

Related Party transactions

Companies Act & LODR

Companies Act, 2013

- Section 2(76) defines Related Party
- Director or his Relative
- KMP or his relative
- A Firm, in which a Director, a Manager or his Relative is a Partner
- A Private Company in which a Director or a Manager is a member or Director
- A public Co., in which Director or Manager is a Director and holds along with his relatives, more than 2% of the paid up Share Capital
- Any body corporate whose Board of Directors, Managing Director or Manager is accustomed to act in accordance with the advice, directions or instructions of a director or manager
- Any person on whose advice, directions or instructions a Director or Manager is accustomed to act (Professional Advice excluded)

Related party

- Holding, subsidiary or associate Company of such Company (**Not Applicable to Private Company**)
- A Subsidiary of a holding company to which it is also a subsidiary (co subsidiaries) (**Not Applicable to Private Company**)
- An Investment Company or the venture of the Company (Associate, 20% voting power)
- Other as may be prescribed.

Relative [2(77)]

- Relative Means:
- They are the members of HUF
- Husband and wife
- Father, Mother, Son, Brother and Sister (including step)
- Son's wife, Daughter and Daughter's Husband

Accustomed to Act

- Sahara India Real Estate Corporation Limited
- SEBI recognized Subrata Roy Sahara, though not a Director because of his major shareholding of 70% treated him as a Related Party.
- KK Birla V/s RL Lodha
- Defined Accustomed to act

Section 184 – Disclosure of Interest by Directors

- To disclose First time and at the First Board Meeting of Financial Year.
- Disclose his concern or interest in any Body Corporate, Firms and association of Individuals.
- Body Corporate – Along with other Directors controlling 2% shareholding or promoter or manager or CEO
- With a firm or other entity – partner, owner or member

Section 184

- Interested Director not to participate in such meeting (Exempted for Private Co., & for section 8 Co. less than 1 Lakh contracts not applicable)
- In case 184(2) violated without disclosure of Director the contract is voidable at the option of the Co.,
- Violation – imprisonment for a term which may extend to one year or with fine which may extend to one lakh rupees or with both.

Section 188 – Related Party Transaction

- Any contract or arrangement except with the consent of the Board:
- Sale, purchase or supply – Goods or Materials
- Selling, disposing & buying of property of any kind
- Leasing of property of any kind
- Availing or rendering any services
- Appointment of any agent for the above
- Appointment of office or place of profit in the Company, subsidiary or associate Co.,
- Underwriting for securities/ derivatives

188 – Shareholders Approval

- Prior, Ordinary Resolution in case of the following (First proviso to sub-section 1):
- Goods/Materials= 10% of T.O or 100 Crores whichever is lower
- Property sell, buy or dispose = 10% of NW or 100 Crores
- Leasing of property = 10% of NW or 100 Crores
- Services = 10% of T.O or 50 Crores
- Office of place of profit Rs. 2.5 lakhs PM
- Underwriting 1% of TO
- In case of WOS, holding Company resolution is sufficient.
- Ratification is permitted within Three Months (sub section 3)

Certain terms not defined..

- Ordinary course of business:

In BNP Paribas v. United breweries Karnataka High court held

“honest dispositions made in the ordinary course business are allowed. While passing orders, the court considers whether transaction in question is in furtherance of cos business and/or in the interest of the company....”

- Ordinary course of business:

In Dilip Kumar Swain v.E.E.cuttack municipal corpn the orissa High court held:

“On the course of professional avocation or current routine of business”

Arms length transaction

- Black's law dictionary 8th edition:

“of or relating to dealing between two parties who are not related or not on close terms and who are presumed to have roughly equal bargaining power”

- Ramanatha Iyers Lexicon:

“transaction negotiated and entered into unrelated parties, each of whom acts in his or her own best interest using fair market values”

arrangement

- Bank of India vs. Ahemadabad Manufacturing & calico printing co.,(Bombay HC)

“any agreement or understanding between parties concerned”

Voting by related party shareholders

- Listed co. no related party can vote in favour
- Cos act only related party to the transaction cannot vote.
- Proxy advisory firms
- Tata sponge iron ltd. Shareholders defeated two resolutions
- Tata motors . Managerial remuneration defeated.
- hdfc

Section 188....

- Audit Committee approval required.
- Violations:
- For listed Co. one year or with fine (25,000 to 5 lakh)
- Other Co., 25000 to 5 lakhs.
- Disqualification under section 164(1)(g)

SEBI(LODR) Regulations

- **Related party** in addition to 2(76) of Co's Act, any person belonging to the promoters group holding 20% or more of the Shareholding.
- **Related Party Transaction** – means a transfer of resources, services or obligations between a listed entity and a related party, regardless of whether a price is charged and a “transaction” with a related party shall be construed to include a single transaction or a group of transaction in a contract.
- **Relative** means 2(77) of Co's Act

LODR – Regulation 23

- Board to formulate policy on materiality and shall be reviewed once in three years.
- Explanation: Material transaction means in excess of 10% of the consolidated turnover of all the transactions.(considering passt transactions)
- 1A – effective 01.07.2019, payments to wards Brand or Royalty 2% of annual consolidated TO shall be material.

LODR Regulations

- All related party transactions require prior approval of Audit Committee.
- Omnibus approval may be granted by the audit committee provided
- It satisfy itself for the need and in the interest of the listed entity.
- Proper names, nature, period and amount of Transactions are disclosed.
- Price or pricing methodology is disclosed.
- Such other conditions the audit committee may deem fit
- In case of unforeseen circumstances omnibus approval may be given subject to value of transaction not exceeding 1 crore.
- Audit committee to review on a quarterly basis the omnibus transactions.
- Omnibus approval valid for 1 year

LODR – Shareholders Approval

- All material related party transaction requires shareholders approval.
- No related party shall vote to approve such resolution (exception not applicable in case of resolution plan approved by Adjudication Authority, subject to disclosure to SE within 1 day).

Exemptions

- Transaction between two govt. Co's
- Between Holding and WOS

Ind AS 24..

- The listed entity shall make disclosures in compliance with the Accounting Standard on “Related Party Disclosures”
- The disclosure requirements shall be as follows:
- Holding Company/subsidiary Co – Loans & advances in the nature of loans to subsidiaries/associates/firms/companies in which directors are interested by name and amount
- Investment by the loanee in the shares of parent company and subsidiary company, when the company has made a loan or advance in the nature of loan.

AS – 24 RPT Disclosures

- Relationships between a parent and its subsidiaries shall be disclosed even if there is no transaction.
- An entity shall disclose key management personnel compensation in total.
- outstanding balances, including commitments to be disclosed
- Aggregation of similar transaction can be done.

Ind AS 24 related party disclosures

- A person or entity related to the reporting entity:
 - (a) a person has control or joint control ;
has significant influence over reporting entity;
kmp of the entity or its parent.
(person includes that persons family)

Ind AS 24...

- (b) parent subsidiary or fellow subsidiary;
one is associate or jv of the other

both entities are joint ventures of the
same 3rd party

one entity is jv and other associate of 3rd
entity