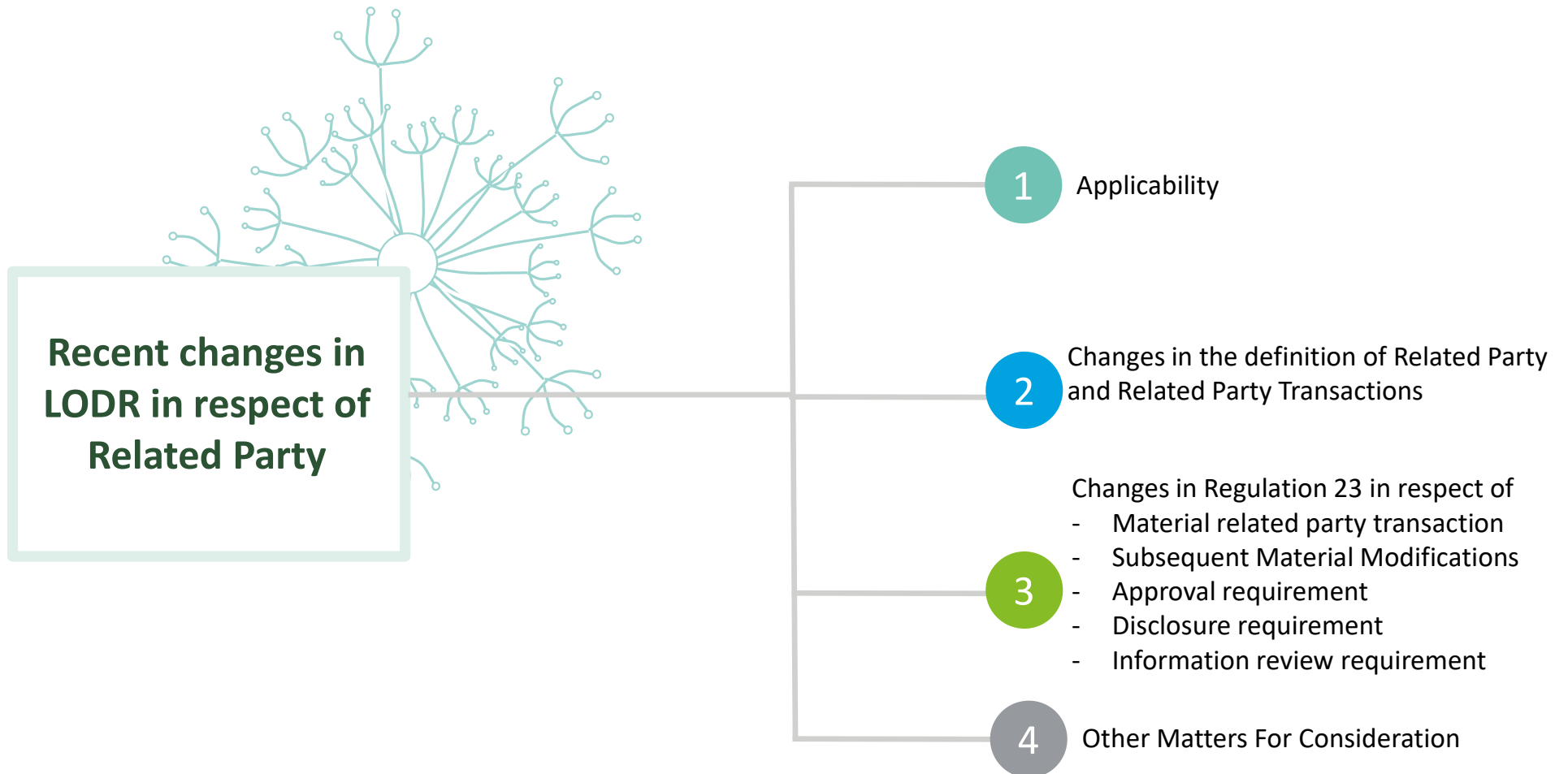




# Recent changes in LODR in respect of Related Party

December 30, 2021

# Contents



## Applicability of the changes in Listing Obligations and Disclosure Requirements (LODR) in respect of Related party

- On November 9, 2021, SEBI has amended the SEBI (LODR) Regulation, 2015 via SEBI (LODR) (Sixth Amendment) Regulation, 2021.
- Amendments will come into force from April 1, 2022 unless otherwise stated.
- The amendments will also apply to High Value Debt Listed entity (HVDL).
- Major Public Shareholder (Holding 20% w.e.f. April 2022 & 10% w.e.f. April 2023) will be now treated as Related Party.
- Now all the RPTs on Standalone basis would be required to be disclosed.

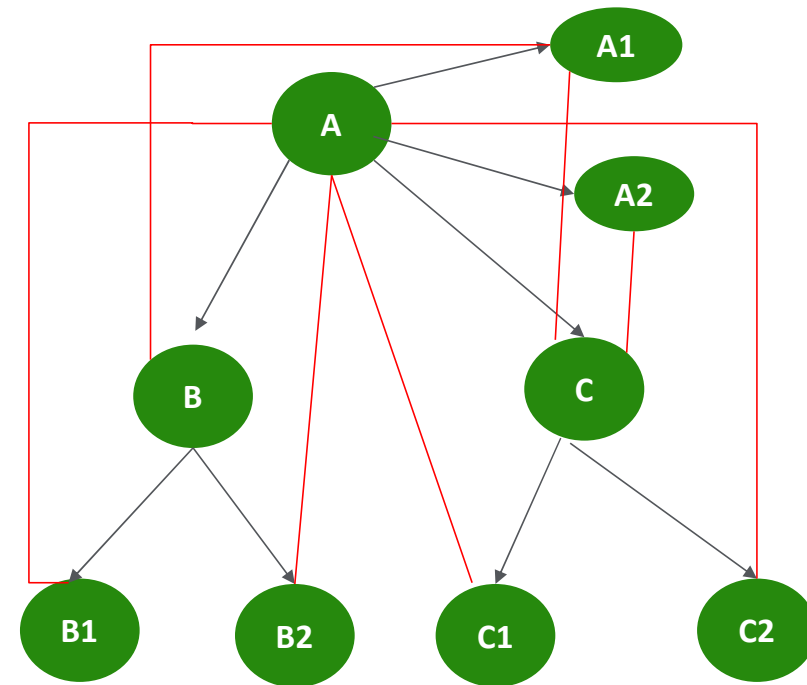
## Related party and Related Party Transactions – As per erstwhile provisions

### Related Party

- Related party means:
  - As defined under 2(76) of Co Act, 2013;
  - Applicable Accounting Standard;
  - Any person/entity
    - Belonging to promoter/promoter group **and**
    - Holding 20% or more of shareholding

### Related Party Transactions

- Related party transactions 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



A is a listed entity; B and C are its subsidiaries. A1/A2, B1/B2 and C1/C2 are related parties of A, B and C respectively

- ← RPT
- ← Not a RPT

## Change in the definition of Related Party

Regulation No	Existing provision	New Provision	Change
First Proviso to Regulation 2(zb)	<p><u>Related party</u>            Provided that any person or entity belonging to the promoter or promoter group of the listed entity <b>and</b> holding 20% or more of shareholding in the listed entity shall be deemed to be a related party</p>	<p><u>Related party</u>            “Provided that:            (a) any person or entity forming a part of the promoter or promoter group of the listed entity; or              (b) any person or any entity, holding equity shares:            (i) of twenty per cent or more; or            (ii) of ten per cent or more, with effect from April 1, 2023;            in the listed entity either directly or on a beneficial interest basis as provided under section 89 of the Companies Act, 2013, <b>at any time</b>, during the immediate preceding financial year; shall be deemed to be a related party:</p>	<p><b>All Promoters and persons belonging to promoter group irrespective of their shareholding</b> will now be deemed to be related party.</p> <p><b>Any person or entity holding, directly or on a beneficial interest basis under Section 89 of CA, 2013, 20% or more of the equity shareholding in the listed entity</b> will be regarded as a related party</p>

