Related Party :- If at anytime during the FY one person has the ability to control or exercise significant influence over the other.

→ Transactions that take place only when the related party relationship exists need to be disclosed.

Who are not considered to be Related Parties

1. **Common Director** :-
If two entities have a common director, they are not considered related parties just because they have a common director.
Unless such common director is able to influence the mutual dealings between such entities.

2. **Economic Dependence** :-

If one entity conducts significant amount of trade with another entity such that there is economic dependence of one over the other, this does not make them related parties.

3. **Normal Dealings** :-

a. Providers of finance
b. Trade unions
c. Public utilities
d. Government departments

even though they may curb my freedom of actions and get involved in decision making process.

Exemption from Disclosure Requirments under AS-18

1. **Confidentiality Requirments** :-

a. Statute
b. Regulator
c. Similar competing authority

* Confidentiality Agreement between two parties doesnot trigger this exemption.

2. **Consolidated Financial Statements** :-

Intra group transaction and relationships neednot be separately disclosed.

3. **State Controlled Enterprises** :-

Transactions of one SCE with the other neednot be disclosed neither the relationship between the two.

Also, transactions between related parties may not be effected at the same terms and conditions as between unrelated parties. Sometimes, no price is charged in related party transactions, for example, free provision of management services and the extension of free credit on a debt.

Also, sometimes 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.** The *mere existence of the relationship* may be sufficient to affect the transactions of the reporting enterprise with other parties. For example, a subsidiary may terminate relations with a trading partner on acquisition by the holding company of a fellow subsidiary engaged in the same trade as the former partner. Alternatively, one party may refrain from acting because of the control or significant influence of another - for example, a subsidiary may be instructed by its holding company not to engage in research and development.

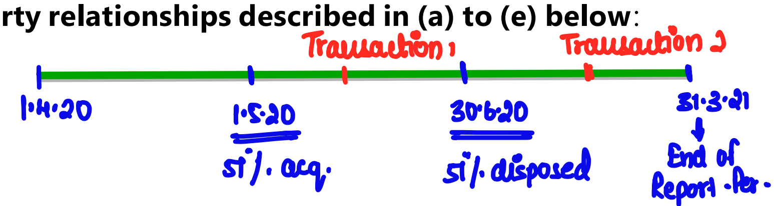
Likewise, in certain cases transactions *would not have taken place* if the related party relationship had not existed. For example, a company that sold a large proportion of its production to its holding company *at cost* might not have found an alternative customer if the holding company had not purchased the goods.

In view of the aforesaid, the resulting accounting measures may not represent what they usually would be expected to represent. Thus, a related party relationship could have an effect on the financial position and operating results of the reporting enterprise.

4.3 RELATED PARTY RELATIONSHIPS, AS CONTEMPLATED UNDER AS-18

Related Party - 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.

It is worthwhile to note that AS-18 provides a definitive list of related party relationships to which AS-18 applies. Accordingly, **AS 18 deals only with the following five types of related party relationships described in (a) to (e) below**:



They were related at any time during the reporting period

Disclose for RPT will be required only for transaction !

(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).

> ***Note:*** This is the case when there is a parent-subsidiary relationship (including relationship among fellow subsidiaries), as illustrated later in this chapter. For meaning of the term control, refer to subsequent discussion under this chapter.

(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.

4.4 WHO ARE NOT DEEMED TO BE RELATED PARTIES UNDER AS-18?

In the context of AS 18, the following are deemed **not to be related parties:**

× 'Related Par'

C1 C2

Director

(a) Two companies are not related parties simply because they have a director in common (unless the director is able to affect the policies of both companies in their mutual dealings). Accordingly, if the common director is able to influence the policies of **both the companies in their mutual dealings** – then related party relationship exists.

(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):

(i) Providers of finance

(ii) Trade unions

(iii) Public utilities

(iv) Government departments and government agencies including government sponsored bodies

4.5 EXEMPTION FROM RELATED PARTY DISCLOSURE IN CERTAIN SITUATIONS

→ Statute
→ Regulator
→ Similar competing authority
↓
Confidentiality

1. **Conflict with the reporting enterprise's duties of confidentiality:** 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.

Put differently, in cases where a statute or a regulator or a similar competent authority governing an enterprise prohibit the enterprise to disclose certain information which is required to be disclosed as per this Standard, disclosure of such information is *not warranted*. For example, banks are obliged by law to maintain confidentiality in respect of their customers' transactions and this Standard *would not override* the obligation to preserve the confidentiality of customers' dealings.

Eg: KM Bank
↓
RP : Kotak

Holding
↓ Google cell
Subsidiary
H+S → 1 company

2. **Consolidated financial statements:** No disclosure is required in consolidated financial statements in respect of intra-group transactions - since disclosure of transactions between members of a group is unnecessary in consolidated financial statements. This is mainly because consolidated financial statements present information about the holding and its subsidiaries *as a single reporting enterprise*.

3. **State-controlled enterprises:** No disclosure is required in the financial

Holding Co. → Standalone FS → RP Disclosures → Transactions with subsidiary.

Subs. Co → standalone FS " " with Holding

H+S → consolidated FR

statements of state-controlled enterprises as regards related party relationships with other state-controlled enterprises and transactions with such enterprises.

4.6 DEFINITIONS OF OTHER TERMS USED IN AS 18

Related party transaction: AS-18 defines related party transaction as, "A transfer of resources or obligations between related parties, regardless of whether or not a price is charged".

