

# Regional Seminar on Corporate Governance for Banks in Asia

## Controlling Related Party Transactions

Speaker: Edward K. F. Chow  
Immediate Past President of HKICPA

20 June 2006, Hong Kong



FINANCIAL STABILITY INSTITUTE

BANK FOR INTERNATIONAL SETTLEMENTS



# **Controlling Related Party Transactions**

**An Analysis by reference to:**

- **Accounting Standards**
- **Listing Rules**

# **Listing Rules**

## **Chapter 14 A of the Rules Governing the Listing of Securities of The Stock Exchange of Hong Kong**

## **Accounting Standards:**

- **IAS 24 (International Accounting Standards / IFRS)**
- **HKAS 24 (Hong Kong Accounting Standards / HKFRS)**

*\* Both effective on accounting periods commencing or after 1 January 2005*

# **Related Party Transaction: IAS / IFRS definition**

**A transfer of resources, services or obligations between related parties, regardless of whether a PRICE is charged.**

# **IAS 24:**

## **Related Party Relationships:**

**A normal feature of commerce and  
business**

**(between people and / or entities)**

# Problems / Questions:

- **Is it reasonable?**
- **Is it unreasonable?**
- **Is it legal?**
- **Is there a level playing field?**
- **Is there a conflict of interest?**
- **Is any body being disadvantageded?**
- **Is anything being stolen?**

# **RELATED PARTY is one who:**

**Directly, or indirectly through one or more intermediaries**

- **Controls / jointly control**
- **Has interest**
- **Has significant influence**



## **Entity's:**

- **Parent, subsidiary, associate**
- **Joint venture partner**
- **Director, key management personnel**
- **Special purpose vehicles**

## **Individual's:**

- **Domestic partner and children**
- **Children of the individual's domestic partner**
- **Dependents of the individual or the individual's domestic partner**

**Senior personnel and compensation**

## **Problem Areas:**

- **Substance of relationship, not merely legal form**
- **Nominees and concert parties**
- **Substance override for **CONNECTED PERSONS****

# **Controls & Safeguards:**

- **Governance structure**
- **Management structure**
- **Regulatory structure**
- **Independent auditors**
- **Independent directors**
- **Independent advisors**
- **Independent shareholder vote**
- **Whistle blowers**

## **Control System:**

- **To log and track connected transactions**
- **To review and audit**
- **To report – internal & external**
- **To disclose — thresholds and rules**
- **To approve (or reject) — thresholds and rules**

## **Disclosure:**

- **Nature of transaction**
- **How connected**
- **Amount**
- **Outstanding balance**
- **Guarantees**
- **Indemnities**
- **Options**
- **Financial assistance**
- **Provisions and expense realized**
- **Aggregation of transactions**

# **Internal Controls & Safeguards:**

- **Corporate Code of Conduct**
- **Independent Advice (legal & financial)**
- **Independent Directors**
- **Independent Shareholder Vote**

# **External Controls & Safeguards:**

- **Regulators — banking, securities**
- **Competing business**
- **Suitability for listing**
- **Directors and officers — fit and proper test**



## **Listing Rule Tests:**

- **Normal commercial terms**
- **Ordinary / usual course of business**
- **In the interest of issuer and shareholders as a whole**
- **Opinion of Independent Advisor and Independent Directors**

# **Bank Specific Problem**

## **Triangular Relationship between:**

- **Offering Party**
- **Accepting Party**
- **Financing related parties**

# **Ultimate Sanctions**

## **Criminal Sanctions:**

- **Under the Securities and Futures Ordinance**
- **Under THEFT and other laws**

**End of Presentation**

**Thank You !**