

RELATED PARTY DISCLOSURES

Scope	<p>This Standard should be applied in reporting related party relationships and transactions between a reporting enterprise and its related parties. The requirements of this Standard apply to the financial statements of each reporting enterprise as also to consolidated financial statements presented by a holding company.</p>
Related Party Relationships	<p><i>Related party - parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.</i></p> <p>AS 18 deals only with related party relationships described in (a) to (e) below:</p> <ol style="list-style-type: none"> a) Enterprises that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting enterprise (this includes holding companies, subsidiaries and fellow subsidiaries). b) Associates and joint ventures of the reporting enterprise and the investing party or venturer in respect of which the reporting enterprise is an associate or a joint venture. c) Individuals owning, directly or indirectly, an interest in the voting power of the reporting enterprise that gives them control or significant influence over the enterprise, and relatives of any such individual. d) Key management personnel and relatives of such personnel and e) Enterprises over which any person described in (c) or (d) is able to exercise significant influence. This includes enterprises owned by directors or major shareholders of the reporting enterprise and enterprises that have a member of key management in common with the reporting enterprise.
No Related Parties	<p><i>The following are deemed not to be related parties:</i></p> <ol style="list-style-type: none"> a) Two companies simply because they have a director in common (unless the director is able to affect the policies of both companies in their mutual dealings). b) A single customer, supplier, franchiser, distributor, or general agent with whom an enterprise transacts a significant volume of business merely by virtue of the resulting economic dependence and c) The parties listed below, in the course of their normal dealings with an enterprise by virtue only of those dealings (although they may circumscribe the freedom of action of the enterprise or participate in its decision-making process): <ul style="list-style-type: none"> ❖ Providers of finance ❖ Trade unions ❖ Public utilities ❖ Government departments and government agencies including government sponsored bodies

Important Definitions	Related party transaction	A transfer of resources or obligations between related parties, regardless of whether or not a price is charged.
	Control	<ul style="list-style-type: none"> ➤ ownership, directly or indirectly, of more than one half of the voting power of an enterprise, or ➤ control of the composition of the board of directors in the case of a company or of the composition of the corresponding governing body in case of any other enterprise, or ➤ a substantial interest in voting power and the power to direct, by statute or agreement, the financial and/or operating policies of the enterprise.
	Significant influence	Participation in the financial and/or operating policy decisions of an enterprise, but not control of those policies. Significant influence may be exercised in several ways, for example, (1) by representation on the board of directors, (2) participation in the policy making process; (3) material inter-company transactions, (4) interchange of managerial personnel or (5) dependence on technical information. Significant influence may be gained by share ownership, statute or agreement.
	Key management personnel	Those persons who have the authority and responsibility for planning, directing and controlling the activities of the reporting enterprise. <i>For example</i> , in the case of a company, the managing director(s), whole time director(s), manager and any person in accordance with whose directions or instructions the board of directors of the company is accustomed to act, are usually considered key management personnel.
	Substantial interest	An enterprise is considered to have a substantial interest in another enterprise if that enterprise owns, directly or indirectly, 20% or more interest in the voting power of the other enterprise. Similarly, an individual is considered to have a substantial interest in an enterprise, if that individual owns, directly or indirectly, 20% or more interest in the voting power of the enterprise.
The Related Party Issue	<ul style="list-style-type: none"> ➤ Related party relationships are a normal feature of commerce and business. ➤ Without related party disclosures, there is a general presumption that transactions reflected in financial statements are consummated on an arm's length basis between independent parties. However, that presumption may not be valid when related party relationships exist because related parties may enter into transactions which unrelated parties would not enter into. Also, transactions between related parties may not be effected at the same terms and conditions as between unrelated parties. 	

	<ul style="list-style-type: none"> ➤ The operating results and financial position of an enterprise may be affected by a related party relationship even if related party transactions do not occur. ➤ Sometimes, transactions would not have taken place if the related party relationship had not existed.
Disclosure Requirements	<p><i>Name</i> of the related party and <i>nature of</i> the related party <i>relationship</i> where control exists should be disclosed irrespective of whether or not there have been transactions between the related parties.</p> <p>If there have been transactions between related parties, during the existence of a related party relationship, the reporting enterprise should disclose the following:</p> <ul style="list-style-type: none"> → The <u>name</u> of the transacting related party; → A <u>description of the relationship</u> between the parties; → A <u>description of the nature</u> of transactions; → <u>Volume</u> of the transactions either as an amount or as an appropriate proportion; → Any <u>other elements</u> of the related party transactions necessary for an understanding of the financial statements; → The <u>amounts</u> or appropriate proportions of <u>outstanding items</u> pertaining to related parties at the balance sheet date and provisions for doubtful debts due from such parties at that date; → <u>Amounts written off</u> or written back in the period in respect of debts due from or to related parties.
Exceptions of disclosure requirements	<ul style="list-style-type: none"> ➤ Related party disclosure requirements as laid down in AS 18 do not apply in circumstances where providing such disclosures would conflict with the reporting enterprise's duties of confidentiality as specifically required in terms of a statute or by any regulator or similar competent authority. ➤ No disclosure is required in consolidated financial statements in respect of intragroup transactions. ➤ No disclosure is required in the financial statements of state-controlled enterprises as regards related party relationships with other state-controlled enterprises and transactions with such enterprises.