### An Analysis

- No change in the definition of promoter or promoter group, however promoter or any person or entity forming part of the promoter group would be construed as a related party even if there is no shareholding by such party
- Concept of ‘beneficial interest’ has been introduced for the first time when determining whether a party is related – the Act places onus on the person or entity who/which holds the beneficial interest to communicate to the listed entity of such interest
- The holding of 20% or more can be ‘at any time’ during the immediately preceding financial year. This would mean that even if a person/entity does not have any holding during the year, but held in the previous year, would be scoped in as related party
- In case of entities that are in the process of being listed, it appears that the provisions of the LODR would not apply
- No transition provisions for a first-time listed entity.

## Change in the definition of Related Party Transaction

Regulation No	Existing provision	New Provision	Change
First Proviso to Regulation 2(zc)	<p><u>Related party transaction (RPT)</u> RPT means a transfer of resources, services or obligations <b>between a listed entity and a related party</b>, 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:</p>	<p><u>Related party transaction (RPT)</u> RPT means a transaction involving a transfer of resources, services or obligations between:</p> <p>(i) a listed entity <b>or any of its subsidiaries on one hand and a related party of the listed entity or any of its subsidiaries on the other hand</b>; or</p> <p>(ii) a listed entity or any of its subsidiaries on one hand, and any other person or entity on the other hand, <b>the purpose and effect of which is to benefit a related party of the listed entity or any of its subsidiaries, with effect from April 1, 2023</b>; 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.</p> <p>There are certain exemptions mentioned as below:</p>	<p>The definition widens the ambit of transactions and as per the amendments; RPT will now be on the basis of combination structure. The definition now includes Related Parties of the Subsidiary as the Related Party of the Listed entity and vice versa.</p> <p>The New definition excludes certain specific corporate action such as Issue of Securities, payment of dividend from the ambit of RPT.</p>

### Exemptions from being considered as a related party transaction

- a) Issue of specified securities on a preferential basis, subject to SEBI-ICDR compliances
- b) The following corporate actions by the listed entity which are uniformly applicable/ offered to all shareholders in proportion to their shareholding:
  - (i) Payment of dividend;
  - (ii) Subdivision or consolidation of securities;
  - (iii) Issuance of securities by way of a rights issue or a bonus issue; and
  - (iv) Buyback of securities
- c) Acceptance of fixed deposits by banks / NBFCs at the terms applicable/offered to all shareholders/public, subject to certain conditions.

### An Analysis:

- Related parties of associates or joint ventures are not scoped in, since the Regulations only address subsidiary as defined under Regulation 2(1)(zm) of the SEBI LODR (i.e., as defined under section 2(87) of the Companies Act, 2013).

## Related party transactions (RPT) – an analysis (Contd.)



Contracting party	Counter party	Remarks
I. Listed entity	Related party to the listed entity	No change
II. Listed entity	Related party of any of the subsidiaries or of the listed entity	New
III. Subsidiary entity	Related party to the listed entity	New
IV. Subsidiary entity	Related party to the subsidiary entity	New
V. Subsidiary entity	Another subsidiary entity of the listed entity	New – covered in (iii) above
VI. Subsidiary entity	Related party of another subsidiary entity	New

*With effect from April 1, 2023, transactions where the purpose and effect is to benefit a related party of the listed entity or any of its subsidiaries are scoped in as related party transactions*

## Change in Materiality – In respect of related party transaction

Regulation No	Existing provision	New Provision	Change
Explanation to Regulation 23(1)	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, <b>exceeds 10% of the annual consolidated turnover of the listed entity</b> as per the last audited financial statements of the listed entity.	“Provided that 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, <b>exceeds Rs 1000 crores or 10% of the annual consolidated turnover of the listed entity</b> as per the last audited financial statements of the listed entity, <b>whichever is lower.</b> ”	Earlier the limit was based on single criteria. Now quantitative limit of Rs. 1000 Crores has also been added.



