

Related Party Transactions

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Mergers and Acquisitions

Increased Duties for Related Party Transactions

The German legislator has adopted a new Act, implementing the European Second Shareholder Rights Directive which, inter alia, sets forth increased transparency and approval requirements for related party transactions. The new Act will come into force on January 1, 2020.

Scope of Application

The new rules only apply to companies whose shares are listed on the regulated market (*regulierter Markt*).

The term “related party transaction” in the new Act is to be understood rather broadly. It covers both contractual and in rem transactions. The term “related party” refers to the respective IAS definition (in particular, IAS 24). In evaluating whether a party is related, the formal legal structure of the relationship is not the decisive factor. Rather, its commercial substance needs to be analyzed.

Related party transactions are subject to the supervisory board's approval if the value of the transaction exceeds 1.5% of the company's total (consolidated) fixed and current assets book value as recorded in its latest approved annual financial statements. The new rules also apply if the aggregate value of several transactions during the current financial year, which individually have not exceeded the 1.5% threshold, exceeds the threshold.

Exempt Transactions

The German legislator has introduced significant exemptions given that related party transactions are already subject to a high level of scrutiny under German law.

In particular, transactions do not qualify as related party transactions if they are made in the ordinary course of business and on an arm's length basis, although the legislator intends this exemption to be interpreted narrowly. In order to regularly assess whether the aforementioned conditions are met, the listed company shall establish an internal procedure from which the related parties involved in the transaction are excluded.

In addition, certain other types of transactions are exempt for which a specific protection of shareholders is not required or is already ensured otherwise. These include, for example, transactions with wholly owned subsidiaries, either directly or indirectly, or with subsidiaries in which no other related party holds a stake.

Likewise, transactions that require the approval of, or authorization by, the general shareholders' meeting are exempt. This includes, in particular, the execution of corporate group agreements (*Unternehmensverträge*), which already contain a sufficient protection level.

Approval Requirement

Related party transactions require prior approval by the supervisory board. The new law also allows the appointment of a supervisory board committee, which can decide, instead of the entire supervisory board plenum, on related party transactions.

If no committee for approving related party transactions is established, the complete supervisory board has to take the decision.

Members of the supervisory board with a conflict of interest are excluded from the vote.

If the supervisory board refuses to approve a related party transaction, the management board may request that the general shareholders' meeting vote on the specific transaction. Related parties involved in the transaction are excluded from participating in the vote on the shareholders' resolution.

Although the legislator has provided for significant exemptions, listed companies should nevertheless review and, possibly, modify their internal processes for related party transactions to ensure compliance with the new rules. In particular, it should be considered to establish a supervisory board committee for the approval of related party transactions.

Disclosure Requirement

Listed companies must publish the major terms, i.e. the related party, the date, and value of the related party transactions that are subject to the approval, within four trading days after the transaction. This requires that all relevant information within the group is available in time. In case of aggregated related party transactions, all aggregated transactions must be disclosed. If the transaction constitutes inside information pursuant to Article 17 of the EU Market Abuse Regulation, the aforementioned information must be included in the respective ad-hoc announcement. Publication of the related party transaction does not dispense the ad hoc publication.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our Mergers and Acquisitions practice:

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