ASSIGNMENT QUESTIONS

Question 1 *(ICAI Study Material)*

Identify the related parties in the following cases as per AS 18:

A Ltd. holds 51% of B Ltd.

B Ltd holds 51% of O Ltd.

Z Ltd holds 49% of O Ltd.

Solution

Reporting enterprise- A Ltd.

- B Ltd. (subsidiary) is a related party
- O Ltd.(subsidiary) is a related party

Reporting enterprise - B Ltd.

- A Ltd. (holding company) is a related party
- O Ltd. (subsidiary) is a related party

Reporting enterprise - O Ltd.

- A Ltd. (ultimate holding company) is a related party
- B Ltd. (holding company) is a related party
- Z Ltd. (investor/ investing party) is a related party (O Ltd. being Associate of Z Ltd.)

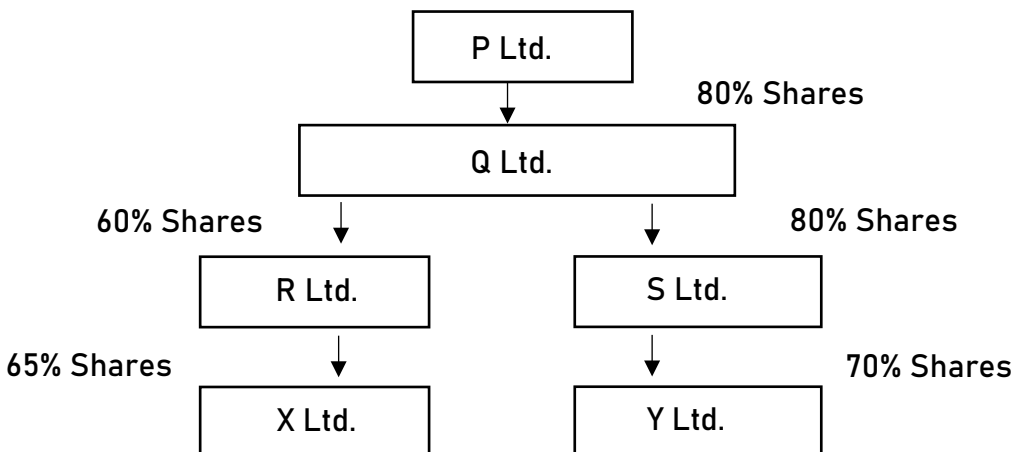
Reporting enterprise - Z Ltd.

- O Ltd. (associate) is a related party

Question 2 *(ICAI Study Material)*

Pg no. _____

Consider the following organization structure related to P Ltd.



Given the above structure: Identify related party relationships, if R Ltd. is reporting enterprise

Solution

The following table identifies related party relationships for R Ltd. (being reporting enterprise)

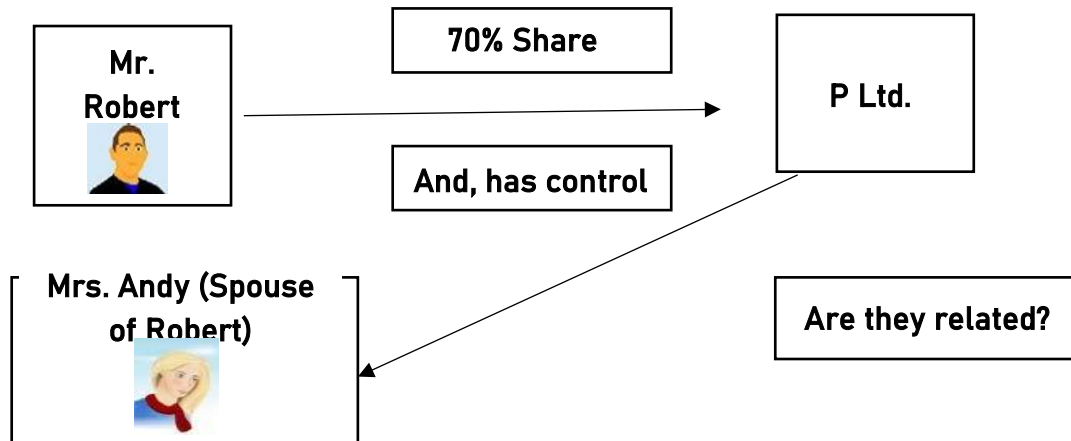
Party Name	Relationship under AS-18
P Ltd.	<ul style="list-style-type: none"> • P Ltd. has indirect control on R Ltd. (through Q Ltd.) • Hence R Ltd. is related to P Ltd.
Q Ltd.	<ul style="list-style-type: none"> • Q Ltd. has direct control of R Ltd. • Hence R Ltd. is related to Q Ltd.
S Ltd.	<ul style="list-style-type: none"> • R Ltd. and S Ltd. are under common control of Q Ltd. • Hence R Ltd. is related to S Ltd.
X Ltd.	<ul style="list-style-type: none"> • X Ltd. is controlled by R Ltd. • Hence R Ltd. is related to X Ltd.

