CASE STUDY 1

Daily Mart, ₹ 99 Store

The country of India whose functional currency is Rupees is home to a large chain of fixed-price discount stores called Daily Mart, which sells ambient goods at a fixed price of ₹ 99. Fixed-price discount chain focus on unbranded commodity goods that they purchase from a number of small suppliers (apart from almonds which they import from California, US), of which these Daily Mart Stores are the most important customers. The products they sell have low profit margins and minimal overheads, and their target price is set. The products are typically functional, standardised, and undifferentiated.

Daily Mart in order to minimise the overhead cost (in light of target price, to push the margins) working on efficiency and effectiveness. To achieve this, the company has strategically invested in automation and advanced technology. It has recently imported 4 advance level machines for printing and labelling on items or packing thereof from Japan which were directly entered for home consumption. These state-of-the-art machines are designed to enhance the speed and precision of printing and labeling on various items and packaging materials. By integrating these advanced machines into its operations, Daily Mart aims to streamline production processes, reduce labour dependency, and minimize wastage, ultimately leading to improved cost efficiency.

Daily Mart has imported four high-tech printing and labeling machines from Japan and the cost structure for these machines includes various components. The price of raw materials amounts to 1,500 thousand Japanese Yen. In addition, processing charges incurred for these machines stand at 300 thousand Japanese Yen. Other expenses associated with the import are estimated at 90 thousand Japanese Yen. Furthermore, the usual profit margin considered in the cost structure is 150 thousand Japanese Yen. The cost of transport for bringing these machines to their destination is 60 thousand Japanese Yen. However,

the cost of insurance for the machines is not ascertainable at this stage. The exchange rates applicable for conversion can be referred to in Annexure 1.

As mentioned earlier, Daily Mart is striving towards effectiveness and efficiency; for this they are working on sync of system, strategy, staff, skill etc. The Management Accountant of Daily Mart had experience of using 7S framework and exited to apply the same framework at Daily Mart to support the drive for efficiency and effectiveness. She made a presentation to C-suite. CEO is convinced with utility that 7S framework is capable to produce, but has queries regarding the application of Mckinsey 7S; moreover, skeptic about; how Daily Mart going to get maximum out of 7S; MD of Daily Mart who is Operation Engineer by education qualification expressed his contentions about 7S in response.

As a result of a prolonged economic downturn in the neighbour country Bangladesh, **'Everything at 99'** bargain stores also have grown therein; which Daily Mart is aware of. At present, there are four major retail chains operating under the ₹ 99 pricing model. These include Retail 99, Club Basket 99, Daily Shopee 99, and Quick Buy 99, each catering to budget-conscious consumers seeking affordable shopping options. Quick Buy 99 out of four stated above started its operations back in April 2023, while other three has been operating for more than 5 years, Retail 99 is oldest one.

Year wise total revenue (converted using appropriate exchange rate in ₹ Lacs) of all four main discount fixed-price chains operating in Country Bangladesh is calculated. For the financial year 2024-25, the combined revenue of these chains reached ₹ 2,260 lakhs. In the F.Y. 2023-24, the total revenue stood at ₹ 2,100 lakhs, reflecting steady expansion in the market. Meanwhile, in F.Y. 2022-23, the revenue was recorded at ₹ 1,450 lakhs, indicating a substantial increase in subsequent years.

These four chains' stores are typically located on the main streets of cities and villages with high rates of economic distress. There are vacant stores in many of these cities and towns that may be rented for a reasonable price. These stores can now be rented for a relatively short

fixed-term lease from landlords who previously demanded hefty rents and asking for lengthy leases. These ‘Everything at 99 store chains’ in Bangladesh promote their expansion intentions through various means. Only a few weeks pass before one of the businesses announces intentions to open many new stores around the nation.

Given the rise of fixed-price discount stores in Bangladesh, Daily Mart is thinking about getting into this/market. Therefore, a brand awareness survey in Bangladesh was recently commissioned by Daily Mart. According to the survey's findings, respondents who work in the retail consumer products industry had a fair amount of knowledge about Daily Mart. The majority of these respondents accurately recognised the business as a major player in the Country India and a discount fixed-price enterprise. However, only 10% of respondents had heard of Daily Mart among ordinary consumers. On the other hand, over 85% of the respondents knew either or all the four fixed-price ‘Everything at 99’ discount shops that are now operating in Country Bangladesh.

The Daily Mart generates ₹ 24 crores in income in F.Y. 2024-25. Because of its cash reserves, it might be able to lease a sizable number of stores in Country Bangladesh and build a solid reputation in the marketplace. Competencies in efficient supplier management and selection, backed by efficient procurement procedures, have been acknowledged. One of the company's main advantages is its logistical systems and procedures.

The success of Daily Mart can be attributed to its diversified and dedicated management team, whose collective expertise and strategic vision have been instrumental in driving the company forward. With vast experience across various domains such as retail operations, supply chain management, finance, marketing, and technology integration, the leadership team has successfully navigated market challenges while capitalizing on emerging opportunities. One of the key strengths of Daily Mart’s management is its proactive approach to innovation and cost optimization. By continuously analyzing consumer trends, implementing advanced technology, and refining operational efficiencies, the team ensures that the company remains competitive in the dynamic retail landscape. Their hands-on decision-making, customer-centric

strategies, and focus on sustainable growth have enabled Daily Mart to maintain a strong foothold in the market.

Additionally, the management fosters a culture of adaptability and teamwork, ensuring that employees at all levels are aligned with the company's vision. This collaborative and forward-thinking approach has played a pivotal role in expanding the business, strengthening supplier relationships, and enhancing customer satisfaction, further solidifying Daily Mart's position as a market leader.

Ms. Ambika recently appointed as additional director. Mr. Dehra, who is also Director on board of Daily Mart went to abroad for 6 months for attending a short-term executive course on business management, in his place Mr. Dun is appointed as alternate director in the manner as specified in Articles of Association. Mr. Dehra is going to retire at 22nd AGM i.e. the upcoming AGM. Mr. Dehra returned back to India after his course.

In Bangladesh, there are also a lot of traditional grocery stores. The biggest of these generates ₹ 8.50 crores in revenue annually (translated using the relevant currency rate). Out-of-town locations are becoming more and more popular among Bangladesh supermarkets since they enable the establishments to stock a greater variety and volume of goods. There is enough of parking for customers, and it is not too difficult for delivery cars to get to these locations. Most supermarkets carry a large variety of ambient goods in addition to nonambient items, frequently with competing brands available. Nevertheless, the cost of these items varies, and no supermarkets have yet to implement the fixed-price discount sales strategy. The big grocery chains generally compete with one another and don't give the 'everything at 99' discount stores much thought. Many supermarkets also offer online home ordering platforms, which allow consumers who are unable or unable to visit the store to have their orders delivered (generally for a fair delivery charge ranging ₹ 25-50 per order).

Daily Mart also sells the retail packing (of 100 grams, at ₹ 99) of almonds, which they import from California, US. Daily Mart owes a California based almond trader/exporter $10,000 due in 3 months' time. The spot exchange rate is (₹ / $) 85.7812 - 85.9345.

Mr. Krishnan who is MD of Daily mart during the year executed certain transactions involving foreign exchange beyond the limits permitted, therefore recently received an order along with penalty notice under the Foreign Exchange Management Act, 1999 which he failed to pay.

Daily Mart has recently introduced a newly developed product line featuring innovative designs and intricate handcrafting techniques. It enters into a contract to sell a product to Max Retail for a total consideration of ₹ 1,21,000, which is payable 24 months after the date of delivery. Max Retail obtains control of the product at contract inception. The contract permits Max Retail to return the product within 90 days. The product being sold is entirely new to the market, which presents a significant challenge in terms of estimating potential returns. Daily Mart has no prior sales history for this particular product, nor does it have access to comparable industry data or market benchmarks that could help forecast the return behavior of customers. In the absence of such data, the entity is unable to make a reliable estimate of the expected returns.

