

Query No. 17

Subject: *Classification of an entity as a subsidiary or joint venture.*¹

A. Facts of the Case

1. A Ltd. (hereinafter referred to as ‘the company’) is a joint venture company floated by W Ltd., X Ltd., Y Ltd. and Z Ltd. The companies have entered into joint venture agreement to regulate their relationship as shareholders and Joint Venture (JV) partners in the company on the mutually agreed terms and conditions as specified in JV agreement. As on 28.03.2019, W Ltd. has acquired 52.63% shareholding of X Ltd.; and X Ltd. has become subsidiary of W Ltd. under the Companies Act, 2013. As on 31.03.2019, W Ltd. was holding 36% (approx.) and X Ltd. was holding 21% (approx.) shareholding in the company. Remaining shares were held by Y Ltd. and Z Ltd.

2. The querist has stated that as per section 2(87) of the Companies Act, 2013, the company qualifies for classification as subsidiary of W Ltd. as W Ltd. along with its subsidiary X Ltd. holds more than one half (36% + 21%) of total equity share capital of the company.

3. The querist has referred to the following extracts from Indian Accounting Standard (Ind AS) 110, ‘Consolidated Financial Statements’:

- (a) **An investor**, regardless of the nature of its involvement with an entity (the investee), **shall determine whether it is a parent by assessing whether it controls the investee.**
- (b) **An investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.**
- (c) **Thus, an investor controls an investee if and only if the investor has all the following:**
 - (i) power over the investee;
 - (ii) exposure, or rights, to variable returns from its involvement with the investee; and
 - (iii) **the ability to use its power over the investee to affect the amount of the investor’s returns.**
- (d) An investor shall consider all facts and circumstances when assessing whether it controls an investee. The investor shall reassess whether it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed in paragraph 7.
- (e) Two or more investors collectively control an investee when they must act together to direct the relevant activities. **In such cases, because no investor can direct the activities without the co-operation of the others, no investor individually controls the investee.** Each investor would account for its interest in the investee in accordance with the relevant Ind ASs, such as, Ind AS 111, *Joint Arrangements*,

¹ Opinion finalised by the Committee on 21.11.2019.

Ind AS 28, *Investments in Associates and Joint Ventures*, or Ind AS 109, *Financial Instruments*.

(Emphasis supplied by the querist.)

4. The querist has also referred to the following extracts from Ind AS 111, *Joint Arrangements* (extracts from text):

(a) **A joint arrangement** is an arrangement of which **two or more parties have joint control**.

(b) A joint arrangement has the following characteristics:

- The parties are bound by a contractual arrangement.
- The contractual arrangement gives two or more of those parties joint control of the arrangement.

(c) A joint arrangement is either a joint operation or a joint venture.

(d) **Joint control** is the contractually agreed sharing of control of an arrangement, which exists only **when decisions about the relevant activities require the unanimous consent of the parties sharing control**.

(Emphasis supplied by the querist.)

5. The querist has provided the following key pointers from JV agreement between promoters of the company:

1. The JV agreement provides that, subject to provisions of section 252 of Companies Act, 1956, the number of Directors of the company shall not be less than four (4) and not more than fifteen (15). Further, one Director each shall be nominated by each of the parties (subject to holding of at-least 10% shareholding by respective party).

2. Paragraph 7.8 of JV agreement specifies “Reserved Matters” on which decision can be taken only with the affirmative vote of the majority of Directors, which **majority shall include affirmative vote of at least one Director each nominated by all parties**.

Matters covered under “Reserved Matters” which merit attention are following:

- (a) **The annual revenue budget** of the company
- (b) Five year **annual plans of development, capital budget** etc.
- (c) Winding up of the company
- (d) Any matter related to transfer, sale, lease, exchange, mortgage and/or disposal otherwise of the whole or substantially the whole of the undertaking of the company or part thereof.
- (e) Increase or otherwise alter the authorised or issued **share capital** of the company.
- (f) **Induction of new investors**
- (g) **Taking of any loan or other borrowing** or issue of any debt or other instrument or security carrying the right or option to convert the whole or part thereof or any such instrument or security, as the case may be, or any accrued interest thereon into the shares of the company.