Y Ltd.	<ul style="list-style-type: none"> • Y Ltd. is the sub-subsidiary of Q Ltd. • Both R Ltd. and Y Ltd. are under common control of Q Ltd. • Hence R Ltd. is related to Y Ltd.
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Question 3 **(ICAI Study Material)** _____ Pg no. _____

Consider a scenario wherein:

- Mr. Robert holds 70% shares and voting rights in P Ltd



Determine: Whether Andy (spouse of Mr. Robert) is a related party to P Ltd. under AS-18?

Solution

Yes – Andy is a related party to P Ltd., in view of the requirements of AS-18.

It may be recalled that under AS-18 'relatives of individuals owning an interest in the voting power of the reporting enterprise that gives them control or significant influence over the enterprise' are considered as related parties.

Question 4 **(RTP May 2020) / (ICAI Study Material)** _____

Narmada Ltd. sold goods for ₹ 90 lakhs to Ganga Ltd. during financial year ended 31-3-2020. The Managing Director of Narmada Ltd. own 100% of Ganga Ltd. The sales were made to Ganga Ltd. at normal selling prices followed by Narmada Ltd. The Chief accountant of Narmada Ltd contends that these sales need not require a different treatment from the other sales made by the company and hence no disclosure is necessary as per the accounting standard. Is the Chief Accountant, correct?

Solution

As per AS 18 'Related Party Disclosures', Enterprises over which a key management personnel is able to exercise significant influence are related parties. This includes enterprises owned by directors or major shareholders of the reporting enterprise and enterprise that have a member of key management in common with the reporting enterprise.

In the given case, Narmada Ltd. and Ganga Ltd are related parties and hence disclosure of transaction between them is required irrespective of whether the transaction was done at normal selling price. Hence the contention of Chief Accountant of Narmada Ltd is wrong.

Question 5 **(ICAI Study Material)** _____

A) Mr. Raj a relative of key management personnel received remuneration of ₹ 2,50,000 for his services in the company for the period from 1.4.2019 to 30.6.2019. On 1.7.2019, he left the service. Should the relative be identified as at the closing date i.e. on 31.3.2020 for the purposes of AS 18?

Solution

According to AS 18 on 'Related Party Disclosures', parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions. Hence, Mr. Raj, a relative of key management personnel should be identified as related party for disclosure in the financial statements for the year ended 31.3.2020.

- B) X Ltd. sold goods to its associate Company during the 1st quarter ending 30.6.2019. After that, the related party relationship ceased to exist. However, goods were supplied as were supplied to any other ordinary customer. Decide whether transactions of the entire year have to be disclosed as related party transaction.

Solution

As per AS 18, transactions of X Ltd. with its associate company for the first quarter ending 30.06.2019 only are required to be disclosed as related party transactions. The transactions for the period in which related party relationship did not exist would not be reported.

Question 6 **(ICAI Study Material)** Pg no. _____

Consider a scenario wherein:

- UK Bank holds 23% equity shares with voting rights in P Ltd.
- The bank has provided a loan of Rs. 20 million to P Ltd. at market interest rate
- As per the terms and conditions of the loan agreement, the bank has appointed one person as its nominee to the board of directors of P Ltd. and any major transaction to be entered into by P Ltd. will require the consent of the Bank.

Determine: Whether under AS-18 - UK Bank is a related party to P Ltd. (the reporting enterprise)?

Solution

In the instant case, the UK Bank holds 23% shares with voting rights in P Ltd. and hence is deemed to exercise significant influence over P Ltd.

The bank is also a provider of finance to P Ltd. (the reporting enterprise) and as per AS-18, parties like providers of finance are deemed not to be considered as a related party in the course of normal dealings with an enterprise by virtue only of those dealings. However, this exemption will not be available to UK Bank in this case - since it exercises significant influence over P Ltd. (by virtue of holding 23% shares with voting rights in P Ltd.)

Accordingly, for P Ltd. (the reporting enterprise), the UK Bank is a related party and it will be required to disclose the transactions with UK Bank in its financial statements.

Question 7 **(RTP May 2019) / (RTP Nov 2019) / (RTP Nov 2022)** _____

SP hotels Limited enters into an agreement with Mr. A for running its hotel for a fixed return payable to the later every year. The contract involves the day-to-day management of the hotel, while all financial and operating policy decisions are taken by the Board of Directors of the company. Mr. A does not own any voting power in SP Hotels Limited. Would he be considered as a related party of SP Hotels Limited?"

Solution

Mr. A will not be considered as a related party of SP Hotels Limited in view of paragraph 3(c) of AS 18 which states, "individuals owning, directly or indirectly, an interest in the voting power of the reporting enterprise that gives them control or significant influence over the enterprise, and relatives of any such individual".

In the above example, in the absence of share ownership, Mr. A would not be considered to exercise significant influence on SP Hotels Limited, even though there is an agreement giving him the power to manage the company.