## Subsequent material modification

Reg No	Existing provision	New Provision	Change
23(2)	All related party transactions shall require prior approval of the audit committee.	All related party transactions <b>and subsequent material modifications</b> shall require prior approval of the audit committee <b>of the listed entity</b> :	Earlier, all related party transactions required prior approval of listed entity. With the amendment, all related party transactions with subsequent modifications thereof require prior approval of audit committee.
23(2) Proviso 2	New Proviso	<p>“Provided further that:</p> <p>(a) the <b>audit committee of a listed entity shall define “material modifications”</b> and disclose it as part of the policy on materiality of related party transactions and on dealing with related party transactions;</p> <p>(b) a related party transaction to which the <b>subsidiary of a listed entity is a party but the listed entity is not a party</b>, shall require prior approval of the audit committee of the listed entity if the value of such transaction whether entered into individually or taken together with previous transactions during a financial year <b>exceeds 10% of the annual consolidated turnover</b>, as per the last audited financial statements of the listed entity;</p> <p>(c) with effect from April 1, 2023, a related party transaction to which the <b>subsidiary of a listed entity is a party but the listed entity is not a party</b>, shall require prior approval of the audit committee of the listed entity if the value of such transaction whether entered into individually or taken together with previous transactions during a financial year, exceeds 10% of the <b>annual standalone turnover, as per the last audited financial statements of the subsidiary</b>;</p> <p>(d) prior approval of the audit committee of the listed entity shall not be required for a related party transaction to which <b>the listed subsidiary</b> is a party but the listed entity is not a party, if regulation 23 and sub-regulation (2) of regulation 15 of these regulations are applicable to such listed subsidiary.</p>	<p><i>New Proviso has been added.</i></p> <p><i>Existing Policy on materiality of related party transactions needs to be modified with definition of material modifications.</i></p> <p><i>Audit committee of a listed entity to define “material modifications” and disclose as part of the policy on materiality of related party transactions and on dealing with related party transactions</i></p>

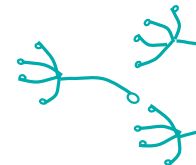
### An Analysis

*The Regulation would cover material modifications to RPT even if the initial transaction was not previously covered under the Regulations but are now covered due to the amendment to the Regulations. As a correlation, material modification to be determined whether covered or not as RPT in these Regulations at the time of such modification independent of whether the initial transaction was a RPT or not.*

## Approval Requirements

Reg No	Existing provision	New Provision	Change
23(4)	All material related party transactions shall require <b>approval</b> of the shareholders through resolution and no related party shall vote to approve such resolutions whether the entity is a related party to the particular transaction or not.	All material related party transactions (RPT) and subsequent material modifications as defined by the audit committee under sub-regulation (2) shall require <b>prior approval</b> of the shareholders through resolution and no related party shall vote to approve such resolutions whether the entity is a related party to the particular transaction or not.	Earlier only material related party transactions required approval of audit committee and shareholders, as the case may be.  With the present amendment, <b>all material RPT and material modification in approved RPT requires prior approval</b> of audit committee and approval of shareholders as the case may be.
Proviso To Regulation 23(4)	New Proviso	“Provided that prior approval of the shareholders of a listed entity shall not be required for a related party transaction to which the listed subsidiary is a party but the listed entity is not a party, if regulation 23 and sub- regulation (2) of regulation 15 of these regulations are applicable to such listed subsidiary.	<b>Exemption from obtaining approval of shareholders:</b> <i>Approval shall not be required if transaction has been undertaken between related party of a listed entity and any of its listed subsidiary, if provisions of regulation 23 and 15(2) are applicable to such listed subsidiary.</i>
23(5)(c)	New Insertion	Transactions entered into between two wholly-owned subsidiaries of the listed holding company, whose accounts are consolidated with such holding company and placed before the shareholders at the general meeting for approval.	<i>Any related party transaction entered into between two wholly-owned subsidiaries of the listed holding company need not requires approval of audit committee/ shareholders approval if accounts are consolidated with such holding company and placed before the shareholders at the general meeting for approval.</i>

