



*Verdict Vista*



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### **SAT: Listed Entities should test the Materiality Threshold by aggregating the value of all RTPs with a Related Party, upholds SEBI order**

Related Party Transactions (RPTs) are a complex set of provisions under the Companies Act, SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, Income Tax provisions, Goods and Service Tax Act, etc. All these laws collectively provide for regulating the approval process by the audit committee or board of directors, regulating the price of the goods or service, materiality threshold for obtaining approval of shareholders, maintaining arm's length pricing or terms of contract, etc. The RPTs are heavily regulated in India, because there is a suspicion that the requisite approvals may not be obtained, or RPT policy may not be complied with, the actual transactions or transactions may not be on arm's length basis, or the funds may be siphoned off, etc. This article is an analysis of the recent order of the SAT (in the matter of Linde India Ltd. vs SEBI, Appeal No. 527 of 2024, Order dated December 5, 2025).

#### **Facts of the case:**

1. Linde India Ltd. (LIL) is listed on the NSE and BSE since June 1999. The primary business of LIL is the manufacturing and sales of gases and related products.
2. Later, in 2018, through a scheme of global merger between Linde AG (holding company, German company) and Praxair Inc. (an American company), Linde Plc. (NASDAQ-listed entity) was formed. Linde Plc. inherited two subsidiaries in India – (i) LIL (listed entity) with 75% beneficial ownership held by Linde Plc., therein, and (ii) Praxair India Private Limited (PIPL), 100% step-down subsidiary of Linde Plc. through Praxair Inc.,

both engaged in the production and supply of gases. The said merger/combination was approved by CCI as well;

3. In 2019, the group decided to form Linde South Asia Services Private Ltd. ('LSASPL'), a joint venture company of LIL and PIPL with 50% stakes each of both. The joint venture and shareholders' agreement (JV & SHA) and Operation and Management Services Agreement (O&M Agreement) dated March 24, 2020 was executed amongst LIL, PIPL, and LSASPL;
4. In terms of the said agreement, geographical allocation of all new business was made to LIL in respect of Eastern, Northern, and Western India, while PIPL was allocated South India, Central India, and industrial bulk business in Maharashtra. In terms of product allocation, the project engineering business was assigned exclusively to LIL, while the CO<sub>2</sub>, HYCO, and green energy businesses went to PIPL;
5. Following this, LIL sought public shareholder's approval by ordinary resolution seeking omnibus approval under section 188 of the Companies Act, in respect of all related party transactions (RPTs) from January 1, 2021 to December 31, 2023 likely to be entered with PIPL and LSASPL, which were, in aggregate, likely to exceed the materiality threshold prescribed under Regulation 23(1) of SEBI (LODR) Regulations, 2015. This was turned down by the public shareholders. Therefore, the company based on certain legal opinions obtained by it, decided not to aggregate all transactions with a Related Party, as in its view, aggregation was to be made only of such transactions, which pertain to a single contract in terms of its interpretation of definition of RPT, as per Section 2(1)(zc) of the SEBI LODR Regulations.
6. Following this, the SEBI received investor complaints alleging that the business allocation was detrimental to LIL's public shareholders. On January 6, 2022, NSE forwarded complaints alleging that LIL, instead of merging with PIPL, had established a JV structure and executed RPTs with PIPL without shareholder's approval, in violation of SEBI LODR Regulations.
7. SEBI appointed the Investigating Authority and pending investigation and passed an interim ex-parte order with certain directions. The Appellant challenged the said order before SAT, and the said order was set aside with the directions to SEBI to grant inspection of documents to the Appellant and pass the order within 30 days. After inspection of documents, reply was filed by appellant, personal hearing was given and additional submissions were file by Appellant. Following this, SEBI passed the order (dated July 24, 2024), by which directions referred to in paragraph No. 1 were issued which was the subject-matter of the present Appeal.

### Issue before SAT:

1. Whether transactions pertaining to a single contract or aggregate of transaction pertaining to all contracts a financial year are to be considered while testing the materiality threshold in under Regulation 23(1) of the LODR Regulations?
2. Whether the business allocation between LIL & PIPL in terms of JV&SHA dated March 24, 2020, amounts to transfer of resources, services, or obligations to be treated as RPT?

### Observations of SAT:

The observations of SAT are summarised as follows:

1. SAT perused the definition of 'related party transaction' under Regulation 2(1)(zc) of the SEBI (LODR) Regulations, 2015, which means a transaction involving a transfer of resources, services or obligations between (certain entities, including listed entity and its 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.
2. SAT observed that Regulation 23(1) of SEBI (LODR) Regulations explicitly uses the term 'Related party transactions' (emphasis on plural) at several places, particularly while putting obligation on the listed entity in formulating a policy on materiality of related party transactions and on the manner of dealing with the related party transactions. SAT stated that the clause 2(1)(zc) of SEBI LODR Regulations, while defining the term 'RPT' in a generic manner, clarifies that 'a transaction with a Related Party' means to include a 'single or a group of transactions in a contract'. SAT stated that *"This limb of definition only clarifies that where in respect of a contract between two related parties, there have been group of transactions, each one of them shall be treated as RPTs and the listed entity shall be governed in respect of all of them by the same procedural requirement as for a single RPT transaction. The ostensible purpose of such a clarification is to ensure that each transaction in a contract, needs to be treated and dealt with in the same manner provided for a 'related party transaction'. This is intended for investor protection."*
3. While interpreting Regulation 23 of the SEBI (LODR) Regulations, SAT observed that *"The machinery provisions of Regulation 23 provide for the manner in which such RPTs are to be treated by a listed entity. It is noteworthy that the Regulation 23(1) consistently uses the plural term 'related party transactions' for addressing RPTs for aggregation, which implies that all transactions qua 'a related party' are to be considered for testing the materiality' (and not qua a single contract). It implies that all transaction(s) undertaken during a financial year with a specific related party, are to be aggregated in terms of Regulation 23(1)."*

