

**REPORTING
RELATED PARTY TRANSACTIONS
AND
CONFLICTS OF INTEREST**

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I. Introduction

1. I have been requested by OECD to draft a paper on reporting related-party transactions and conflicts of interests in the South East European countries, more specifically Croatia, Bulgaria, Albania, Romania, Serbia, Macedonia, Bosnia and Montenegro. The paper was commissioned for the Roundtable on transparency and disclosure issues in the region, scheduled in June 2004 in Macedonia.

2. The paper is limited in scope due to the lack of relevant information from Albania, Bosnia, Macedonia and Montenegro. Consequently, our focus will be solely on Romania, Croatia, Bulgaria and Serbia. In this paper, 'countries in the region', save as otherwise specifically indicated, will mean only the four countries from and on which we had available information.

3. Our purpose is to explain how 'related party' and 'conflicts of interest' are understood and regulated by local laws and to investigate whether the existing legal requirements for reporting related party transactions and conflicts of interest and the manner in which they are implemented are capable of ensuring appropriate transparency and disclosure.

4. This analysis centres primarily on company law, securities regulations and stock exchange listing requirements. While the 'related party' concept appears to have been regulated for the first time under tax regulations and/or competition laws, references to such regulations exist in this paper if and to the extent that they were pointed out by the information providers as having a bearing on the legal treatment applicable in a particular country.

5. Most of the information used in this paper was obtained from law practitioners and therefore may put forward a fragmentary view of the phenomenon, especially as regards practices on reporting related party transactions and conflicts of interests. On the other hand, in a move to provide as complete as possible a picture of the existing legal requirements in the region, we have used almost all information obtained, even if in certain cases, the information was not fully relevant for the limited purpose of this paper.

6. As regards 'conflicts of interests', it was not the purpose of this paper to look into this issue where public office and civil service are concerned, given the appointment requirements in the field and the relationships with public persons. However, there is a global trend towards passing legislation/ updating existing laws on the matter (e.g. in Serbia a law on the prevention of conflicts of interests in the field of public activities has recently been passed).

7. This paper is based on the legislation in force at the time when it was prepared. Major legislative changes are expected in corporate and securities laws. A new Corporate Law is in the pipeline in Croatia, while in Romania a new Consolidated Law on Capital Market is expected to pass through Parliament in June 2004. For the purposes of this analysis, our coverage of the Romanian legal environment is based on the draft Consolidated Law on Capital Market available at 1 May 2004. On the other hand, there are countries (i.e. Serbia) where new laws have been recently enacted, with any pattern of interpretation or consistent practice of implementation yet to be developed.

8. For the purpose of this paper we have used the English translations of the relevant regulations received from each country. We did not intervene on these translations, except for superficial interventions, for not changing the meaning of the relevant provisions. As regards Romanian regulations we have used the official English translation in all cases when such translations existed.

II. Summary and main conclusions

1. General conclusions

1.1. Even if in part of countries there is the opinion that the existing legal framework is not totally proper as to support and/or to impose an appropriate transparency and disclosure of related party transactions and conflicts of interest (e.g. Serbia, Romania), the existing legal framework contains important provisions in this respect. At this moment, due to inappropriate practices (part of the existing provisions are not yet implemented) it is hard to say to what extent the existing legal framework itself should be improved.

1.2. There is a confusion at the level of all the analysed countries as regards what is covered by 'related parties transactions' and what is covered by 'conflicts of interest'. Thus a 'related party transaction' does not lead necessarily to conflicts of interest, but in many cases depending on the actual transactions to be performed, 'related parties transactions' are likely to lead in certain cases to conflicts of interest. However, in case of 'conflicts of interest' there is an additional condition to be met – the conflicting interests – that would prohibit a person, that could be a related party, from performing a transaction, exercising a function etc. On the other hand 'conflicts of interests' do not limit to related parties (i.e. they cover also providers of specialised services etc.).

1.3. Due to the existing confusion at conceptual level there are also inconsistencies in the legal regime of 'related party transactions' and 'conflicts of interests'. Thus, it is not very clear why certain related parties transactions not leading to conflicts of interest (for example related parties transactions performed at arm's length) are still prohibited. It should be mentioned that there are cases when the national law presumes certain agreements/transactions as involving conflicts of interest because the person that should take a decision (likely to be a 'related party') as regards a transaction is the other part of that transaction (e.g. the Serbian legislation considers a conflict of interests granting by the company of loans to its directors or securing their debts etc.). In such cases the presumed conflicts of interests are 'solved' by moving the competence to take such decision to a different corporate body. However, it is hard to believe that in such cases the other corporate body would accept the performance of the transactions if it would involve an interest contrary to the one of the company.

1.4. A clear distinction between 'related party transactions' and 'conflicts of interest' would prove relevant for reporting, as disclosing 'related party transactions' may be made before or after being performed but as regards 'conflicts of interest' they should be disclosed as soon as they started to exist.

1.5. Notwithstanding the above we have noticed a general tendency as the techniques and the mechanisms meant to ensure the transparency and adequate disclosure of related party transactions and conflicts of interest to become more sophisticated as to answer to the actual needs revealed by the practice.

1.6. Currently, in none of the four countries exists trust that the existing practices ensure a total transparency and disclosure of related party transactions and conflicts of interest. This general impression is accompanied by the lack of trust in the capacity of the competent authorities to impose adequate practices.

1.7. Currently, when reporting related party transactions and conflicts of interest the reporting is made in a 'formal', non-creative manner, made rather for ensuring compliance with existing provisions than answering actual needs of the market.

1.8. The information reported to relevant authorities is not always relevant information (e.g. the information on beneficial owner is not reported) and the authorities have not resources/possibilities to check it.

2. Reporting related party transactions. Legal framework and practices

2.1. The laws of the countries in the region generally do contain definitions to 'related parties', without further spelling out the meaning of 'related party transactions'. The concept of 'related parties' is defined in similar manner in the laws of the countries under examination. Generally, legislators have taken two different and successive standpoints: (i) firstly, there are certain categories of persons (legal entities and individuals) qualified by law as 'related parties'; (ii) secondly, a general wording is inserted to allow any person capable of exercising an influence over another party in the making of decisions to be qualified as a related party.

2.2 As regards the classes of persons qualified by law as 'related parties' in the four national legislations examined these are mainly the following: (i) Persons qualifying as related parties by virtue of their involvement in the management of a company; (ii) Persons qualifying as related parties due by virtue of their participation towards the company's share capital; (iii) Persons qualifying as related parties in light of the 'control' criterion; (iv) Persons qualifying as related parties by virtue of family relations; (v) Persons qualifying by virtue of other existing relations; (vi) Cross shareholding.

2.3. None of the national laws of the countries investigated deals specifically with 'beneficial ownership' versus 'nominal ownership' issue. The 'beneficial ownership' criterion has largely the same effect in terms of producing a qualification as 'related parties' as the 'indirect' participation or control or the general wording in the definition of 'related parties'. However, these are applicable as long as the beneficial owner is disclosed, which, especially in the case of foreign beneficial owners, does not always happen.

2.4. The 'forms' of reporting related party transactions vary from country to country and depending on the transaction. The most common forms of reporting are: reporting to the General Shareholders Meeting – in most cases the approval of the General Shareholders Meeting being necessary, reporting to the Securities Commissions transactions performed between related parties and further to the shareholders, publishing in the Official Gazette.

2.5. Generally, there are no clear regulations as regards who, within a company, is under an obligation to report related-party transactions. It should be established by internal regulations who should report related-party transactions. In practice, though, it seems that such internal regulations do not exist in many cases. Ultimately, the obligation to report is split between the directors, auditors and shareholders (shareholders mostly as regards their shareholding).

2.6. The breach of existing prohibitions to related-party transactions carry severe sanctions (e.g. the deeds constitute criminal offence and carry fines or prison terms, and from the standpoint of civil law the transactions are considered null and void). The applicable sanctions may be: civil sanctions, administrative sanctions and criminal sanctions.

2.7. The relevant authorities imposed by now mainly administrative sanctions. In certain cases criminal files were prepared and sent to the prosecutor for further investigations. By now there are very rare cases when criminal sanctions were imposed.

3. Reporting conflicts of interest. Legal framework and practices

3.1. Generally, there are no definitions for 'conflicts of interest'. The concept 'conflicts of interest' is less precisely regulated than 'related party transactions' as definitions exist at least for 'related party'. The concept of 'conflicts of interest' is likely to cover any kind of situation and relationships that could result in conflicting interests.

3.2. A very important aspect related to conflicts of interest is the prohibition of inside trading in case of publicly-held companies. Even if it is not specifically mentioned under the investigated legislations that the inside trading has a component of 'conflicts of interest', in our opinion, holding an inside information puts the holder in the situation of having conflicting interests with the issuer.

3.3. The main categories of conflicts of interest regulated by the investigated legislations are the following (i) Conflicts of interests arising within a company; (ii) Conflicts of interest arising between specialised companies acting on regulated markets and their clients; (iii) Conflicts of interest arising in case of providers of specialised Services Providers; (iv) Conflicts of interest regulated under specific regulations

3.4. On the other hand it should be mentioned that the interest conflicting may be very diverse.

3.5. The lack of specific requirements as regards the disclosure of 'beneficial ownership' could also lead to cases when the actual conflicts of interest may not be identified. In such cases it is not possible to ensure appropriate disclosure or to observe the legal regulations on conflicts of interests.

3.6. The form of reporting is also diverse: reporting to the members of the Board of directors, reporting to the shareholders, reporting to the client. There are rare cases when the conflicts of interests are reported to an authority. The legal regime applicable to conflicts of interest is different to the legal regime of the related parties transactions when once disclosed the transactions may be further approved and performed, the results of identifying conflicts of interest are rather that the conflicting activity may not be longer performed. Generally there are no exceptions from the rules to be followed in case conflicts of interest are identified.

3.7. Currently the sanctions imposed in practice are rather civil or administrative sanctions. In very rare cases criminal sanctions were applied. There are also rare cases when the minority shareholders challenged the non-observance of a reporting obligation of conflicts of interest.

III. Reporting related party transactions

“Related party” concept

1. General comments

1.1. It results from our analysis of the available information that the laws of the countries in the region generally contain definitions of/references to ‘related parties’, without further spelling out the meaning of ‘related party transactions’. In light of the definition of ‘related party’, ‘related party transactions’ should mean any kind of transactions concluded between related parties. However, in certain cases, transactions between related parties must be reported only if a number of additional conditions are met (e.g. a specific threshold is exceeded).

1.2. Definitions of ‘related parties’ exist in both corporate laws and securities regulations. In some cases, Company law and the securities regulations of the same country provide dissimilar definitions of ‘related parties’, tailored to the purposes of the relevant piece of legislation.

1.3. The concept of ‘related parties’ is defined in similar manner in the laws of the countries under examination. Generally, legislators have taken two different and successive standpoints: (i) firstly, there are certain categories of persons (legal entities and individuals) qualified by law as ‘related parties’; (ii) secondly, a general wording is inserted to allow any person capable of exercising an influence over another party in the making of decisions to be qualified as a related party.

1.4. As regards the classes of persons qualified by law as ‘related parties’, part of them are common to all the countries investigated; others exist only in the legislation of only one country. In certain cases, differing criteria are used within the very same class of persons, as detailed below.

