and concluded on normal market terms.*

In terms of Listing Rule 5.140, in vetting related party transactions, the Audit Committee shall give due consideration to a number of variables which include whether the transaction is in the ordinary course of an Issuer's business or its subsidiary undertaking, as applicable as well as whether the transaction gives rise to preferential treatment to the related party. The present listing rules require the Audit Committee to scrutinise related party transactions. Such an internal control procedure cannot be properly executed if related party transactions entered into the ordinary course of business and concluded on normal market terms are excluded.

- c) Entered into by credit institutions on the basis of measures, aiming at safeguarding their stability;*

Feedback received did not justify the inclusion of the exemption and therefore for transparency reasons the Authority does not agree with the inclusion of this exemption.

2.3 Aggregation of Same Related Party Transactions

2.3.1 Nature of the Related Party Transaction

I. Feedback Received

One of the respondents noted that the concept of aggregation being transposed through the inclusion of a new definition, in order to define Material Related Party Transactions is not clear. Specifically, the respondent explained that it is not clear as to how an entity is to aggregate related party transactions which are not of the same nature.

II. Listing Authority Position

Issuers should refer to paragraph 24 of IAS 24 Related Party Disclosures when determining the manner in which an entity should aggregate related party transactions which are not of the same nature. Specifically, paragraph 24 of IAS 24 states that, "Items of a similar nature may be disclosed in aggregate except when separate disclosure is necessary for an understanding of the effects of related party transactions on the financial statements of the entity."

2.3.2 The Legal Entity of the Related Party

I. Feedback Received

The Authority has been recommended to issue a clarification to the industry where the reporting entity enters into separate transactions with different entities within the same Group.

II. Listing Authority Position

The aggregation provision set out in Article 9c(8) of the SRD II requires that transactions with the **same** related party that are not material, individually, need to be aggregated and, effectively announced and approved by the Board of the Directors, if the materiality threshold, as defined, is reached.

For the sake of clarity and good order, aggregation should be done in the case of same legal entities. That is, where the reporting entity enters into separate transactions with different entities within the same Group, those transactions should not be aggregated as they would have been entered into with separate legal entities and not with the same related party.

2.3.3 Public Announcement

I. Feedback Received

A specific question received is whether an issuer is expected to publish detailed information on each non material transactions that, when aggregated, result in a material related party transaction.

II. Listing Authority Position

The aggregation provision set out in Article 9c(8) of the SRD II requires that transactions with the same related party that are not material, individually, need to be aggregated and, effectively announced and approved by the Board of the Directors, if the materiality threshold, as defined, is reached. Such related party transactions should be publicly announced in aggregate.

2.4 The Role of the Audit Committee

I. Feedback Received

It has been brought to the attention of the Listing Authority that it is unclear whether the proposed changes to the Listing Rules will remove the obligation of the Audit Committee to vet and approve related party transactions which are immaterial, individually.

II. Listing Authority Position

Related Party transactions which on an individual basis are not material shall not be vetted by the Audit Committee. But if upon aggregation, such related party transactions cross the materiality threshold, the Audit Committee will be expected to review the underlying related party transactions.

For the purposes of determining whether a related party transaction is material, transactions with the same related party, that are not material, individually, need to be aggregated and effectively, if the materiality threshold is crossed, have to be publicly announced following approval by the Board of Directors.

2.5 The Proposed Materiality Threshold

I. Feedback Received

The Authority has been requested to reconsider the proposed threshold of 5% and, provided the Authority does not have compelling reasons supporting this percentage, a significantly higher threshold should be adopted.

II. Listing Authority Position

The Authority has proposed the threshold of 5% based on research carried out both locally as well as with foreign jurisdictions. The approach of adopting an either or approach in terms of the class tests is also based on foreign research which approach is deemed appropriate to be applied locally.