Control: As per AS-18 Control means:

(a) ownership, directly or indirectly, of more than one half of the voting power of an enterprise, or

(b) 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

(c) a substantial interest in voting power **and** the power to direct, by statute or agreement, the financial and/or operating policies of the enterprise.

It is pertinent to note that the above definition of control under AS-18 is relatively wider than that under AS-21 *Consolidated Financial Statements*. This is so because - clause (c) in the definition of control under AS-18 is an addition, which is not found in AS-21 *Consolidated Financial Statements*.

Also, AS-18 clarifies that for the purpose of AS 18, an enterprise is considered to **control the composition** of the board of directors of a company or governing body of an enterprise, if it has the power, without the consent or concurrence of any other person, to appoint or remove all or a majority of directors/members of the governing body of that company/enterprise. Put differently, control to the composition of the Board of directors is determined with reference to the **authority of an enterprise** *to appoint or remove all or majority of directors of another enterprise* ***without concurrence of any other person*.**

Further, an enterprise is **deemed** to have the power to appoint a director/ member of the governing body, if *any of the following conditions* is satisfied:

(a) A person cannot be appointed as director/member of the governing body majority ownership by another investing party does not necessarily preclude an investing party from having significant influence.

Key Management Personnel: As per AS-18, Key Management Personnel are those persons who have the authority and responsibility for planning, directing and controlling the activities of the reporting enterprise.

For example, in the case of a company, (1) the managing director(s), (2) whole time director(s), (3) manager and (4) 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.

AS-18 further provides an explanation that a non-executive director of a company -is not considered as a key management person under this Standard by virtue of *merely* his being a director unless he has the authority and responsibility for planning, directing and controlling the activities of the reporting enterprise.

The requirements of AS 18 should not be applied in respect of a non-executive director even if he participates in the financial and/or operating policy decision of the enterprise, unless he falls in any of the categories of 'related party relationships' discussed above.

Relative: As per AS-18, a Relative in relation to an individual, means the spouse, son, daughter, brother, sister, father and mother who may be expected to influence, or be influenced by, that individual in his/her dealings with the reporting enterprise.

Joint Venture - AS-18 defines a Joint Venture as a contractual arrangement whereby two or more parties undertake an economic activity which is subject to joint control.

Joint Control–AS-18 defines a Joint Control as the contractually agreed sharing of power to govern the financial and operating policies of an economic activity so as to obtain benefits from it. Accordingly, when two or more parties *contractually* agree to share power to govern the financial and operating policies of an economic activity, this contractual agreement is termed as joint control.

It is pertinent to note that joint venture ***does not*** depend upon *voting power of the parties involved*. Rather, it is linked to the ***ability to exercise joint control over an economic activity.***

A Co. B Co.
VP 60% 40%
↓ ↓
Full control No control

No a JV

Holding Company–AS-18 defines Holding Company as a company having one or more subsidiaries

Subsidiary AS 18 defines a Subsidiary – as a company:

(a) in which another company (the holding company) holds, either by itself and/or through one or more subsidiaries, more than one-half, in nominal value of its equity share capital; or

(b) of which another company (the holding company) controls, either by itself and/or through one or more subsidiaries, the composition of its board of directors.

Fellow Subsidiary–AS-18 clarifies that a company is considered to be a fellow subsidiary of another company if both are subsidiaries of the same holding company.

Illustration 1

Identify the related parties in the following case 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.

$A \xrightarrow{51\%} B \xrightarrow{51\%} O \xleftarrow{49\%} Z$

A → B, O

B → A, O

O → B, A, Z

Z → O

Solution

In relation to Reporting enterprise - A Ltd.

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

In relation to Reporting enterprise - B Ltd.

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

In relation to 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

Illustration 2

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.?

Control SI

$A \xrightarrow{60\%} B \xrightarrow{30\%} C$

$A \xrightarrow{22\%} C$

Ind → SI

Total Voting in C

A = 22 B = 30

N(cons) group (A+B)

= 52%

Indirect Control

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.

Illustration 3

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.)*

X Ltd.

↓ *28 % Voting* rights

Y Ltd. Assoc. Co. of X

↓ *32 % Voting* rights

Z Ltd. Assoc Co of Y

Associate of an associate is not an associate of the investing co.

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.