- (h) Any matter relating to
 - promotion of new company/companies including formation of subsidiary company/companies.
 - **entering into partnership and/or arrangement of sharing profits.**
 - taking or otherwise acquiring and holding shares in any other company.
 - pledging or encumbering of any assets of the company and the issuance of corporate guarantee or incurring of usual liability, except as set forth in the annual operating and capital budget or as required for the procurement of working capital needs, or as may be required by any government authorities or for any tax purposes.
 - **Recommendations / approval of dividend by the company**
 - Arrangement involving **foreign collaboration** proposed to be entered by the company.
- (i) Change in the name of the company.
- (j) Entering into any profit sharing or any share option or other similar schemes for the benefit of the officers and other employees of the company.

(Emphasis supplied by the querist.)

(A copy of the JV agreement has been supplied separately by the querist for the perusal of the Committee.)

6. Contention of W Ltd.:

- (i) Keeping in view restrictions imposed through “Reserved Matters” paragraph (discussed above) in joint venture agreement wherein unanimous of all the JV partners is required, W Ltd. is of the view that the company should be treated as a jointly controlled entity for the purpose of accounting and should be consolidated using equity method of consolidation.
- (ii) Following may also be considered in support of W Ltd.’s view:
 - a) Recommendation and approval of dividend has been categorised under reserved matter. Thus, it restricts the ability of W Ltd. to use its power over the investee (the company) to affect the amount of the investor’s returns which is an important condition to establish control.
 - b) One of the public sector undertaking, in its critical judgment section, in consolidated financials for Financial Year (F.Y.) 2017-18 has given the following note:

‘In case of H Ltd. and C Ltd wherein subsidiary company ABC Ltd. held majority voting rights of these companies (74% stake), other JV partner has substantive participative rights through its right to affirmative vote items. Accordingly, being a company with joint control, H Ltd. and C ltd. have been considered as Joint Venture company for the purpose of consolidation of financial statement under Ind AS. However, for the purpose of Companies Act 2013, these companies have been classified as subsidiary companies as defined under section 2 therein’
 - c) Paragraph 9 of Ind AS 112, Disclosure of Interests in Other Entities, inter-alia, requires that an entity shall disclose significant judgements and assumptions made in determining that it does not control another entity even though it holds more than half of the voting rights of the other entity.

From the above, it is clearly evident that Ind ASs requires classification not merely on the basis of shareholding more than 50%.

7. Contention of the auditor of W Ltd.:

One of the statutory auditors of W Ltd. is of the view that since, W Ltd. holds directly and indirectly more than 50 % of voting rights in the company, it should be classified as subsidiary and should be consolidated on line by line basis.

8. The querist has separately provided the details of shareholding pattern of the company as on 31.03.2019 as under:

Party Name	As on 31/3/19 % age holding	As on 31/3/18 % age holding
Y Ltd.	36.36%	31.71%
W Ltd.	36.36%	31.71%
X Ltd.	21.70%	31.71%
Z Ltd.	5.58%	4.87%

Further, the details of shareholding pattern as on 30.06.2019 are as under:

Party Name	As on 30/6/19	% of Shares
Y Ltd.	3,654,880,000	41.29
W Ltd.	2,455,000,000	27.73
X Ltd.	2,181,000,000	24.64
Z Ltd.	561,183,500	6.34
TOTAL	8,852,063,500	100

The composition of directors of the company has also been provided by the company separately for the perusal of the Committee.

B. Query

9. What should be the classification of the company in the standalone books of W Ltd. and how it should be consolidated in consolidated accounts of W Ltd. (equity method or line by line consolidation)? W Ltd. while finalising financial statements for financial year 2018-19, has classified it as a joint venture company and followed equity method of accounting.