The cash selling price of the product is ₹ 1,00,000 which represents the amount that the customer would pay upon delivery for the same product sold under otherwise identical terms and conditions as at contract inception. The entity's cost of the product is ₹ 80,000. The contract includes an implicit interest rate of 10 per cent (i.e. the interest rate that over 24 months discounts the promised consideration of ₹ 1,21,000 to the cash selling price of ₹ 1,00,000).

Annexure 1

The exchange rate between Rupees and Japanese Yen (₹ / ¥):

Notified by	On the date of filing of Bill of Entry	On the date of arrival of vessel
RBI (FBIL)	56.75	55.20
CBIC	57.05	55.50

Annexure 2

Currently prevailing interest rate per annum in India and US are as follows:

	Borrowing	Deposit
India	8%	6%
US	4%	3.2%

Note - Ambient goods include things like stationery, small plastic items, cleaning supplies and specially packed consumables, which can be kept at room temperature and don't require any special storage facility.

I. Multiple Choice Questions

1.1 What is the assessable value of 4 advance level machines for printing and labelling in JPY (¥)?

(a) ¥ 21,64,950

(b) ¥ 21,22,950

(c) ¥ 21,65,625

(d) ¥ 21,23,625

1.2 How much Daily Mart need to pay in three months' time in ₹ to settle $10,000 payment to the supplier of almonds based in California, if Daily Mart decided to hedge the exposure using Money Market Hedge (round-off calculation to the nearest full unit of currency)?

(a) ₹ 8,68,056

(b) ₹ 8,99,321

(c) ₹ 8,69,607

(d) ₹ 8,32,705

1.3 Which of the exchange rates shall be used to calculate assessable value of 4 advance level machines for printing and labelling in ₹ ?

(a) ₹ / ¥ 56.75

(b) ₹ / ¥ 55.20

(c) ₹ / ¥ 57.05

(d) ₹ / ¥ 55.50

1.4 Presuming AGM of BPL took place within the time in which it shall be conducted, you are required to check validity of following statements:

I. Mr. Dun shall hold office till conclusion of 22nd AGM i.e. the upcoming AGM

II. Ms. Ambika shall hold office till upcoming AGM

Options

(a) Statement I is correct but statement II is incorrect

(b) Statement II is correct but statement I is incorrect

(c) Both I and II are correct

(d) Both I and II are incorrect

1.5 Regarding failure to make payment of the penalty imposed under the Foreign Exchange Management Act, 1999, which of the following statements are/is incorrect;

I. Adjudicating Authority may, by order in writing, authorise an officer of Enforcement not below the rank of Assistant Director to recover any arrears of penalty

II. Order of recovery shall be issued if the person upon whom penalty is imposed failed to make full payment within a period of sixty days from the date on which the notice for payment of such penalty is served on him.

IIII. Such authorised officer of enforcement has all the like power which are conferred on the land revenue collector.

Options

(a) II only

(b) III only

(c) I and III

(d) II and III

II. Descriptive Questions

1.6 Using appropriate model to Assess the attractiveness, to Daily Mart, of entering the discount fixed-price retail market in Bangladesh.

1.7 The MD at Daily Mart is of opinion, that Strategy is one among the 7 elements of 7S framework that is core to all remaining elements of 7S and Hard S elements have more important than Soft S elements; therefore, need to more focused upon. Evaluate the validity of his 3 contentions and Advice.

1.8 Analyse the transaction between Daily Mart and Max Retail with respect to the recognition of revenue and financing component.

ANSWERS TO THE CASE STUDY 1

I. Answers to the Multiple Choice Questions

1.1 (b) ¥ 21,22,950

Reason: As per Rule 8 (computed value) read with Rule 3 and Rule 10 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007, value of imported goods shall be based on a computed value, which shall consist of the sum of the cost or value of materials and fabrication or other processing employed in producing the imported goods; an amount for profit and general expenses equal to that usually reflected in sales of goods of the same class or kind as the goods being valued which are made by producers in the country of exportation for export to India; and the cost or value of all other expenses under sub-rule (2) of rule 10.

So, FOB value (in '000) shall be ¥ 2,040 (i.e.1,500 + 300 + 90 + 150)

Transport Cost given is ¥ 60

Cost of Insurance to the place of Import, since not ascertainable, hence 1.125% of FOB value i.e. 1.125% of 2,040 is equal to ¥ 22.95

Hence, Assessable Value (in '000) shall be 2040 + 60 + 22.95 = 2122.95 or **¥ 21,22,950**

1.2 (c) ₹ 8,69,607

Reason: Liability in $ to be paid in 3 months' time = $10000

Deposit such number of dollars in the US, that it will become $10000 in three months' time = $10000 / (1+0.8%*) = $ 9921

* 3.2% is annual rate, to calculate quarterly rate simply divide it by 4.

To deposit $9921, Daily Mart must have to borrow in ₹ to convert same in $ (but transaction for $) at spot market exchange rate i.e. ₹ 85.9345 per $ (because market will sell at higher). Daily Mart have to borrow ₹ 8,52,556 @8%p.a. for three months.

Daily Mart have to pay back the ₹ borrowing in three months' time i.e. 8,52,556+2% i.e. ₹ 869607.

(**Note:** All calculation round-off to nearest full unit of currency.)

1.3 (c) ₹ / ¥ 57.05

Reason: For imported goods, the conversion to ₹ shall be done with reference to rate of exchange prevalent on the **date of filling of bill of entry** under section 46 of the Customs Act, 1962.

For custom valuation the rate of exchange means rate of exchange determined by the board or ascertain in such manner as the board may direct.

Note for better understanding of students: The exchange rates of 22 currencies is published online in advance for ease of all importers and exporters. These exchange rates would be made available on the ICEGATE website twice a month i.e., on the evening of the first and third Thursdays of the month and would be effective from midnight of the following day. Detailed procedural modality has been explained in the ***Circular 07/2024-Customs dated 25.06.2024.***

1.4 (b) Statement II is correct but statement I is incorrect

Reason: Second proviso to section 161 (2) of the Companies Act 2013, provides that an **alternate director shall not hold office** for a period longer than that permissible to the director in whose place he has been appointed and shall vacate the office if and **when the director in whose place he has been appointed returns to India;** hence first statement is **incorrect.**

Further, second statement is **correct,** because as per section 161(1) of the Companies Act 2013, the articles of a company may confer on its Board of Directors the power to appoint any person, other than a person who fails to get appointed as a director in a general meeting, as an **additional director** at any time who shall hold office up to the **date of the next annual general meeting or the last date on which the annual general meeting should have been held, whichever is earlier.**

1.5 (d) II and III

Reason: As per sub-section 1 to section 14A of the Foreign Exchange Management Act, 1999, the Adjudicating Authority may, by **order in writing, authorise an officer of**

Enforcement not below the rank of Assistant Director to recover any arrears of penalty from any person who fails to make full payment of the penalty imposed on him under section 13 within the period of ninety days from the date on which the notice for payment of such penalty is served on him.

Further, sub-section 2 provides that the officer referred to in sub-section (1) shall exercise all the like powers which are conferred on the income-tax authority in relation to recovery of tax under the Income-tax Act, 1961 (43 of 1961) and the procedure laid down under the Second Schedule to the said Act shall mutatis mutandis apply in relation to recovery of arrears of penalty under this Act.

II. Answers to the Descriptive Questions

1.6 One of the most often used business strategy tools for organisations to have a better understanding of the primary competitive forces operating in their market is Porter's Five Forces model.

Michael Porter, a professor at Harvard Business School, developed the Five Forces Model, which was initially released in 1979. Porter's Five Forces are competitive rivalry, supplier power, buyer power, threat of substitution, and threat of new entry.

When evaluating strategy, the model advises firms to take into account external factors rather than only their direct rivals. Organisations can strengthen and improve their competitive position in the market by redefining their strategy, identifying areas for improvement, and making better judgements by comprehending these influences.

