Journal of
Taxation and Regulatory Framework

Volume 6, Issue 1, 2023
(January-June)
DOI (Journal): 10.37591/JTRF

http://lawjournals.celnet.in/index.php/jtrf/index

Case Study JTRF

SEBI vs. R.T. Agro (P.) Ltd.: Critical Analysis in RPT

Monika Jain*

Abstract

Related party transactions are those that take place between a business and its own management, directors, primary owners, or affiliates. These transactions, which are varied and frequently complex, provide a problem for corporate governance. SEBI was unjustified in punishing a Company by adopting an overly technical interpretation of the legislation on related party transactions. The Securities and Exchange Board of India vigorously regulates and oversees the Indian financial markets. However, there have been other instances in recent years where SEBI's enforcement measures have been questioned. This important decision highlights the value of balanced regulatory monitoring and the necessity to guard against regulatory authorities going beyond their authority. This study launches related party transactions as a topic for financial research. These transactions are efficient transactions that satisfy a company's logical economic requirements while creating conflicts of interest that jeopardise management's duty to shareholders and directors' oversight responsibilities. Regulations regulate these kinds of transactions and stop their misuse. This study looks at the effects of stricter regulations that were implemented in India for listed businesses' RPT disclosure.

Keywords: Related party transactions, corporate governance, Indian companies

INTRODUCTION OF THE CASE: SECURITIES AND EXCHANGE BOARD OF INDIA VS. R.T. AGRO (P.) LTD.

Allegations of failure to comply with rules governing transactions between related parties are at the centre of the case SEBI vs. R.T. Agro (P.) Ltd. Agro-processing and trading business R.T. Agro (P.) Ltd. is based in India. R.T. Agro the SEBI, the organisation in charge of overseeing related party transactions in the Indian stock markets, accused Agro of violating the regulations [1]. Transactions involving a firm and its relatives, directors, and other important executive individuals are referred to as related party transactions [2]. These transactions may not always be conducted fairly and may result in conflicts of interest. Related party transactions are governed by rules and standards set forth by SEBI in an effort to maintain transparency and safeguard the interests of minority shareholders. R.T. Agro was accused by SEBI of failing to get the appropriate shareholder disclosures and board of directors' approval before engaging in certain related party activities. Due to R.T. Agro's non-compliance with its rules and regulations, SEBI fined the company money [3].

***Author for Correspondence**
Monika Jain
E-mail: advmonikajain@gmail.com

Senior Advocate Delhi High Court, Sher Shah Road, New Delhi, India

Received Date: July 11, 2023
Accepted Date: August 09, 2023
Published Date: August 21, 2023

Citation: Monika Jain. SEBI vs. R.T. Agro (P.) Ltd.: Critical Analysis in RPT. Journal of Taxation and Regulatory Framework. 2023; 6(1): 15–19p.

Issues of this Case

The SEBI Regulations, 2015, were evidently out of order by R.T. Agro. These rules improve listed firms' corporate governance, transparency, and accountability. According to SEBI, R.T. Agro disregarded the regulations' provision that linked party transactions must first receive board of director permission before proceeding. The business was charged with failing to fully inform its shareholders of these transactions. Due to these acts, R.T. Agro was penalised financially by SEBI for violating the rules.

The Supreme Court's Verdict

When SEBI challenged the fine before the Supreme Court of India, R.T. Agro claimed that SEBI had taken an unduly technical interpretation of the law governing related party transactions. The business argued that its actions had not been motivated by fraud and had not harmed its shareholders. In its decision, the Supreme Court recognised the need to strike a balance between regulatory scrutiny and the promotion of an environment that is favourable to business [4]. According to the Court, SEBI's fixation on strict adherence to procedural formalities in this case was not warranted because it ignored the substance of the transactions or any potential fraudulent purpose. The Court emphasised that laws should be balanced in their interpretation and application, taking into account the underlying goal and impact of related party transactions [5]. The SEBI vs. R.T. Agro (P.) Ltd. emphasises the necessity for regulatory authorities to employ their powers wisely, putting substance over just following procedures. It establishes a precedent for regulatory authorities to evaluate related party transactions without getting too hung up on details and instead take the object and purpose of regulations into account [6].