4. In this case, SAT applied the Literal Rule of Interpretation and stated that *“the literal interpretation of this term, there is no need to rely upon purposive interpretation of this term”*. SAT also referred to the book of Justice G.P Singh’s Principles of Statutory Interpretation;
5. With respect to the applicability of RPT provisions, SAT stated that though the provisions of Section 188 of the Companies Act are applicable to both listed and unlisted companies, keeping in view the specialised nature of the SEBI (LODR) Regulations applicable for a listed entity considering implications for public shareholders, higher standard of disclosure is made necessary;
6. Based on Regulation 23 of the SEBI (LODR) Regulations, SAT stated that the compliance requirements with respect to ‘related party transactions’ as provided in Regulation 23(1) of the LODR Regulations, 2015 clearly require that the materiality threshold is to be tested in respect of ‘all transactions entered individually and taken together, with previous transactions during a financial year’. SAT stated that *“It does not provide for a situation that may restrict such testing only in respect of transactions pertaining to a single contract only.”*
7. On the point w.r.t. inclusion or exclusion of the related party transactions in the definition of SEBI (LODR) Regulations (i.e. Reg. 2(1)(zc)), SAT observed as follows *“It is noteworthy that the LODR Regulations specifically excludes certain transactions with RPs for materiality threshold testing. Certain RPTs are defined as not RPTs under Regulation 2(1)(zc), and are to be excluded. Further, Regulation 23(1A) defines separate materiality threshold in respect of other category of transactions being in the nature of payment for Brand usage or royalty, where the threshold is kept low at 5% of the annual consolidated turnover.... Therefore, these transactions are the only transactions to be excluded from the prescribed threshold under Proviso to Regulation 23(1). There is no provision for excluding transactions of one contract for calculating materiality of other contract.”*
8. Based on the above points and observations, SAT agreed with the observations of SEBI Wholetime Member (WTM) that LIL should test materiality threshold by aggregating value of all transactions with the related party whether for transfer of resources, services or obligations during the financial year and if the same exceeds materiality threshold, LIL will have to seek the shareholders’ approval in terms of Regulation 23 of the LODR Regulations;
9. Another issue before SAT was applicability of RPT provisions for the business allocation between LIL & PIPL in terms of JV&SHA. SAT noted that through the business allocation agreement, certain geographies and products, in which LIL was operating had foregone in favour of PIPL, which was the dominant player in those territories. It was noted that the existing business of LIL at South, Central and West-1 regions have been

assigned to PIPL without any consideration paid to LIL. At the same time, LIL has gained the entire business of East, North and West-2 geographies at the cost of PIPL in those regions. On this arrangement, SAT observed that *“It is evident that through the said Business Allocation agreement, there was a transfer of an entire business undertaking from Linde to Praxair and vis-a-vis in different geographies and product lines. Thus, we hold that it amounts to a clear cut transfer of ‘profit making apparatus’ from one entity to another and vice-versa along with all assets and liabilities including intangibles (goodwill, brands), order book and future cash flow.”*

#### **Analysis & impact of the SAT order in interpreting RPT provisions:**

The observations of SAT in this case are quite important and relevant from the perspective of obtaining the approval of the shareholders of listed entity. Seeking approval of the relevant stakeholder (i.e. Audit Committee or shareholders) at an appropriate point of time is one of the integral parts of Related Party Transactions. Apart of approval, requisite disclosures, maintenance of RPT Policy, maintenance of statutory records are also important aspects of RPTs. This order of SAT in Linde India Limited provides clarity (or reconfirms the interpretation) that listed entities should test materiality threshold by aggregating value of all transactions with the related party whether for transfer of resources, services or obligations during the financial year and if the same exceeds materiality threshold, the listed entity shall seek shareholders’ approval in terms of Regulation 23 of the LODR Regulations. Based on the facts of the case, the observations of SAT clears air over the question whether listed entities are required to consider single contract or multiple contracts with a related party for different transactions for determining the materiality threshold. Based on the observations of SAT, it can be concluded that materiality threshold shall be considered by aggregating value of all transactions with the related party, irrespective of the number of contract(s) entered into by the listed entity with said related party. In the same order, SAT has also observed that through the JV&SHA, business is foregone and business is gained for both the related parties i.e. there was a transfer of an entire business undertaking from listed entity to its related party and vis-a-vis in different geographies and product lines. SAT held that this amounts to a transfer of ‘profit making apparatus’ from one entity to another and vice-versa along with all assets and liabilities including intangibles (goodwill, brands), order book and future cash flow. Ultimately, SAT concluded that business allocation is treated as transaction, tantamounting to a ‘related party transactions’ under Regulation 2(1)(zc) of SEBI LODR Regulations. These two observations by SAT are quite important and relevant for listed entities in structuring transactions with related party transactions, drafting of joint venture agreement and shareholders agreement/business transfer agreements after taking into consideration of RPT.