Assessment

Force 1 - Existing competitive rivalry

There are currently four competitors on the market, and it seems like there is fierce competition. These businesses would probably oppose a newcomer to the market, especially a big, global

competitor like Daily Mart. This would most likely be accomplished by tightening supplier contracts, expanding stores quickly, and increasing marketing.

Nevertheless, despite the recession, the scenario's data indicates that the "everything at 99" shop market sector is still expanding. This would imply that rivals may enhance their outcomes by just keeping up with industry performance. Because other geographic areas that aren't yet fully supplied by the current competitors can be exploited, the market may even gain legitimacy and continue to grow as a result of Daily Mart's entry.

Moreover, Daily Mart is making income (bottom line) of 24 crores in existing country; which more than total revenue (top line) of all four ‘everything at 99’ stores taken together i.e. 22.60 crores; hence size of operation is a plus for Daily Mart.

Force 2 - Bargaining power of suppliers

The bargaining strength of Daily Mart's suppliers is minimal. Daily Mart Stores are the primary clients of several small suppliers, with the exception of the almond provider. Due of the lack of differentiation in the items, Daily Mart can easily switch suppliers. It is improbable that any of these vendors could use forward integration to compete with their present clients.

The suppliers of Daily Mart don't have much negotiating power. Their primary clients are Daily Mart Stores, and there are several small suppliers (apart from the almond supplier). Additionally, the items lack differentiation, making it simple for Daily Mart to switch vendors. By using forward integration, none of these providers are likely to become rivals of their present clients.

Force 3 - Bargaining power of customers

Customers of Daily Mart have significant negotiating leverage. There are several reasons for this:

a. Customers looking for cheaper purchase costs are drawn to the products because of their low profit margin.

b. The buyer can easily move to a different supplier because Daily Mart provides unbranded commodity goods. As a result, switching costs are minimal.

c. Other suppliers can readily offer standard, undifferentiated products. In order to get the best terms of supply, customers can thus select which supplier to work with and pit the businesses against one another.

d. Because they are probably extremely price sensitive, customers will make significant efforts to secure the best terms of supply.

Force 4 - Threat of substitutes

The "everything at 99" stores could be replaced by traditional supermarkets since they provide a large selection of ambient goods, frequently with rival brands available. The prices varies, though, and no supermarket has yet to use the discount fixed-price sale strategy; instead, they prefer to set themselves apart with well-known brands. Since the supermarkets are out of town with plenty of parking and easy access by car, location is also a crucial factor. However, because Daily Mart is a well-known and significant participant in the fixed-price sector, supermarkets may change their strategy as a result of its entry into the Bangladesh countries.

Traditional supermarkets also provide home delivery and online shopping. The internet might also be viewed as a substitute channel because ambient items, like those sold at ‘everything at 99’ stores, are ideally suited to this strategy. However, considering how sensitive buyers are to pricing, the ₹ 25-50 delivery fee might lessen this threat.

Moreover, Daily Mart is making income (bottom line) of 24 crores in existing country; while the largest traditional supermarket player in

county Bangladesh has revenue (top line) of 8.5 crores in F.Y. 2024-25; hence size of operation is a plus for Daily Mart or act a back-up to be there and overcome initial hard days in the country Bangladesh.

Force 5 - Potential entrants and barriers to entry

The substantial amount of capital needed to have a credible presence in this sector is a major barrier to entrance. This is not expected to be an issue for Daily Mart, though, since it has the funds on hand to lease a sizable number of stores in Bangladesh and build a respectable presence in the region.

Since many towns and cities now have empty stores that are reasonably priced to rent, the lower rental costs that are now available in Bangladesh also help to lower capital expenditures. Additionally, more and more landlords are agreeing to rent these establishments for a comparatively short fixed-term lease, whereas previously they demanded exorbitant prices and lengthy leases. As a result, this market's departure costs are decreased.

Brand awareness is one entry barrier that could pose a challenge for Daily Mart. The current competitors have more than 85% brand recognition rate, while only 10% of people are familiar with Daily Mart. If Daily Mart wants to succeed in this market, it could need to invest a lot of money in a big marketing campaign.

(Note – Answer is explanatory in nature, reasonable amount of explanation by students is also acceptable; provided they cover/consider all important facts/points)

1.7 All the elements of 7S framework have equal importance, while shared values are core to rest of elements. Hard and Soft S are different from each other only in respect to identification and influence that can be exercised by the management.

Strategy, Structure, and Systems are feasible and easy to identify. These can be found in strategy statements, corporate plans,

organizational charts and other documentations. They are easier to change than the others. Therefore, called hard S elements.

While Skills, Staff, Style, and Shared Values are not change-feasible. These are harder to describe since capabilities, values and elements of corporate culture are continuously developing and changing. They are highly determined by the people at work in the organization. Hence these are harder to change directly, and typically take longer to do so. Therefore, called soft S elements.

Effective companies tend to pay equal attention to these soft S factors as much as they pay to the hard S's. Hence Daily Mart advised to focus on all the 7Ss.

1.8 As per Ind AS 115 "Revenue from contracts with customers", revenue is recognized when control of goods or services is transferred to the customer. The standard introduces a 5-step model for revenue recognition, centred around the core principle that revenue should reflect the transfer of promised goods or services in exchange for consideration expected. If a contract includes a significant financing component, the transaction price must be adjusted for the time value of money— as the timing of payments provides either the customer or the entity with a significant financing benefit. Under Ind AS 115, when goods are sold with the right of return, revenue is recognized only to the extent that it is highly probable that a significant reversal of revenue will not occur when the uncertainty is resolved. Recognize revenue for the portion of goods expected not to be returned. Refund liability is recognized for the amount expected to be refunded.

Daily Mart will recognize revenue when control of the goods is transferred to Max Retail and it becomes probable that no significant reversal will occur i.e., after the 90-day return period, as the product is new and the return history is unavailable. The contract also includes a significant financing component. This is evident from the difference between the amount of promised

consideration of ₹ 1,21,000 and the cash selling price of ₹ 1,00,000 at the date that the goods are transferred to the customer.

The contract includes an implicit interest rate of 10 per cent (i.e. the interest rate that over 24 months discounts the promised consideration of ₹ 1,21,000 to the cash selling price of ₹ 1,00,000). The entity evaluates the rate and concludes that it is commensurate with the rate of interest that would be reflected in a separate financing transaction between the entity and its customer at contract inception.

At the time of delivery:

- A contract liability of ₹ 1,00,000 is recognized, deferring revenue recognition.
- After 90 days, when returns are no longer expected, the contract liability is reversed and revenue of ₹ 1,00,000 is to be recognized.

Financing component of ₹ 21,000 shall be recognized as interest income over the period of 2 years. Until the entity receives the cash payment from the customer, interest revenue would be recognized in accordance with Ind AS 109. In determining the effective interest rate in accordance with Ind AS 109, the entity would consider the remaining contractual term.

CASE STUDY 2

YayIn Airlines Limited (YIAL)

YayIn Airlines Limited (YIAL) is an Indian airline, headquartered in Mumbai. Until the year 2024 YIAL was full service airline offering full service (premium) flying experience to its guests. It primarily focussed on tourist travel to exotic locations. Premium flying required YIAL to focus on connectivity between tourist destinations like Srinagar, Gangtok, Lakshadweep Islands, Andaman and Nicobar Islands and Darjeeling. The number of routes were limited, primarily originating from Mumbai or Delhi. Passengers were mainly luxury travel guests, who could afford exotic travel vacations but have limited time therefore preferring to fly to these destinations. Premium flying service allowed YIAL the ability to charge premium (higher than economy class market rates) to passengers.

Increased margin pressures – full service model

In the recent years, the number of players in the aviation sector has increased, thereby increasing the competition including that on the routes to the destinations mentioned above. Most of the rivals are offering economy seat travel. While there is a difference in the service offering, high inflationary conditions in the country has lead air travel passengers to become more price sensitive. Therefore, aircraft capacity was not getting utilized fully due to this price sensitivity combined with intense competition. Profit margins were getting squeezed.

