

First Notes



SEBI issues clarification on certain provisions pertaining to RPTs

29 April 2022

First Notes on

- Financial reporting
- Corporate law updates
- Regulatory and other information**
- Disclosures

Sector

- All**
- Banking and insurance
- Information, communication, entertainment
- Consumer and industrial markets
- Infrastructure and government

Relevant to

- All**
- Audit committee
- CFO
- Others

Transition

- Immediately**
- Within the next three months
- Post three months but within six months
- Post six months
- Forthcoming requirement

Background

On 9 November 2021, the Securities and Exchange Board of India (SEBI) notified certain amendments to the SEBI (Listing Obligations and Disclosure Requirement) Regulations, 2015 (Listing Regulations) with regard to provisions pertaining to Related Party Transactions (RPTs) (amendments). Subsequently, on 22 November 2021, SEBI specified some additional disclosure requirements to be provided by listed entities with regard to RPTs. The amendments in notifications dated 9 November 2021 and 22 November 2021 mainly relate to the following areas:

- Widening the definition of related parties and Related Party Transactions (RPT)
- Amendments have been made to the audit committee’s approval mechanism
- Amendments have been made to the materiality threshold, thus broadening the number of RPTs requiring shareholders’ approval
- Enhanced disclosures are required to be made to the stock exchange, the audit committee and to shareholders¹.

The amendments are applicable in a phased manner, with certain amendments coming into effect from 1 April 2023 and remaining amendments are applicable from 1 April 2022.

New development

Based on representations received from listed entities and industry bodies, SEBI, on 30 March 2022 and 8 April 2022 issued certain clarifications and guidance in relation to the amendments (clarifications).

These circulars are applicable from 1 April 2022.

In this issue of first notes, we aim to provide an overview of the clarifications issued by SEBI.



¹For further information on these amendments, please refer our first notes issued on 24 December 2021.

Overview of clarifications issued by SEBI

A. Requirement for shareholders’ approval post 1 April 2022

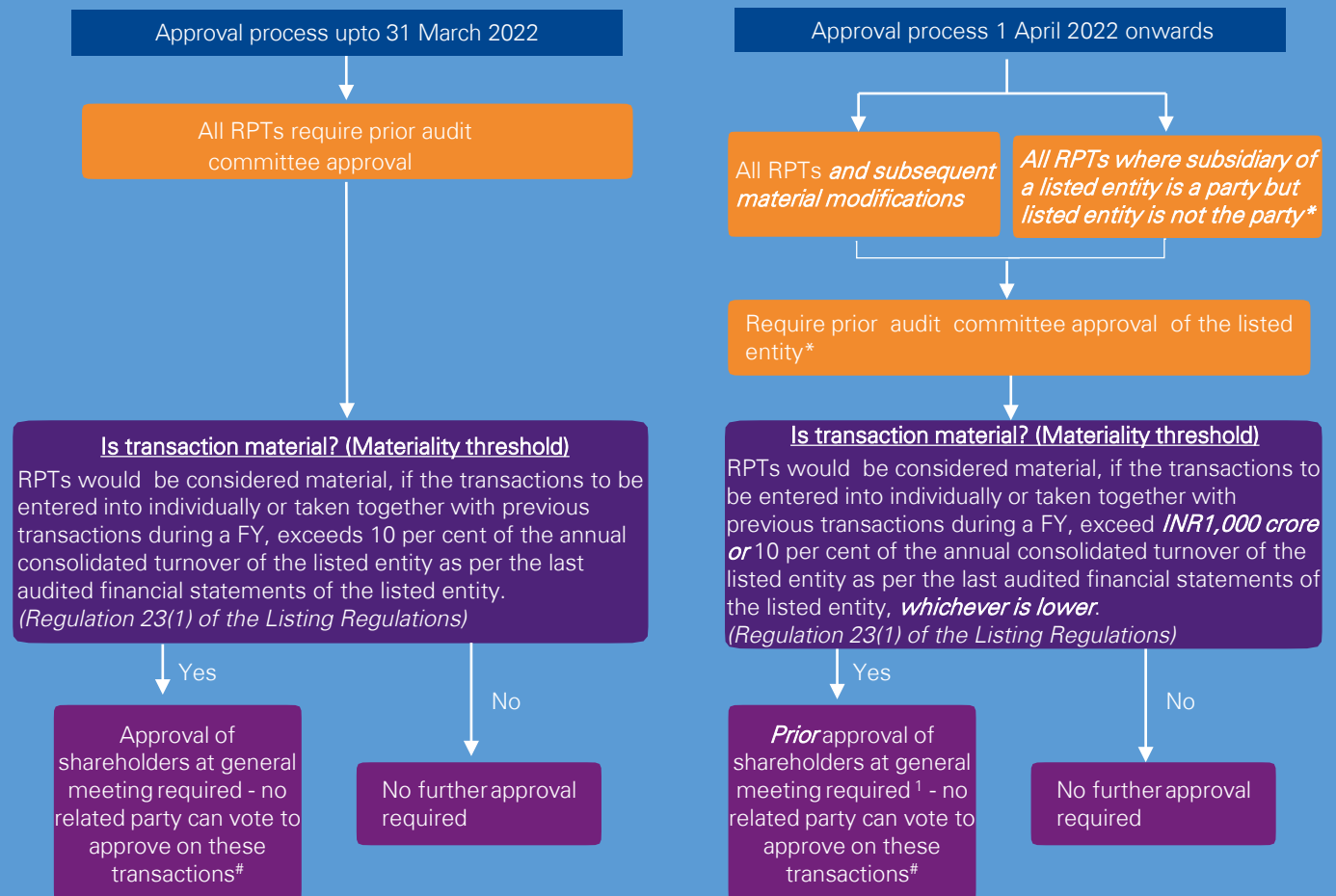
a. Shareholders’ approval where prior approval of audit committee’s has been obtained