Illustration 4

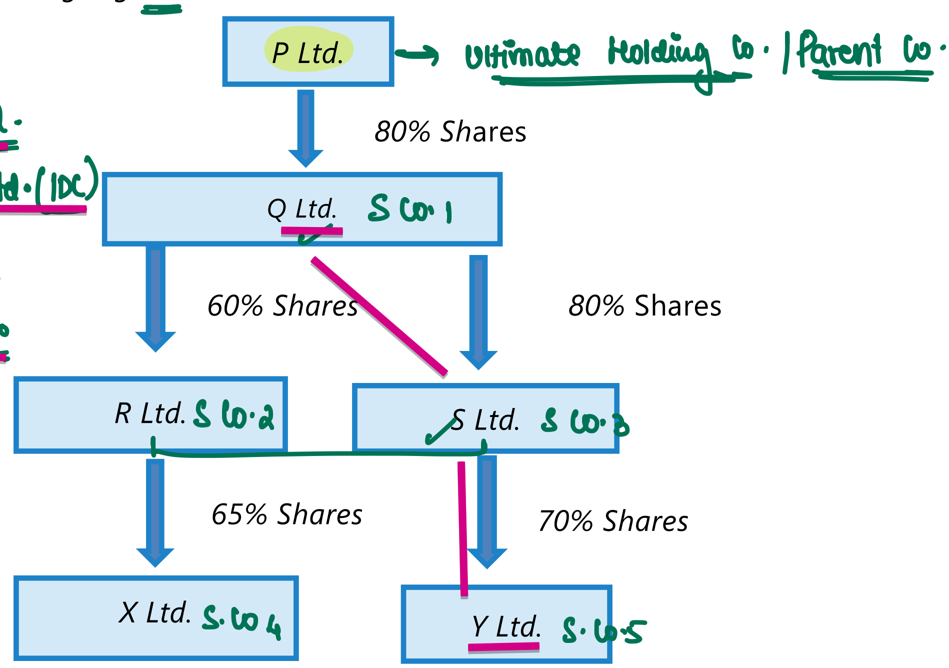
Consider the following organization structure related to P Ltd.

Reporting Entity

R Ltd. : Controls :→ X Ltd.

Controlled by :- Q Ltd. (DC), P Ltd. (IDC)

Under Common Control :- S Ltd. Y Ltd.



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

Solution

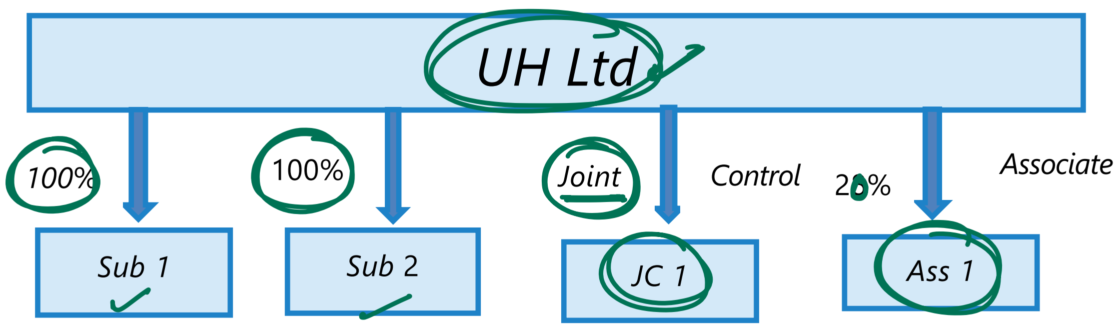
The following table identifies the related party relationships for R Ltd. (being the reporting enterprise):

Party Name	Relationship under AS-18
P Ltd.	♦ P Ltd. has *indirect control* on R Ltd. (through Q Ltd.) ♦ Hence R Ltd. is related to P Ltd.
Q Ltd.	♦ Q Ltd. has direct control of R Ltd. ♦ Hence R Ltd. is related to Q Ltd.
S Ltd.	♦ R Ltd. and S Ltd. are under common control of Q Ltd. ♦ Hence R Ltd. is related to S Ltd.
X Ltd.	♦ X Ltd. is controlled by R Ltd. ♦ Hence R Ltd. is related to X Ltd.
Y Ltd.	♦ 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.

Illustration 5

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*
- *20% 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.

UH → S1 S2 JC1 A1
S1 → UH, S2
S2 → UH, S1
JC1 → UH
Assoc → UH

Solution

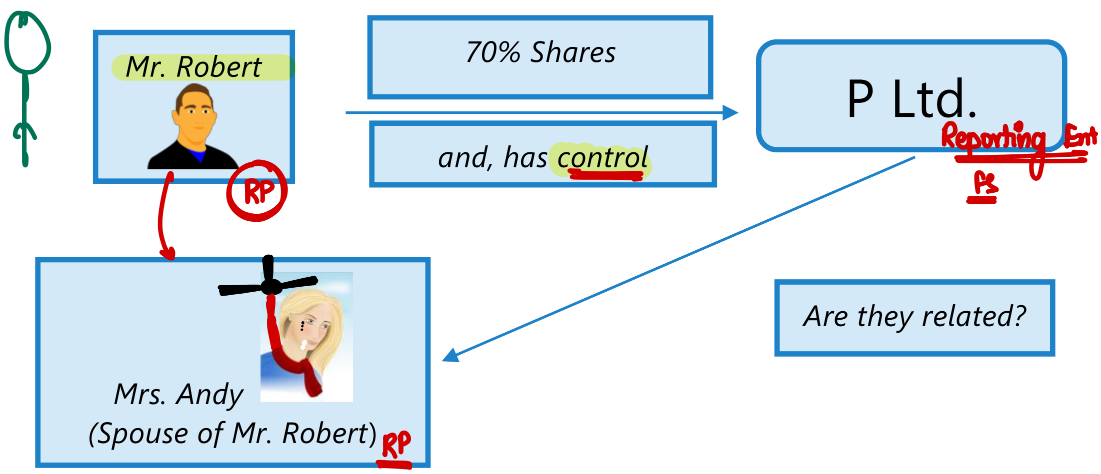
The following table identifies the related party relationships for each of the entities in the Group:

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.