Route viability assessment

The network route development team, headed by Mr. Jithendra Singh develops route network and assesses its financial and operational viability. The team collaborates with the finance analysis team of YIAL, headed by CA Gopal Verma, to determine the financial viability of the route. Both Jithendra Singh and Gopal Verma then present their analysis to the Mr. Ravi Mehta, Director- Flight Operations, YIAL. Once a route is approved, the flight starts operating on that route after due regulatory

approval. Every 6 months, a detailed analysis is done to look into the operational issues related to that route as well as consider whether the route should continue to be operated on based on its financial viability.

In an effort to improve the company's performance, consideration is being given to cancel flight routes that appear unprofitable. YayIn airlines has the flexibility to cancel flight operations on particular routes after following due operational and regulatory procedures. The forthcoming meeting between Jithendra Singh, Gopal Verma and Ravi Mehta is scheduled to be held next week. The agenda is to decide whether to continue operations of Flight 7J6622 between Mumbai and Srinagar. YIAL has the data to compute the income statement for each flight that it operates. Please refer Annexure 1 for the income statement of flight 7J6622 operating on the Mumbai-Srinagar route. CA Gopal Verma would use this in the discussions next week.

Change in business model into a low cost airline

Due to increased margin pressures, the management realized that growth opportunities in the full service premium flying segment catering to tourist destinations alone, was not a sustainable business model. Increased competition due to rivals offering newer routes to passengers combined with price sensitive travellers, forced the senior management to rethink its strategy.

Therefore, in March 2024, the senior management of the company took the decision to become a low cost airline instead. The flying experience would be similar to economy class travelled that is popular and being offered by other players in the market. The strategy to sustain profits was to build cost efficiencies into the operations along with expanding market reach. Mumbai and Delhi would serve as the main hub of operations, but there would be many more routes developed to cover other cities, not just to tourist destinations. This will result in Increase fleet size and expand the network of routes offered. The fleet will be of single type of aircraft to reduce maintenance and operational costs. Any future acquisition of planes will be leased rather than bought outright. In current market conditions, leasing was working out cheaper. Airfare will be

charged at market competitive rates, attracting enough customers to ensure that flight capacity is fully utilized. In flight entertainment, food and beverage will be charged extra and not included in the ticket cost. Digitalize processes to make them efficient, error free and cost effective. Encouraging online booking and check in is one such process. Premium flying will be phased out completely.

Operations as a low cost airline: New vision and mission of YIAL, increased scale of operation

With the change in business model, the company had a new Vision and Mission statement as outlined below.

Vision: “Yay! In for better connectivity at affordable rates!”

Mission: “Our large fleet will fly guests across to destinations, new and old, on time, in comfort and at industry best fares.”

YIAL has based its success on three parameters using which it wishes to build a loyal customer base – (1) affordable rates, (2) on time performance and (3) courteous and hassle free service. These are reassurances that YIAL provides its customers (guests).

In April 2024, YIAL executed a 12 year lease agreement with Airway Inc. for the lease of 5 aircrafts. Refer to terms of the lease in Annexure 2. With increase in fleet size and corresponding increase in passenger traffic, the scale of operations is slated to increase manifold. The entire project of change in business model was completed in September 2024.

Hub-spoke model versus point to point model

YayIn now works on a hub-spoke model, where flights on different routes pass through either Mumbai or Delhi and then onward to their destination. The passengers have to disembark from their original flight when it reaches the hub and then reboard the next fight that will take them to their final destination. The idea was to club together passengers travelling to a final destination from different origins to group together at the hub that will take them to their final destination in a different aircraft. This will maximize the capacity utilization of the aircraft. Fixed costs form

a major portion of the cost structure of this business. Hence, if capacity utilization is better, it enable YIAL to offer competitive ticket price to the passengers. Therefore, the price sensitive passengers are satisfied due to cheaper airfare. On the other hand, the hub-spoke travel model explained above increased the travel time by at least twice as compared to a point-to-point model. This model results in longer queues at the check-in counter, security check and results in a crowded airport. However, the price sensitive passenger is willing to bear the wait and hassle since the ticket is available at a more affordable rate. The hub-spoke model attracts huge crowd, due to which there is enormous pressure on the limited infrastructure and staff resources at each of these airports (check-in-counter staff, CISF security staff, ground crew handling luggage etc).

The point-to-point model involves the aircraft flying non-stop (directly) from its origin to its destination. Many business travellers and some passengers who prefer hassle free travel, prefer this model. Recently the feedback taken from such type of passengers showed that they were dis-satisfied with inordinately long travel time under the hub-spoke model. With increasing wealth and booming business environment, the chunk of such travellers in slowly increasing. However, operating a point-to-point model from Mumbai or Delhi works out costlier.

Streamlining operations:

Ever since the low cost airline operations have begun, Mr. Ravi Mehta has been insisting on building cost efficiencies into the company's operations. He has encouraged employees to imbibe lean thinking strategies as part of their roles. He has approached the network route development team and the financial analysis team to find a solution to the above problem.

Jithendra's network development team has suggested that efficient management of queue management at the check-in counter and boarding gates at the airport by allowing for online web-check in. Bring uniformity to the size and type of luggage that can be carried by the passengers. With proper regulatory approval from the authorities like

DGCA, passengers must carry check-in and hand luggage of specified dimensions. Else, the passengers have to bear an extra cost for handling non-uniform luggage. Start point-to-point travel for travellers who prefer convenient and faster travel. Since their numbers are smaller, use smaller aircrafts so that (a) capacity utilization is faster and (b) the aircraft turnaround time due to maintenance and repair work by the ground staff can be done faster. Due to lesser passengers the queues will be shorter and there will be minimum disruption to travel time.

The team led by CA Gopal Verma has proposed that to have different pricing structures for hub-spoke model travellers and the point-to-point model travellers. To maintain profitability in operations resort periodic to across-the-board reduction of staff of ground staff in order to reduce costs of operations.

Mr. Prem Chabbra, a director of YIAL was appointed as its Managing Director on 1st April 2023. One of the terms of appointment was that in the absence of adequacy of profits or if the company has no profits in a particular year, he will be paid remuneration in accordance with the provisions contained in the Companies Act, 2013. As per the financial results for FY 2024-25, YIAL has incurred a heavy loss of ₹ 55 crores. However, these losses are primarily due to the extensive change in business model that was undertaken during the year. The company was not in a position to pay any remuneration to Mr. Chabbra but he was paid ₹ 2 crore for the year. This payment was approved by a special resolution passed by the shareholders. The effective capital of the company is ₹ 215 crores.

Tax Deduction at Source (TDS) on passenger service fee (PSF):

Passenger service fee (PSF) is a charge that airlines collect from passengers to cover the cost of airport security and passenger facilities. Facilities include security, baggage trolleys, escalators, air-conditioning etc. All these contribute towards enhancing passenger experience and makes flying comfortable and secure. The airport operators at Mumbai and Delhi, who manage the airports and their infrastructure would collect this fee from the airline.

Mayank Saxena has joined the vendor payment team of the accounting department at YIAL recently. He is making his very first payment to the airport operators at Mumbai and Delhi for PSF. These payments are made along with rental payments to the airport operators that YIAL pays for use of the airport space for operating its business. He is confused whether tax has to be deducted for payments made for PSF to airport operators under the relevant sections of the Income Tax Act, 1961.

Pursuing two business models simultaneously

YIAL has been successfully operating as a low cost airline for the past few years now. In the recent years, the tourism travel industry has been promoting many locations within India as vacation spots. Hence, YIAL's original operating routes like Srinagar, Gangtok, Lakshadweep Islands, Andaman and Nicobar Islands and Darjeeling are gradually becoming popular again. Again, there are different customer segments, some preferring affordable travel while others preferring comfortable premium experience.