## Approval requirements (Contd.)



Contracting party	Approval matrix at the listed entity level	Audit committee (AC) <sup>1</sup>	Shareholders <sup>1</sup>
Listed entity	All related party transactions	Prior approval <sup>3</sup>	
Listed entity	All material (as defined by the AC of the listed entity) related party transactions	Prior approval <sup>3</sup>	<b>Prior approval</b>
Listed entity	All subsequent material modifications (as defined by the AC of the listed entity)	<b>Prior approval</b>	<b>Prior approval</b>
Subsidiary entity <sup>2,4</sup>	RPT entered where value of transactions individually or taken together with previous transactions during a financial year exceeds 10% of the annual consolidated turnover as per the last audited financial statements of the listed entity (some exemptions are available)	<b>Prior approval</b>	<b>Prior approval (if material)</b>

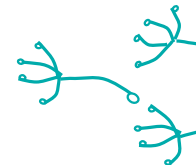
**Notes**

1. Audit committee and shareholders of the listed entity
2. Even if the listed entity is not party to the RPT
3. No change in the matrix; omnibus approvals may be sought subject to certain conditions
4. With effect from April 1, 2023, threshold is 10% of the annual standalone turnover of the subsidiary
5. Transactions between two wholly owned subsidiaries are exempt from the Regulations, if they are consolidated with such holding company and placed before the shareholders at the general meeting for approval

**Amendments highlighted in green font**

*All existing (continuing) material related party contracts or arrangements shall be placed for approval of shareholders in the first subsequent general meeting (this by corollary would extend to AC approvals)*

## Approval requirements



### An analysis

#### *Shareholder approval*

- Because a transaction is considered as a related party transaction, the parties involved in the transaction need not be related parties to the listed entity unless such parties are covered as a related party under the Regulations.
- Accordingly, parties who are not considered as related parties of the listed entity under the Regulations will not be proscribed from voting as a shareholder of the listed entity to approve the RPT irrespective of whether they are a related party to the transaction or not

#### *Both Audit Committee and Shareholder approval*

- In the case of newly incorporated subsidiaries, where there will not be a last audited financial statements, it is currently not clear as to what the basis for determining RPT for prior approval – SEBI to clarify if the basis could be consolidated financial statements.
- Criteria for 'subsequent modification' – could be based on a percentage of the initial transaction value, modification of any criteria which was the basis for the initial approval, those impacting changes in cash flows which in turn adversely impacts the cash flow position of the entity, those that could result in additional costs, should ideally be lower than the materiality as determined in accordance with the Regulations

