

Clarification on matters relating to Related Party Transactions.

Government has received representations from stakeholders seeking certain clarifications on related party transactions covered under section 188 of the Companies Act, 2013. These representations have been examined and the following clarifications are given:

1. Scope of second proviso to Section 188(1):

Bare Act Language: Second proviso to sub-section(1) of section 188 said No Member of the company shall vote on such special resolution, to approve any contract or arrangement which may be entered into by the company, if such member is a related party.

Circular Language: It is clarified that 'related party' referred to in the second proviso has to be construed with reference only to the contract or arrangement for which the said special resolution is being passed. Thus, the term 'related party' in the above context refers only to such related party as may be a related party in the context of the contract or arrangement for which the said special resolution is being passed.

Example-1: There is Two Company XYZ and PQR. Company XYZ and PQR entering into a Contract/Transaction. Mr. A is Director in Company XYZ and Mrs. A is Member in XYZ. So Mrs. A is member and related party for company XYZ. {Before this circular peoples were saying that According to this example Mrs. A can't participate in such transaction} But this circular clarify that Mrs. A is related party but she is not interested in contract so she can vote on Special Resolution pass for contract/ transaction b/w company XYZ and PQR.

Example-2: If in the above Example. Mr. A is Director in Company XYZ, and Mrs. A is Member in XYZ and Mr. A also director in PQR. So in this case Mrs. Can't vote on Special Resolution. Because Mrs. A is now interested in transaction because her husband is Director in PQR company with whom XYZ going to enter into contract. {So Mrs. A is member and related party like above example but in this example she is also interested because her husband is interested in this transaction so Mrs. A can't vote on such resolution.}

Opinion: According to this clarification of MCA, my opinion is that if a member is related party as per *Section 2(76) of Companies Act, 2013 but member is don't have any interest in transaction then member can vote on Special Resolution even he/she is related party.

2. Applicability of Section 188 to Corporate Restructuring- Amalgamation:

Circular Language: It is clarified that transactions arising out of Compromises, Arrangements and Amalgamations dealt with under specific provisions of the Companies Act, 1956/Companies Act, 2013, will not attract the requirements of section 188 of the Companies Act, 2013.

Example: Section 188 (Related Party Transaction) of Companies Act, 2013 applicable on Both Public & Private Company. But as per General Circular No. 30/2014 if a company going for Compromise, Arrangements and Amalgamation then there is no need to follow provisions of Section-188.

Company can enter into scheme of Compromise, Arrangements and Amalgamation exempt from applicability of Section-188. So mean because of Compromise, Arrangements and Amalgamation if any related party transaction attract, company can proceed with scheme without follow the provision of Section-188.

3. Requirement of fresh approvals for Past Contracts Under Section 188:

Circular Language: Contracts entered into by companies, after making necessary compliances under Section 297 of the Companies Act, 1956, which already came into effect before the commencement of Section 188 of the Companies Act, 2013, will not require fresh approval under the said section 188 till the expiry of the original term of such contracts. Thus, if any modification in such contract is made on or after 1st April, 2014, the requirements under section 188 will have to be complied with.

Example: If a Company XYZ Limited has entered into any related party transactions/contract as per Section-297 of Companies Act, 1956 by making necessary compliances under section 297 of Companies Act, 1956 and such transaction has already came into effect before the commencement of Section 188 of the Companies Act, 2013 then it is not necessary for company XYZ Limited to comply the provisions of Section-188 till the Expiry of Original Term of Contract.

In Above Example if, original terms of contract expire after 1st April, 2014 and company wants to renew such contract then company have to comply with the provisions of Section- 188 of Companies Act, 2013.

Opinion:

Section- 188 of Companies Act, 2013 will be applicable in following situations, when:

1. When company enter into related party transaction after 1st April, 2014.
2. Renewal of Related Party Contract after 1st April, 2014.

But Provisions of Section 188 will not apply in following situations:

1. When company entered into transaction before 1st April, 2014.
2. When there is no renewal of contract entered before 1st April, 2014.

****Definition of Related Party Transaction: Section 2(76):** “Related Party”, with reference to a company, means—

i.	a director or his relative;
ii.	a key managerial personnel or his relative;
iii.	a firm, in which a director, manager or his relative is a partner
iv.	a private company in which a director or manager is a member or director;
v.	a public company in which a director or manager is a director or holds along with his relatives, more than two per cent. of its paid-up share capital;
vi.	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
vii.	any person on whose advice, directions or instructions a director or manager is accustomed to act: Provided that nothing in sub-clauses (vi) and (vii) shall apply to the advice, directions or instructions given in a professional capacity
viii.	any company which is— (A) a holding, subsidiary or an associate company of such company; or (B) a subsidiary of a holding company to which it is also a subsidiary;
ix.	such other person as may be prescribed