Mr. Chabbra has been working with YIAL for the past 25 years. From his experience, he feels that YIAL can re-start its full service premium flying to these locations again. The rest of the management team is not convinced about this proposal. Their primary concern is that YIAL has switched to low-cost, affordable travel model in the recent years. By restarting premium flying, YIAL will be catering to different customer segments at the same time. While price sensitive travel flyers will not be willing to pay higher ticket fare, the prospective premium flying passengers will not be happy to experience the economy class flight experience (affordable, but reduced service travel offering). Hence, there will be a lot of confusion about YIAL's brand offering. They feel that a single model namely the low cost affordable travel model that YIAL is currently following should be maintained, there is no confusion in the minds of passengers about the service to expect.

YayIn acquired an aircraft from Boeing (Boeing 767) on 1st April, 2019 for ₹ 400 crore. Over a period of four years, the aircraft was used in operations and depreciated accordingly. By the end of this four-year

period, the aircraft had a carrying amount of ₹ 255 crore, which reflected its estimated value in use. This value was arrived at after charging cumulative depreciation of ₹ 110 crore and an impairment loss of ₹ 35 crore.

On 1st April, 2023, the company decided to classify the aircraft as "held for sale" due to a proposed transition towards acquiring new-generation aircraft (Boeing 787 Dreamliner). At the time of classification, the carrying amount of the existing aircraft was ₹ 255 crore. However, the fair value less costs to sell was assessed at ₹ 250 crore, indicating a shortfall in recoverable value. At the next reporting date, 31st March, 2024, market conditions improved and the fair value less costs to sell of the aircraft was reassessed at ₹ 265 crore. By 1st October, 2024, the market for aircraft had continued to strengthen, and the fair value less costs to sell rose further to ₹ 300 crore.

Annexure 1

Income statement of Flight 7J6622 operating from Mumbai to Srinagar (per flight)

Particulars	**₹**	**₹**
Ticket Revenue (200 seats × 40% occupancy × ₹ 22,500 ticket price)		18,00,000
Less:		
Variable expenses per person (200 Seats × 40% Occupancy × ₹ 15,000 Variable expense)		(12,00,000)
Contribution margin (Ticket revenue less variable expense)		6,00,000
Flight expenses:		
Salaries, Flight crew	2,00,000	
Salaries, Flight Assistants	80,000	
Baggage Loading and Flight Preparation	70,000	
Overnight costs for flight crew and assistants at destination	80,000	
Fuel for aircraft	2,50,000	
Depreciation of aircraft*	75,000	
Liability insurance	1,50,000	
Flight promotion	50,000	
Hanger parking fee for aircraft at destination	25,000	

Total flight expenses		(9,80,000)
Net Gain/ (Loss)		**(380,000)**
*Based on obsolescence		

The following additional information is available about flight 7J6622 from Mumbai to Srinagar.

1. Members of the flight crew are paid fixed annual salaries, whereas the flight assistants are paid by the flight.
2. The baggage loading and flight preparation expense is an allocation of ground crew's salaries and depreciation of ground equipment.
3. One third of the liability insurance is a special charge assessed against flight 7J6622 because in the opinion of insurance company, the destination of the flight is in a "high- risk" area.
4. Flight promotion expense is specific to the route, in this case relate only to flight 7J6622.
5. The hanger parking fee is a standard fee charged for aircraft at all airports.
6. If flight 7J6622 is dropped, YIAL Airlines has no authorization at present to replace it with another flight.

Annexure 2: Lease agreement terms for 5 aircrafts

Lease Agreement

This Lease Agreement is made and entered into as of 01/10/2024, by and between **YIAL** (YayIn Airlines Limited) and **Airway Inc.** for five aircrafts.

The following were the terms of the lease:

- Lease commencement date for each of the aircraft would be October 1,2024.
- YIAL must pay Airway Inc. the first monthly rental payment of ₹ 10 lakh per aircraft upon execution of the lease.
- Airway Inc. will pay YIAL ₹ 50 lakh per aircraft cash incentive to enter into lease payable upon execution.

YIAL incurs an initial direct cost of ₹ 1 lakh per aircraft, which is payable on October 1, 2024. YIAL has calculated the initial lease liability as the present value of the lease payments discounted using incremental borrowing rate because the rate implicit in the lease could not be readily determined. Thus, the initial lease liability is arrived at as ₹ 8.50 crores per aircraft.

YIAL has to undertake a planned check after every 100,000 flight hours for each aircraft. At the end of lease period, that is 12 years YIAL must have a check performed (or refund the costs to Airway Inc.), irrespective of the actual number of flight hours.

I. Multiple Choice Questions

2.1 What will be the carrying amount of an aircraft and gain or loss to be recognised on subsequent remeasurement as on 1st Oct 2024, for an aircraft purchased in Apr 2019, as per relevant Ind AS?

(a) On subsequent remeasurement as on 1st Oct 2024, aircraft shall be carried at ₹ 300 crore and there will be gain of ₹ 35 crore to be recognised in the books as per Ind AS.

(b) On subsequent remeasurement as on 1st Oct 2024, aircraft shall be carried at ₹ 290 crore and there will be gain of ₹ 25 crore to be recognised in the books as per Ind AS.

(c) On subsequent remeasurement as on 1st Oct 2024, aircraft shall be carried at ₹ 265 crore and there will be loss of ₹ 15 crore to be recognised in the books as per Ind AS.

(d) On subsequent remeasurement as on 1st Oct 2024, aircraft shall be carried at ₹ 255 crore and there will be loss of ₹ 35 crore to be recognised in the books as per Ind AS.

2.2 Which of the following would reflect the spirt of employees adopting lean thinking while working for the organization?

(i) Efficient management of queue management at the check-in counter and boarding gates at the airport by allowing for online web-check in.

(ii) Across the board reduction of staff of ground staff in order to reduce costs of operations.

(iii) Streamlining processes to allow for faster baggage drop and pick up at the departure and arrival lounge by bringing uniformity in the luggage type and size.

(iv) Streamlining flight operations and use of smaller aircraft types to allow for minimum disruption of travel time.

Options

(a) (i), (ii) and (iii)

(b) (ii), (iii) and (iv)

(c) (i), (iii) and (iv)

(d) (i), (ii) and (iv)

2.3 YIAL is using the Kano Model to assess the impact switching to low-cost airline model have on customer satisfaction. Under which attribute of Kano Model would YIAL's ability to provide extensive connectivity at affordable rates fall under:

(a) Performance attribute

(b) Threshold attribute

(c) Delight attribute

(d) Questionable attribute

2.4 Referring to the provisions contained in the Companies Act, 2013, assess the validity of payment of ₹ 2 crore made to Mr. Chabbra for FY 2024-25:

(a) As per the provisions of Companies Act, 2013, Mr. Chabbra is not entitled to any remuneration since YIAL incurred heavy losses in FY 2024-25.

(b) As per the provisions of Companies Act, 2013, Mr. Chabbra is entitled to only ₹ 120 Lakh as remuneration in FY 2024-25 and it cannot be increased in any circumstances.

(c) As per the provisions of Companies Act, 2013, Mr. Chabbra is entitled to only ₹ 24 Lakh as remuneration in FY 2024-25.

(d) As per the provisions of Companies Act, 2013, Mr. Chabbra is entitled to ₹ 2 crores as remuneration in FY 2024-25.

2.5 Which of the following strategies can possibly support Mr. Chabbra's proposal to operate both affordable low cost model and the premium full service model simultaneously?

(a) Operate affordable low cost model and premium full service model under different brands of YIAL. Pricing of tickets can be differentiated based on which model that particular flight is offering, higher price for premium full service tickets and lower price for affordable tickets.

(b) Operate affordable low cost model and premium full service model under the a single brand of YIAL. Pricing of tickets can be differentiated based on which model that particular flight is offering, higher price for premium full service tickets and lower price for affordable tickets.

(c) Increase marketing and advertising spend to spread awareness of which route offers full service flying and which offers low cost affordable flying.

(d) It is not possible to operate both models simultaneously.

II. Descriptive Questions

2.6 Prepare an ANALYSIS showing what impact dropping flight 7J6622 would have on the airline's profit. CA Gopal Verma would be using this analysis in his forthcoming meeting.