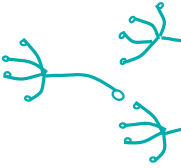
## Disclosure Requirements

Reg No	Existing provision	New Provision	Change
23(9)	The listed entity shall submit within 30 days from the date of publication of its standalone and consolidated financial results for the half year, disclosures of related party transactions on a <b>consolidated basis</b> , in the format specified in the relevant accounting standards for annual results to the stock exchanges and publish the same on its website.	The listed entity shall submit to the stock exchanges disclosures of related party transactions in the format as specified by the Board from time to time, and publish the same on its website.	<i>Earlier related party transactions <b>on a consolidated basis</b> were required to be disclosed to stock exchange(s) within 30 days of date of publication of results to stock exchange(s).</i>  <i>With the amendment, two significant changes have been made. Firstly, time limit of making the disclosure to stock exchange(s) <b>has been reduced to 15 days.</b></i>  <i>Secondly, the amendment has deleted the word “on a consolidated basis”. This call for enhanced disclosure as RPTs on consolidated basis didn’t include transactions with entities that are consolidated and now all the RPTs on Standalone basis would be required to be disclosed.</i>
23(9) Proviso	Provided that a ‘high value debt listed entity’ shall submit such disclosures along with its standalone financial results for the half year.	Provided that a ‘high value debt listed entity’ shall submit such disclosures along with its standalone financial results for the half year.	
23(9) Proviso 2	New Insertion	Provided further that the listed entity shall make such disclosures every six months within 15 days from the date of publication of its standalone and consolidated financial results.	
23(9) Proviso 3	New Insertion	Provided further that the listed entity shall make such disclosures every six months on the date of publication of its standalone and consolidated financial results with effect from April 1, 2023.”	<i>With effect from April 1, 2023, the time limit of fifteen days will not be provided with effect from April 1, 2023.</i>

### An Analysis

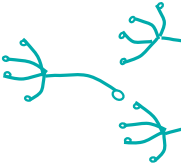
- In the case of high value debt listed entity, the requirement is to submit the disclosures of related party transactions along with the financial results. SEBI to therefore clarify if the auditors are required to submit these to a limited review or audit, as applicable.

## Information review requirements for audit committee and shareholders



- On November 22, 2021, SEBI has specified extensive information requirement which is to be provided to the audit committee and shareholders for review include, inter-alia, value of the RPT, tenure, source of funds, nature of security where secured, applicable terms, purpose for which funds will be utilised by ultimate beneficiary, justification as why the RPT is in the interest of the listed entity, valuation report, etc.
- The audit committee is required to review status of long-term (more than one year) or recurring RPTs on an annual basis. This would therefore require review of RPT wherein omnibus approval was previously granted.
- Specific format to be used for reporting of RPTs to the Stock Exchange every six months within fifteen days from the date of publication of its standalone and consolidated financial results. The format covers substantially all of the information that is required to be reviewed by the audit committee/shareholders. The format includes details to be provided for RPT including commitments. It appears that such commitments would need to be disclosed in the format (as aligned with the disclosure requirements of Ind AS 24) even if no transactions have occurred pursuant to the commitment.

## Other matters for consideration

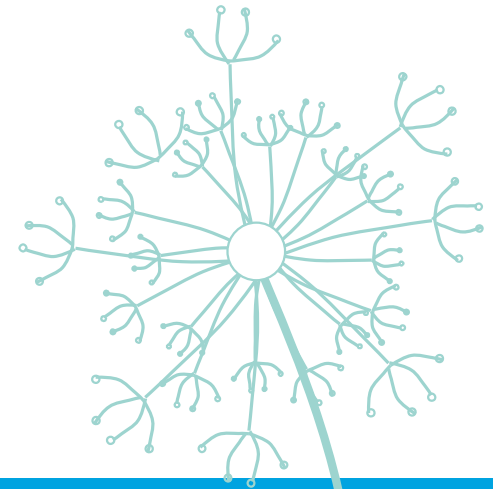


- Identifying beneficial interest and whether a transaction is to the benefit (purpose and effect) of a related party (e.g., a loan provided to a third party who in turn onwards lends to a related party of a subsidiary will also be scoped in as RPT)
- Risk control matrices (RCM) to be updated to factor in the changes to the Regulations. Auditors will be required to audit such RCM
- Completeness in identifying related party transactions across the group and will require changes to be made to the various databases to capture required information
- Reasons for dissenting votes (independent directors /shareholders) if any, to be clearly documented
- Omnibus approvals by audit committee are applicable only in respect of RPT proposed to be entered into by the listed entity. As such, such omnibus approvals cannot be provided for RPT of the subsidiary now covered as RPT
- Omnibus approvals cannot be given by shareholders
- No scope for any ratification if prior approval is not obtained from Audit committee or Shareholders



# Questions





# *Thank you*

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