2. Classes of persons qualified by law as ‘related parties’

2.1. We set out below the main classes of persons/criteria used for determining the persons qualified as ‘related parties’ in the four national legislations examined:

- **Persons qualifying as related parties by virtue of their involvement in the management of a company:** generally, it is considered that the members of management bodies of a company and the key executive officers qualify as related to the company in whose management they are involved. This criterion is applicable even if the manager is a legal entity and covers direct or indirect involvement.
- **Persons qualifying as related parties due by virtue of their participation towards the company’s share capital:** shareholders who own more than the prescribed threshold of a particular company’s shares are treated as related party to that company. Generally, to qualify as a related party, a shareholder should have at least a significant interest (but this is not necessary in all cases), even if holding disclosure requirements apply to lower levels of shareholding (e.g. holdings of 5%). This also covers direct or indirect holdings.

- **Persons qualifying as related parties in light of the ‘control’ criterion:** generally, according to this criterion, the following are treated as related parties: the person exercising control over another party and that other controlled person; the persons controlling together a third party; the persons under the control of a third party. The ‘control’ criterion also covers direct or indirect control.
- **Persons qualifying as related parties by virtue of family relations:** This covers spouses and relatives; there are differences as regards the degree of kinship and affinity. Generally, this criterion is also used for determining indirect involvement in management, indirect participation towards the share capital or indirect control.
- **Persons qualifying by virtue of other existing relations:** The regulations qualify as ‘related parties’ the persons between whom certain relations, other than family relations, are established: employer and employee, commercial agent and beneficiary, commercial partners, donor and donee, etc. The commercial agent criterion is also helpful in determining indirect involvement in management, indirect participation towards the share capital or indirect control.
- **Cross shareholding:** companies with cross-shareholdings also qualify as related parties.

3. ‘Related parties’ qualification based on the general wording

3.1. As mentioned above, the general wording in the definition of ‘related parties’ allows any person capable of exercising an influence over another party in making decisions as a ‘a related party’. Since the qualification as ‘related parties’ in reliance on this general wording involves a process of interpretation, transactions between related parties which do not fall within any of the categories specifically set out by law are the least disclosed, there being no clear basis on which to claim or prove that a transaction between related parties has taken place.

4. Beneficial ownership

4.1. None of the national laws of the countries investigated deals specifically with ‘beneficial ownership’ versus ‘nominal ownership’ issue. This is a consequence of the fact that the relevant national laws do not recognise the legal concept of ‘beneficial ownership’ and ‘nominal ownership’. The ‘beneficial ownership’ criterion has largely the same effect in terms of producing a qualification as ‘related parties’ as the ‘indirect’ participation or control or the general wording in the definition of ‘related parties’. However, these are applicable as long as the beneficial owner is disclosed, which, especially in the case of foreign beneficial owners, does not always happen.

5. Concept of ‘related parties’ under Romanian law

5.1. Provisions regarding the concept of ‘related party’ exist in the Romanian securities regulations. Romanian tax regulations prescribe certain rules for transactions between related parties (e.g. the requirement of transactions at arm’s length), while the concept of related parties is referred to in legislation such as competition law, privatisation law, banking law, etc.

5.2. Under Romanian Company Law (Law no. 31/1990, as subsequently amended), there is no clear definition of ‘related parties’. However, based on the latest amendments to Company law (2003) it can be argued that Company Law treats as related party of a company: (i) the founder/shareholder – regardless of the shareholding in the first two years of the company’s

business (Art. 143¹), (ii) the director (Art.145¹, Art. 148), the executive manager (Art. 148), the spouses and relatives of the director or the executive manager, up to the fourth degree of kin (Art.145¹, Art. 148), the company wherein the director or the executive manager holds, by himself or together with the spouse or relatives at least 20% of the subscribed share capital (Art. 148). Also, under Art. 265 paragraph 3, the director of a company and a company controlled by the company where he acts as director, as well as the company controlling the company it administers also seem to qualify as related parties. All the provisions relevant to related parties, save for Art. 265, were inserted in Law 31/1990 in 2003. Consequently, no consistent practice has developed in the field. Pursuant to Company Law, the employer and employee are not seen as related parties. Moreover, in certain cases, employees enjoy a preferential treatment compared to third parties (e.g. granting loans to buy company shares, etc.)

5.3. The securities regulations currently in effect (i.e. Emergency Ordinance no. 28/2002, as subsequently amended – ‘EO 28/2002’) contain definitions for:

- (i) ‘affiliated person’ – *a person controlled by an entity or which controls directly or indirectly this entity. The persons being affiliated at the same time with the same entity are considered as being affiliated themselves, and*
- (ii) ‘person involved’ – *spouses and any relative of the person holding a control position up to the third degree of kin (1/3 from the voting rights to be exercised in the Shareholders General Meeting), directors and the executive management of a publicly-held company or the legal entity where this individual, by itself or together with other involved persons holds a control position.*

Both ‘affiliated person’ and ‘involved person’ are presumed, until the contrary proof, to act in concentrated manner.

5.4. For the purpose of Article 123 of EO 28/2002 (stipulating mainly the reporting obligation), related party is considered: the director, the employees, the majority shareholder, the affiliated person and the involved person.

5.5. The draft Consolidated Law on Capital Market carries only a definition of ‘person involved:

- a) *persons who control or are controlled by an issuer or which are under joint control;*
- b) *persons participating directly or indirectly in the conclusion of agreements for the joint exercise of voting rights, if the shares forming the subject-matter of the agreement ensure a controlling position;*
- c) *individuals having managerial or control powers within the issuer;*
- d) *spouses and relatives of the individuals under a), b) and c) up to the second degree of kinship;*
- e) *persons who can appoint the majority of members to the Board of directors within an issuer.*

5.6. The draft Consolidated Law on Capital Market also includes a definition for ‘close relationships’, but this definition seems to have been inserted with the aim of establishing certain conditions for the financial investment services companies.

6. Concept of ‘related party’ in Bulgarian law

6.1. The existing Bulgarian legal framework relevant to related parties defines several categories of related parties. There are differences between the definitions in the Commercial Act and those in the securities regulations.

6.2. Under Clause 1 of the Supplementary provisions of the Commercial Act (CA), related parties are defined as follows:

‘(1) For the purposes of this Act, related parties means:

1. Spouses, lineal relatives up to any degree, collateral relatives up to the fourth degree of kin, and relatives by marriage up to the third degree of affinity inclusive;
 2. Employer and employee;
 3. Any two persons, one of whom participates in the management of a corporation of the other;
 4. Partners;
 5. A corporation and a person which or who holds more than 5 percent of the voting interests and shares issued by the said corporation;
 6. Any number of persons, whose activity is directly or indirectly controlled by a third party;
 7. Any number of persons, who or which jointly control a third party, whether directly or indirectly;
 8. Any two persons, one of whom acts as commercial agent for the other;
 9. Donor and donee of a gift.
- (2) "Related parties" furthermore means any person that participates, whether directly or indirectly, in the management, control or capital of another person or persons and therefore may agree among themselves on terms other than the customary ones.'

6.3. In the Bulgarian securities law there is a definition of related parties in Clause 1, point 12 of the Supplementary Provisions of the Public Offering of Securities Act (POSA)

Related parties are:

- a) The parties, where one of them controls¹ the other one or is a subsidiary company thereof;
- b) The parties whose activities are controlled by a third party;
- c) The parties that jointly control a third party;
- d) Spouses, lineal relatives up to any degree, collateral relatives up to the third degree of kin, and relatives by marriage up to the third degree of affinity inclusive.

7. Concept of 'related party' under Croatian law

7.1. Under Article 473 of Croatian Company Law, related companies are legally independent companies whose mutual relationships are as follows:

1. 'a company that has the majority holding in another company or has the majority right where decision-making is concerned (explained in Article 474);
2. dependant and main company (Article 475);
3. a company of concerns (Article 476 defines a concern);
4. companies with reciprocal shares (defined under Article 477);
5. companies joined by entrepreneurial contracts.'

8. Concept of 'related party' under Serbian law

8.1. Article 59 of the Serbian Corporate Law defines transfer prices as follows:

- (1) A transfer price shall be understood to mean the price created by means of transactions of assets or making commitments among related parties.
- (2) A person associated with a taxable person shall be understood to be an individual or legal entity capable of exercising control or exerting considerable influence over business decision-making.

¹ Under Paragraph 1, point 13 of the supplementary provisions of the Public Offering of Securities Act a party is deemed to have control over a company, if it:

- a) Possesses, incl. through a subsidiary or under an agreement with a third party more than 50% of the votes in the General Assembly of a company; or
- b) Can appoint directly or indirectly more than a half of the members of the Governing Body of a company; or
- c) Can otherwise decisively influence the making of decisions relevant to a company's activities.

(3) *The possession of more than 50% or the largest number of shares or stakes shall mean the possibility to control the taxpayer.*

(4) *Besides the case referred to in paragraph 3 of this Article, influence on a taxable person's business decisions also exists when a person associated with a taxable person has more than 50% or the largest number of votes individually in the taxpayer's managing bodies.*

(5) *A person associated with a taxable payer shall also be understood to mean the legal entity under the control and supervision of, or held by, the entities exercising control and supervision or having an interest in the taxpayer, as determined in paragraphs 3 and 4 of this Article.*

8.2. In addition, under Serbian law, companies may become related by means of **equity or agreements** (related companys - parent and subsidiary companies)

8.3. **Related companies** include: holding and subsidiary companies (joint-venture, trust), cross-share companies, and holding companies. Competition regulations may bar companies from becoming related.

8.4. **Parent and Subsidiary Companies:** If a company has a majority (50%) or significant (25%) holding in another company or if, under an agreement with another company, it has the right to appoint the majority or at least a quarter of the members of the Board of Directors of the other company, or if it has a majority or at least a quarter of the votes in the General Meeting, it is treated as a parent company, with the other company deemed to be its subsidiary. A **holding company** is a company that owns shares or stock in a subsidiary company, its business being primarily to exercise control, acquire an interest in other companies in the form of shares, stock or convertible debentures (formation, lasting investment, purchase, swap), as well as to manage the securities. A holding company may be incorporated as a general partnership, limited partnership, joint-stock company, limited liability company, socially owned company and public company.

Legal treatment of related party transactions. Reporting 'related party' transactions

1. General comments

1.1. Under the laws subject to our review, certain transactions between related parties are forbidden and therefore the reporting requirements in these cases are rather for reporting the related parties. In our analysis below we will focus especially on the reporting requirements.

1.2. The 'forms' of reporting vary from country to country and depending on the transaction. The most common forms of reporting are: reporting to the General Shareholders Meeting – in most cases the approval of the General Shareholders Meeting being necessary, reporting to the Securities Commissions and further to the shareholders, publishing in the Official Gazette.

1.3. There are cases in which the reporting requirements apply only if the related-party transactions meet a number of additional conditions (e.g. transactions whose value exceeds a specified threshold, etc.).

1.4. During our analysis we have identified exceptions from the rules governing the reporting of related-party transactions. One of these exceptions has already been mentioned under 5.2. above on the regulations existing under Romanian Company Law on the relations between employer and employee.