Further, the fact that Mr. A does not have the ability to direct or instruct the board of directors does not qualify him as a key management personnel

Question 8 *(RTP May 2018) / (RTP May 2023) (Similar)*

Is remuneration paid to Key Managerial Personnel or Non Executive Directors or Board of Directors a related party transaction?

Solution

Key Managerial Personnel (KMP) are those persons who have the authority and responsibility for planning, directing & controlling the activities of the reporting enterprise.

In case of a company, the Managing Director, Whole time Director, Manager & any person in accordance with whose directions or instructions the board of directors of the company is accustomed to act, are usually considered KMP.

Persons who do not have the authority & responsibility for planning, directing & controlling the activities of the enterprise would not be KMP. Conversely, persons without any formal titles may be considered to be KMP, if they plan, direct & control the activities of the enterprise.

A non executive director may not be involved in either of these activities mentioned above. In fact besides his activity is more in the nature of an advisory and guiding function. Even if he is involved in planning stage, being non executive, he will not be involved in controlling the activities. Hence remuneration paid to nonexecutive director is not a related party transaction.

Further as per Companies Act, 2013 a related party includes a director or his relative. The Act defines a director as a director appointed to the Board of a company. Therefore as per Companies Act, a non executive director would be considered as a related party. Hence remuneration paid to them will be considered as related party transaction.

Question 9 *(RTP Nov 2021)*

(a) Omega Bank Limited holds 25 per cent of the voting power of B Limited. Omega Bank Limited also provides finance by way of a loan to B Limited at market rates of interest, on account of which, Omega Bank Limited would have the power to nominate one person to the board of directors of B Limited. Any major transactions proposed to be entered into by B Limited would need the consent of Omega Bank Limited. Would Omega Bank Limited be considered as related party for B Ltd. (reporting enterprise)?

(b) A Limited has two Associates, B Limited and C Limited, and owns 25 per cent of the voting power of B Limited and 30 per cent of the voting power of C Limited. Would B Limited be considered a related party for the purpose of financial statements of C Limited?

Solution

(a) Omega Bank Limited would be a related party of B Limited. As per AS 18 “associates and joint ventures of the reporting enterprise and the investing party of venture in respect of which the reporting enterprise is an associate or a joint venturer” are related party relationship. Further, an associate has been defined as “an enterprise in which an investing reporting party has significant influence and which is neither a subsidiary nor a joint venture of the party”. Significant influence has been defined to be “participation in the financial and /or operating policy decisions of an enterprise, but not control of those policies”. Further, it is given in the standard that significant influence may be gained by

share ownership, agreement or statute. As regards share ownership, there is a presumption that ownership of 20 per cent or more of the voting power enables the enterprise to exercise significant influence, unless it could be clearly demonstrated otherwise. In the given example, Omega Bank Limited exercises significant influence over B Limited by virtue of ownership of 25 per cent of the voting power.

Omega Bank Limited is also a provider of finance for B Limited (as it has provided a loan to B Limited), and as per the standard, a provider of finance is deemed not to be a related party during its normal dealings with the enterprise by virtue only of those dealing. However, in this case, the exemption would not be available to Omega Bank Limited as the exercise of significant influence of Omega Bank Limited over B Limited has been demonstrated on account of ownership of more than 20 per cent of voting power. Accordingly, Omega Bank Limited would be construed to be a related party in the financial statements of B Limited and consequently, the latter would be required to disclose the transactions with Omega Bank Limited in its financial statements.

- (b) Both B Limited and C Limited are 'associates' of A Limited. Fellow-associates cannot be regarded as a related parties only by virtue of the relationship. AS 18 states that "enterprise that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting enterprise" are related parties. Further, it is given that "associates and joint ventures of the reporting enterprise and the investing party or venture in respect of which the reporting enterprise is an associate or a joint venturer" are also related parties. As B Limited is not an associate of C Limited, nor is it being controlled, directly or indirectly, by C Limited or is not so controlling C Limited, it is not a related party of C Limited.

Question 10 ***(ICAI Study Material)***

ABC Limited is in the business of manufacturing textiles. It has certain commercial contracts with its customers and those customer contracts carry various clauses, imposing restriction on ABC Limited for disclosure of certain information. Accordingly, the company doesn't intend to provide related party disclosure under AS-18 in its ensuing financial statements. Is this correct?

Solution

As per AS-18 stipulate that related party disclosure requirements under AS-18 do not apply in circumstances, where providing such disclosures would conflict with the reporting enterprise's duties of confidentiality, as specifically required in terms of a statute or by any regulator or similar competent authority.

In case, where (1) a statute or (2) a regulator or (3) a similar competent authority governing an enterprise prohibit the enterprise to disclose certain information, which is required to be disclosed as per AS 18, disclosure of such information is not warranted. For example, banks are obliged by law to maintain confidentiality in respect of their customers' transactions and AS-18 would not override the obligation to preserve the confidentiality of customers' dealings.

However, this exemption is not available in respect of confidentiality provisions in a commercial contract between two enterprises - where confidentiality is not specifically required in terms of (1) a statute or (2) by any regulator or (3) similar competent authority.