C. Points considered by the Committee

10. The Committee notes that the basic issue raised in the query relates to classification of the company as joint venture company or subsidiary company in the consolidated financial statements of W Ltd. for the financial year 2018-19. The Committee has, therefore, considered only this issue and has not considered any other issue that may arise from the Facts of the Case, such as, accounting for transactions between the joint venture partner companies, accounting in the books of the company, X Ltd., Y Ltd. and Z Ltd., manner of consolidation in the books of W Ltd., impact on classification due to changes in shareholding pattern and other changes after 31.03.2019, classification of joint arrangement as joint venture or joint operation, etc. Further, the Committee has opined purely from accounting perspective and not from any legal perspective, such as, legal interpretation of Joint Venture Agreement, legal compliance with any Act or Law in force, etc.

11. At the outset, the Committee notes that W Ltd. holds directly and indirectly more than 50% of the voting rights in the company and therefore, the auditors are contending that it should be classified as subsidiary in the consolidated financial statements of W Ltd. In this

regard, the Committee notes that vide Notification G.S.R 680(E) dated 4th September 2015, issued by the Ministry of Corporate Affairs (MCA), the following Rule has been inserted in the Companies (Accounts) Rules, 2014:

“4A Forms and items contained in financial statements.- The financial statements shall be in the form specified in Schedule III to the Act and comply with Accounting Standards or Indian Accounting Standards as applicable:

Provided that the items contained in the financial statements shall be prepared in accordance with the definitions and other requirements specified in the Accounting Standards or the Indian Accounting Standards, as the case may be.”

Further, the Committee notes the following paragraphs from the Guidance Note on Division II- Ind AS Schedule III to the Companies Act, 2013 (Revised July, 2019 Edition) which states as follows:

“8.1.8.4. ...

The terms ‘subsidiary’, ‘associate’ and ‘joint venture’ shall be as defined in the respective Ind AS. ...”

“8.2.1.16. ...

...The terms ‘subsidiary’ and ‘associate’ should be understood as defined under Ind AS 110 and Ind AS 28. ...”

“12. Part III – General Instructions for Preparation of Consolidated Financial Statements

The Act defines a ‘subsidiary company’ and an ‘associate company’ which is different from the definition of a ‘subsidiary’, an ‘associate’ and a ‘joint venture’ under Ind AS. An amendment to Companies (Accounts) Rules, 2014 on 4 September 2015, newly inserted Rule 4A which state that *“financial statements shall be in the form specified in Schedule III to the Act and comply with Accounting Standards or Indian Accounting Standards as applicable, provided that the items contained in financial statements shall be prepared in accordance with the definitions and other requirements specified in the Accounting Standards or the Indian Accounting Standards, as the case may be.”*

The Act mandates that the companies which have one or more subsidiaries or associates (which as per the Act includes joint ventures) are required to prepare Consolidated Financial Statements (CFS), except under certain circumstances exempted under the Act and Rules.

Accordingly, Ind AS definitions of subsidiary, associate and joint venture shall be considered for assessment of control, joint control and significant influence even though the requirement of preparation of CFS will be governed by the Act.”

From the above, the Committee is of the view that for the purpose of preparation of financial statements, the requirements of Ind ASs have to be considered. Therefore, in the extant case, the term ‘subsidiary’ should be understood as it is defined under Ind AS 110, ‘Consolidated Financial Statements’. In this context, the Committee notes that Appendix A to Ind AS 110 defines ‘subsidiary’ as “an entity that is controlled by another entity”. Thus, the determination of a subsidiary is to be made on the basis of ‘control’ as given in Ind AS 110, and not merely on the basis of shareholding.