1.5. Generally, there are no clear regulations as regards who, within a company, is under an obligation to report related-party transactions. It should be established by internal regulations who should report related-party transactions. In practice, though, it seems that such internal regulations do not exist in many cases. Ultimately, the obligation to report is split between the directors, auditors and shareholders (shareholders mostly as regards their shareholding mostly).

2. Reporting requirements under Romanian law

2.1. Both Romanian Company Law and the securities regulations contain reporting requirements. Securities regulations are considered special rules in derogation from the treatment prescribed by Company Law. Therefore, Company Law applies to publicly-held companies, unless otherwise provided by the securities laws.

2.2. The most important requirements under Romanian Company Law are set out below:

- under Article 143¹ *‘The acquisition by a company of a good from a founder or a shareholder: a) in a period of maximum 2 years from the incorporation of the company or from the date the when the company was authorised to start its activity; and b) in return for an amount or other consideration accounting for at least 10% of the subscribed share capital must be submitted for approval to the Shareholders General Meeting, meet the requirements under articles 37 and 38 (i.e. these articles require that a valuation be performed by an independent appraiser), be published in the Official Gazette and in a wide circulation newspaper. (2) Acquisitions performed in the normal course of business of the company, as well as those made in on the basis of a decision by an administrative authority, or based on a court ruling, or made on a regulated stock exchange do not fall under the above provisions.’*

- under Article 145¹ the director may conclude with the company sale or purchase transactions exceeding 10% of the company’ s net assets subject to prior approval from the Shareholders General Meeting. The prior approval is also necessary if spouses or relatives of the director are involved in the transaction, or if the transaction is concluded with a company where the director or its spouses or relatives act as a director, or holds, individually or together with others, at least 20% of the subscribed share capital, save for the case where one company is the subsidiary of the other;

-under Article 148 it is forbidden to grant compensations or any other amounts or advantages to directors and auditors, other than under a resolution by the Shareholders General Meeting. Similarly it is forbidden for a company to make loans to its directors or executive managers in respect of any kind of transactions, if the amount exceeds EURO 5,000 and the transaction is performed other than in the normal course of business.

2.3. The effective securities regulations (E.O. 28/2002) lay down the following main reporting obligations:

-article 115 under paragraph 1 states that any acquisition, sale, swap or collateral posting operation involving the assets of a publicly-held exceeding during a financial year individually or cumulate 20% from the total assets less accounts receivables may be concluded by directors or executive managers only after they have obtained the approval of the Shareholders General Meeting. Paragraph 2 of the same article states that the loan of company assets worth more than the 20% threshold to a related party is subject to prior approval by the Shareholders General Meeting;

- pursuant to article 113, internal and financial auditors of publicly-held companies are responsible for checking the management of the company, and the accuracy and appropriateness of transactions or acts/documents concluded by the company with its directors, employees, company shareholders or affiliated persons or persons involved therewith;

- the holdings of two related parties in a publicly-held company are always considered together (i.e. as the sum total of their individual holdings – for any trading operation, it is the aggregate percentage that is taken into account);

- under article 123 the following reporting obligations are regulated: *'(1) The directors of a publicly-held company shall be bound to present to the NSC current reports, which shall be compulsorily published in the Commission's Bulletin, wherein they shall state any juridical act concluded by the company with the directors, employees, majority shareholders of the company or persons involved or affiliated thereto worth jointly at least the ROL equivalent of 50,000 euro.(2) In the case that the company concludes juridical acts with the persons under paragraph (1), these shall be concluded in compliance with the company's interest in relation with the offers of the same type existing in the market.(3) The reports shall contemplate in a special chapter the juridical acts as concluded or the amendments thereto and shall specify the following: the parties that concluded such juridical act, the date of execution and the nature of the act, a description of the object thereof, the aggregate value of the juridical act, the amount due by the parties to each other, the security, as well as the terms and modalities of payment.(4) The reports shall also mention any other information needed to establish the effects of such juridical acts on the financial situation of the company and any other information required in accordance with the NSC regulations.'*

2.4. The draft Consolidated Law on the capital market sets out obligations similar to those under Article 115 and Article 123. As regards the obligation which is similar to that under Article 123 above, the threshold was raised to EUR 100,000. While under the securities regulations in force contributions in kind to the share capital of publicly-held companies are forbidden, under the draft Consolidated Law on the capital market they are allowed subject to an independent valuation and if voted for by shareholders holding at least 75% of the share capital.

2.5. Under the Law on judicial reorganisation and bankruptcy procedure there are the following relevant provisions: *'(2) The following trading operations, concluded during the year preceding the opening of the procedure, with persons having legal relations with the debtor, may also be cancelled and the services recovered if they prejudice the interests of the creditors:*

- a) with an active partner or a partner owning at least 20% of the trading company's capital, in case the debtor is a limited partnership company or, respectively, a general partnership company;*
- b) with a shareholder owning at least 20% of the debtor's shares, in case the debtor is the respective joint-stock company;*
- c) with an administrator, director or member of supervising bodies of the debtor, joint-stock company;*
- d) with any other natural or legal person having a dominant position over the debtor or over its activity;*
- e) with a co-owner over a common asset.'*

3. Reporting requirements under Bulgarian legislation

3.1. The Bulgarian corporate and securities law does not prescribe a systematic legal treatment of activities involving related parties. However, there are many provisions imposing restrictions on the appointment of related parties to certain corporate bodies or on transactions involving related parties. In most cases, related parties transactions are forbidden and as far as there is any need for reporting, it is for reporting that the parties are not related². However there are cases in which additional conditions have to be met. An example is Art. 235-a of Company Act: *- The contracts between a company and the single shareholder of that company (who or which represents it) shall be made in writing.*

² An instance of a specific form of reporting in this case is Art. 656, par.2 CA. Before being appointed by the court the trustee has to declare in a **notarised statement** that there are no obstacles under Art.665 CA to his appointment.

3.2. There are cases in which various forms of reporting are imposed:

- Art. 240-b CA – *‘(1) The members of the Managing Board or Board of Directors³ should inform the Managing Board, respectively the Board of Directors if they or parties related to them enter into contracts with the company, when these contracts are out of the scope of the customary activities of the company or differ substantially from the market conditions⁴.*

(2) The contracts under Art. 240-b, par.1 CA shall be concluded only upon a decision of the Managing Board, respectively the Board of Directors.

(3) A contract concluded in breach of Art. 240-b, par.2 CA shall be valid but the party to such contract that has known or could learn that there has not been a decision under Art. 240-b, par.2 CA shall be liable for the damages caused to the company.’

-Securities law: - Art. 114, par. 2 POSA - Transactions by the publicly-held company with an interested party⁵ shall be approved in advance by the Managing Body of the company.

In these examples (especially in Art. 240-b, par. 1 CA) contracts required to be reported to the Managing Board or Board of Directors are those that fall outside the scope of the company’s objects or that differ substantially from the customary market conditions.

3.3. Under the Bulgarian law, there are no specific requirements as regards the form of the reporting. However, any approval by the Managing Board or Board of Directors of the joint-stock company must be in writing, with protocols signed by all the members of such Body or Board to be prepared for all the resolutions passed (Art.239 CA).

3.4. Bulgarian law regulates an exception from the restriction to concluding certain related-party transactions, i.e. the restriction under Art. 23, par. 3 POSA does not apply to the state when its holding is in the form of non-cash contributions.

3.5. There are also many cases in when prohibitions to the performance of related-party transactions are regulated, as below:

- Art. 647 CA - regulates several revocatory actions for the annulment of certain transfers of assets by the debtor subject to bankruptcy proceedings to related parties, executed before the opening of the bankruptcy proceedings.

- Art.662, par.1 CA - The trustee in bankruptcy proceedings shall not enter into contracts in the name of the company either with himself or with a party related to him⁶.

In the securities law:

- Art. 23, par.2 POSA -A shareholder of the stock exchange⁷ shall not possess, directly or through related parties, more than 5% of its shares⁸.

- Art. 172, par.1 POSA -(1) The members of the Managing or Supervisory Bodies of the managing company or the members of the Managing or Supervisory Bodies of the investment company shall not invest Company assets in securities issued by them or by parties related to

³ These are the two types of governing bodies of the joint-stock companies in Bulgaria.

⁴ The members of the Company’s Managing Bodies and the Company are related parties. Please see Clause 1 of the SP of the CA above.

⁵ Art. 114, par.5 POSA defines interested parties as the members of the managing or Supervisory Bodies, the procurators, and the persons holding more than 25% of the votes in the General Meeting.

⁶ There is a similar restriction on agents under Art.38 of the Obligations and Contracts Act, but in the latter case the restriction does not apply when there is an express consent by the principal for such agreements.

⁷ The stock exchange in Bulgaria is a joint-stock company.

⁸ In this case, there are arguments to contend that related-party transactions may occur when a shareholder gains control over another shareholder (when they both hold more than 5% of the shares of a third company). The parties to the transaction are related under the definition of Clause 1, p.12, ”c” SP of the POSA and the transaction will be null and void, given that it breaches Art.23, par.2 POSA. There are similar restrictions on the indirect acquisition of more than a specified amount of company shares in other cases as well – for instance in banks, in investment companies, etc.

them; (2) The members of the Managing or Supervisory Bodies of the investment company or parties related to them shall not enter into transactions with the investment company other than as shareholders.

- Art. 176, par.2, p.3, "b" POSA - The investment company shall not invest in securities issued by persons controlling the investment company or by parties related to them.

4. Reporting requirements under Croatian law

4.1. There are several forms of reporting under Croatian law:

-Article 478 of Company Law states that as soon as a company acquires over one fourth of stocks or shares in another company having its headquarters located in the Republic of Croatia, it shall notify that company of this fact, in writing and without delay;

- Article 497 of Company Law states that, unless a contract on the conduct of company business operations has been signed, within the first three months of the financial year the managing board of the dependent company shall make a report on the relations between the company and the related companies. This report shall set out all legal operations carried out by the company in the preceding year, with regard to the main company or to the companies related to the main company or according to the instructions following the interests of these companies, as well as all other operations conducted or not conducted in the previous year in accordance with the instructions received from these companies. In matters concerning legal operations, both activities and reciprocal activities shall be set out. In matters concerning other operations, reasons for their performance, as well as advantages and disadvantages they have caused to the company. With regard to the loss, it shall be individually specified how the loss from the previous financial year has been actually compensated or on what particular items was the company allowed to submit a claim. The aforementioned report shall be made in conformity with the principles of conscientiousness and accuracy. At the end of the report, the management board shall state, with reference to the circumstances known at the time when a particular legal operation or activity was performed or not performed, whether adequate consideration was given in respect of each legal transaction and whether any of the activities performed or not performed caused damage to the company. If the company sustained any damage, the management board shall also be obliged to declare whether the damage was compensated. The statement shall be included in the report on the position of the company as well. The report need not be submitted if a contract on the assignment of profits has been signed between the main company on the one hand and the dependent company on the other hand.

- Article 498 of Company Law provides that, whenever the company's annual financial statements need to be audited, the auditor shall be provided with the afore-mentioned report together with the annual financial statements and the report on the state of the company.