Supreme Court's Ruling in Securities and Exchange Board of India vs. R.T. Agro (P.) Ltd

SEBI vs. R.T. Agro (P.) Ltd. decision by the Supreme Court addressed SEBI's accusations that R.T. Agro has broken the related party transaction restrictions. In its decision, the Court ruled that SEBI's punishment of the corporation was unlawful because the regulatory body had adopted an overly technical interpretation of the statute. When interpreting and executing legislation, the Supreme Court emphasised the necessity for a fair approach, particularly when there can be serious repercussions for non-compliance [7].

The Court acknowledged the crucial part that regulatory bodies like SEBI play in safeguarding investor interests and preserving market integrity. It also issued a warning against using regulatory authority excessively or unjustly, which might potentially hinder legal business operations and deter entrepreneurship. The Court stated that SEBI's emphasis on strict adherence to procedural formalities in this case was unreasonable given the nature of the related party transactions and the lack of fraudulent intent [8]. It was emphasised that the rules governing related party transactions are intended to safeguard minority shareholders and stop unfair business practises. While transparency and accountability are essential, a narrow focus on procedural requirements without taking into account how the legislation will really affect shareholders or their interests could have unforeseen repercussions. The Supreme Court emphasised in its ruling that content should take precedence over form when assessing related party transactions [9]. While regulatory authorities should not unnecessarily burden legitimate commercial transactions with onerous procedural procedures, the restrictions are meant to prevent misuse and promote fairness. The Court understood the value of striking a balance between maintaining regulatory control and promoting an atmosphere that encourages innovation and economic growth [10]. The judgement in SEBI vs. R.T. Agro (P.) Ltd. has wider repercussions for regulatory agencies in India. It serves as a reminder to regulators to use caution while exercising their authority and to stay away from the minutiae in favour of focusing on the intent and goals of the legislation. It highlights the requirement to pay attention to the impact and content of related party transactions while following the fundamental rules of corporate governance and shareholder protection [11].

The decision of the Supreme Court in this case highlights the significance of a balanced regulatory environment and guards against regulatory excess that can obstruct legal commercial activity. It establishes a precedent for regulatory bodies to assess related party transactions fairly and comprehensively, encouraging accountability and openness while fostering an environment that is favourable for business and economic progress [12].

Section 188 related party transactions: (1) No corporation shall engage into any agreement or contract with a related party with respect to without the consent of the Board of Directors given by resolution at a meeting of the Board and subject to any conditions that may be required.

a. Sale, purchase or supply of any goods or materials;

b. Selling or otherwise disposing of, or buying, property of any kind;
c. Leasing of property of any kind;
d. Availing or rendering of any services;
e. Appointment of any agent for purchase or sale of goods, materials, services or property;
f. Such related party's appointment to any office or place of profit in the company, its subsidiary company or associate company; and
g. Underwriting the subscription of any securities or derivatives thereof, of the company [13].

With the caveat that, in the case of a business with a paid-up share capital of not less than such an amount, or transactions exceeding such sums, no contract or arrangement may be entered into without the prior authorization of the company by a resolution. Furthermore, if a member of the company is a related party, that person may not vote on the resolution to authorise any agreement that the firm may engage into.

Furthermore, save for transactions that are not on an arm's length basis, nothing in this sub-section shall apply to any transactions that the corporation enters into in the normal course of business [14].

2(zc) "related party transaction" means a transfer of resources, services or obligations between a listed entity and a related party, regardless of whether a price is charged and a "transaction" with a related party shall be construed to include a single transaction or a group of transactions in a contract: Provided that this definition shall not be applicable for the units issued by mutual funds which are listed on a recognised stock exchange(s) [15].