12. The Committee further notes the requirements of Ind AS 111, ‘Joint Arrangements’, as follows:

- “4 A joint arrangement is an arrangement of which two or more parties have joint control.**
- 5 A joint arrangement has the following characteristics:**
- (a) The parties are bound by a contractual arrangement (see paragraphs B2–B4).**
 - (b) The contractual arrangement gives two or more of those parties joint control of the arrangement (see paragraphs 7–13).”**
- “7 Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.**
- 8 An entity that is a party to an arrangement shall assess whether the contractual arrangement gives all the parties, or a group of the parties, control of the arrangement collectively. All the parties, or a group of the parties, control the arrangement collectively when they must act together to direct the activities that significantly affect the returns of the arrangement (ie the relevant activities).
- 9 Once it has been determined that all the parties, or a group of the parties, control the arrangement collectively, joint control exists only when decisions about the relevant activities require the unanimous consent of the parties that control the arrangement collectively.”
- “12 An entity will need to apply judgement when assessing whether all the parties, or a group of the parties, have joint control of an arrangement. An entity shall make this assessment by considering all facts and circumstances (see paragraphs B5–B11).”
- “B3 When joint arrangements are structured through a separate vehicle (see paragraphs B19–B33), the contractual arrangement, or some aspects of the contractual arrangement, will in some cases be incorporated in the articles, charter or by-laws of the separate vehicle.”
- “B5 In assessing whether an entity has joint control of an arrangement, an entity shall assess first whether all the parties, or a group of the parties, control the arrangement. Ind AS 110 defines control and shall be used to determine whether all the parties, or a group of the parties, are exposed, or have rights, to variable returns from their involvement with the arrangement and have the ability to affect those returns through their power over the arrangement. When all the parties, or a group of the parties, considered collectively, are able to direct the activities that significantly affect the returns of the arrangement (ie the relevant activities), the parties control the arrangement collectively.
- B6 After concluding that all the parties, or a group of the parties, control the arrangement collectively, an entity shall assess whether it has joint control of the arrangement. Joint control exists only when decisions about the relevant activities require the unanimous consent of the parties that collectively control the arrangement. Assessing whether the arrangement is jointly controlled by all of its parties or by a group of the parties, or controlled by one of its parties alone, can require judgement.
- B7 Sometimes the decision-making process that is agreed upon by the parties in their contractual arrangement implicitly leads to joint control. For example, assume two

parties establish an arrangement in which each has 50 per cent of the voting rights and the contractual arrangement between them specifies that at least 51 per cent of the voting rights are required to make decisions about the relevant activities. In this case, the parties have implicitly agreed that they have joint control of the arrangement because decisions about the relevant activities cannot be made without both parties agreeing.

- B8 In other circumstances, the contractual arrangement requires a minimum proportion of the voting rights to make decisions about the relevant activities. When that minimum required proportion of the voting rights can be achieved by more than one combination of the parties agreeing together, that arrangement is not a joint arrangement unless the contractual arrangement specifies which parties (or combination of parties) are required to agree unanimously to decisions about the relevant activities of the arrangement.

Application examples

Example 1

Assume that three parties establish an arrangement: A has 50 per cent of the voting rights in the arrangement, B has 30 per cent and C has 20 per cent. The contractual arrangement between A, B and C specifies that at least 75 per cent of the voting rights are required to make decisions about the relevant activities of the arrangement. Even though A can block any decision, it does not control the arrangement because it needs the agreement of B. The terms of their contractual arrangement requiring at least 75 per cent of the voting rights to make decisions about the relevant activities imply that A and B have joint control of the arrangement because decisions about the relevant activities of the arrangement cannot be made without both A and B agreeing.”

- “B9 The requirement for unanimous consent means that any party with joint control of the arrangement can prevent any of the other parties, or a group of the parties, from making unilateral decisions (about the relevant activities) without its consent. If the requirement for unanimous consent relates only to decisions that give a party protective rights and not to decisions about the relevant activities of an arrangement, that party is not a party with joint control of the arrangement.”

From the above, the Committee notes that in order to determine the nature of arrangement that exists between the parties, it is to be evaluated that whether the arrangement is jointly controlled by all of its parties or by a group of the parties, or controlled by one of the parties (viz., W Ltd.) alone. The Committee also notes that the concept of ‘joint control’ involves concept of ‘control’, which is dealt with in detail in Ind AS 110, ‘Consolidated Financial Statements’. Accordingly, the Committee examines the requirements of Ind AS 110 on the concept of control in the paragraph 13 below.