- Article 499 provides that the management board shall submit to the supervisory board: the report about relations with the related companies, the auditor's report and, if annual financial statements need to be investigated by the auditor, the auditor's report as well. The supervisory board shall examine the report on relations with the related companies and present a written report on the issue to the general meeting.

- Article 500 provides that, if requested by one of the stockholders or by a member of the limited liability company, the court may order a special investigation into the business relations of the company with the main company or with a related company.

- The supervisory board is at any time entitled to request the management board to report on the legal and business relationships with related companies.

- The management board is required to provide information on the legal and business relations with related companies to each shareholder, at his/her request, at the general meeting.

5. Reporting requirements under Serbian law

5.1. Under the Corporate Profit Tax Law (Article 60), the taxable person is required to

report in the balance sheet such transaction as set out in Article 59 (i.e. transactions between related parties). The taxable person is also required to state the value of the transactions by reference to the to prices that would have been charged for the same transaction between unrelated parties. The transactions are stated in the Corporate Profit Tax Return Form.

5.2. Pursuant to Corporate Law, shareholders can request any information concerning the business of the company. There is no specific provision to prescribe the obligation of the company's General Manager or other (management) body to report (state) the related-party transactions in their regular reports to the shareholders. Nevertheless, having in mind the company's obligation to report related-party transactions (and transfer prices) in accordance with the Corporate Profit Tax Law, such transactions should be reported in the official documents presented to the tax authorities. These documents furnish shareholders (as well as public authorities) with information on related-party transactions. Our experience so far is that companies do not report related-party transactions.

5.3. There are no specific conditions to be met for a company to be under an obligation to report related-party transactions (e.g. transactions exceeding a certain threshold, etc.).

5.4. A subsidiary may acquire shares in the parent company and exercise its voting rights carried by the shares already at its disposal, pursuant to the Law on cross-share companies (i.e. the acquisition of significant, majority and mutual capital share has to be transparent, e.g. entered in the Register and published in the Official Gazette).

5.5. Cross-share companies are related companies, each holding shares in the other. If the cross-shares are of relatively equal value, each company shall reduce its share in the initial capital of the other one by 10%.

5.6. If a company holds shares making up more than 10% of the initial capital of another company, the cross share of the latter company may not be greater than 10% of the initial capital of the former company. A company that acquires a share in the capital of another that is greater than 10% shall notify the latter accordingly forthwith. Starting from the date of receipt of notification, the notified company may not buy shares or stocks of the company, which has acquired more than 10% of its initial capital. If the notified company holds shares accounting for more than 10% of the initial capital of the company from which it has received the notification, the capital share of one company in the capital of the other shall be reduced to not more than 10% by mutual agreement. In the event of such an agreement, the company having a smaller share in the capital of the other shall transfer its shares up to 10% of the initial capital of the other company within a year from receipt of the notification. The right to vote may not be exercised on the basis of shares which a company has to transfer.

Sanctions for breaching the legal treatment of related-party transactions

1. General comments

1.1. Generally, the breach of existing prohibitions to related-party transactions carry severe sanctions (e.g. the deeds constitute criminal offence and carry fines or prison terms, and from the standpoint of civil law the transactions are considered null and void).

1.2. The sanctions for acting in breach of requirements for the reporting of related-party transactions vary from immaterial to severe sanctions. The applicable sanctions may be: civil sanctions, administrative sanctions and criminal sanctions.

1.3. Generally, the applicability of a sanction for breaching related-party transactions does not depend on whether the transaction caused any damage to the company.

2. Civil sanctions

2.1. Civil sanctions consist mainly in the cancellation of the transaction or the possibility to claim in Court the cancellation of the transaction performed in breach of the relevant legal provisions.

2.2. There are cases when the civil sanctions are applicable by virtue of the law (e.g. there is a specific provision to the effect that the transactions performed in breach of the provisions regarding the reporting of related-party transactions are considered null and void). In other cases, the interested persons are entitled to file a court action seeking cancellation of a transaction performed in breach of the reporting rules.

2.3. Minority shareholders face a special situation, given that they are generally the most likely to be affected by related-party transactions.

3. Administrative sanctions

3.1. Administrative sanctions are regulated to apply to cases in which the related party acting in breach of the rules governing related-party transactions is a supervised company (in particular by the Securities Commission). Administrative sanctions can go all the way to withdrawal of the authorisation.

4. Criminal sanctions

4.1. As mentioned above, criminal sanctions apply mainly to breaches of clear prohibitions against the performance of related-party transactions. However, there are cases when criminal offences apply to violations of rules governing the reporting of related-party transactions.

5. Sanctions under Romanian law for non-compliance with the requirements for related-party transactions

5.1. Under Company Law, where the prior approval of the Shareholders' General Meeting is required, it is debatable what civil sanction should apply. The law does not contain a specific provision in this respect. There are strong arguments to claim that the civil sanction would be the relative nullity of the transaction performed in breach of the relevant provisions, provided that the director/board of directors concluded the transaction.

5.2. On the other hand, Company Law prescribes the following criminal sanctions: *'It is to be sentenced to prison in the range of 1 up to 3 years the founder, the manager, the director, the executive director or the legal representative of the company, who:*

1. acquires, on the company's account, shares belonging to other companies for a price of which he is aware that it is well superior to their real value or sells, on behalf of the company, shares belonging to the company for prices about which he is aware they are well under their real value, with the purpose to obtain a profit, for him or for others, to the prejudice of the company;

2. uses, in bad faith, the company's assets or prestige for a purpose contrary to its interests or to his own benefit or in order to favour another company he is directly or indirectly interested in;

3. borrows, in any form, directly or by an interposed person, from the company he is managing or from a company under its control or from a company which controls the one he

is managing or paves the way so that one of these above mentioned companies grant him any kind of guarantee for his own debts;'

5.3. The current securities regulations lay down that:

- In the case of a breach of the article 115 of E.O. 28/2002 (i.e. transactions whose value exceed 20% from the net assets), any of the shareholders may ask the court to annul the concluded juridical act and to entail the liability of the directors for the reparation of the prejudice caused to the company.
- In case of breach of articles regarding reporting related parties transactions (mentioned above) the applicable sanctions could be fine or even imprisonment.

6. Sanctions under Bulgarian law for failure to comply with the requirements for related-party transactions

6.1. As far as the securities regulations are concerned, the Financial Supervision Commission has a broad discretion to impose different administrative measures in order to restore the observance of every legal rule in its area of competence. Some of them are - to order the observance of certain measures; to stop temporarily the public offering of securities; to appoint quaestors⁹ etc.

6.2. In addition to these administrative measures, administrative penalties are provided. For instance – for failing to report a transaction under Art.114, par.2 POSA the administrative penalty is from 2,500 EUR to 5,000 EUR (Art. 221, par. 1, point 4 POSA). These administrative measures and penalties are applicable irrespective of whether the transaction caused damage to the company.

6.3. There is a general provision in the CA, which may be used in the securities law as well – for instance in respect of public companies: Art. 71 CA - Any member of a corporation may bring an action before the district court exercising jurisdiction over the corporation's registered office to defend his (her or its) right of membership and any particular right arising from the said membership, where any such right has been violated by corporate bodies.

7. Sanctions under Croatian legislation for breaching requirements for related-party transactions

7.1. Article 502 provides that the members of the management board who, having offended their duties, fail to mention in their report on the relations between the dependent company and the related companies, all disadvantageous legal operations or activities or if they fail to mention that these operations or activities have caused damage to the company and that it has not been compensated, shall be held responsible if they fail to carry out their duty to review the report on the relations with the related companies and to notify the shareholders meeting about their findings.

7.2. Members of the management board, members of the supervisory board or liquidators who: 1. in their controls or surveys of assets, in debates or in information laid before the company meeting, make false representations or fail to disclose the complete state of affairs of the company, including their relations with the related companies, or 2. in their explanations and information furnished to the controllers of the company or the controllers of a related company, make false representations or fail to disclose the company's true state of affairs, shall be subject to fines or sentenced to prison terms of up to two years.

⁹ They are individuals who replace the management bodies and manage the activities of the company.

8. Sanctions under Serbian law for acting in breach of requirements for related-party transactions

8.1. The taxable person will be liable to fines amounting to CSD 2,000-200,000 if they fail to record as a separate entry in their balance sheet the related-parties transactions (transfer prices). The report should be submitted to the special administrative body in Public Revenue Administration of the Republic of Serbia who specializes in tax offences.” Any taxpayer shall declare in its tax statement separately, together with the related-party transactions the value of such transactions at prices that would have been fetched on the market for such or similar transactions had an associated person not been involved (the "arm's length" principle). According to Corporate Profit Tax Law, the company may be forbidden to perform any business activities in a period between three months to one year, if it does not duly report related parties' transactions in its tax balance (tax report or declaration).

8.2. There are also regulated other kind of sanctions: companies may not link themselves up if such linking is contrary to monopoly regulations. So, if someone breaches monopoly regulations on related-party transaction bases, he/she or it will be responsible in accordance with this specific regulations.

8.3. Under the Corporate Law the criminal act of “Preparing false balances” state as follows: “Any person who prepares a false balance sheet in an company or some other business, declaring the company's profits or losses, or declaring the share of each company member in profits or losses, with a view to obtaining benefit for himself or some other person, or with a view to causing damage to another person, shall be punished for a criminal offence to three months to three years of imprisonment.”

8.4. Other sanctions are not namely prescribed for this specific issue, but various criminal acts (for instance the heading 18 of the Basic Penal Code concerning criminal acts “against market” etc) may be the starting base for prosecuting responsible persons, as well as other commercial offences (Such as under Article 439 of the Corporate Law- ‘An company or other business having the status of a body corporate shall be fined from CSD 45,000 to 450,000 for the commercial offence if it prepares an untrue annual statement of account declaring the company profits or losses and the share of each company member in the profits or losses’) and offences prescribed under various laws. Anyone who has suffered direct damage, and is in a position to prove it may sue the related companies (whether it is concerning any legal transactions, monopoly or any other action that unlawfully caused damage). The specific procedures and other possible criminal acts are mentioned and explained under the “conflicts of interests” part.

8.5. Minority shareholders may raise the question of non-reporting of transfer prices in front of the competent body within the company. Minority shareholders should report related parties' transactions if they were not presented in the tax balance (or report). Please note that in the Law on Companies, it is defined that if a parent company rings a subsidiary company into a position to make a any legal transaction which is harmful to it, or to do or fail to do something to its own detriment, it shall indemnify the subsidiary company for the damage caused on such grounds. The claim for damages may also be filed on behalf of the subsidiary company, by the shareholders and members of the subsidiary company owning or representing at least a tenth of the initial capital of that company or such a smaller portion as is determined by the articles of association, as well as the company's creditors whose claims amount to more than a tenth of the subsidiary company's initial capital. In addition to the parent company, joint and several liabilities shall be borne by members of the parent company's management who brought the subsidiary company into a position to make a harmful legal transaction to itself or to do or fail to do something to its own detriment. Joint and several liabilities shall also be borne by members of the subsidiary company's

management for violation of their duty, unless they were acting on instructions from the parent company's management.

8.6. Investors may only report that to relevant public authorities, but it is for those authorities to decide to conduct an inspection on the taxpayer. Nevertheless, anyone may report possible criminal acts or commercial offences. For the authorities themselves, the tax control is obliged to control the taxpayer for all of its possible breaches of the law.