No related party may vote to approve any contract or arrangement in which he is a related party, according to Section 188 of the Companies Act and Regulation 23(7) of the LODR Regulations. We determine that the appellants did not violate any of the aforementioned explicit provisions in Section 188 of the Companies Act and Regulation 23 of the LODR Regulations. The AO committed an error in holding that they had violated Regulation 23 of the LODR Regulations [16].

Substance is More Important than Form

In many fields of law and commerce, the idea of substance over form is crucial. It emphasises the need of taking into account a situation's or transaction's fundamental nature or economic reality as opposed to just concentrating on its formal or technical features. For a number of reasons, this principle is extremely significant in legal, financial, and regulatory contexts [17].

- Accurate Transaction Representation.
- Justice and Equity.
- Avoiding Regulatory Arbitration.
- Economic efficiency.
- Flexibility and innovation.
- Efficient risk assessment is all important [18].

In conclusion, the idea of content over style is crucial in a variety of legal, financial, and regulatory contexts. Transparency, justice, equity, economic efficiency, and efficient risk management are all supported by giving priority to the genuine economic substance of transactions. It strikes a balance between the need to maintain regulatory monitoring and the promotion of a supportive business environment, ensuring that laws and regulations fulfil their intended functions while enabling legal company operations and growth [19].

IMPLICATIONS FOR REGULATORY AUTHORITIES

Balanced Regulatory Approach

- Risk-Based Regulation.
- Adaptive Regulations.

- Preventing Regulatory Arbitrage.
- Stakeholder for regulatory agencies.
- A Balanced Approach to Regulation.
- Regulation based on risk.
- Adjustable Rules.
- Avoiding Regulatory Arbitration.
- Engagement of Stakeholders and Transparency.
- Compliance Advice and Education [20].

In general, the idea of substance above form pushes regulatory bodies to take a more comprehensive and practical approach to regulation. Authorities can improve the efficiency of their monitoring, advance justice and openness, and foster an atmosphere that fosters the growth of legal economic activity by concentrating on the substance of transactions [21]. In general, the idea of substance above form pushes regulatory bodies to take a more comprehensive and practical approach to regulation. Authorities can improve the efficiency of their monitoring, advance justice and openness, and foster an atmosphere that fosters the growth of legal economic activity by concentrating on the substance of transactions [22].

CONCLUSION

The need of maintaining a balanced regulatory environment is emphasised by the Supreme Court's decision in SEBI vs. R.T. Agro (P.) Ltd. Although the Court's decision emphasises the need to avoid regulatory overreach and avoid overly technical interpretations of the law, SEBI's role is crucial for protecting investor interests [23]. The case sets a standard for how regulatory agencies should assess related party transactions, taking into account the underlying substance rather than becoming bogged down in formalities. By doing this, regulators can encourage openness, responsibility, and a favourable business environment, so, promoting economic growth and safeguarding the interests of investors [24]. The revisions to the Listing Regulations are a welcome move towards improving corporate governance because they aim to examine and reinforce the regulatory standards relevant to RPTs done by listed businesses in India [25]. The regulatory adjustments would strengthen safeguards for minority shareholders' interests in major corporations and increase openness in their favour. By importing a wider meaning to related party and RPTs, SEBI has increased the field of its scan to keep an eye over many entities and transactions of the listed entities as well as their unlisted subsidiaries [26]. Due to this requirement for greater transparency in their interactions with parties that might be regarded as related parties, listed entities and their subsidiaries will also have to do so. However, what remains to be seen is the change in the current regulatory framework for unlisted companies, which the legislature may bring in order to harmonize the framework under the Listing Regulations and the Companies Act [27].