13. The Committee notes the following paragraphs of Ind AS 110:

- “6 An investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.**
- 7 Thus, an investor controls an investee if and only if the investor has all the following:**
- (a) power over the investee (see paragraphs 10–14);**

(b) exposure, or rights, to variable returns from its involvement with the investee (see paragraphs 15 and 16); and

(c) the ability to use its power over the investee to affect the amount of the investor's returns (see paragraphs 17 and 18).

8 An investor shall consider all facts and circumstances when assessing whether it controls an investee. The investor shall reassess whether it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed in paragraph 7 (see paragraphs B80–B85).

9 Two or more investors collectively control an investee when they must act together to direct the relevant activities. In such cases, because no investor can direct the activities without the co-operation of the others, no investor individually controls the investee. Each investor would account for its interest in the investee in accordance with the relevant Ind ASs, such as Ind AS 111, *Joint Arrangements*, Ind AS 28, *Investments in Associates and Joint Ventures*, or Ind AS 109, *Financial Instruments*.

Power

10 An investor has power over an investee when the investor has existing rights that give it the current ability to direct the *relevant activities*, ie the activities that significantly affect the investee's returns.

11 Power arises from rights. Sometimes assessing power is straightforward, such as when power over an investee is obtained directly and solely from the voting rights granted by equity instruments such as shares, and can be assessed by considering the voting rights from those shareholdings. In other cases, the assessment will be more complex and require more than one factor to be considered, for example when power results from one or more contractual arrangements.”

Further, the Committee notes the following paragraphs from Appendix B of Ind AS 110, reproduced below, which provides application guidance on the requirements of Ind AS 110:

“B5 When assessing control of an investee, an investor shall consider the purpose and design of the investee in order to identify the relevant activities, how decisions about the relevant activities are made, who has the current ability to direct those activities and who receives returns from those activities.

B6 When an investee's purpose and design are considered, it may be clear that an investee is controlled by means of equity instruments that give the holder proportionate voting rights, such as ordinary shares in the investee. In this case, in the absence of any additional arrangements that alter decision-making, the assessment of control focuses on which party, if any, is able to exercise voting rights sufficient to determine the investee's operating and financing policies (see paragraphs B34–B50). In the most straightforward case, the investor that holds a majority of those voting rights, in the absence of any other factors, controls the investee.”

“B8 An investee may be designed so that voting rights are not the dominant factor in deciding who controls the investee, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements. In such cases, an investor's consideration of the purpose and design of the investee shall also include consideration of the risks to which the investee was designed to be exposed, the risks it was designed to pass

on to the parties involved with the investee and whether the investor is exposed to some or all of those risks. Consideration of the risks includes not only the downside risk, but also the potential for upside.”

“B11 For many investees, a range of operating and financing activities significantly affect their returns. Examples of activities that, depending on the circumstances, can be relevant activities include, but are not limited to:

- (a) selling and purchasing of goods or services;
- (b) managing financial assets during their life (including upon default);
- (c) selecting, acquiring or disposing of assets;
- (d) researching and developing new products or processes; and
- (e) determining a funding structure or obtaining funding.

B12 Examples of decisions about relevant activities include but are not limited to:

- (a) establishing operating and capital decisions of the investee, including budgets; and
- (b) appointing and remunerating an investee’s key management personnel or service providers and terminating their services or employment.”

“B15 Examples of rights that, either individually or in combination, can give an investor power include but are not limited to:

- (a) rights in the form of voting rights (or potential voting rights) of an investee (see paragraphs B34–B50);
- (b) rights to appoint, reassign or remove members of an investee’s key management personnel who have the ability to direct the relevant activities;
- (c) rights to appoint or remove another entity that directs the relevant activities;
- (d) rights to direct the investee to enter into, or veto any changes to, transactions for the benefit of the investor; and
- (e) other rights (such as decision-making rights specified in a management contract) that give the holder the ability to direct the relevant activities.

B16 Generally, when an investee has a range of operating and financing activities that significantly affect the investee’s returns and when substantive decision-making with respect to these activities is required continuously, it will be voting or similar rights that give an investor power, either individually or in combination with other arrangements.”