8.8. The Law on content and form of takeover bid contains as integral parts "Manual on content and form of takeover bid" and "Manual on content and form of announcement of Board of Directors concerning takeover bid". According to these documents the bidder has to make a "takeover bid" if the bidder is to acquire through a new purchase (whether it or its subsidiary already possesses shares of target company or not) the total amount of 25% or more of votes in the General Assembly of the targeted company. When creating a takeover bid, the bidder is obliged to provide detailed data in the takeover bid on its company/bidder, and especially the following: data concerning persons that poses more than 10% votes in bidder's Assembly, or ten major shareholders (or stakeholders) with a right to vote; data on General Manager, members of Board of Directors and Supervisory Board; data on the company's participation in the nominal capital of another legal person (related persons) and subsidiaries of bidder; data on important business and contract concluded between bidder and targeted joint stock company; data on possible negotiations between bidder and members of the targeted joint stock company management concerning the takeover bid as well as the outcome of those negotiations; data on concluded contracts or protocols, or the intention to do so, between the bidder and the members of the target joint stock company management concerning payment of remuneration because of the previous recall or discharge of duties because of company management control overtake; data on concluded contracts or protocols between bidder and shareholders or other securities holders concerning takeover bid etc.

Practices as regards related-party transactions

1. General comments

1.1. As highlighted by our investigations, related-party transaction reporting is rather an undeveloped exercise in the region. In many cases, law practitioners said they did not know how the relevant provisions were normally implemented, given the lack of clear procedures.

1.2. It seems that not all existing provisions on the reporting of related-party transactions are currently implemented. Moreover, whenever undertaken, the reporting of related-party transactions is done in a 'formal', non-creative manner, merely to ensure compliance with the legal provisions, rather than to lend legitimacy to transactions.

1.3. There is little confidence, if any, in the four countries under review, that existing procedures ensure full transparency and disclosure of related-party transactions. This compounds the lack of confidence in the ability of the relevant authorities to lay down and implement adequate procedures.

1.4. The information reported to relevant authorities is not always relevant (e.g. the information on beneficial owner is not reported) and the authorities have no resources/possibilities to check it.

1.5. Sanctions imposed by law and/or relevant authorities consist in civil penalties or administrative sanctions. Rarely are criminal sanctions imposed. The sanctions are imposed

by the relevant authorities, rather than by a corporate body/judicial court. There are few cases in which minority shareholders brought a claim for the company's failure to meet its reporting obligation.

2. Reporting practices in Romania

2.1. According to information obtained off-the-record from employees of the National Securities Commission, an efficient related-party transaction reporting procedure is used in respect of publicly-held companies. Related-party transactions are indeed subject to reporting, as indicated by the National Securities Commission, also off-the-record. However, from our experience, publicly-held companies have a very poor record of meeting their reporting obligations in general, to say nothing about the reporting of related-party transactions.

2.2. Lately, the National Securities Commission has paid more attention to how publicly-held companies observe their reporting obligations (including by imposing sanctions on non-compliant companies). Therefore, companies have started to implement the legal provisions on reporting, including provisions governing the reporting of related-party transactions.

2.3. As mentioned above, related-party transactions are reported in a report to be submitted by the director to the National Securities Commission. Nevertheless, the National Securities Commission does not currently have the technical capabilities to verify the accuracy of such reports. Therefore, there is no practice as regards, for instance, incomplete reporting.

2.4. What the National Securities Commission has imposed so far is mainly administrative sanctions. The Commission has referred a number of cases to the prosecution services, for investigation under criminal law. Only in a very limited number of cases have criminal sanctions been imposed.

2.5. In the practice of the publicly-held companies it is generally the director of the publicly-held company who reports the related-party transactions (when these transactions are indeed reported), in compliance with the legal provisions in effect.

2.6. As regards the form of reporting related-party transactions pursuant to Company law, to the best of our knowledge generally such transactions are made in practice with the approval of the Shareholders' General Meeting. However, there are many cases when the related party is the majority shareholder itself. In such cases, once the requirement of having the approval of the Shareholders' General Meeting has been duly met, there is no other legal route for the shareholders to challenge transactions detrimental to their interests. We are not aware of much case-law in this respect .

3. Practices in Bulgaria

3.1. We asked several law practitioners whether they thought the existing regulatory framework governing the reporting of related-party transactions was appropriate. They were reluctant to giving their opinion on the issue, presumably because the legal framework is not fully implemented and it is therefore difficult to establish whether the provisions (at least as far as the concepts are concerned) are sufficient and appropriate.

3.2. It seems that sanctions (mostly civil penalties) were imposed in certain cases for the failure to observe the requirements relevant to related-party transactions. Some Supreme Court case-law appears to have developed on the matter.

3.3. In certain cases, the related-party transactions were challenged by minority shareholders or by the authorities, and their number is rising.

4. Practices in Croatia

4.1. We have not received relevant information on related-party practices in Croatia.

5. Practices in Serbia

5.1. Based on the information we have received from Serbia, the existing regulatory framework governing the reporting of related-party transactions is not sufficient or appropriate. The tax provisions are considered too vague, with no further guidance for implementation.

5.2. It seems that related parties generally do not report transactions between them. Civil penalties are seldom imposed, with hardly ever any criminal sanctions being instructed.

5.3. There is no practice as regards the challenging of related-party transactions by the minority shareholders or by the authorities.

IV. REPORTING CONFLICTS OF INTERESTS

Concept of conflicts of interests

1. General Comments

1.1. Generally, there are no definitions of 'conflicts of interests'. There are no separate definitions under company law or the securities laws of 'conflict' or 'interest' respectively. The legislations we have reviewed carry hints as to what can be deemed to constitute a 'conflict of interests' (e.g. having competing interests to those of the represented, managed legal entity; having a personal interest when voting in a corporate body), but fail to provide an exhaustive list of what is covered by 'conflicts of interests'.

1.2. The 'conflicts of interests' concept is less precisely regulated than 'related party'. It is likely to cover any kind of situation and relationship that may result in conflicting interests.

1.3. A critically important aspect, as far as conflicts of interests are concerned, is the prohibition of inside trading in the case of publicly-held companies. The legislations under review do not specifically state that inside trading carries a component of 'conflicts of interest'. Nevertheless, in our opinion it could be sustained that, by holding inside information, the holder actually engages in a conflict of interests with the issuer.

2. Main categories of conflicts of interest

2.1. The main categories of conflicts of interests regulated by company law and securities regulations are the following:

- **Conflicts of interests arising within a company:** the most common conflicts of interests at corporate level arise between the interests of one member of the corporate bodies and the interests of the company itself. The member of a corporate body could be a director, executive officer, a shareholder, a legal representative. A conflict of interests may also arise when a relative or spouse of one of the members sitting on a corporate body has any interest in a transaction to be approved by that corporate body.
- **Conflicts of interest arising between specialised companies acting on the regulated markets (e.g. brokerage companies) and their clients:** generally, brokerage companies are required to give priority to their clients' interests and refrain from satisfying their own interests first, to the detriment of the clients' interests.
- **Conflicts of interests between members of certain professions rendering services to specialised Services Providers:** the most common case is that of auditors, censors (internal auditors). There may be a wide array of conflicting interests (e.g. under Romanian law, an auditor is deemed to face a conflict of interests if it engages in any kind of relations with the company or with a third party with whom the audited company has a relationship).
- **Conflicts of interest regulated under specific regulations (i.e. banking regulations):** generally, with certain companies, 'conflicts of interest' are regulated more specifically (e.g. as is the case under Romanian banking law, which includes an entire chapter on the bank director's conflicts of interests).

3. Beneficial ownership

3.1. The lack of specific requirements as regards the disclosure of ‘beneficial ownership’ could also lead to cases where the actual conflicts of interests may not be identified. In such cases it is not possible to ensure appropriate disclosure or to observe the legal regulations on conflicts of interests.

4. Concept of ‘conflicts of interest’ under Romanian law

4.1. Under Romanian Company Law and Securities Law, there are provisions on conflicts of interests. They cover both conflicts of interests within a company and as regards the providers of specialised services. There is no definition of conflicts of interests under either Company Law or the securities regulations.

4.2. The most relevant Company Law provisions regarding conflicts of interests refer to possible competing interests between a shareholder and the company, a director and the company, internal auditors (censors) and persons holding other offices in the companies and/or in certain public institutions, the executive manager and the company, and the legal representative of a company. There is no Company Law provision regulating potential conflicts of interests of external financial auditors. Rules on conflicts of interests exist in the regulations governing auditor’s profession. Save for the case of internal auditors, the law does not presume the existence of a conflict of interests in the other cases.

4.3. Under the securities regulations in force, conflicts of interests may arise between brokerage companies and their clients.

4.4. The draft Consolidated Law on the capital market contains references to conflicts of interests between the brokerage (intermediary) companies and also to persons conducting studies on financial instruments and publishing information on such instruments. Any conflict of interests in connection with the financial instruments must be made public.

4.5. Rules regarding conflicts of interests are also set out in the regulations regarding financial auditors (Emergency Ordinance 75/1999, as subsequently amended). Under these regulations, a conflict of interests exists whenever the auditor is not independent, i.e. being in any kind of relationship with the company or with a third party with which the audited company has a relationship.

4.6. Under Banking Law (Law 58/1998 as amended subsequently), there are specific clauses regarding the director’s conflict of interests with the bank.

5. Concept of ‘conflicts of interests’ under Bulgarian law

5.1. Banking Law regulates in detail the legal treatment of conflicts of interests. The most relevant provisions of the Banking Act (BA) on the issue are as follows:

-Art. 31 BA: ‘(1) Each administrator in a bank shall disclose in writing before its managing body every substantial commercial, financial or other business interest that he or a member of his family has from the conclusion of a commercial contract with the bank;

(2) Substantial business interest shall be deemed to exist in each case when a party to the contract with the bank is: a) The administrator or a member of his family; b) A person with whom the administrator or a member of his family is economically connected by: 1.

Possessing directly or indirectly qualified majority of the shares; 2. Being his administrator; 3. By being a co-shareholder in a limited liability company, general or limited partnership.

(3) Each administrator shall declare once every six months in writing before the Managing Board (or the Board of Directors):

- The names and the addresses of the persons, economically connected with him or with the members of his family as well as
- The business interests, which they have with the bank at the moment of lodging the declaration.

(4) Administrator who has business interest from the conclusion of a contract with the bank shall not take part in the negotiations and in the taking decisions for its conclusion.

(5) The administrators and the other employees of the bank shall regard the interests of the bank and the clients thereof as dominating over their personal interests.

5.2. Furthermore there are legal provisions in the security laws:

- Art. 25 of the Special Investment Purpose Companies Act (SIPCA): (1) The persons who manage and represent special investment purpose companies shall fulfil their obligations in good faith and with due care for protection of the investors and shall prefer the company interest before their own interest.

(2) The persons under par.1 above shall declare annually before the Financial Supervision Commission their property and business interests.

(3) The persons under par.1 above shall avoid conflicts between their personal interest and the company interest. Should such conflicts occur they shall disclose them in a way convenient for the investors and shall not take part in the decision making in such a case.