Therefore, in the given case AS-18 related party disclosures would have to be made by ABC Limited in its ensuing financial statements.

Question 11 *(RTP Jan 2025)*

Will transactions with related parties, for services provided/received free of cost, be required to be disclosed?

A Limited has a corporate communications department, which centralises the public relations function for the whole group of A Limited and its subsidiaries. No charges are, however, levied by A Limited on its subsidiaries and accordingly, these transactions are not given accounting recognition. Would these constitute related party transactions requiring disclosure under AS 18 in the standalone financial statements of A Limited?

Solution

These transactions would require disclosure under AS 18 in the standalone financial statements of A Limited. As per paragraph 10 of AS 18, a related party transaction is “a transfer of resources or obligations between related parties, regardless of whether or not a price is charged”. In the given situation, there is a transfer of resources from A Limited to its subsidiaries, though no price is charged for the same. Hence, it will constitute as related party transaction and will require disclosure in the financial statements of A Ltd.

Question 12 *(Inter Jan 2025) (4 Marks)*

The following information is provided for the year ended 31st March, 2024:

- a) AX Limited holds 70% shares of BX Limited
- b) BX Limited holds 30% shares of CX Limited
- c) DX Limited holds 40% shares in CX Limited
- d) DX Limited holds 49% shares in EX Limited

You are required to:

- (i) Identify the related parties for the reporting entities AX Limited, CX Limited and EX Limited.
- (ii) If DX Limited would have sold its investment in EX Limited on 1st October, 2023, but goods were continued to be supplied by DX Limited to EX Limited throughout the year, will this scenario change your answer with respect to any of reporting entity mentioned in point (i)? Give reasons for your answer as per AS 18.

PRACTICE QUESTIONS

Question 1 *(Inter May 2019) (5 Marks) / (ICAI Study Material) / (RTP Nov 2023)*

Identify the related parties in the following cases as per AS-18

- (i) Maya Ltd. holds 61 % shares of Sheetal Ltd.
 Sheetal Ltd. holds 51 % shares of Fair Ltd.
 Care Ltd. holds 49% shares of Fair Ltd.
 (Give your answer - Reporting Entity wise for Maya Ltd., Sheetal Ltd., Care Ltd. and Fair Ltd.)
- (ii) Mr. Subhash Kumar is Managing Director of A Ltd. and also holds 72% capital of B Ltd.

Solution

(i)

(a) Reporting entity- Maya Ltd.

- Sheetal Ltd. (subsidiary) is a related party
- Fair Ltd.(subsidiary) is a related party

(b) Reporting entity- Sheetal Ltd.

- Maya Ltd. (holding company) is a related party
- Fair Ltd. (subsidiary) is a related party

(c) Reporting entity- Fair Ltd.

- Maya Ltd. (ultimate holding company) is a related party
- Sheetal Ltd. (holding company) is a related party
- Care Ltd. (investor/ investing party) is a related party

(d) Reporting entity- Care Ltd.

- Fair Ltd. (associate) is a related party

- (ii) Mr. Subhash Kumar is Key management personnel as he has the authority for planning, directing and controlling the activities of A Ltd. He also holds substantial interest in B Ltd. as he holds 72% capital of B Ltd. Thus, Mr. Subhash is related party for both A Ltd. and B Ltd. Moreover, as per the definition of related party relationship described in para 3 of AS 18, enterprises over which Subhash is able to exercise significant influence are also related parties. Thus, A Ltd. and B Ltd. will also be construed as related to each other.

Question 2 *(RTP Nov 2020)*

(a) Identify the related parties in the following cases as per AS-18

X Ltd. holds 60 % shares of Y Ltd.

Y Ltd. holds 55 % shares of W Ltd.

Z Ltd. holds 35% shares of W Ltd.

- (b) Himalaya Ltd. sold goods for ₹ 40 lakhs to Aravalli Ltd. during financial year ended 31st March 2020. The Managing Director of Himalaya Ltd. owns 80% shares of Aravalli Ltd. The sales were made to Aravalli Limited at normal selling prices followed by Himalaya Ltd. The Chief accountant of Himalaya Ltd contends that these sales need not require a different treatment from the other sales made by the company and hence no disclosure is necessary as per AS 18. You are required to comment on this.

Solution

- A) X Ltd., Y Ltd. & W Ltd. are related to each other. Z Ltd. & W Ltd. are related to each other by virtue of associate relationship. However, neither X Ltd. nor Y Ltd. is related to Z Ltd. and vice versa since neither control nor does significant influence exist between them.

B) Himalaya Ltd. and Aravalli Ltd. are related parties since key management personnel of Himalaya Ltd. i.e. its managing director holds 80% shares in Aravalli Ltd. and hence disclosure of transaction between them is required irrespective of whether transaction was done at normal selling price. Hence the contention of Himalaya Ltd. that these sales require no disclosure under related party transactions is wrong.

Question 3 *(ICAI Study Material)* _____ Pg no. _____

Consider a scenario wherein:

- A Ltd. has 60% voting right in B Ltd.
- A Ltd. also has 22% voting right in C Ltd.; and
- B Ltd. has 30% voting right in C Ltd.

