

RELATED PARTY TRANSACTION - MEANING

A “Related Party” in a broad sense refers to any transaction entered into by a Company with its subsidiaries, associates, directors, their relatives, through joint ventures, etc. It is hence any transaction by a person or company who may be in a position to exercise any significant influence on such a transaction being a contract or arrangement.

The terminology ‘Related Party Transaction’ is a new addition to the Companies Act, 2013. It is dealt in Section 188 of the 2013 Act. It lays down a prohibition to enter into any transaction by way of any contract or arrangement, without the consent of the Board of directors, with a related party with respect to sale or purchase of goods and materials, selling/disposing or buying of any property, leasing of property, availing or rendering services, appointment of agent for purchase/sale of goods/materials/services, appointment of related party in the company or its subsidiary and underwriting the subscription of securities/derivatives.

Related Party in this context can be understood by looking into Section 2(76) of the 2013 Act. It lays down the following to be a ‘related party’:

- i. *a director or his relative¹*
- ii. *a key managerial personnel or his relative*
- iii. *a firm, in which a director, manager or his relative is a partner*
- iv. *a private company in which a director or manager or his relative is a member or director*
- v. *a public company in which a director or manager is a director or holds along with his relatives, more than two per cent of its paid-up share capital*
- vi. *any body-corporate whose Board of Directors, managing director or manager is accustomed to act in accordance with the advice, directions or instructions of a director or manager*
- vii. *any person on whose advice, directions or instructions a director or manager is accustomed to act*
Provided that nothing in sub-clauses (vi) and (vii) shall apply to the advice, directions or instructions given in a professional capacity:
- viii. *any company which is*
 - a. *a holding, subsidiary or an associate company of such company*
 - b. *a subsidiary of a holding company to which it is also a subsidiary*
- ix. *such other person as may be prescribed.*

The Companies Act, 1956 did not have the terminology “Related Party Transaction” anywhere in the Act. However a bare reading of the 1956 Act along with the 2013 Act brings about certain similarities between both the Legislations.

¹ Section 2(77) of the Companies Act, 2013 and Section 6 of the Companies Act, 1956 and define relative as; members of a Hindu Undivided Family, husband/wife, and a person related to another in such manner as may be prescribed

A glance at Section 297, 299, 300 and 314 is necessary in order to understand the concept of “Related Party Transactions” as it existed in the 1956 Act in a different nomenclature.

The 1956 Act lays down a similar concept of related persons through the terminology “interest”. It adjudges the “Related Party Transactions” by way of interest that a director possesses in any contract or arrangement.

Section 297 of the 1956 Act lays down the “*Board’s sanction to be required for certain contracts in which particular directors are interested*”.

Clause (1) of the section prohibits:

- a director or his relative
- firm in which such a director or relative is a partner
- any other partner in such a firm
- or a private company of which the director is a member or director

From entering into any contract without consent of the Board of Directors of a company, concerning:

- sale, purchase or supply of any goods, materials or services
- underwriting the subscription of any shares in, or debentures of, the company

The section further provides for companies having a paid up share capital of above Rs. 1 Crore to enter into such contracts only with the prior approval of the Central Government.

Thus an apparent difference can be seen under certain provisions of the 1956 Act in comparison to the 2013 Act previously stated. The 2013 Act has defined related persons so as to make the concept distinctively clear. It has further broadened its ambit to include certain persons who might not hold any position in the body yet exercise authoritative command through advice, directions or instructions as under sub-clause (vi) and (vii) of 2(76) to be considered as a related person for the said purpose.