- Art.6, par.1 Regulation on the Requirements to the Activity of Investment Intermediaries (RRAII): The investment intermediary shall not perform activity on the account of a client before informing him for the potential conflicts of interests, as well as for the conflicts of interest with another client if in this way no requirement for confidentiality is broken and no interests of the other client are affected.

- Paragraphs B.3.1. and B.3.2. of Appendix 5 to Art. 3, par.3, p.3 of the Regulation on Prospectuses for Public Offering of Securities (RPPOS): 3.1. If one of the experts or consultants referred to in the documents¹⁰ possesses considerable portion of the company shares or shares of a subsidiary of this company; has considerable direct or indirect economic interest in the company and/or his remuneration depends on the success of the public offering, for which the prospectus is prepared a short information about these circumstances shall be disclosed; 3.2. The conflicts of interests connected with the public offering shall be disclosed in details as to the essence of the conflicts and the parties related thereof.

Art.7, par.2 of the Regulation on the Requirements to the Activity of Managing Companies (RRAMC): The managing company shall not take investment decisions even when they are in the scope of the investment strategy and aims of the company whose investment activity or portfolio is managed before informing the company in a convenient way for the potential conflicts of interests; in such cases the managing company shall request approval in advance for the investment decision taken.

5.3. In the corporate law there is only one provision on the conflict of interests. It is in Article 229 of the Commercial act (CA), entitled “Conflicts of interests” and it reads “a shareholder or its representative cannot take part in the voting concerning:

- The lodging of claims against him or
 - Taking actions to carry into effect his liability in his relations with the joint-stock company”.
- However there is no definition of Conflict of interest in the general corporate law.

5.4. As far as the professional standards are concerned I found a provision on the conflicts of interest in Par.1, point 3 of the Supplementary provisions of the Independent Financial Audit Act (IFOA): A violation of the principle for independence of the auditor and conflict of interests occur when:

¹⁰ The documents referred to in this paragraphs are those forming the prospectus when the latter consists not in a single document, but in several separate documents

- The registered auditor has financial interest in the activity of the company audited, consisting in possessing portions of the capital, shares or other securities issued by the company and/or participation in the activities thereof;
- The registered auditor takes part in the managing of the company audited;
- The registered auditor is in matrimonial or in blood relations with the management of the company audited;
- There is a pending suit case between the registered auditor and the company audited.

6. Concept of ‘conflicts of interests’ under Croatian law

6.1. The Law on Bookkeeping stipulates that the International Accounting Standards are applicable in the Republic of Croatia.

6.2. According to the Croatian Company Law, without having consent of the supervisory board a member of the management board shall not be allowed, either for his or for someone else’s account, to perform activities within the scope of the company business, to act as a management or supervisory board member in another company engaged in similar business to that of the company, or to perform in the company’s premises activities for his own or for another person's account. Without the aforementioned consent the management board member shall not be the member of another trading company holding personal responsibility for that company's obligations if business operations of that company interfere with business activities of the company.

7. Concept of ‘conflicts of interests’ under Serbian law

7.1. An entirely new Corporate Law is expected to be implemented in 2004. The information below is based on the existing law.

7.2. Conflicts of interests are defined in the Corporate Law in the chapter 16.7,

- Article 93 “*Conflicts of interests in carrying out business activities (conflicts of interests clause)*” as follows:

(1) A partner in a general partnership, a general partner in a limited partnership, a member of a limited liability company, and a member of the company management, Supervisory Board and Executive Board of Directors of a limited liability company, corporation and a socially owned and public enterprise, and a procurator, may enter into a contract with the enterprise in which they have that status, concerning a contract on loan, surety, guarantee, backing and collateral, as well as any other legal affair prescribed in foundation act and/or in articles of association, with the approval of other members and/or the Board of Directors or the Supervisory Board.

(2) The approval referred to in paragraph 1 of this Article shall also be required for any legal affair entered into by other persons, in which the persons referred to in that paragraph have an interest.

(3) An interested person referred to in paragraph 1 of this Article may not vote in the Board of Directors or Supervisory Board when approval is being decided on.

(4) All members or shareholders in the company will be notified of any approval as that referred to in paragraph 1 of this Article at the next General Meeting of the Assembly.

(5) The foundation act and/or articles of association may prescribe that approval is not necessary for affairs made under usual conditions.

(6) A natural person acting in the capacity of the founder, shareholder and member of a one-person (member) company may not enter into a contract with his own company such as a contract on loan, deposit, guarantee, backing guarantee and surety.

- Another provision on conflicts of interests concerning only a joint stock company is the provision in chapter 21.11: Article 259 “Exclusion from voting”:

‘A shareholder may not vote at the General Meeting of the Assembly when deciding:

- (1) *On the release from duties and liabilities of the shareholder concerned*
- (2) *On the grant of facilities to the shareholder concerned at the expense of the company*
- (3) *On the establishment of the company's claims from the shareholder concerned*
- (4) *On the starting or giving up from any legal action (procedure) against the shareholder concerned*
- (5) *In any other cases when, the interests of the shareholder concerned are contrary to the interests of the company (conflicts of interests clause)'.*

7.3. Law on Securities Market: Conflicts of interests are defined in the Serbian Law on Securities Market in the Article 123 "Conflicts of interests" as follows:

- (1) *A broker-dealer company cannot put its own interests in front of the interests of the client.*
- (2) *A broker-dealer company is obliged to present possible conflicts of clients interests and company interests, as well as interests of other broker-dealer company clients.*
- (3) *A broker-dealer company is obliged to organize its business in such a manner to minimize possible conflicts of interests among its employees, clients and other broker-dealer companies.*

Legal treatment of conflicts of interests. Reporting conflicts of interests

1. General comments

1.1. Different types of 'conflicts of interests' are subject to different legal treatments. The applicable legal treatment may consist in (i) disclosure obligations (reporting conflicts of interest), (ii) prohibitions against performing certain transactions or against involvement in the decision-making process in the event of a conflict of interests, (iii) prohibitions on continuing to provide specific services (e.g. auditing) after a conflict of interests arose, (iv) obligations to implement procedures meant to avoid conflicts of interests, etc.

1.2. Notwithstanding the above, reporting conflicts of interests is instrumental to rendering other provisions applicable.

1.3. There are different versions of reporting: reporting to the members of the Board of Directors, reporting to the shareholders, reporting to the client. There are few cases in which conflicts of interests are reported to an authority.

1.4. Generally, the obligation to determine whether a conflict of interests exists rests with the person engaged in such a conflict. Such an obligation exists from the moment the conflict arose.

1.5. Unlike related-party transactions, which can be further approved and performed once disclosed, conflicts of interests, once identified, cause the competing activity to cease.

1.6. Generally, there are no exceptions from the rules to be followed if conflicts of interests are identified.

2. Differences between conflicts of interests and related-party transactions

2.1. In our opinion, the concept of 'conflicts of interests' revolves around competing or conflicting interests. Most categories of persons qualifying as related party are also subject to regulations governing conflicts of interests. Nevertheless, acting as a 'related party' may result in a 'conflict of interests', although this is not necessarily the case. The purpose of

regulating 'conflicts of interests' differs from the purpose for regulating 'related-party transactions', which warrants the dissimilar legal treatments of related-party transactions and conflicts of interests.

3. Reporting conflicts of interests under Romanian law

3.1. The legal treatment of conflicts of interests under Company Law consists mainly in the following:

-Art. 126: '(1) *The shareholder who, with regard to a certain operation, has a personal or, as proxy of another person, an opposite interest to that of the company, will have to refrain from taking part in the proceedings concerning that operation.* (2) *The shareholder who breaks this provision is liable for damages caused to the company if, without his vote, the required majority would not have been met.*'

- ART. 142: '(1) *Nobody may act in more than three managing boards at the same time.*

(2) *The interdiction stipulated by paragraph (1) does not refer to cases when the person elected on the managing board is the owner of at least a quarter of the stock or administrates a company which possesses the mentioned quarter.*

(3) *The one who will not observe the above-mentioned provision, will loose by right this capacity as manager, obtained by exceeding the legal number of appointments in a chronological order and will be sentenced, for the benefit of the state, to pay back the remuneration and other due benefits, as well as to hand back the sums of money he cashed in.*

(4) *The action against managers can be brought by any shareholder or by the Ministry of Finance.*

(5) *The members of the managing committee and the directors of a joint-stock company can neither be managers, members of the managing committee, auditors or associates with unlimited liability, without the authorization of the managing board, in other competing companies or having the same object, nor can they exercise the same trade or another competing one, on their own account or on another person's account, under the penalty of being dismissed and held liable for damages.'*

- Art. 145: '(1) *The manager who, in a certain operation, has, directly or indirectly, interests opposed to those of the company, must inform the other managers and the auditors about this matter and must not take part in any proceeding concerning the respective operation.*

(2) *The manager has the same obligation in case he knows that, in a certain operation, his wife, relatives and affines up to the fourth degree included take an interest. ...*

(4) *The manager who didn't observe the provisions of paragraphs (1) and (2) shall be liable for the damages resulting for the company.'*

3.2. Under the securities regulations in force, the main provisions setting out the treatment of related-party transactions are the following:

- Art. 153 - (2) *Financial investment services companies and their agents shall be forbidden to fulfil their functions or duties in the case of a conflict of interest between the client and the intermediary.*

Under the Regulation regarding the authorisation of financial services companies, procedures for the conduct of activities likely to give rise to conflicts of interests in separate departments must be laid down in the internal regulations of these companies.

3.3. Under the Draft Law on the capital market, the provisions regarding conflicts of interests applicable to brokerage companies include the ones mentioned under 3.2. above (taking into account the status of brokerage companies conducting business in Romania, under the supervision of overseas supervisory authorities). In addition a new article was inserted (Art. 258, paragraph 2): *'The persons producing or distributing studies regarding financial instruments or financial instruments issuers, as well as the persons producing or dispensing other information through which they recommend or suggest investment strategies using mass media tools must make sure that such information are accurately presented. These persons*

will indicate the nature of their interest or possible conflicts of interest affecting the financial instruments for which these studies are made.

3.4. Regulations on the audit profession state that a person is disallowed from acting as a financial auditor for a legal entity, if he is an employee of that particular entity or if he is in any way affiliated to this legal entity or with any other person with whom the legal entity has a relationship likely to lead to incompatibility or conflicts of interests. Further details on this are available in the Auditors' Code of Conduct.

3.5. Under the banking regulations, a director's conflicts of interests are regulated as follows:
-Art. 29: *'The manager shall notify the bank in writing on the nature and extent of his or her material relation or interest, if he or she:*

a) is party to a contract with the bank;

b) is manager of a juristic person that is party to a contract with the bank;

c) has a material interest or a material relation with a person who is party to a contract with the bank except contracts of deposit or custody of securities.'

-Art. 30: *'The obligation provided under Art. 29 devolves upon the manager when he has known or should have known the fact that such a contract was concluded or was under way of being concluded.'*

-Art. 31: *'The manager of a bank shall be under an obligation, whenever necessary, but not less than once a year, to present in writing to the Managing board of the bank a statement showing the names and addresses of his or her associates and data with reference to the material interest of financial, commercial, agricultural, industrial or of another nature of the manager and of his or her family.'*

-Art. 32: *'A manager having a material interest or a material relation in the sense of articles 29, 31 and 33 shall not participate in the debates on the contract and shall abstain from voting on any problem in connection with this contract.'*

For the purpose of achieving the necessary quorum for taking a decision on the contract in question, the manager will be considered present.'