2.7 In respect of lease Agreement with Airway Inc.:

(i) How should YIAL record and measure the lease with Airway Inc.?

(ii) How should YIAL account for the cost of planned checks and check to be performed at the end of the lease term?

2.8 ADVISE Mayank Saxena about whether tax has to be deducted for payment of PSF to airport operators in Mumbai and Delhi?

ANSWERS TO THE CASE STUDY 2

I. Answers to the Multiple Choice Questions

2.1 (b) On subsequent remeasurement as on 1st Oct, 2024, aircraft shall be carried at ₹ 290 crore and there will be gain of ₹ 25 crore to be recognised in the books as per Ind AS.

Reason: As per Ind AS 105, An entity should measure a non-current asset (or disposal group) classified as held for sale at the lower of its carrying amount and fair value less costs to sell. On 1st April, 2023, the fair value less costs to sell of the aircraft was determined to be ₹ 250 crore, which was lower than its carrying amount of ₹ 255 crore at that time. Accordingly, an impairment loss of ₹ 5 crore was recognised in the profit and loss account, and the aircraft was carried at ₹ 250 crore. Following classification as held for sale, no further depreciation is required to be recognised.

On 31st March, 2024, fair value less costs to sell has been reassessed at ₹ 265 crore. Accordingly, there is gain of ₹ 15 crore, which is less than the cumulative impairment losses recognised to date (₹ 35 crore + ₹ 5 crore = ₹ 40 crore). Accordingly, it is credited in profit or loss and the property shall be carried at ₹ 265 crore.

Subsequently, on 1st Oct, 2024, the fair value less costs to sell further increased to ₹ 300 crore. There is further gain of ₹ 35 crore, however, Gain to be recognised on remeasurement is restricted to the cumulative impairment losses recognised to date (₹ 35 crore + ₹ 5 crore – ₹ 15 crore = ₹ 25 crore). Accordingly, a restricted gain of ₹ 25 crore is credited in profit or loss and the property shall be carried at ₹ 290 crore.

2.2 (c) (i), (iii) and (iv)

Reason: The correct answer is (c). Lean thinking is an organized management philosophy to reduce waste. In the above case scenario (i), (iii) and (iv) represent reduction of waiting time for guests. Waiting time is a form of waste in a lean system. Across the board reduction of ground staff to reduce cost of operations on the other hand does not necessarily lead to reduction of waste. While cost efficiencies are important, indiscriminate across the board reduction of ground staff can cause inefficiencies in the process flow of operations. Since there is a lot of passenger volume, this rather increases the possibility of generating waste in the form of inefficient operations since there may be insufficient staff to handle the operations.

2.3 (a) Performance attribute

Reason: The answer is (a) Performance attribute. This one dimensional shows the linear relationship between YIAL's investment in providing extensive connectivity at affordable rates to that of customer satisfaction. Better the connectivity and better the affordability by the customer, better the customer satisfaction.

2.4 (d) As per the provisions of Companies Act, 2013, Mr. Chabbra is entitled to ₹ 2 crores as remuneration in FY 2024-25.

Reason: The correct answer is (d). Under Section II of Part II of Schedule V to the Companies Act, 2013, the remuneration payable to managerial personnel is linked to the effective capital of the company. Schedule V states that where in any financial year during the tenure of a managerial person or other director, a company has no profits or inadequate profits, it may pay remuneration to the managerial person not exceeding ₹ 120 Lakh (₹ 1.2 crores) in the year in case the

effective capital of the company is between ₹ 100 crores and ₹ 250 crores. However, the remuneration in excess of ₹ 120 Lakh maybe paid if the resolution passed by the shareholders is a special resolution.

YIAL has an effective capital of ₹ 215 crores. From the foregoing provisions as contained in Schedule V, the payment of ₹ 2 crore in FY 2024-25 to Mr. Chabbra is more than ₹ 120 Lakh (₹ 1.2 crores) specified limit for companies with effective capital between ₹ 100 crores and ₹ 250 crores. However, the remuneration of ₹ 2 crores has been approved by a special resolution passed by the shareholders. Hence, Mr. Chabbra is entitled to ₹ 2 crores as remuneration in FY 2024-25.

2.5 (a) Operate affordable low cost model and premium full service model under different brands of YIAL. Pricing of tickets can be differentiated based on which model that particular flight is offering, higher price for premium full service tickets and lower price for affordable tickets.

Reason: The correct answer is (a). Operate affordable low cost model and premium full service model under different brands of YIAL. Pricing of tickets can be differentiated based on which model that particular flight is offering, higher price for premium full service tickets and lower price for affordable tickets.

This concept is based on multi-brand strategy with the goal of catering to different customer segments simultaneously. By operating under different brands for example, YIAL Express (for low cost affordable travel) and YIAL Comfort (for full service premium travel), the passengers can clearly understand the expected level of service offering from the flight. Pricing will also be accordingly charged based on the level of service. Hence, this will help avoid confusion about the service offering for the flight, enabling YIAL to operate both models simultaneously.

II. Answers to the Descriptive Questions

2.6 As per the statement given in the problem, Flight 7J6622 incurs a net loss of ₹ 380.000. This is the net result of revenue less costs. Revenue is entirely variable depending upon passenger occupancy. Costs are both variable and fixed nature. To analyze the impact of dropping Flight 7J6622, we need to re-compute net gain/ (loss) that YIAL earns when it operates the flight based on relevant costing principles.

Net Gain/ (Loss) = Revenue earned from flight operations less Variable costs of operation

Revenue earned is the ticket revenue earned from flight operations of 7J6622, this is entirely variable. Variable costs of flight operations are those expenses that would be incurred only when the flight is operated. These include variable expenses per passenger, salaries flight assistants, overnight costs for flight crew and assistants, fuel for aircraft, a third portion of flight insurance that is specifically related to this flight sector and flight promotion expense. These are expenses that will not be incurred if the flight is not operated. Hence, relevant for decision making.

Other expenses like salaries of flight crew and hanger parking fees for aircraft are fixed expenses that will be incurred even if the flight does not operate. Loading and flight preparation expense is an allocated cost that will continue to be incurred even if flight 7J6622 does not operate. Depreciation of aircraft and liability insurance expense (2/3rd portion not related to a specific flight sector) are sunk costs. These expenses have already been incurred and hence are irrelevant to decision making. Therefore, these fixed, allocated and sunk expenses are ignored while analyzing the decision whether to continue operating flight 7J6622.

Statement showing Net Gain / (loss) if flight operations continue	₹	₹
Contribution margin if flight operations continue		600,000

Less: Relevant costs if flight operations continue		
Salaries, Flight Assistants	80,000	
Fuel for Aircraft	250,000	
Liability Insurance (1/3 which is the special charge for high risk destinations)	50,000	
Flight Promotion	50,000	
Overnight Costs for Flight Crew and Assistants	80,000	
Total relevant costs if flight continues to operate		510,000
Net Gain / (Loss)		90,000

If YIAL discontinues flight 7J6622, profits will reduce by ₹ 90,000. The statement showing loss in operations of ₹ 380,000 is misleading for decision making purpose because it accounts for costs that are fixed and irrelevant. However, since flight 7J6622 yields a net gain of ₹ 90,000, flight operations should continue.

2.7 (i) **Initial measurement of right-of-use of each aircraft would be calculated as follows:**

Particulars	**Amount (₹)**
Initial measurement of lease liability for each aircraft	8,50,00,000
Initial lease payments made to Airway Inc. on 1st October, 2024, the lease commencement date (per aircraft)	10,00,000
Lease incentives received from Airway Inc. (per aircraft)	(50,00,000)
Initial direct cost per aircraft	1,00,000
Initial measurement of right-of-use of each aircraft	8,11,00,000

Right-of-use of each aircraft will be ₹ 8.11 crores. For 5 aircrafts, the total lease will be recognized at ₹ 40.55 crores.

