

GENERAL MANDATES FOR RELATED PARTY TRANSACTIONS: A REVIEW OF THE NEW RULES GOVERNING RELATED PARTY TRANSACTIONS

Related Party Transactions have been under great scrutiny in recent times, with the regulators wanting to have better visibility into the terms of related party transactions. An example was the introduction of transfer pricing regulations by the tax authorities about a year ago. The Nigerian Stock Exchange (the 'NSE') has also now published new *Rules Governing Transactions with Related Parties or Interested Persons* (the '[Related Party Rules](#)')¹ to govern all related party transactions involving listed Nigerian companies. This article provides an overview of these rules and considers in particular the introduction of a general mandate requirement.

The NSE has sought to put safeguards in place that require the issuer to not only disclose such transactions to the NSE and its shareholders, but to also seek shareholders' approval before entering into such transactions. The rules also provide the opportunity for a company to seek the NSE's guidance, at an early stage of a transaction, in determining whether the NSE will classify the transaction as a related party transaction. The rules recognise two types of related party transactions, the non-recurring transaction usually of a special or significant nature and the recurring transaction carried out in the ordinary course of business.

WHAT IS A RELATED PARTY TRANSACTION?

The NSE Rules define related party transactions as transactions between an issuer, its subsidiary or an associated company ("entity at risk") and any of its directors, controlling shareholders or any person connected to such persons ("interested party"). The definition of "related party" under the NSE Rules is sufficiently broad to capture both company and family relationships that may exist and influence transactions.

Examples of related party transactions are:

- i. Inter-company loans or guarantees;
- ii. Assignment, leasing or licensing agreement between the entity at risk and the interested party;
- iii. Transactions involving the sale or purchase of goods;
- iv. Transactions involving the transfer of intangible items (e.g. research and development, trademarks, license agreements); and

¹ <http://www.nse.com.ng/regulation-site/IssuersRules/Rules%20Governing%20Transactions%20with%20Related%20Parties%20or%20Interested%20Persons.pdf>.

- v. Transactions involving the provision, receipt, or guarantee of financial services (including loans and deposit services).

DISCLOSURE AND APPROVAL REQUIREMENTS UNDER THE RULES

The rules emphasise the need for disclosure when an issuer is entering into a transaction with a related party. In addition to making a formal disclosure to the NSE, an issuer is also required to disclose the relevant transaction to its shareholders and in its accounts. These transactions include transactions with a value equal to, or more than, 5% of the group's latest audited net tangible assets or its issued share capital. These apply both to a single transaction that crosses the threshold and also to transactions with the same related party which in aggregate come to 5% or more in one financial year. The issuer must disclose the transaction that takes the value up to the threshold and all subsequent transactions to be entered into with the same interested party.

Where a company wishes to sell any of its property units to an interested party, it must make a public announcement in a national newspaper and inform the NSE within two weeks, of the sale.

Internally, the board of directors of the company and the audit committee are required to have reviewed and agreed that the transaction would not be prejudicial to the interests of the company and its minority shareholders. If the related party transaction exceeds the 5% threshold, the company must obtain shareholders' approval not later than 6 weeks prior to the date of the sale

RECURRENT RELATED PARTY TRANSACTIONS AND RULES OF GENERAL MANDATES

The NSE rules discussed above apply to related party transactions that are significant in value, unusual or involve the sale or acquisition of property or machinery. These are generally not transactions that occur in the ordinary course of business and are the types of transactions that are scrutinized the world over. The requirement for shareholder approval of recurrent related party transactions is, however, a different matter. These are transactions that are carried out on an on-going basis and are necessary for a company's day-to-day business operations without which the company may be unable to operate as part of a multinational entity. These are transactions such as supply contracts for required raw materials and are also exactly the types of transactions that are already well regulated by the transfer pricing regulations, to ensure that they are priced on an arm's length basis.

The NSE requirement that these transactions must get shareholders' approval, on which the parent company cannot vote has therefore caused a little apprehension. If the shareholders refuse to approve this, the company would effectively be unable to operate. Unlike the transfer pricing rules, which will simply ensure that the proper pricing is applied, these rules have the potential of halting business altogether. That said, similar provisions apply to companies in some Asian countries such as China and Singapore.

To mitigate the risk and cost of having to put each contract to the approval of shareholders, rule 6.0 of the [Related Party Rules](#) provides that a company may seek a general mandate, subject to annual renewal, from its shareholders authorising it to carry out recurrent transactions. As with non-recurrent related party transactions, the company must disclose the general mandate, with details of the aggregate value of transactions conducted during the financial year, in the annual report of the company and the aggregate value of the transactions must be announced to the market. In other jurisdictions where a similar requirement exists, the passing of a resolution granting this general mandate becomes one of the standard resolutions that are sought at the AGM of a listed company in much the same way as approval for the directors to determine the remuneration of auditors is sought. The NSE rules do not specify the type of resolution and therefore, this would need to be passed as an ordinary resolution of the company.

An example of the type of resolution that would need to be passed to grant a general mandate can be found at [General Mandate](#).

It is important to note that the NSE rules do not permit general mandates to be given in respect of non-recurrent transactions.

Although not a specific requirement under the NSE Rules, the best practice is for a company to formulate and adopt a related party transactions policy. This will ensure consistency in the application of the NSE rules and reduce incidences of non-compliance. The policy should be tailored to work within the company's governance framework and contain detailed advice and examples that are specific to the company and its related parties.

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