Background

The amendments to the Listing Regulations have enhanced the scope for an audit committee and shareholders’ approval for RPTs, including enhancing the materiality threshold. An overview of the approval mechanism prior to the amendment and post the amendment is given in the chart below.

Overview of the approval process for RPTs prior to and post amendments is given below:

Approval process for RPT upto 31 March 2022 and from 1 April 2022 under the Listing Regulations



Notes

- #No approval is required in case of transactions entered into
- between two government companies
 - between a holding company and its wholly-owned subsidiary whose accounts are consolidated with such holding company and placed before the shareholders at the general meeting for approval

Notes

- *When the value of RPT whether entered individually or taken together with previous transactions during a FY exceeds
- 10 per cent of the annual consolidated turnover as per the last audited financial statements of the listed entity (effective 1 April 2022)
 - 10 per cent of the annual standalone turnover, as per last audited financial statements of the subsidiary (effective 1 April 2023)

- #No approval is required in case of transactions entered into
- between two government companies
 - between a holding company and its wholly-owned subsidiary whose accounts are consolidated with such holding company and placed before the shareholders at the general meeting for approval
 - 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 approval.

¹Prior approval of the audit committee and shareholders’ of the listed entity would not be required for RPTs where listed subsidiary is a party but the listed entity is not a party, if the subsidiary is subject to compliance with Regulation 23 and Regulation 15 (2) of the Listing Regulations. For RPTs of unlisted subsidiaries of a listed subsidiary, prior approval of the audit committee of the listed subsidiary would suffice.

Source: KPMG in India’s analysis, 2022 read with the Listing Regulations and SEBI circular dated 9 November 2021

Clarifications issued by SEBI

SEBI considered two scenarios where RPTs were approved by the audit committee prior to 1 April 2022.

1

RPT has been approved by the audit committee and shareholders prior to 1 April 2022.

No requirement to seek fresh approval from the shareholders post 1 April 2022

2

RPT has been approved by the audit committee prior to 1 April 2022. RPT continues beyond such date and becomes material as per the revised materiality threshold (thus requiring shareholder approval)

RPT should be placed before the shareholders in the first general meeting held after 1 April 2022 in accordance with Regulation 23(8) of Listing Regulations²

Source: KPMG in India's analysis, 2022 read with the Listing Regulations and SEBI circular dated 30 March 2022

b. Shareholders' approval required where omnibus approval of audit committee obtained**Background**

As per Regulation 23(3) of the Listing Regulations, an audit committee of a listed entity may grant omnibus approval for an RPT proposed to be entered into by a listed entity, subject to certain prescribed conditions.

Further, as per Regulation 23(4) of the Listing Regulations, all material RPTs and subsequent material modifications as defined by the audit committee, are required to obtain a prior approval of shareholders through a resolution.

Clarification issued by SEBI

SEBI reiterated that an RPT for which the audit committee has granted omnibus approval should continue to be placed before the shareholders if it is material in terms of Regulation 23(1)³ of the Listing Regulations.