“Power with a majority of the voting rights

B35 An investor that holds more than half of the voting rights of an investee has power in the following situations, unless paragraph B36 or paragraph B37 applies:

- (a) the relevant activities are directed by a vote of the holder of the majority of the voting rights, or
- (b) a majority of the members of the governing body that directs the relevant activities are appointed by a vote of the holder of the majority of the voting rights.

Majority of the voting rights but no power

B36 For an investor that holds more than half of the voting rights of an investee, to have power over an investee, the investor's voting rights must be substantive, in accordance with paragraphs B22–B25, and must provide the investor with the current ability to direct the relevant activities, which often will be through determining operating and financing policies. If another entity has existing rights that provide that entity with the right to direct the relevant activities and that entity is not an agent of the investor, the investor does not have power over the investee.”

From the above, the Committee notes that the assessment of ‘control’ or ‘joint control’ is a matter of judgement, which should be evaluated in the particular facts and circumstances and considering the requirements of any specific contractual arrangement between the parties concerned. In this regard, the Committee notes that the companies W Ltd., X Ltd., Y Ltd. and Z Ltd. have entered into the Joint Venture Agreement which contains their rights and obligations in relation to the company.

14. The Committee notes the following clauses from the Joint Venture Agreement (as modified/amended from time to time by the Supplementary Agreement(s)) and Articles of Association, as supplied by the querist for the perusal of the Committee:

Joint Venture Agreement

“WHEREAS

...

- d) In a meeting taken by Secretary (Power) held on 29th October 2008, wherein the issue of creation of a separate corporate entity exclusively dealing with energy efficiency implementation was discussed and proposed a need for strong Government led leadership to unlock the market potential in Energy Efficiency. Further, it was also decided on 6th July 2009 that all the promoting CPSUs shall subscribe equal equity participation i.e. ... for creating the company. ...
- e) The Parties hereto as leaders in the area of Power generation, power project financing, power transmission and rural electrification projects have agreed to collaborate for setting up JV Company for implementation of Energy Efficiency projects. The parties have also agreed to set forth more elaborately the objectives in the Memorandum of Association of the JVC for realisation of the above intent.
- f) In pursuance of the above, the Parties hereto have agreed to incorporate a Joint Venture Company for achieving the above objectives. The Parties have, therefore, entered into this Agreement to regulate their relationship as shareholders and Joint Venture partners in the JVC on the mutually agreed terms and conditions as hereinafter specified.”

“1.0 DEFINITIONS

...

- iv) “Affiliates”/ “Associates” in relation to “Y Ltd.”, “W Ltd.”, “Z Ltd.” and “X Ltd.”, respectively shall mean person(s)/ body corporate of which “Y Ltd.”, “W Ltd.”, “Z Ltd.” and “X Ltd.”, as the case may be, is owner or beneficial owner of not less than 50% of the paid-up share capital/voting rights.

...”

- “xiii) “JVC” or the company shall mean the Joint Venture Company incorporated under the Act pursuant to this Agreement.”

“7.1 The JVC shall be managed by its Board of Directors. The Board shall be responsible for the overall functioning of the JVC. The Business of the JVC shall always be carried on in accordance with the policies laid down by the Board from time to time.”

“7.3 The Board of the JVC shall comprise maximum 13 (Thirteen) Directors that include Nominee Directors, Part-Time Directors, Independent directors & Functional Directors.

The PROMOTERS shall be entitled to nominate one Director each on the Board of JVC provided that the shareholding of each such Party does not fall below 10% of the paid up share capital of the JVC.

Apart from the Directors nominated by PROMOTERS, two Part-Time Directors and Independent Directors will be nominated by MoP, GOI, one of whom would be from BEE.

The Managing Director and other Functional Directors shall be appointed in accordance with Clause 8.0(c) & 8.0(f) of this agreement.

... The Board shall be responsible for overall functioning of the JVC. The business of the JVC shall always be carried on in accordance with the policies laid down by the Board from time to time.”