Whether C Ltd. is to be treated under AS-18 as a party related to A Ltd.?

Solution

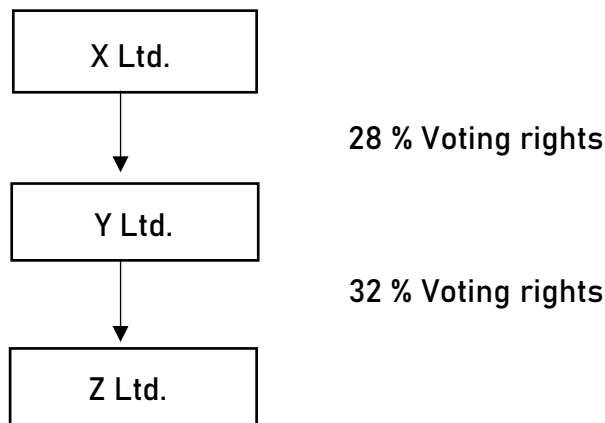
Yes – in relation to A Ltd. (the reporting enterprise), C Ltd. is a related party under AS-18. This is because A Ltd. indirectly controls C Ltd.

In this case, A Ltd. (together with its subsidiary B Ltd.) controls more than one half of the voting rights of C Ltd.

Question 4 *(ICAI Study Material)* _____ Pg no. _____

Consider a scenario wherein:

- X Ltd. holds 28% voting right in Y Ltd. (and hence Y Ltd. is an associate of X Ltd.)
- Y Ltd. holds 32% voting right in Z Ltd. (and hence Z Ltd. is an associate of Y Ltd.)



In the above case, since Y Ltd. is an associate of X Ltd. – Y Ltd. is a related party to X Ltd. Likewise, since Z Ltd. is an associate of Y Ltd. – Z Ltd. is a related party to Y Ltd. The question is: Whether Z Ltd. is to be treated under AS-18 as a party related to X Ltd.?

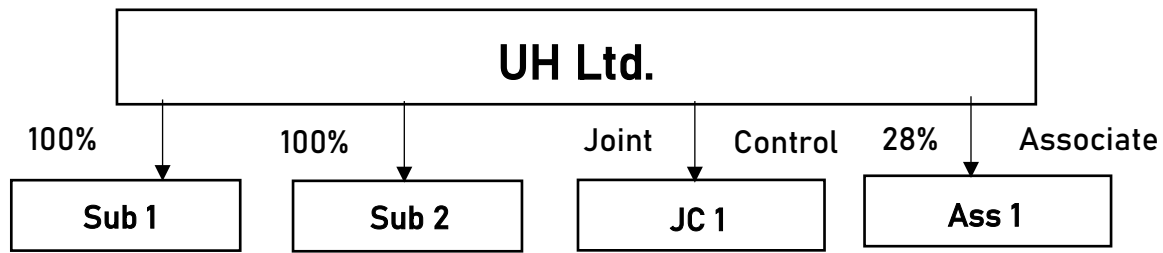
Solution

No – in relation to X Ltd. (the reporting enterprise), Z Ltd. is a **not** a related party. This is because as per the requirements of AS-18, 'associate of an associate' is **not** a related party.

Question 5 *(ICAI Study Material)* _____ Pg no. _____

Consider the following organization structure related to UH Ltd. (the ultimate parent company of a Group), wherein UH Ltd. has made the following investments:

- Investment in two of the wholly owned subsidiaries, viz. Sub 1 and Sub 2
- Investment in JC 1, in which UH Ltd. has a joint control
- 28% investment in Ass 1 (and hence, Ass 1 is an associate of UH Ltd.)



Given the above structure: Identify related party relationships for each of the above entities under AS-18

Solution

The following table identifies related party relationships for each of the entities in the Group:

Reporting enterprise	Related Party as per AS-18
UH Ltd.	All the four entities (viz. Sub 1, Sub 2, JC 1 and Ass 1)
Sub 1	Only two of the entities in the Group (viz. UH Ltd. and Sub 2)
Sub 2	Only two of the entities in the Group (viz. UH Ltd. and Sub 1)
JC 1	Only UH Ltd.
Ass 1	Only UH Ltd.

Question 6 (RTP Nov 2018)

Sun Ltd. sold goods for ₹ 50 lakhs to Moon Ltd. during financial year ended 31st March 2020 at normal selling price followed by Sun Ltd. The Managing Director of Sun Ltd. holds 75% shares of Moon Ltd. The Chief accountant of Sun Ltd contends that these sales need not require a different treatment from the other sales made by the company and hence no disclosure is necessary as per the accounting standard. You are required to examine and advise whether the contention of the Chief Accountant is correct?

Solution

As per AS 18 'Related Party Disclosures', Enterprises over which a key management personnel is able to exercise significant influence are related parties. This includes enterprises owned by directors or major shareholders of the reporting enterprise and enterprise that have a member of key management in common with the reporting enterprise. In the given case, Sun Ltd. and Moon Ltd are related parties and hence disclosure of transaction between them is required irrespective of whether the transaction was done at normal selling price. Hence the contention of Chief Accountant of Sun Ltd is wrong.