Where a prior approval of shareholders was not obtained for such transactions prior to 1 April 2022, it could be obtained in the first general meeting held after 1 April 2022. In order to facilitate listed entities to align their processes to conduct AGMs and obtain omnibus shareholders' approval for material RPTs, SEBI through its circular dated 8 April 2022 issued another clarification. Shareholders' approval of omnibus RPTs approved in an AGM would be valid upto the date of the next AGM for a period not exceeding 15 months.

However, where omnibus approvals for material RPTs was obtained from shareholders in general meetings other than AGMs, the validity of such omnibus approvals would not exceed one year.

C. Enhanced disclosures to shareholders

On 22 November 2021, SEBI issued a circular which *inter alia* prescribed additional information to be included in the notice being sent to shareholders seeking approval for proposed RPT. The circular is applicable from 1 April 2022. The information prescribed in the circular included:

- a. **Details of transaction**, including the material terms, tenure, value of the proposed transactions
- b. **Details of the related party**, name of the related party and its relationship with the listed entity or its subsidiary, including nature of its concern or interest (financial or otherwise)
- c. **Transaction value as a percentage of turnover**

²As per Regulation 23(8) of the Listing Regulations, all existing material related party contracts or arrangement entered into prior to the date of notification of these regulations and which may continue beyond such date shall be placed for approval of the shareholders in the first General Meeting subsequent to notification of these regulations.

³As per Regulation 23(1) of the Listing Regulations, 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, exceeds INR1,000 crore or ten percent of the annual consolidated turnover of the listed entity as per the last audited financial statements of the listed entity, whichever is lower.

- d. **Transaction relating to loans, Inter-Corporate Deposits (ICDs), advances or investments**, specific information is required to be disclosed where transaction relates to loans, ICDs, advances, etc.
- e. **Justification** as to why the RPT is in the interest of the listed entity
- e. A copy of the **valuation report or external party report**, if any such report has been relied upon
- f. **Percentage of the counter-party's annual consolidated turnover** that is represented by the value of the proposed RPT, on a voluntary basis
- g. Any **other information** that may be relevant

Clarification

SEBI stated that listed entities should endeavor to provide relevant and detailed information to enable and empower shareholders for taking a view whether the terms and conditions of the proposed RPT are not unfavorable to the listed entity, compared to the terms and conditions, had similar transaction been entered into between two unrelated parties.

The circular also clarified that the information so provided should not be limited to the information specified in the SEBI circular dated 22 November 2021.

Our comments



With most of the amendments pertaining to RPTs being applicable from 1 April 2022, the SEBI's clarification reiterates the need to obtain shareholders' approval for all material transactions entered into by the listed entity. Some of the key clarifications issued include:

- **Listed entities have been given time till general meeting to obtain shareholders' approval:** According to the revised approval mechanism for RPTs prescribed in the Listing Regulations, a **prior approval** of shareholders is required for all material RPTs. However, SEBI has now provided listed entities time till the first general meeting to be held post 1 April 2022 to obtain such approvals.

As per the Companies Act, 2013 (2013 Act), companies are required to hold their annual general meetings within six months from the end of the financial year⁴. Thus, listed entities have some time at hand to determine the 'material' RPTs that will be transacted during the financial year, for which they need to obtain shareholders' approval.

- **Shareholders' approval required for transactions receiving omnibus approval:** As per the Listing Regulations and the 2013 Act, an audit committee of a listed entity is permitted to provide an omnibus approval to RPTs proposed to be entered into by the entity. With the clarifications issued by SEBI dated 30 March 2022 and 8 April 2022, entities that have obtained omnibus approvals of the audit committee prior to 1 April 2022, will need to get an omnibus shareholders' approval for material RPTs in the AGM held post 1 April 2022. Such shareholders' approval would be valid till the next AGM, but not for a period exceeding 15 months. However, where the omnibus approval of shareholders is obtained in a general meeting, which was not an AGM, the validity of such approval would be only 12 months. It is important to note that the validity of omnibus approval of the audit committees still remains 12 months. Accordingly, an omnibus audit committee's approval would need to be renewed on an annual basis. In future when there is a material modification to the terms of a contract for which an omnibus approval was obtained earlier then the entity would need to take a fresh approval of the audit committee and of the shareholders, as if it were a new transaction.
- **Approval of the Board of directors:** As per the Listing Regulations, an approval of the Board of Directors is not required for RPTs. However, as per the 2013 Act, a board's approval is required for RPTs if they are not in the ordinary course of business or are not at an arm's length. Entities should consider the provisions of both, the 2013 Act and the Listing Regulations while seeking approvals for RPTs.