“7.5 The non-executive Chairman of the Board shall be amongst the Directors nominated by the Promoters on the Board of the JVC for a period of two years. The Chairman of the Board shall be rotated amongst the Promoters. The first Chairman of the proposed JVC shall be nominated by Y Ltd. and subsequent Chairman shall be nominated by W Ltd., X Ltd. and Z Ltd. in order of sequence. The Chairman shall not be below the level of Director of the Promoters. ...”

“7.8 Reserved Matters

7.8.1 Neither the Board of Directors nor a committee thereof (whether at a Board Meeting or at a committee meeting or by circular resolution or otherwise) nor its MD or any other person purporting to act on behalf of the JVC shall take any action in respect of any of the following matters (Reserved Matters) except with the affirmative vote of the majority of Directors, which majority shall include affirmative vote of at least one Director each nominated by all Promoters.

- a. The annual revenue budget of the JVC.
- b. The Five Year Annual Plans of development, the capital budget of the Company and processing of any modernisation, expansion schemes including programme of capital expenditure or purchase of capital equipment which exceeds Rs. 10 Crore.
- c. Winding up of the company.
- d. Any matter relating to the transfer, sale, lease, exchange, mortgage and/or disposal otherwise of the whole or substantially the whole of the undertaking of the Company or part thereof.
- e. Increase or otherwise alter the authorized or the issued share capital of the Company.
- f. Induction of New investors

- g. Taking of any loan or other borrowing or issue of any debt or other instrument or security carrying the right or option to convert the whole or part thereof or any such instrument or security, as the case may be, or any accrued interest thereon into the Shares of the JVC.
- h. Any matter relating to
 - the promotion of new company/companies including formation of subsidiary company/companies.
 - ...
 - pledging or encumbering of any assets of the JVC and the issuance of corporate guarantee... except as set forth in the annual operating and capital budgets or as required for the procurement of working capital needs, or as may be required by any government authorities or for any tax purposes.
 - Recommendations/approval of dividend by the Company
 - ...
- i. Change in the name of the Company
- j. Entering into any profit sharing, or any share option or other similar schemes for the benefit of the officers and other employees of the JVC ...”

“7.9 Meetings of the Board of Directors

...

(c) The quorum for a meeting shall be determined from time to time in accordance with the provisions of Section 287 of the Act, provided that there shall be no quorum in any meeting unless at least one nominee Director each from atleast three Parties is present.”

“8.0 Functional Management

(a) JVC shall have its own professional management team of Managing Director (MD) and functional directors. The professional management team will be headed by Managing Director.

(b) The Board shall delegate to the MD such powers and authorities as would enable him to have operational autonomy in the day-to-day management of business and affairs of the Company and in like manner may withdraw or annul any such power and/or authority as may be considered necessary.

(c) Subject to the provision of the Act, Managing Director of the Company shall be selected by Search and Selection Committee comprising of:

1. Secretary (Power)
2. CMD of the PROMOTERS
3. DG, BEE,

and appointed by the Board on such terms and conditions as the recruitment rules approved by the Board, to manage the affairs and business of the Company.

(d) The functional management of the JVC including sourcing, purchasing, personnel, finance and other commercial and managerial decisions shall vest with the MD, who shall have authority and responsibility for the management of day-

to-day affairs of the JVC for which appropriate power may be delegated to him by the Board. ...

(f) Subject to the provisions of the Act and Clause 7.3 of the JV Agreement, the other Functional Directors of the Company except Managing Director, shall be selected by Selection Committee comprising of:

1. Chairman of the company
2. Managing Director of the company,
3. one representative each from Promoter Companies, Ministry of Power (Government of India), Bureau of Energy Efficiency,

from the Promoter Companies for period up-to 5 years or through Open Recruitment in case no suitable candidate could be selected from the Promoter Companies, on such terms and conditions as may be approved by the Board from time to time.”

“14.0 Articles of Association

14.1 The Parties shall cause the JVC to fully adopt, ratify, consent to and fully agree to be bound by this agreement.

14.2 The Articles of Association of the JVC shall be suitably framed / amended to incorporate the main provisions of this Agreement to the extent permissible under the Act.”