(ii) YIAL is required to perform a planned check after every 1,00,000 hours of flight hours for each aircraft. This obligation is dependent on future circumstances. For example, YIAL may terminate the lease prematurely. Therefore, this does not lead to an obligation and therefore there is no need to make any provision for these checks. However, at the end of 12 years lease term, YIAL is obliged to carry out a final check irrespective of the number of hours actually flown by the aircraft. Hence, YIAL has to provide for these costs at the present value of expected costs. This provision has to be made at the beginning of the lease term i.e. in the FY 2024-25. The costs must be included in the cost of the right-of-use (ROU) asset pursuant to para 24 (d) of Ind AS 116.

2.8 Section 194-I requires deduction of tax at source at specified percentage on any income payable to a resident by way of rent. Explanation to this section defines the term "rent" as any payment, by whatever name called, under any lease, sub- lease, tenancy or any other agreement or arrangement for the use of any (a) land; or (b) building; or (c) land appurtenant to a building; or (d) machinery; or (e) plant; or (f) equipment; or (g) furniture; or (h) fitting, whether or not any or all of them are owned by the payee.

On the issue of whether payment of PSF by an airline to an Airport Operator qualifies as rent to attract TDS under section 194-I, the Bombay High Court relied on the Apex Court ruling in Japan Airlines and Singapore Airlines case, wherein it was observed that the primary requirement for any payment to qualify as rent is that the payment must be for the use of land and building and mere incidental/minor/insignificant use of the same while providing other facilities and service would not make it a payment for use of land and buildings so as to attract section 194-I. Accordingly, the Bombay High Court declined to admit the ground relating to the applicability of the provisions of section 194-I on PSF charges holding that no substantial question of law arises. The provisions of section 194-I shall not be applicable. Therefore, Mayank Saxena need not deduct TDS on the PSF payments made to airport operators at Delhi and Mumbai.

CASE STUDY 3

JayZee Ltd.

Indian automotive industry is a cornerstone of the nation's economy, contributing around 7.1% to the GDP and nearly 49% to the manufacturing GDP. In the fiscal year 2020-2021, the industry produced over 22 million vehicles, including passenger cars, commercial vehicles, and two-wheelers. The two-wheeler segment dominates the market, with over 80% of the total automotive sales. In the same period, India exported approximately 4.5 million vehicles, showcasing its growing influence in the global automotive market. The government aims to make India a hub for electric vehicles (EVs), targeting a 30% EV adoption rate by 2030. This ambitious goal is supported by policies such as the Faster Adoption and Manufacturing of Hybrid and Electric Vehicles (FAME) scheme, which allocates significant funds to boost EV infrastructure and adoption.

Raj Malhotra, founder of JayZee Ltd., a leading manufacturer of automotive spare parts, envisioned the company's potential during one of his visits to the USA. In 1998, he anticipated the forthcoming boom in the Indian automotive industry, particularly from 2011 to 2020. Foreseeing this growth, he decided to establish JayZee Ltd. to provide high-quality and affordable spare parts for the Indian market. The company is based in Gurgaon, Haryana, with manufacturing facilities in Uttarakhand and Uttar Pradesh strategically located to leverage government benefit schemes.

Over the years, JayZee Ltd. has expanded its product range to include various components such as engine parts, brake systems, suspension systems, electrical components, and more. The company has a state-of-the-art manufacturing facility spread over 20 acres, equipped with advanced machinery imported from Germany and Japan. JayZee Ltd. employs over 1,000 skilled technicians, engineers, and support staff dedicated to maintaining the highest standards of quality. JayZee Ltd.’s

commitment to quality has earned it a reputation as a trusted supplier among domestic and international customers. The company follows stringent quality control measures adhering to international standards like ISO 9001, TS 16949, and IATF 16949, ensuring its products meet stringent performance, safety, and environmental regulations. While Raj Malhotra provided the technical vision, his sons Arjun and Karan, have been instrumental in driving the company's financial strategy and decision-making processes. Their astute financial acumen and business insights have played a crucial role in JayZee Ltd.'s growth and expansion plans.

In addition to the domestic market, JayZee Ltd. has a strong global presence, exporting to over 30 countries across Asia, Europe, Africa, and North America. Major export destinations include the UAE, Saudi Arabia, South Africa, Germany, USA, and Canada. The company has established robust distribution networks and partnerships in these regions. In line with the government’s vision, Raj Malhotra knows that the next decade, from 2021 to 2030, will be a boom period for the EV market in India. He foresees this due to the recent government push towards Atmanirbhar Bharat with its Production Linked Incentive (PLI) Scheme and the global shift towards India as part of the China Plus One strategy. This strategy essentially means that companies do not want all their manufacturing footprint in China due to geopolitical tensions. Additionally, the fast acceleration towards EVs is driven by climate and sustainability strategies of companies.

To meet the burgeoning demand, JayZee Ltd. has implemented aggressive expansion plans, including the construction of two new state-of-the-art manufacturing units in Gujarat and Tamil Nadu. The company has also invested heavily in R&D, collaborating with leading automotive engineering institutes to develop innovative products using advanced materials and cutting-edge technologies.

Apr’2023 Begining

To support the company's strategic objectives, JayZee Ltd. relies on its skilled workforce, who are considered as the backbone of the

organization. In order to foster long-term loyalty and engagement, the company is offering Employee Stock Ownership Plans (ESOPs) to its employees. As the company achieves its earnings targets, shares will vest, granting employees ownership in the company. JayZee Ltd. grants 100 shares to each of its 500 employees on 1st April, 2023. The employees should remain in service during the vesting period. Annexure 1 containing Terms and Conditions of Employee Stock Option Plan has been approved by the shareholders of JayZee Ltd. passing a special resolution.

JayZee Ltd.'s success is attributed to its strong leadership team, employee-friendly policies, continuous training programs, and a culture that fosters innovation. The company provides competitive compensation, growth opportunities, and a positive work-life balance, resulting in high employee satisfaction and low attrition rates. Despite challenges like increased competition, fluctuating raw material prices, and regulatory changes, JayZee Ltd. has maintained a steady growth trajectory with consistent profitability and a strong balance sheet.

Guided by Raj Malhotra's principles and the financial expertise of his sons, Arjun and Karan, JayZee Ltd. Ltd thrived under the directors' unwavering dedication and the collective efforts of its team. As JayZee Ltd. looked towards the future, the directors' global vision and local roots served as a powerful combination, propelling the company's success in the competitive automotive spare parts industry.

JayZee Ltd. is focused on enhancing its manufacturing processes and assessing the efficiency of its operations in relation to their full potential, while also identifying areas of loss. The company has a state-of-the-art production facility that operates in two shifts of 9 hours each, for 6 days a week. Under the leadership of Raj Malhotra, the founder, and his sons Arjun and Karan, the company emphasizes efficiency and productivity in its operations. One of JayZee Ltd.'s critical production lines, responsible for manufacturing essential spare parts, has been closely monitored by the team. Over the last 4 weeks, the following details have been collected for one of their important equipment: Lunch break is 30 mins and other

miscellaneous breaks add up to 15 minutes; Hours for Planned Preventive Maintenance is 15 minutes per shift; For Breakdown Maintenance is 6 hours total; Set up Changes require 14 hours in total; Power Failure is 4 hours in total; Standard Cycle Time per piece is 3 minutes; No of Parts Produced per shift are 140; and Parts Accepted per shift are 131.

Year Ended Mar 2024

In an effort to build long-term loyalty and enhance employee engagement, the company introduced Employee Stock Ownership Plans (ESOPs) in 2023. The ESOPs were designed to provide employees with a direct stake in the company's growth and success. By offering employees the opportunity to become shareholders, the company aims to foster a culture of ownership, where every team member has a vested interest in the organization's performance and outcomes. One year has now elapsed since the implementation of the ESOPs. The program has proven to be an effective way to show appreciation for the hard work of employees and to build stronger ties between the workforce and the company.

At the end of FY 2023-24, earnings is 11%, and 29 employees left the organisation. The company expects that the shares will vest at the end of March 2025 subject to earnings target achieve. The company also expects that an additional 31 employees will leave the organisation in the FY 2024-25 and that 440 employees will receive their shares at the end of the FY 2024-25.