Illustration 6

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

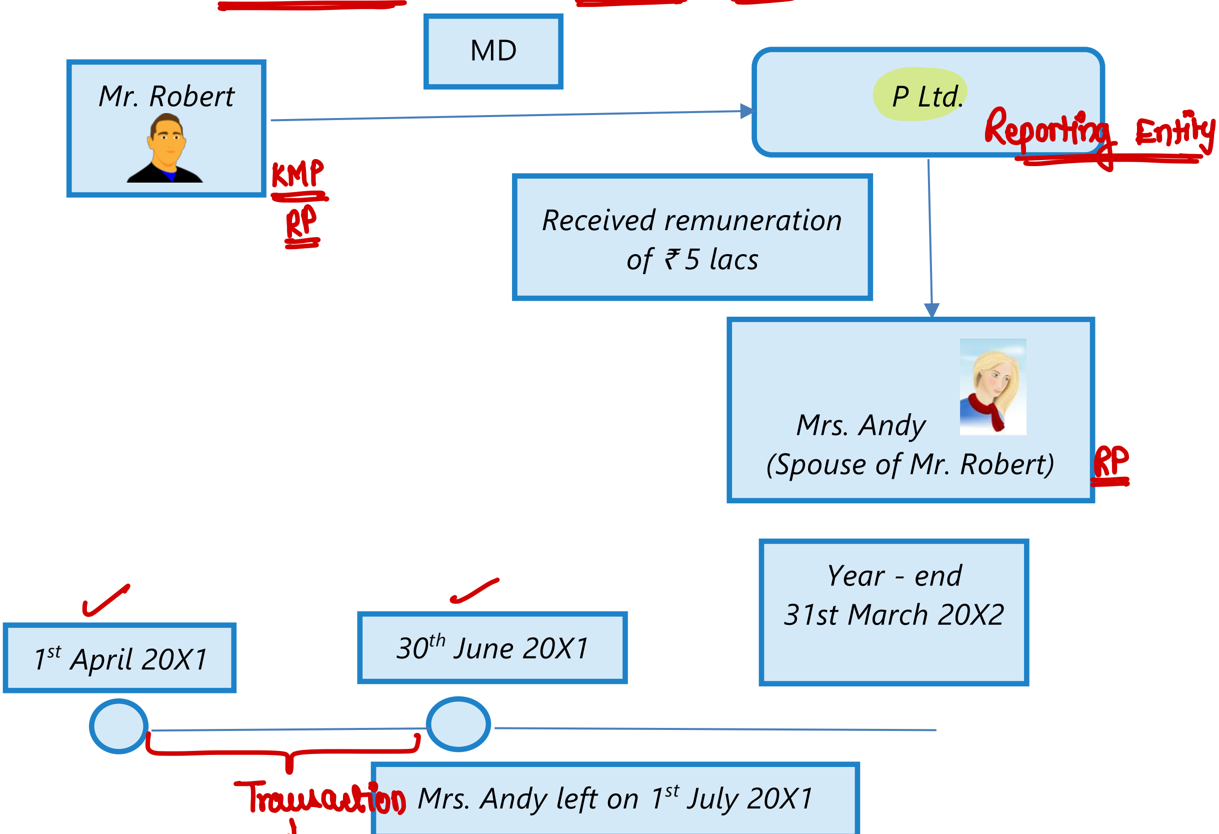
Yes – Andy is a related party to P Ltd., in view of the requirements of AS-18.

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.

Illustration 7

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 20X1 through 30th June 20X1*
- *Andy left the services of P Ltd. on 1st July 20X1*
- *Consider 31st March 20X2 as the year-end date for P Ltd.*



"Disclose" → 1) Name 2) Nature 3) Transactions 4) Volume 5) O/s 6) P.D.D. 7) B.D w off

Whether Andy is to be identified as related party at the year-end date (31st March 20X2) 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 20X2). This is because the remuneration Andy received from P Ltd. (for the period April 20X1 to 30 June 20X1) *falls within the reporting year April 20X1 to March 20X2.*

Illustration 8

Consider a scenario wherein:

- *UK Bank holds 23% equity shares with voting rights in P Ltd.*

  "Provider of Finance"
- *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*

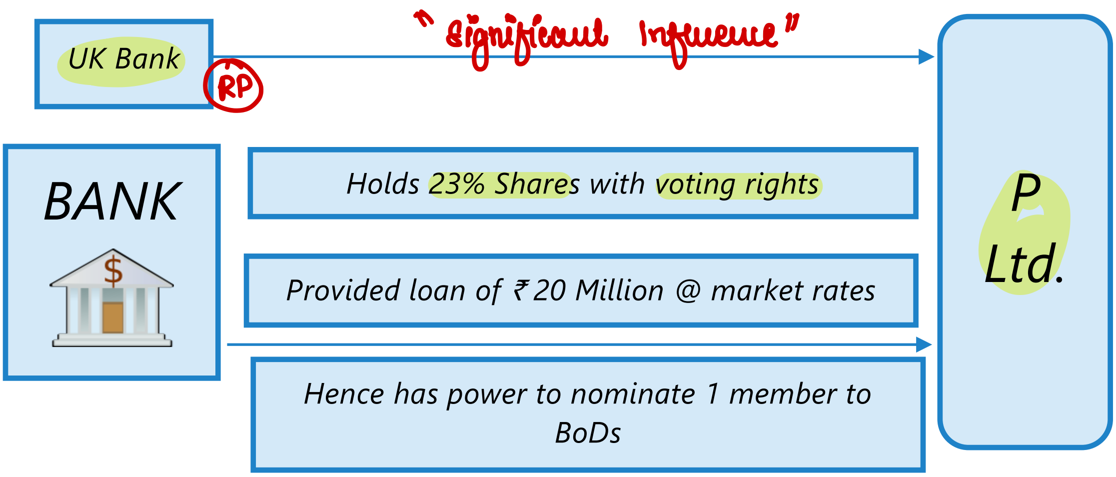
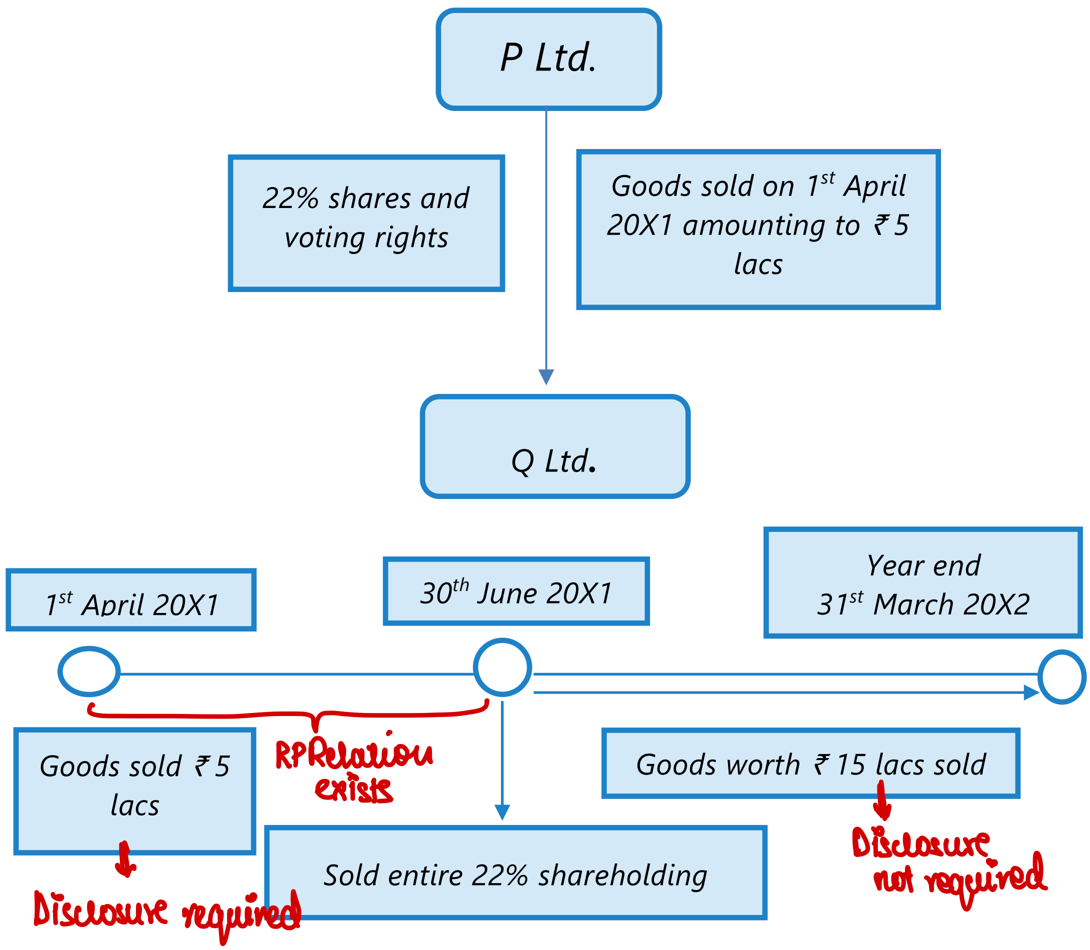


Illustration 9

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 20X1, P Ltd. sold certain goods to Q Ltd. amounting to Rs. 5 lacs*
- *On 30th June 20X1, P Ltd. sold its entire 22% stake in Q Ltd. (and hence the related party relationship ceased to exist after 30th June 20X1)*
- *However, P Ltd. continued supply goods to Q Ltd. subsequent to 30th June 20X1 (just like any other customer) and sold goods worth Rs. 15 lacs during 9-month period ended 31st March 20X2*
- *Consider 31st March 20X2 as the year-end date for P Ltd.*



Determine whether the transaction for the entire year (ending on 31st March 20X2) 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 20X1* (being sale of goods worth Rs. 5 lacs) are required to be reported / disclosed under AS-18.

Transactions entered into after 30th June 20X1 are **NOT required** to be disclosed under AS-18.

$N \xleftarrow[\text{KMP}]{\text{MD of N ltd.}} \quad \xrightarrow[\text{control (S.I. min)}]{\text{100\% shares}} G$

Illustration 10

Narmada Ltd. sold goods for ₹ 90 lakhs to Ganga Ltd. during financial year ended 31-3-20X1. The Managing Director of Narmada Ltd. owns 100% shares of Ganga Ltd. The sales were made to Ganga Ltd. at normal selling prices 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.**

TEST YOUR KNOWLEDGE

Multiple Choice Questions

1. *According to AS-18 Related Party Disclosures, which ONE of the following is not a related party of Skyline Limited?*

   (a) *A shareholder of Skyline Limited owning 30% of the ordinary share capital* SI

   (b) *An entity providing banking facilities to Skyline Limited in the normal course of business* ✗