Question 7 - (ICAI Study Material)

Pg no. _____

Consider a scenario wherein:

- Mr. Robert is a Managing Director of P Ltd.
- Andy (spouse of Robert) received a remuneration of Rs 5 lacs from P Ltd. – for the services she rendered to P Ltd. for the period 1st April 2021 through 30th June 2021
- Andy left the services of P Ltd. on 1st July 2021
- Consider 31st March 2022 as the year-end date for P Ltd.

Whether Andy is to be identified as related party at the year-end date (31st March 2022) for the purposes of AS-18?

Solution

Yes – This is because as per AS-18, parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Hence Andy (being the spouse and relative of the KMP of P Ltd.) needs to be reported as related party at the year-end date (i.e. 31st March 2022). This is because the remuneration Andy received from P Ltd. (for the period April 2021 to 30 June 2021) falls within the reporting year April 2021 to March 2022.

Question 8 – **(ICAI Study Material)** Pg no. _____

Consider a scenario wherein:

- P Ltd. hold 22% shares and voting rights in Q Ltd. (and hence Q Ltd. is an associate of P Ltd.)
- On 1st April 2021, P Ltd. sold certain goods to Q Ltd. amounting to Rs. 5 lacs
- On 30th June 2021, P Ltd. sold its entire 22% stake in Q Ltd. (and hence the related party relationship ceased to exist after 30th June 2021)
- However, P Ltd. continued supply goods to Q Ltd. subsequent to 30th June 2021 (just like any other customer) and sold goods worth Rs. 15 lacs during 9-month period ended 31st March 2022
- Consider 31st March 2022 as the year-end date for P Ltd.

Determine whether the transaction for the entire year (ending on 31st March 2022) is required to be disclosed under AS-18 as related party transaction.

Solution

No – This is because as per AS-18, the disclosure requirements under the Standard relate only to the period during related party relationship existed.

Accordingly, only transactions between P Ltd and Q Ltd till 30th June 2021 (being sale of goods worth Rs. 5 lacs) are required to be reported / disclosed under AS- 18.

Transactions entered into after 30th June 2021 are not required to be disclosed under AS-18.

Question 9 **(Inter Nov 2018) (5 Marks)**

Following transactions are disclosed as on 31st March, 2018:

- Mr. Sumit, a relative of Managing Director, received remuneration of ₹ 2,10,000 for his services in the company for the period from 1st April, 2019 to 30th June, 2019. He left the service on 1st July, 2019. Should the relative be identified as a related party as on closing date i.e. on 31-3-2020 for the purpose of AS-18.
- Goods sold amounting to ₹ 50 lakhs to associate company during the 1st quarter ended on 30th June, 2019. After that related party relationship ceased to exist. However, goods were supplied as was supplied to any other ordinary customer. Decide whether transactions of the entire year have to be disclosed as related party transactions.

Solution

- According to AS 18 'Related Party Disclosures', parties are considered to be related if at any time during the reporting period, one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions. Hence, Mr. Sumit a relative of key management personnel should be identified as related party as at the closing date i.e. on 31.3.2020 as he received remuneration for his services in the company from 1st April, 2019 to 30th June, 2019 and this period comes under the reporting period.

b) As per provision of AS 18, the transactions only for the period in which related party relationships exist need to be reported. Hence, transactions of the entity with its associate company for the first quarter ending 30.06.2019 only are required to be disclosed as related party transactions. Transactions of the entire year need not be disclosed as related party transactions and transactions for the period (after 1st July) in which related party relationship did not exist need not be reported. Hence transaction of sale of goods with the associate company for first quarter ending 30th June, 2019 for ₹ 50 Lakhs only are required to be disclosed as related party transaction on 31.3.20.

Question 10 — *(Inter July 2021) (5 Marks) / (RTP May 2024)*

- (i) Khushi Limited enter into an agreement with Mr. Happy for running a business for a fixed amount payable to the later every year. The contract states that the day-to-day management of the business will be handled by Mr. Happy, while all financial and operating policy decisions are taken by the Board of Directors of the Company. Mr. Happy does not own any voting power in Khushi Limited.
- (ii) Shri Bhanu a relative of key management personnel received remuneration of ₹ 3,50,000 for his services in the company for the period from 1st April, 2020 to 30th June, 2020. On 1st July, 2020, he left the service.

You are required to suggest how the above transactions will be treated as at the closing date i.e. on 31st March, 2021 for the purposes of AS 18- Related Party Disclosures.

Solution

- (i) Mr. Happy will not be considered as a related party of Khushi Limited in view of provisions of AS 18 "Related Party Disclosures" which states, "individuals owning, directly or indirectly, an interest in the voting power of the reporting enterprise that gives them control or significant influence over the enterprise, and relatives of any such individual are related parties".

In the given case, in the absence of share ownership, Mr. Happy would not be considered to exercise significant influence on Khushi Limited, even though there is an agreement giving him the power to manage the company. Further, the fact that Mr Happy does not have the ability to direct or instruct the board of directors does not qualify him as a key management personnel.