-Art. 33: *'An interest shall be considered material in the sense of the provisions under articles 29 and 31, if it refers to the wealth, affairs or interests of the family (of the husband or wife, relatives, and in-laws up to twice removed inclusive) of the person who has an interest.'*

- Art. 34: *'When a manager fails to declare a conflict of interests, conformably to the provisions under the present chapter:*

a) the bank, or one of its shareholders, or the National Bank of Romania may petition the appropriate judicial instance to annul any contract in which the respective manager has an undeclared material interest, in keeping with the provisions under the present chapter;

b) according to Art. 70, the National Bank of Romania may request the bank the suspension of the manager over a period not exceeding one year, or his/her replacement.'

4. Reporting 'conflicts of interest' under Bulgarian law

4.1. The Bulgarian law regulates in detail the legal treatment of conflicts of interests. The most relevant provisions of the Banking Act (BA) are set out below:

-Art. 31 BA: *'(1) Each administrator in a bank shall disclose in writing before its managing body every substantial commercial, financial or other business interest that he or a member of his family has from the conclusion of a commercial contract with the bank;*

(2) Substantial business interest shall be deemed to exist in each case when a party to the contract with the bank is: a) The administrator or a member of his family; b) A person with whom the administrator or a member of his family is economically connected by:1.

Possessing directly or indirectly qualified majority of the shares; 2. Being his administrator;

3. By being a co-shareholder in a limited liability company, general or limited partnership.'

(3) Each administrator shall declare once per six months in writing before the Managing Board (or the Board of Directors):

- *The names and the addresses of the persons, economically connected with him or with the members of his family as well as*

- *The business interests, which they have with the bank at the moment of lodging the declaration.*

(4) Administrator who has business interest from the conclusion of a contract with the bank shall not take part in the negotiations and in the taking decisions for its conclusion.

(5) The administrators and the other employees of the bank shall regard the interests of the bank and the clients thereof as dominating over their personal interests.

4.2. Furthermore, there are relevant legal provisions under the security laws:

- Art. 25 of the Special Investment Purpose Companies Act (SIPCA): *(1) The persons who manage and represent special investment purpose companies shall fulfil their obligations in good faith and with due care for protection of the investors and shall prefer the company interest before their own interest.*

(2) The persons under par.1 above shall declare annually before the Financial Supervision Commission their property and business interests.

(3) The persons under par.1 above shall avoid conflicts between their personal interest and the company interest. Should such conflicts occur they shall disclose them in a way convenient for the investors and shall not take part in the decision making in such a case.

- Art.6, par.1 Regulation on the Requirements to the Activity of Investment Intermediaries (RRAII): *The investment intermediary shall not perform activity on the account of a client before informing him for the potential conflicts of interests, as well as for the conflicts of interest with another client if in this way no requirement for confidentiality is broken and no interests of the other client are affected.*

- Paragraphs B.3.1. and B.3.2. of Appendix 5 to Art. 3, par.3, p.3 of the Regulation on Prospectuses for Public Offering of Securities (RPPOS):3.2. *The conflicts of interests connected with the public offering shall be disclosed in details as to the essence of the conflicts and the parties related thereof.*

-Art.7, par.2 of the Regulation on the Requirements to the Activity of Managing Companies (RRAMC): *The managing company shall not take investment decisions even when they are in the scope of the investment strategy and aims of the company whose investment activity or portfolio is managed before informing the company in a convenient way for the potential conflicts of interests; in such cases the managing company shall request approval in advance for the investment decision to be taken.*

4.3. The Commercial Act (the corporate law) contains only one provision on conflicts of interests, i.e. Article 229 headed "Conflicts of interests". Article 299 reads: "*a shareholder or its representative cannot take part in the voting concerning:*

- *The lodging of claims against him or*

- *Taking actions to carry into effect his liability in his relations with the joint-stock company".*

4.4. As far as professional standards are concerned, there is a provision on the conflicts of interests in Par.1, point 3 of the Supplementary provisions of the Independent Financial Audit Act (IFOA): A violation of the principle for independence of the auditor and conflict of interests occur when:

- The registered auditor has a financial interest in the activity of the audited company, consisting in possessing portions of the capital, shares or other securities issued by the company and/or participation in the activities thereof;

- The registered auditor takes part in the management of the audited company;

- The registered auditor is related by marriage or kinship with the management of the company audited;

-There is a pending lawsuit between the registered auditor and the audited company.

4.5. It seems that there are no exceptions from the rules regarding reporting conflicts of interest.

5. Reporting ‘conflicts of interests’ under Croatian law

5.1. Under Croatian Company Law, without the consent of the supervisory board, no member of the management board shall be allowed, either for his or for someone else’s account, to perform activities falling within the scope of company objects, to act as a manager or as a supervisory board member in another company engaged in business similar to that of the company, or to perform on the company premises activities for his own or for another person’s account. Without the said consent, the management board member shall not be the member of another trading company holding personal responsibility for that company’s obligations if business operations of that company interfere with business activities of the company.

5.2. If a management board member acts contrary to the aforementioned ban, the company may ask him to make up for the damage caused to the company. Instead of doing so, the company may also ask the management board member to allow that business operations which he had concluded for his own account are considered as business operations concluded for the account of the company or to transfer his receipts following from the business concluded for someone else’s account to the company, i.e. to cede his claim for payment of the remaining part of his receipts to the company. The company’s aforementioned demand shall become obsolete three months after other members of the management and supervisory boards have learnt about the event on the grounds of which compensation for the damage may be demanded. The demand shall become obsolete in any case, regardless of the knowledge about the aforesaid event, five years after the aforementioned event took place.

5.3 Provisions stipulated for the issues related to the management board members shall also be applicable to their deputies.

5.4. A member of the supervisory board cannot at the same time be a member of the management board, a permanent deputy of a management board member, a procurator or a representative of the company.

6. Reporting ‘conflicts of interest’ under Serbian law

6.1. Conflicts of interests are defined in the Corporate Law in chapter 16.7,

- Article 93 “*Conflicts of interests in carrying out business activities (conflicts of interests clause)*” as follows: (1) *A partner in a general partnership, a general partner in a limited partnership, a member of a limited liability company, and a member of the company management, Supervisory Board and Executive Board of Directors of a limited liability company, corporation and a socially owned and public enterprise, and a procurator, may enter into a contract with the enterprise in which they have that status, concerning a contract on loan, surety, guarantee, backing and collateral, as well as any other legal affair prescribed in foundation act and/or in articles of association, with the approval of other members and/or the Board of Directors or the Supervisory Board.*

(2) *The approval referred to in paragraph 1 of this Article shall also be required for any legal affair entered into by other persons, in which the persons referred to in that paragraph have an interest.*

(3) *An interested person referred to in paragraph 1 of this Article may not vote in the Board of Directors or Supervisory Board when approval is being decided on.*

(4) *All members or shareholders in the company will be notified of any approval as that referred to in paragraph 1 of this Article at the next General Meeting of the Assembly.*

(5) *The foundation act and/or articles of association may prescribe that approval is*

not necessary for affairs made under usual conditions.

(6) A natural person acting in the capacity of the founder, shareholder and member of a one-person (member) company may not enter into a contract with his own company such as a contract on loan, deposit, guarantee, backing guarantee and surety.

Without approval, none of the persons mentioned above may conclude such contracts. The contracts concluded in this case have no legal force. Such contracts will be annulled by the relevant corporate body, or in the event of a dispute, will be voided by court ruling following litigation before the competent Commercial Court. The Law allows for any other legal affair prescribed in the Constitutive Document and/or in the Articles of Association to qualify as a conflict of interests, besides the five contracts, i.e. loan, surety, guarantee, backing and collateral).

It should be mentioned that this article is an evidence for the confusion existing in the legislations as regards 'related party transactions' versus 'conflicts of interest'. Thus this article despite the fact that defines 'conflicts of interest' covers rather transactions between related parties that may be performed if certain approvals are obtained.

6.2. Article 259 "Exclusion from voting" (chapter 21.11) also refers to conflicts of interests, but only in respect of joint-stock companies:

'A shareholder may not vote at the General Meeting of the Assembly when deciding:

(1) On the release from duties and liabilities of the shareholder concerned

(2) On the grant of facilities to the shareholder concerned at the expense of the company

(3) On the establishment of the company's claims from the shareholder concerned

(4) On the starting or giving up from any legal action (procedure) against the shareholder concerned

(5) In any other cases when, the interests of the shareholder concerned are contrary to the interests of the company (conflicts of interests clause)'. The Meeting is the corporate body (in the joint-stock company) having the power to annul resolutions passed in breach of Article 259. In the event of a dispute, this issue will be resolved by litigation in front of the relevant Court.

6.3. The Law on Securities Market: Conflicts of interests are defined in Serbian Law on Securities Market in Article 123 "Conflicts of interests" as follows:

(1) A broker-dealer company cannot put its own interests in front of the interests of the client.

(2) A broker-dealer company is obliged to present possible conflicts of clients interests and company interests, as well as interests of other broker-dealer company clients.

(3) A broker-dealer company is obliged to organize its business in such a manner to minimize possible conflicts of interests among its employees, clients and other broker-dealer companies.

6.4. If someone identifies a conflict of interests he/she should report it. The company should suspend all activities concerning conflict of interests, and abrogate all decisions brought by breaching the conflict of interests' clause if the competent public body decides that the clause has been breached. In case of recognition, the conflict of interests by the competent public body, and all consequences deriving from decision/contract may be nullified. In litigation, the plaintiff should start the lawsuit along with the injunction for suspending all activities deriving from conflicts of interests. Other effects will arise upon the competent body's decision in the specific case.

6.5. Article 68 of the Law regulates the Incompatibility of Functions in the following cases:

(1) In the case of related companies, the General Manager of a parent company may not be the General Manager of a subsidiary, and the General Manager of a subsidiary enterprise may not be the General Manager of the parent enterprise.

(2) In the case of linked enterprises, the General Manager of a parent enterprise may not be the Chairman of the Board of Directors of a subsidiary, and the General Manager of a subsidiary enterprise may not be the Chairman of the Board of Directors of a parent enterprise.

(3) The General Manager of that company, the General Manager of the related companies, a member of the Executive Board of Directors, a member of the Supervisory Board and a member of the Board of Directors might not represent the socially owned capital at the General Meeting of an enterprise.

(4) Membership of the Board of Directors and the Supervisory Boards of related companies shall be regarded as membership of one Board.

Sanctions for failing to report conflicts of interests

1. General comments

1.1. Generally, the breach of effective provisions regarding conflicts of interests carry severe sanctions, even more severe than those for reporting related-party transactions (e.g. the deeds constitute criminal offence and carry fines or prison terms, and from the standpoint of civil law the transactions are considered null and void).

1.2. The applicable sanctions for failing to comply with the 'requirements' for reporting conflicts of interests include: civil penalties, administrative sanctions and criminal sanctions. It is not only the failure to disclose that is punishable, but also any document concluded without disclosing the existence of a conflict of interests.