   (c) *An associate of Skyline Limited*

   (d) *Key management personnel of Skyline Limited*

2. *Are the following statements in relation to related parties true or false, according to AS-18 Related Party Disclosures?*

   (A) *A party is related to another entity that it is jointly controlled by.* T

   (B) *A party is related to another entity that it controls.* T

	Statement (A)	Statement (B)
(a)	False	False
(b)	False	True
(c)	True	False
(d)	True	True

3. *Which of the following is not a related party as envisaged by AS-18 Related Party Disclosures?*

   (a) *A director of the entity* (MD)

   (b) *The parent company of the entity*

   (c) *A shareholder of the entity that holds 1% stake in the entity*

   (d) *The spouse of the managing director of the entity*

4. *According to AS-18 Related Party Disclosures, related party transaction is a transfer of resources or obligations between related parties – provided a price is charged for such transfer.*

   (a) True

   (b) False

anytime during the reporting period.

5. *According to AS-18 Related Party Disclosures, parties are considered to be related, if and only if at the end of 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.*

   (a) True

   (b) False

Theoretical Questions

6 *Who are related parties under AS 18? What are the related party disclosure requirements?* 5

7 *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?* → NOT CORRET

Statute
Regulator
Similar competing authority
↓
Confidential
↓
Only then exemption from disclosure.

8 *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?*

Scenario based Question

9. *Mr. Raj, a relative of key management personnel, received remuneration of ₹ 2,50,000 for his services in the company for the period from 1.4.20X1 to 30.6.20X1. On 1.7.20X1, he left the service of the company.*

   Should the relative be identified as at the closing date i.e. on 31.3.20X2 for the purposes of AS 18?

10. *X Ltd. sold goods to its associate company during the 1st quarter ended 30.6.20X1. 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.* → Only the transactions during the relationship → "Disclose"

11. *You are required to identify the related parties in the following cases as per AS 18:*

M —61%→ S ltd. —51%→ F ltd. ←49%— C

M Ltd. holds 61 % shares of S Ltd.

S Ltd. holds 51 % shares of F Ltd.

C Ltd. holds 49% shares of F Ltd.

M → S, F

S → M, F

F → S, M, C

C → F

(Give your answer - Reporting Entity wise for M Ltd., S Ltd., C Ltd. and F Ltd.)

ANSWERS/HINTS

Answers to the Multiple Choice Questions

1.	(b)	**2.**	(d)	**3.**	(c)	**4.**	(b)	**5.**	(b)

Answers to the Theoretical Questions

6. 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:

(i) The name of the transacting related party;

(ii) A description of the relationship between the parties;

(iii) A description of the nature of transactions;

(iv) Volume of the transactions either as an amount or as an appropriate proportion;

(v) Any other elements of the related party transactions necessary for an understanding of the financial statements;

STUDENT NOTES

QUESTION 3

Hanuman Ltd is a 100% subsidiary of Agnihotri Ltd. Which of the following are considered as Related Party Transactions for the purpose of Consolidated Financial Statements?

Answer:

Situation	Whether Related Party Transaction or not, for CFS
Salary paid to Employees of Hanuman Ltd. paid by H ltd.	*Salaries and Loans given to Employees are in the course of normal dealings of business* " No disclosure required "
Loans given to Employees of Agnihotri Ltd. not KMP	*Also, Employees are not considered as Related Party for an Entity* Loans given to employees (not KMPs) are in the ordinary course of business. Not considered RP.
Inter-Company Sales between Agnihotri Ltd and Hanuman Ltd.	*Holding and Subsidiary Companies are Related Parties, since ~~they are said to be under common control~~ for the purpose of Consolidated Fin. Statements. However, no disclosure is required for Inter-Company Sales between Holding and Subsidiary, in the Consolidated Fin. Statements. [Para 7]* because they are considered as one single co.
Loan given by Hanuman Ltd to Managing Director of Agnihotri Ltd. H Loan A ND KMP one	*Since, the Managing Director of Agnihotri Ltd directly or indirectly owns an interest in the voting power of the Reporting Enterprise that gives him control or significant influence over its subsidiary Hanuman Ltd, the loan given to him by Hanuman Ltd will be treated as a Related Party Transaction.* Disclosure is required as loan is given to KMP of the consolidated company.
Transfer of Asset by Agnihotri Ltd to Hanuman Ltd.	*Since, Holding and Subsidiary Companies are Related Parties as per Para 3(a), transfer of asset by Holding Company Agnihotri Ltd to its Subsidiary Hanuman Ltd will be considered as Related Party Transaction.*

Holding co. control Subs co.

Since both companies are treated as one for consolidated FS, intra-company transactions donot require separate disclosure in CFS.

However, in separate FS a disclosure will be needed.

Subs — L → Holding → MD (KMP)

Sep Disc ×

CA Tejas Suchak

STUDENT NOTES

QUESTION 4

KGF Ltd sold to RRR Ltd, goods having a Sale Value of ₹ 25 Lakhs during a Financial Year. Mr. Strength, the Managing Director and Chief Executive of KGF Ltd owns nearly 100% of the Capital of RRR Ltd. The Sales were made to RRR Ltd at the normal Selling Price of KGF Ltd. The Chief Accountant of KGF Ltd does not consider that these Sales should be treated any differently from any other sale made by the Company despite being made to a Controlled Company, because the sales were made at normal and, that too, at arm's length prices. Comment.