“16.2 In the event of a Party ceasing to hold at least 10% (ten percent) of the paid-up share capital of the JVC, all rights of such Party under the Agreement shall cease.”

“21.0 Ratification of this agreement

The Parties’ rights and obligations shall be governed primarily by this Agreement, which shall also prevail inter-se amongst the Parties in the event of any ambiguity or inconsistency between this Agreement and the Memorandum and Articles of the Association to the extent permissible under law.”

Articles of Association

“180 After Incorporation, the Company shall adopt the Joint Venture Agreement executed among Y Ltd., W Ltd., Z Ltd. and X Ltd. and in case of any inconsistency between this Articles of Association and Joint Venture Agreement, the provisions of latter will prevail, subject to provisions of the Act.”

Adoption of JVA

15. The Committee notes from the above that the purpose of entering into this JV agreement is to establish a special purpose vehicle, viz., the company, which is intended to be a joint arrangement/ joint venture company. The Committee also notes that as per clause 7.8.1 of the Joint Venture Agreement, extracts of which are also given in paragraphs 5 and 14 above, any action in respect of ‘reserved matters’ shall be taken only with the affirmative vote of the majority of Directors, which majority shall include affirmative vote of atleast one Director each nominated by all the promoters. The reserved matters include matters related to annual revenue budgets; 5 year annual plans of development, capital budget and capital

expenditure or purchase of major capital equipment; the transfer, sale, lease, exchange, mortgage and/or disposal otherwise of the whole or substantially the whole of the undertaking of the company or part thereof, increase or otherwise alter the authorised or issued share capital, induction of new investors, recommendation of dividend, etc. Considering these matters and other rights as per other clauses of the JV agreement, such as, quorum, participating rights in the board meetings for other matters like appointment of Managing Director and Functional Directors of the company who shall be responsible for the functional and day-to-day management of the company, etc., the Committee is of the view that these activities are in the nature of relevant activities as per the requirements of Ind AS 110 reproduced above and therefore, may entitle the parties to the JV Agreement 'control' of the company. Further, the provisions of JV Agreement have been adopted in the Articles of Association (AoA) of the company as noted from the above-reproduced clause of AoA and therefore the clauses of the JV Agreement are also binding on the company. As far as W Ltd. is concerned, the Committee notes that it holds directly or indirectly by virtue of shareholding or other rights in X Ltd., majority shareholding in the company, which may be argued to be providing W Ltd. with the ability to 'control' the company.

The Committee also notes that Z Ltd. holds less than 10% shareholding and accordingly, as per the Joint Venture agreement, Z Ltd. will not be entitled to nominate the directors on the Board of Directors of the company (A Ltd.) and therefore, while considering the reserved matters, Z Ltd. shall not be considered. However, since in respect of reserved matters, directors of all the parties to the JV agreement have to unanimously agree before any action can be taken in respect of such matters and for the purpose of quorum of board meetings also, at least one nominee Director each from atleast three Parties has to be present and also after considering the composition of the board of directors, separately provided by the company, etc. the Committee is of the view that inspite of its majority shareholding, W Ltd., unilaterally will not be able to take the decisions about the relevant activities of the company.

Thus, inspite of shareholding and other rights in the X Ltd., since for taking decisions in the reserved matters of the company, as per the JV agreement, the exercise of voting by the director nominated by Y Ltd. is also essential, the Committee is of the view that in case of the company, W Ltd. cannot take important decisions about the relevant activities of the company unilaterally. Therefore, W Ltd. cannot be considered as controlling the activities of the company, unilaterally. Accordingly, the company is not a subsidiary of W Ltd., rather is a joint arrangement and therefore, W Ltd. should not do line by line consolidation of the financial statements of the company; rather should consider it as a joint arrangement and accordingly, account for the same as per the requirements of Ind AS 111.

D. Opinion

16. On the basis of the above, the Committee is of the opinion that the company in the extant case is not a subsidiary of W Ltd. The said arrangement is to be considered as a joint arrangement and accordingly should be accounted for as per the requirements of Ind AS 111, for the reasons mentioned in and as discussed in paragraph 15 above.