1.3. Generally, the applicability of a sanction for breaching the legal regime of conflicts of interests does not depend on whether the transaction caused any damage to the company.

2. Civil sanctions

2.1. Civil sanctions consist mainly in the annulment of the transaction or the possibility to be claimed in Court the cancellation of the transaction performed in breach of the relevant legal provisions. There are cases in which civil sanctions are applicable by operation of the law (e.g. there is a specific provision to the effect that transactions performed in breach of the provisions regarding the reporting of conflicts of interests are considered null and void). In other cases, the interested persons are entitled to file a court action seeking cancellation of a transaction performed in breach of the reporting rules.

2.2. Other civil sanctions laid down by the laws under review include: the obligation to cover any damages caused to a company by breaching the rules on conflicts of interests; the obligation to repay sums received for exercising certain positions filled in breach of the rules on conflicts of interests, etc.

3. Administrative sanctions

3.1. Administrative sanctions apply to cases in which an individual or legal entity acts in breach of the rules governing conflicts of interests. Administrative sanctions can go all the way to withdrawal of the authorisation (i.e. for brokerage companies, for bank directors, etc.).

4. Criminal sanctions

4.1. There are many criminal sanctions applicable to breaches of the legal treatment of conflicts of interests.

5. Sanctions under Romanian law for failing to observe requirements for the reporting of conflicts of interests

5.1. Pursuant to Company Law, Art. 266: *'It is to be sentenced to prison in the range of 1 up to 3 years the founder, the manager, the director, the executive director or the legal representative of the company, who:*

2. uses, in bad faith, the company's assets or prestige for a purpose contrary to its interests or to his own benefit or in order to favour another company he is directly or indirectly interested in;

Romanian Company Law also regulates civil sanctions. Civil sanctions consist mainly in the obligation for the shareholder/director to cover any damage caused to the company.

5.2. Under the securities regulations the applicable sanctions are rather administrative sanctions (e.g. withdrawal of the authorisation), sanctions for minor offences or criminal sanctions.

5.3. Under the regulations governing the audit profession, if an auditor no longer meets the requirements for exercising its profession independently, he is under an obligation to immediately relinquish its engagement, and notify to its client the termination of the agreement, as well as the grounds for such termination. Should the relevant authority determine the existence of independence breaches, it will take action against the auditor and inform the authority which received the financial statements prepared by the relevant auditor.

5.4. Under banking regulations, the sanctions that may be imposed on the director acting in breach of these rules include the following: the replacement of the directors and the annulment of the agreements to which the director is a party.

6. Sanctions under Bulgarian law for failing to observe the requirements regarding the reporting of conflicts of interest

6.1 Under Art. 32 of the Banking Act: The contracts concluded by the administrator in breach of Art. 31 shall be null and void. The court upon a request by the bank, The Central Bank of Bulgaria or another interested party shall establish this fact. When the central bank establishes the fact that the administrator is in breach of Art.31 it shall order the bank to suspend his powers in a defined term or shall suspend his powers if the bank does not fulfil the order to do so in the given term.

6.2. Section 4 also prescribes several sanctions under *'Legal regime of conflicts of interest'*. Generally, the sanctions are applicable regardless of whether the transactions affected by conflicts of interests are detrimental to the company/issuer.

7. Sanctions under Croatian law for breaching requirements for the reporting of conflicts of interest

7.1. Croatian law prescribes civil sanctions for failing to observe the rules on conflicts of interests. These sections are presented under section 5 of *'Legal regime of conflicts of interest'*.

8. Sanctions under Croatian law for failing to observe the requirements for the reporting of conflicts of interests

8.1. Under part V of Company Law - "Penal provisions", the Law prescribes criminal acts, commercial offences and offences by the company or the person in charge within the company. If someone's actions contain any elements of criminal act or any other offence, he/she should be reported to the relevant public authorities (police or public prosecutor). Any individual or the official/employee of the company can file the report or charge against the relevant person (natural or legal). Conflicts of interests may be reported under Article 439 of the Law, a company or other merchant having the status of a legal entity shall be subject to fines ranging between Serbian Dinars ("CSD") 45,000 to 450,000 for the commercial offence if, acting as a member or shareholder, mismanages the company with a view to meeting for itself an unlawful objective or causing damage to its creditors, or if contrary to law, it treats the enterprise assets as its own, or if it reduces the enterprise assets for its own benefit or the benefit of some other person, although this article refers to the other legal concept prescribed by law – "Disguise of the legal person".(i.e. The institute of "the legal person Disguise" is defined under the Article 54 of the Law as: "The founders, members and shareholders, directors and members of the executive board of directors shall be liable for an enterprise's commitments to the extent of their total assets: (1) If they have misused the enterprise for the purpose of reaching an objective which is prohibited for them; (2) If they have misused the enterprise for the purpose of causing damage to their creditors; (3) If contrary to regulations, they have treated the enterprise assets as if they were their own assets; (4) If they have decreased the enterprise assets for their own benefit or for the benefit of any other person, when they knew or must have known that the enterprise will not be able to meet its commitments to third parties."). Conflicts of interests may, as well, be reported under the Article 440 of the Law, an enterprise or other commercial subject having the status of a legal person shall be fined of from CSD 15,000 to 150,000 for offence (breach) if as a company member, a director or member of some other body of the company or enterprise concerned, he makes a legal transaction with the company or enterprise concerned, without prior approval of other company members or competent body (this Article directly refers to Article 93 of the Law which defines conflicts of interests).

If someone's actions contain any elements of criminal act prescribed by the Penal Code of Serbia or the Basic Penal Code or other special law, as well as any other (offence), he/she should be reported to the relevant public authorities. In that case he/she will not be responsible just on the basis of conflicts of interests but on the basis of other provisions of the competent law. His/hers criminal or offence responsibility will arise from the definition of the criminal act/offence that has been committed.

8.2. The sanctions for failing to report any breach of regulation are criminal sanctions for a natural person, or a commercial offence and offence sanctions for natural and legal person. Under chapter 15 "Criminal Acts Against Commerce" of the Penal Code of Republic of Serbia there is a whole scope of criminal acts and sanctions prescribed for various criminal actions, such as "Undue performing of business activities" Article 136, "Harm of creditors" Article 138, "Abuse of power in commerce" Article 139 etc. All of these criminal acts have to be done with intention (e.g. negligence is not possible). Also, those acts have to be carried out in order to obtain some benefit for such person or someone else. Otherwise, it could be only the criminal act of "Assistance to offender (committer of the crime)" Article 204 of the Penal Code. In this case intention is also required.

Concerning commercial offences and offences, we have to state that those violations are prescribed by every separate law. If someone commits any action complying with those

offences, he/she will be responsible for it. In other words, if failing to report conflicts of interests also means committing of any offence prescribed by law, sanctions are prescribed for every separate case. If a conflict of interests was performed by an employee or appointed person, he/she may be dismissed/ discharged as well, according to Serbian legislation.

8.3. A minority investor may challenge activities made in breach of the law. First, they can report a crime, commercial offence and offence. Second, they can intervene in the administrative procedure (if such procedure is pending), but they have to prove their interests. Third, they can start litigation if they have suffered any damage that they can duly prove in front of the Court (as well as to prove their legal interest). On the other hand, authorities are almost always obliged to intervene in situations when there is a breach of law, except in litigation, where the will of an injured subject is the only relevant matter for starting the procedure (for compensation of tort, for instance).

The Management of the company (Board of Directors and General Manager) have to give all the information to minority shareholders, which were given to majority shareholders. But, the Management does not have to give to creditors all the information that was given to shareholders, which is clear enough. Under Heading II, chapter 21.3, Article 251 "Protection of Minority Shareholders" it is stated that shareholders who own at least a tenth of the initial capital or such a smaller portion as is provided by the articles of association (further: minor shareholders), may request the Board of Directors to summon the General Meeting, stating the reasons for summoning it and the matters the General Meeting should decide on. Should the Board of Directors fail to convene the General Meeting pursuant to a request made in writing by the minor shareholders, within 15 days from the request filing date, the minor shareholders may summon the General Meeting.

Should the General Meeting not be held within 15 days from the dates of the requests, the Supervisory Board may summon the General Meeting within a further 15 days. Should the General Meeting not be held for the reasons mentioned above the joint-stock company shall buy up the shares of the minor shareholders, in conformity with Corporate Law.

8.4. Conflicts of interest have to be reported in any case, irrespective if they are detrimental to the company.

8.5. Law on Securities Market: Article 247 of the Law prescribes that the broker-dealer company or authorized bank will pay a fine between CSD 60,000-600,000 for a commercial offence if it puts its interests in front of the clients interests, or if it does not present to the client possible conflicts of client interests and company interests, or other clients' interests. The procedure is the same as for all other commercial offences, i.e. as explained above.

Practices

1. General comments

1.1. Further to our investigations it results that in the region the practices as regards the reporting of conflicts of interest are better implemented than the ones regarding reporting of related party transactions.

1.2. However, in none of the four countries exists trust that the existing practices ensure a total transparency and disclosure of conflicts of interest. This general impression is accompanied by the lack of trust in the capacity of the competent authorities to impose adequate practices.

1.3. Currently the sanctions imposed in practice are rather civil or administrative sanctions. In very rare cases criminal sanctions were applied. There are also rare cases when the minority shareholders challenged the non-observance of a reporting obligation.

2. Romanian practices

2.1. In the practice of the Romanian National Commission it seems that breaches of legal regime of conflicts of interests were sanctioned administratively, without further criminal sanctions being applied by the relevant authority.

2.2. As regards the practice of the closed companies, generally the provisions of the Company law on conflicts of interest are observed.

3. Bulgarian practices

3.1. The law practitioners to whom we have addressed a question as regards the appropriateness of the existing regulatory framework governing the reporting of conflicts of interest did not express any opinion on it.

3.2. As regards the disposing of sanctions for non-observance of the requirements regarding conflicts of interest, it seems that in Bulgaria there are cases when sanctions were disposed (it seems that generally they are civil sanctions). It seems also that currently there is a practice of the Supreme Court in this respect.

4. Croatian practices

4.1. We have not obtained relevant information on this.

5. Serbian practices

5.1. Regulations and monitoring of conflicts of interest situations is not well developed in Serbia. Employment / shareholder relationships have been closely linked and in some cases are indistinguishable. This is a legacy of a socialist orientation. There was little will, either politically or from businesses, to give publicity to such conflict of interest situations and to promote them through the legal system.

5.2. The existing regulatory framework is inadequate. Concerned persons may rely more on criminal legislation, and penal provision prescribed in Corporate Law concerning institutes of unfair competition, and "the disguise of the legal person" lawsuits in cases where conflicts of interests may be started in front of the competent courts against legal or natural persons, but the outcome is unpredictable and proceedings are likely to be protracted.

5.3. A new Corporate Law is expected to be adopted in 2004. Hopefully this will create the framework for improved regulation of conflicts of interests.

5.4. The Law on Securities Market is in force only for a few months. Consequently there has been little opportunity to assess the practical implementation of conflicts of interest provisions.

5.5. A new Law on Preventing Conflicts of Interests in Performing Public Activities was adopted very recently, and should enter into force soon. It will be crucial to monitor the application of this law.

5.6. There is very little precedent for civil / professional sanctions rather than criminal sanctions.