KGF ← MD/CEO KMP — 100% Cont (S.I min) → RRR

Sales = 25L

→ Disclosure is required of sale to RRR of 25L-

Answer:

Quote: *As per the provisions of AS- 18: Related Party Disclosures, Related Party Relationship covers the following relationships –*

(a) Enterprises that control the Reporting Enterprise,
(b) Enterprises that are controlled by the Reporting Enterprise, or
(c) Enterprises that are under common control with the Reporting Enterprise (this includes Holding Companies, Subsidiaries, and fellow Subsidiaries),

Further, AS- 18 is applicable irrespective of whether or not the transactions with related parties are made at arm's length prices.

Analysis: *Hence, in the given case, KGF Ltd has a Related Party Relationship with RRR Ltd since both the Companies are under the common control of a single person (Mr. Strength).*

Conclusion: *Hence, KGF Ltd should disclose the information required under AS-18 in relation to its Sales to RRR Ltd during the entire Financial Year.*

B ltd. ← 34% VP S.I. — HW — 100% Control (SI min) → PF

raw material supply → disclosure required.

STUDENT NOTES

QUESTION 5

A husband and wife are controlling 34% of voting power in Banarsi Limited. They have a separate Partnership Firm, which supplies the main Raw Material to the Company. The Management says that the above transaction need not be disclosed. How will you deal with the above situation?

of Banarsi ltd.

Answer:

Quote: *As per the provisions of AS- 18: Related Party Disclosures, the definition of Related Party Relationship covers "Enterprises owned by the Directors or Major Shareholders of the Reporting Enterprise."*

Further, Significant Influence is presumed to exist, if an investing party holds 20% or more of the voting power of the Enterprise (Such holding may be direct or indirect through Intermediaries).

AS- 18 requires disclosure if there have been transactions between Related Parties, irrespective of whether or not the transactions have been entered into at arm's length prices.

Analysis: *In this case, the individuals hold 34% of the voting power.*

Conclusion: *Hence have a significant influence. Disclosure is required as per AS..*

QUESTION 6 → Homework

Pawan Ltd owns 60% of the voting power of Jhumpi Ltd. Jhumpi Ltd in turn owns 70% of the voting interest in Rohan Ltd. Further, Pawan Ltd also directly owns 15% of the voting interest in Rohan Ltd. Would Pawan Ltd be deemed to have control over Rohan Ltd or would it only be considered as exercising significant influence?

Answer:

Quote: *As per the provisions of AS- 18: Related Party Disclosures,*

(a) If a Parent owns along with its Subsidiary more than one-half of the voting power in an enterprise, that Enterprise will be considered as a Related Party of the Parent, by virtue of the ability to control.

(b) As per AS- 18, Control includes ownership, directly or indirectly, of more than one-half of the voting power of another enterprise.

Analysis: *Pawan Ltd is a majority Shareholder (60%) in Jhumpi Ltd and it has control over it. Also, Pawan Ltd and Jhumpi Ltd, together are majority shareholders (15% + 70% = 85%) in Rohan Ltd. Thus, Pawan Ltd has indirect control over Rohan Ltd.*

Conclusion: *(a) In the given case, Pawan Ltd has the ability to control Rohan Ltd, based on the holding of more than one-half of the voting power.*

(b) Hence, Pawan Ltd has control over Rohan Ltd and not just significant influence.

STUDENT NOTES

QUESTION 7

Teja Ltd has two Non-Executive Directors on its Board. State whether AS -18 is applicable if –

(1) A, a Non-Executive Director is in a position to exercise significant influence by virtue of owning an interest in the voting power in the Company. → Disclosure required for any trans. that have taken place with RP.

(2) B, a Non-Executive Director does not enjoy the authority and responsibility for planning, directing, and controlling the activities of the Company.

Answer: B → not a KMP → no disclosure required.

Quote: *As per the provisions of AS- 18: Related Party Disclosures, AS- 18 applies to Non-Executive Directors as under:*

AS - 18 not applicable
a) A Non-Executive Director of a Company should not be considered as Key Management Person under AS- 18 by virtue of his merely being a Director, unless he has the authority and responsibility for planning, directing, and controlling the activities of the Reporting Enterprise. *(b) AS- 18 should not be applied in respect of a Non-Executive Director, even if he participates in the financial and/or operating policy decision of the Enterprise.* *(Note: Mere participation is different from authority to plan / direct / control)*

AS -18 applicable
A Non-Executive Director would be covered by AS- 18 if he is a Key Management Person, when - *(a) He has the authority and responsibility for planning, directing, and controlling the activities of the Reporting Enterprise, or* *(b) He is in a position to exercise control or significant influence by virtue of owning an interest in the voting power.*

Raman Ltd. MD KMP F S 100% → Firm

Job work = 2 lakh → Disclosure required.

STUDENT NOTES

QUESTION 8

A Firm of a Father and Son received ₹ 2 Lakhs towards job work done for Raman Ltd, during the year ended 31st March. The total Job Work Charges paid by Raman Ltd during the year are over ₹ 50 Lakhs. The father is a Managing Director of Raman Ltd having substantial holding. The Managing Director told the Auditor that since he is not involved in the activities of the Firm, and since the amount paid to it is insignificant, there is no need to disclose the transaction. He further contended that such a payment made in the last year was not disclosed. Is the M.D. right in his approach?

