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Pricing of RPTs under Cos. Act & Listing Regulations

Pricing of Related Party Transactions under Companies Act, 2013:

Pursuant to the provisions of Section 188 of Companies Act, 2013 ('CA, 2013'), a transaction will qualify as 'related party transactions' ('RPT') if a company [private company or public company] enters into any prescribed transaction [7 transaction laid down in Sec. 188 of CA, 2013] with a prescribed related party [in accordance with Sec. 2(76) of CA, 2013]. For crystallizing the mode of approval, it is necessary to determine whether such transaction is in the ordinary course of business and at arm's length basis. Pursuant to the third proviso to sub-section (1) of Section 188 of CA, 2013, if the transaction is not entered in the ordinary course of business or / and at arm's length basis, then the company is required to obtain the approval of the board of directors and shareholders, in addition to Audit Committee (as may be applicable). CA, 2013 does not provide any guidance for a transaction to be in the 'ordinary course of business', however, Explanation (b) to Section 188(1) of CA, 2013 defines the expression 'arm's length transaction' means a transaction between two related parties that is conducted as if they were unrelated, so that there is no conflict of interest.

Third proviso to sub-section (1) of Section 188 of the CA, 2013, lays emphasis on the transaction being at arm's length basis, i.e. pricing, terms and conditions etc, as there is no reference to 'arm's length pricing' but there is reference to 'arm's length transaction' and the same has been explained as a transaction between two related parties that is conducted as if they were unrelated, so that there is no conflict of interest. The board of directors or the audit committee of the company can take necessary guidance from the provisions of Income Tax Act, i.e. Domestic Transfer Pricing and International Transfer Pricing provisions.

Pricing of RPTS under SEBI (Listing Obligations and Disclosure Requirements), Regulations, 2015:

After elaborate deliberation and consultation process, SEBI notified¹ the Listing Obligations and Disclosure Requirements, Regulations, 2015 ('Listing Regulations') on September 2, 2015 and the same is ought to be implemented in 90-days i.e. December 1, 2015. The Listing Regulations consolidates and streamlines the provisions of existing listing agreements for different segments of the capital market. The Listing Regulations have thus been structured to provide ease of reference by consolidating into one single document across various types of securities listed on the Stock exchanges.

'Related Party Transaction' are defined in sub-regulation (zc) of Regulation 2 of the Listing Regulations as *it means 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 transactions in a contract, however, the definition of 'related party transaction' excludes, the units issued by mutual funds which are listed on a recognised stock exchange(s).*

¹vide the Press Release No. 226 / 2015 dated September 3, 2015

Therefore, the pricing of RPTs by a listed entity is irrelevant under Listing Regulations, as the definition of RPT under Listing Regulations provides for a term ‘regardless of whether a price is charged’. The price charged by the listed entity for transfer of services, resources or obligation to a related party need not be at arms’ length, but can be at fair value, face value, discounted value or free of charge.

Balancing the ‘pricing’ factor:

Pursuant to the sub-regulation (4) of Regulation 23 of Listing Regulations, all the ‘material’ related party transactions shall require approval of the shareholders through resolution. The threshold for ‘material’ related party transaction has been defined in an explanation to sub-regulation (1) of Regulation 23 as: *A transaction with a related party shall be considered ‘material’ if the transaction(s) to be entered into individually or taken together with previous transactions during a financial year, exceeds 10% of the annual consolidated turnover of the listed entity as per the last audited financial statements of the listed entity.*

The listed company is required to balance the compliance of the CA, 2013 and Listing Regulations, not just for the RPT compliance, but also for other provisions like: Independent Directors, Audit Committee, disclosures in Boards’ Report, etc. So, if a listed entity enters into a transaction with related party, not on arm’s length price but at discounted value, there would be thorough compliance of Listing Regulations but the company would be required to obtain the approval of the board of directors and shareholders, pursuant to the third proviso to Section 188(1) of the CA, 2013, in spite of not breaching the threshold prescribed in Listing Regulations.

Further, the listed company is required to pass an ordinary resolution for obtaining the approval of the shareholders of the company for all ‘material’ related party transactions, even if such are at arms’ length basis (contemplated under third proviso to Section 188(1) of CA, 2013 read with sub-regulation (4) of Regulation 23 of Listing Regulations).

Therefore, if the listed entity enters into such transaction on arms’ length basis and the ‘material’ threshold is not breached, the entity complies with both (CA 2013 and Listing Regulations), and it will not be required to obtain the approval of the board of directors and shareholders, but the approval of Audit Committee will be required as provided in the Listing Regulations.

Decode the Code: drop by drop

PREFIXING CS TO MEMBERS NAME



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The Council of the Institute in its 173rd meeting held on June 23-24, 2007 has decided that a member of the Institute may prefix CS to his name in order to distinguish himself from other professionals and to create brand image of the CS profession. It means that only the members of the ICSI, both practicing and non-practicing are allowed to use the prefix CS.



The global practice of prefixing designation, in case the designation is of two words such as Company Secretary, Chartered Accountant, etc. is to use the acronym of the same. Therefore the correct way of prefixing Company Secretary designation to your name is, CS and not C.S., CS., ACS or FCS.

Trivia: A doctorate who is also an active member of the ICSI and not in employment or practicing company secretary may prefix both CS & Dr. designation to his name.