- (ii) According to AS 18 on 'Related Party Disclosures', parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Hence, Shri Bhanu, a relative of key management personnel should be identified as related party for disclosure in the financial statements for the year ended 31.3.2021 as he received remuneration for his services in the company for the period from 1st April,2020 to 30th June,2020.

Question 11 *(ICAI Study Material)*

Pg no. _____

Who are related parties under AS 18? What are the related party disclosure requirements?

Solution

Parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions. If there have been transactions between related parties, during the existence of a related party relationship, the reporting enterprise should disclose the following:

- a) the name of the transacting related party;

- b) a description of the relationship between the parties;
- c) a description of the nature of transactions;
- d) volume of the transactions either as an amount or as an appropriate proportion;
- e) any other elements of the related party transactions necessary for an understanding of the financial statements;
- f) the amounts or appropriate proportions of outstanding items pertaining to related parties at balance sheet date & provisions for doubtful debts due from such parties at that date; &
- g) amounts written off or written back in the period in respect of debts due from or to related parties.

Question 12 **(Inter May 2023) (5 Marks)** Pg no. _____

Answer the following with respect to AS-18:

- a. ABC Ltd. sold goods of ₹ 2,00,000 to its associate company for the 1st quarter ending 30.06.2022. After that the related party relationship ceased to exist. However, goods were supplied to any other ordinary customer. Decide whether transactions of the entire year have to be disclosed as related party transactions.
- b. If the majority of directors of Arjun Ltd. constitute the majority of the Board of another Company Bheem Ltd. in their individual capacity as professionals (and not by virtue of their being Directors in Arjun Ltd.). Are both the companies related?
- c. Asha Ltd. sells all the manufactured furniture of ₹1,00,00,000 to Sasha Ltd. as per agreement. Sasha Ltd. is the only customer to Asha Ltd. In the financial statements, Asha Ltd. wants to present Sasha company as a related party. Comment on the disclosure requirement.

Solution

- a) As per AS 18, parties are considered to be related if any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party. Transactions of ABC Ltd. with its associate company for the first quarter ending 30.06.2022 only are required to be disclosed as related party transactions as the company has the ability to exercise significant influence only till 30.6.2022. The transactions for the period in which related party relationship did not exist need not be reported.
- b) In the given case, Arjun Ltd. cannot be said to control the composition of board of directors of Bheem Ltd. as the directors have been appointed in their individual capacity as professionals and not by virtue of their being directors in Arjun Ltd. Hence, it cannot be concluded that the companies are related merely because the majority of the directors of one company became the majority of the directors of the second in their individual capacity as professionals.
- c) In the context of AS 18, a single customer, supplier, franchiser, distributor, or general agent with whom an enterprise transacts a significant volume of business cannot be construed as Related Party Relationship merely by virtue of the resulting economic dependence. There is an economic dependence between the companies but no one controls or exercise significant influence on the other. In the given case, Asha Ltd. need not report Sasha Company as its related party in its financial statements.

Question 13 – **(RTP May 2022)** _____

In respect of a key supplier who is dependent on the company for its existence and the company enjoys influence over the prices of this supplier (which may not be formally demonstrable), can the supplier and the company be considered as related parties?

Solution

The supplier and the company cannot be considered to be related parties merely because the latter is able to influence the transaction price between the parties. Paragraph 3 of AS 18 states that “enterprises that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting enterprise” are considered to be related party relationships. However, the conditions which define the existence of control, as follows, are not satisfied in the given example.

- ‘ownership, directly or indirectly, of more than one-half of voting power of an enterprise, or
- Control of the composition of the board of directors in the case of a company or of the composition of the corresponding governing body in case of any other enterprise, or
- a substantial interest in voting power and the power to direct, by statute or agreement, the financial and/or operating policies of the enterprise”.

Paragraph 10 of the standard defines significant influence as “participation in the financial and/or operating policy decisions of an enterprise, but not control of those policies”. In the given example, although the supplier and the company have entered into a commercial transaction, the terms of which are influenced by the latter because of its better bargaining power in the specific market for such goods, it cannot be concluded that there is participation in the financial and/or operating policy decisions. Therefore, as the conditions specified by the Standard for being classified as a related party are not satisfied in the given example, the company cannot be said to be related to the supplier. This view is supported by paragraph 4 (b) of the Standard which states that “a single customer, supplier, franchiser, distributor, or general agent with whom an enterprise transacts a significant volume of business merely by virtue of the resulting economic dependence” would not be deemed to be related parties.

Question 14 – (ICAI Study Material)

Should the related parties be identified as at the reporting date (i.e. balance sheet date) for the purposes of AS-18? In disclosing transactions with related parties, are the transactions of the entire reporting period to be disclosed or only those for the period during which related party relationship exists?

Solution

As per the definition of related parties in AS-18, the existence of a related party relationship should be identified at all points during the year (and not only at the close of the financial year). However, AS 18 requires disclosure of transactions with these parties only during the existence of the related party relationship.