REFERENCES

1. SEBI vs. R.T. Agro (P.) Ltd civil appeal 2957, 2022.
2. ICSCI Guidance Note on Related Party Transactions, pf.7 of 100.
3. CFA Society India. (2020). 2019-2020 ANNUAL REPORT serving the community by promoting Financial Literacy CFA Society India, promoting financial literacy to the community. [Online] Available from: https://cfasocietyindia.org/wp-content/uploads/Media-Uploads-Regulatory-Disclosures/IAIP-AGM-2019-20/IAIP-Annual-report2019-20_Annual-report.pdf.
4. Supra n1.
5. Ibid.
6. Ibid.
7. Organisation for Economic Co-operation and Development. Related Party Transactions and Minority Shareholder Rights. Paris: OECD Publishing; 2012. doi:10.1787/9789264168008-en.
8. ICSI. SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015. A Referencer SEBI (LODR) Series – Debt Securities. New Delhi: The Institute of Company Secretaries of India (ICSI); 2016.

9. Indian Accounting Standard (Ind AS) 24 Related Party Disclosures contents paragraphs objective 1 scope 2-4b purpose of related party disclosures 5–8 definitions 9–12 disclosures All entities 13–24A Government-related entities 25–27 illustrative examples appendix 1 Comparison with IAS 24, Related Party Disclosures. [Online]. [cited 2023 Aug 9]. Available from: https://www.mca.gov.in/Ministry/pdf/Ind_AS24.pdf
10. Shrimi Choudhary. (2020 Feb 21). SEBI Probe Finds Violation of Listing and Disclosure Norms by Sun Pharma. [Online]. Business Standard.
11. Ibid
12. SEBI. (2020). Report of the Working Group on Related Party Transactions. [Online]. SEBI. [cited 2023 Aug 9]. Available from: https://www.sebi.gov.in/reports-and-statistics/reports/jan-2020/report-of-the-working-group-on-related-party-transactions_45805.html
13. Section 188(1) of the Companies Act.
14. Regulation 2(zc) of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.
15. Section 188 (2) (zc).
16. Section 188 of the Companies Act and Regulation 23(7).
17. Afza T, Nazir MS. Role of Institutional Shareholders' Activism in Enhancing Firm Performance: The Case of Pakistan. Glob Bus Rev. 2015; 16(4): 557–570.
18. Khan A, Yusof Z. Terrorist economic impact evaluation (TEIE) model: the case of Pakistan. Qual Quant. 2017; 51(3): 1381–1394.
19. Williams MP, Taylor DW. Measuring and Explaining the Extent of Corporate Propping Transactions: Evidence from China. Global Review of Accounting and Finance. 2014; 5(1): 76–92.
20. Javaid F, Saboor A. Impact of Corporate Governance index on Firm Performance: evidence from Pakistani manufacturing sector. Journal of Public Administration and Governance (JPAG). 2015; 5(2): 1–21.
21. Gordon EA, Henry E. Related party transactions and earnings management. SSRN Electronic Journal. 2005.
22. Amzaleg Y, Barak R. Ownership Concentration and the Value Effect of Related Party Transactions (RPTs). J Mod Acc Aud. Feb 2013; 9(2): 239–55.
23. Kohlbeck M, Mayhew BW. Valuation of firms that disclose related party transactions. J Account Public Policy. 2010; 29(2): 115–137.
24. Gopalan R, Jayaraman S. Private control benefits and earnings management: evidence from insider controlled firms. J Account Res. 2012; 50(1): 117–157.
25. Padmini Srinivasan. An Analysis of Related Party Transactions in India. IIM-Bangalore, Working Paper No. 402. 2013; 3.
26. Tambunan ME, Siregar H, Manurung AH, Priyarsono D. Related Party Transactions and Firm Value in the Business Groups in the Indonesia Stock Exchange. J Appl Financ Bank. 2017; 7(3): 1–20.
27. Mehboob F, Tahir SH, Hussain T. Impact of Family Ownership on Financial Decisions of a Firm: An Analysis of Pharmaceutical and Chemical Sectors in Pakistan. Euro-Asian J Econ Financ. 2015; 3(2): 103–112.