⁴ As per Regulation 44(5) of the Listing Regulations, the top 100 listed entities by market capitalisation need to hold their AGMs within five months of the date of closing of the financial year.

- **Enhanced disclosures to shareholders:** SEBI highlighted the importance of transparency, accountability and shareholder empowerment as the bedrock of robust corporate governance. It has urged listed entities to comply with the spirit of law and provide relevant and detailed information to shareholders to enable them to take an informed decision while approving the RPTs. Thus, the explanatory statement contained in the notice sent to the shareholders for seeking approval for an RPT should contain detailed information about the RPT and not be restricted to the information prescribed in the circular issued by SEBI on 22 November 2021 or that prescribed in the 2013 Act.
- **Clarifications awaited on some more aspects:** While the clarifications issued by SEBI are a welcome step, further clarifications are required with regard to certain provisions pertaining to the amendments, such as:
 - The definition of related parties has been widened to include any person or entity having shareholding of 20 per cent or more (from 1 April 2022) or 10 per cent or more (from 1 April 2023) in the listed entity as related parties. SEBI should provide clarification on whether routine transactions entered into by a listed entity with its institutional investors (such as banks, insurance companies, etc.) having the said shareholding in the listed entity require appropriate approvals and disclosures
 - The definition of RPTs has been widened to include a transaction between a listed entity or any of its subsidiaries, and any other person or entity, the purpose and effect of which is to benefit a related party of the listed entity or any of its subsidiaries (this is effective 1 April 2023). SEBI needs to clarify what would be considered as 'purpose and effect of which is to benefit', and whether routine transactions would also be covered in this definition.



The Bottom line

Through its circular, SEBI has reiterated the importance of empowering shareholders in terms of reviewing RPTs and making comprehensive information available to shareholders for performing such review. While the industry has issued representations to SEBI for increasing the materiality threshold for seeking shareholders' approval, SEBI has stood its ground, recapitulating the importance of a close scrutiny of RPT by both, the audit committee and shareholders.

Listed entities have been provided time till the first general meeting to be held post 1 April 2022 to obtain shareholders' approval on all material transactions. Entities should use this time to adequately identify all RPTs planned during the year and obtain shareholders' approvals for the ones falling within the materiality threshold.



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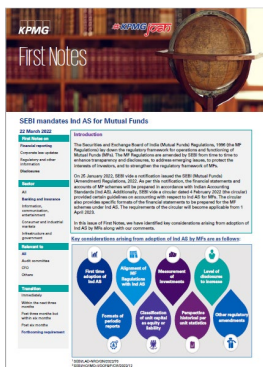
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Issue no. 68 – March 2022

The topics covered in this issue are:

- SEC proposes rules for climate-related amendments
- Property, plant and equipment – Directly attributable expenses
- Regulatory updates



SEBI mandates Ind AS for Mutual Funds

22 March 2022

On 25 January 2022, SEBI vide a notification issued the SEBI (Mutual Funds) (Amendment) Regulations, 2022. As per this notification, the financial statements and accounts of MF schemes will be prepared in accordance with Indian Accounting Standards (Ind AS). Additionally, SEBI vide a circular dated 4 February 2022 (the circular) provided certain guidelines on accounting with respect to Ind AS for MFs. The circular also provides specific formats of the financial statements to be prepared for the MF schemes under Ind AS. The requirements of the circular will become applicable from 1 April 2023.

In this issue of First Notes, we have identified key considerations arising from adoption of Ind AS by MFs along with our comments.

Voices on Reporting



KPMG in India is pleased to present Voices on reporting (VOR) – a series of knowledge sharing calls to discuss current and emerging issues relating to financial reporting.

On 7 April 2022, KPMG in India held a VOR webinar to discuss key financial reporting and regulatory matters that are expected to be relevant for shareholders. The webinar covered key updates for the quarter ended 31 March 2022 and certain important updates relevant for financial year 2022-23.

To access the presentation and recording, please click [here](#).



VOR quarterly publication for the year ended 31 March 2022

Annual updates publication (for the year ended 31 March 2022) provides a summary of key updates from the Securities and Exchange Board of India (SEBI), the Ministry of Corporate Affairs (MCA), the Institute of Chartered Accountants of India (ICAI) and the Reserve Bank of India (RBI).

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