Answer:

Quote: *As per the provisions of AS- 18: Related Party Disclosures,*

(a) 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 decisions.

(b) As per AS- 18, 'Significant Influence' is said to exist in case the investing party has 20% or more voting power in the Enterprise.

Analysis: *In the above case, the Managing Director of Raman Ltd is a Partner in the Firm with his son, and the Firm has been paid ₹ 2 Lakhs as Job Work Charges. The Managing Director has a substantial holding in the Firm. The Managing Director is also a Key Management Personnel of Raman Ltd.*

Conclusion: *Hence, there is a Related Party relationship & transaction, requiring disclosure under AS- 18.*

Acharya —1 Chairman→ Anshul   Total = 12 BOD   Control of comp. of BOD → ×

1 BOD

QUESTION 9

Acharya Ltd acquired 12% voting power in Anshul Ltd. Acharya, being the single largest shareholder of Anshul, appoints the Chairman and one other Member of the Board of Directors of Anshul Ltd (out of a total of 12 Directors). These nominees of Acharya Ltd are not Directors of Acharya Ltd. By virtue of its representation on the Board (through two nominees) of Anshul Ltd, Acharya participates in the financial and operating policy decisions of the enterprise taken at the Board Meetings. Would Acharya be considered as exercising control over Anshul Ltd?

Control ×

Significant Influence exists.

Answer:

Quote: *As per the provisions of AS- 18: Related Party Disclosures, when an enterprise owns less than 20% voting power in the other enterprises there is no significant influence unless the contrary is proved.*

Analysis: *In this case, since the Shareholding is only 12%, Acharya Ltd does not have the ability to control Anshul Ltd. Also, there is no agreement or statute, which gives Acharya Ltd, the power to direct the policies of Anshul Ltd*

Conclusion: *In the above case, being the single largest shareholder, Acharya Ltd participates in the financial and operating policy decisions of Anshul Ltd. So, it is clearly demonstrated that Acharya has significant influence over Anshul Ltd. Therefore, Anshul Ltd is a Related Party of Acharya Ltd, even if 20% voting power is not satisfied.*

QUESTION 10

Abhishek Ltd owns 30% of the Equity Capital of Boom Ltd. Boom Ltd in turn owns 35% of the Equity Capital of Chunnu Ltd, and 40% of Equity Capital in Dev Ltd. Answer the following questions

A —30%→ B —35%→ C; B —40%→ D

(1) Is Boom Ltd a Related Party to Abhishek Ltd? → Assoc

(2) Is Chunnu Ltd a Related Party to Abhishek Ltd? → No : Assoc of Assoc

(3) Are Chunnu Ltd and Dev Ltd Related Parties? → No : Common Assoc. not related.

Answer:

1) *Associates and Joint Ventures of the Reporting Enterprise are Related Parties. Since Abhishek Ltd holds more than 20% of the voting power in Boom Ltd, by virtue of this, it has substantial interest and significant influence in Boom Ltd. So, Boom Ltd is an Associate, and hence is Related Party to Abhishek Ltd.*

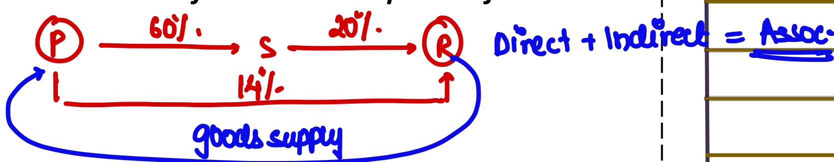
2) *An Associate of an Associate is not a Related Party. Only in the case of a Holding Company, a Subsidiary of a Subsidiary (Sub-Subsidiary) also becomes a Related Party.*

3) *Chunnu Ltd and Dev Ltd are Co-Associates. Co-Subsidiaries become Related Parties because of common control. In the case of Co-Associates, this common control is missing, and therefore they are not Related Parties.*

STUDENT NOTES

QUESTION 16

Pawan Ltd. has 60% voting right in Sonu Ltd. Sonu Ltd. has 20% voting right in Ravi Ltd. Also, Pawan Ltd. directly enjoys the voting right of 14% in Ravi Ltd. Ravi Ltd. is a listed company and regularly supplies goods to Pawan Ltd. The management of Ravi Ltd. has not disclosed its relationship with Pawan Ltd. How would you assess the situation from the viewpoint of AS- 18 on Related Party Disclosures?



Answer:

Quote: *As per the provisions of AS- 18: Related Party Disclosures, defines related party as one that has at any time during the reporting period, the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions. Here, Control is defined as ownership directly or indirectly of more than one-half of the voting power of an enterprise; and Significant Influence is defined as participation in the financial and/or operating policy decisions of an enterprise but not control of those policies.*

Analysis & Conclusion:

1. *Pawan Ltd. Has a direct economic interest in Ravi Ltd to the extent of 14%, and through Sonu Ltd. in which it is the majority shareholders, it has further control of 12% in Ravi Ltd. (60% of Sonu Ltd's 20%). These two taken together (14% + 12%) make the total control of 26%.*

2. *In the present case, the control of Pawan Ltd. in Ravi Ltd. directly and through Sonu Ltd., does not go beyond 26%. However, as per Para 12 of AS- 18, significant influence may be exercised as an investing party (Pawan Ltd.) holds, directly or indirectly through intermediaries 20% or more of the voting power of Ravi Ltd.*