JayZee Ltd., has always been proactive in capitalising on strategic opportunities for growth and diversification. Under the astute leadership of Raj Malhotra, the founder, and his sons, Arjun and Karan, the company has consistently made sound investment decisions to strengthen its position in the market.

JayZee Ltd. acquired a building from Moon Ltd, another reputed manufacturing company, for a cost of ₹10 million on 1st April, 2020. The building, which Moon Ltd had previously used as a factory, was

accounted for under the cost model. At the time of acquisition, JayZee Ltd.'s management, guided by their financial advisors, estimated the building's expected useful life to be 10 years.

Initially, JayZee Ltd. had plans to repurpose the building and integrate it into their expanding operations. However, a few years down the line, the company faced a significant decline in demand for one of its product lines. As a result, the need for an additional factory became redundant. Recognizing the opportunity to generate alternative revenue streams, Arjun and Karan, known for their strategic foresight, proposed renting out the building to a third party. On 1st April, 2024, after conducting a thorough market analysis and obtaining necessary approvals, JayZee Ltd. successfully leased (in an operating lease agreement) the building to a reputable tenant, ABC Industries.

At the time of leasing, JayZee Ltd.'s valuation experts assessed the fair value of the building to be ₹8 million, reflecting the current market conditions and the building's condition. In accordance with the company's accounting policies, JayZee Ltd. adheres to the cost model for recognizing its owned investment properties.

With Arjun and Karan’s strategic guidance, JayZee Ltd. is well-positioned to capitalise on emerging trends and maintain its leadership in the automotive spare parts industry. At the helm of JayZee Ltd. were three dynamic directors - Mr. Rajesh Sharma, Mr. Anil Gupta, and Ms. Priya Mehta. These directors were globetrotters, frequently travelling abroad to develop and secure sustainable business opportunities for JayZee Ltd. From exploring new markets to forging strategic partnerships, they left no stone unturned in their pursuit of growth. Despite their global pursuits, the directors remained deeply rooted in Gurgaon, understanding the importance of maintaining a strong presence at the company's registered office for legal compliance and organizational stability.

Mr. Raj Malhotra is dedicated to developing and securing sustainable business opportunities while exploring new markets and forging strategic partnerships. His recent business tour took him to North America, where he visited the USA and Canada to identify potential business ventures.

After 4 months, Mr. Raj is now preparing to return to India. During his stay abroad, he acquired various items and, being a responsible citizen, he is mindful of the customs regulations. He sent an email (Annexure 2) to Mr. Sanjay, Finance and Taxation head to sought guidance his guidance, who is well-versed in legal and financial matters.

Year Ended Mar 2025

Gumber & Associates has been appointed as Statutory Auditor for JayZee Ltd. for the financial year 2024-25. With a strong track record of excellence, Gumber & Associates has experience in auditing and tax advisory services, ensuring the highest standards of financial oversight and compliance. The firm has earned a stellar reputation for its meticulous attention to detail, in-depth knowledge of regulatory frameworks, and a proactive approach to addressing complex financial and tax matters.

It has already been two years lapsed since the launch of ESOP 2023. At the end of FY 2024-25, the company's earnings is 19%. Therefore, the shares did not vest, only 29 employees left the organisation during second year. Company believes that additional 23 employees will leave during the third year and earnings will further increase so that the performance target will be achieved in FY 2025-26.

Additionally, it's important to note that JayZee Ltd. has consistently maintained high standards of corporate governance and regulatory compliance, as overseen by Arjun and Karan. The company's financial statements are audited annually by a reputed firm, ensuring transparency and adherence to accounting principles. In a significant strategic move, JayZee Ltd. was considering expanding its market reach through acquisition of BM Autos Ltd., a company renowned for its strong foothold in the global automotive sector. Arjun and Karan, with their financial expertise, meticulously analysed the acquisition's potential benefits. They anticipated that the combined resources and expanded market reach would significantly bolster JayZee Ltd.'s position in the industry. This strategic acquisition was not just about expanding market presence but also about integrating innovative technologies and best practices

from BM Autos Ltd. into JayZee Ltd.'s operations. JayZee Ltd.’s shares are currently traded at ₹ 20. The company has 25,00,000 shares outstanding and its earnings after taxes (EAT) amounted to ₹ 50,00,000. On the other hand, BM Autos Ltd. had 12,50,000 shares outstanding, with a current market price of ₹ 10. Its EAT was ₹ 12,50,000.

After extensive deliberation, BM Autos Ltd. agreed to be get acquired under which JayZee Ltd. would offer the current market value of BM Autos Ltd.'s shares in a stock swap exchange. This acquisition was seen as a strategic fit, enabling JayZee Ltd. to leverage BM Autos Ltd.’s robust market presence and enhance its competitive edge. The acquisition promised to enhance shareholder value, improve operational efficiencies, and foster a more resilient business model, well-equipped to navigate the complexities of the global automotive market.

JayZee Ltd. places a strong emphasis on its employees as key assets to the company, understanding that their well-being and professional growth directly contribute to the organization’s achievements. For many years, JayZee Ltd. has consistently paid bonuses to its employees, recognizing the constructive obligation to reward their hard work and dedication.

JayZee Ltd. discovered that a provision for constructive obligation for payment of bonus to selected employees in the corporate office (material in amount), which was required to be recognized in the annual financial statements for the year ended 31st March, 2023, was not recognized due to oversight of facts. The bonus was paid during the financial year ended 31st March, 2024 and was recognized as an expense in the annual financial statements for the year 2024-25.

JayZee Ltd. has significantly expanded its global presence by acquiring a major stake in a Singapore-based company. During the financial year 2022-23, JayZee Ltd. acquired a 54% stake in SYD Pte Ltd. (SPL), marking its first subsidiary company. This move underscored JayZee Ltd.'s commitment to international presence and leveraging new market opportunities.

Mr. Rajesh Sharma, one of the dynamic directors at JayZee Ltd., was instrumental in this acquisition. His vision strengthening its for international expansion aligned perfectly with the company's growth strategy. Moreover, in the financial year 2024-25, his daughter, Sunita, who has been residing in Singapore for the past six years, was appointed as a director in SPL. Sunita's extensive experience in the region made her a valuable asset to SPL. She was appointed at a monthly remuneration of SGD 5082. (SGD 1 = INR 59). Sunita's appointment was a strategic decision aimed at ensuring strong leadership and effective governance at SPL. Her presence in Singapore facilitated smoother operations and stronger ties between JayZee Ltd. and its first international subsidiary. This expansion into Singapore not only broadened JayZee Ltd.'s market reach but also reinforced its position as a formidable player in the global automotive spare parts industry.

Gumber & Associates has worked with a wide range of industries, providing tailored auditing services that align with the unique needs of each client, and has a long history of successfully navigating intricate tax laws to deliver optimal solutions. The firm's commitment to quality is reflected in its robust internal processes and a team of highly skilled professionals who continually update their expertise to stay ahead of industry trends. CA. Krish, engagement partner, is concerned about the non-verification of physical inventory.

Management of JayZee Ltd. has not undertaken the physical verification of inventories at regular intervals. Inventories constitute 30% of the total assets of the company. Due to non-maintenance of adequate inventory records at the factory, audit team could not undertake the physical verification of inventory. Hence value of inventory as on 31st March, 2025 could not be verified.

Annexure: 1

JayZee Ltd.

(Regd. Office: JayZee tower, Gurgaon, Haryana) Jz

Employees Stock Option Plan 2023

(Plan as approved by the Shareholders through Special Resolution)

1. Name, Objective and Term of plan

1.1 This Employee Stock Option Plan shall be called Employee Stock Option Plan 2023 ("ESOP 2023" / "Plan").

1.2 The objective of ESOP 2023 is to reward employees for association, dedication and contribution to the goals of the Company.

1.3 ESOP 2023 is applicable with effect from 1st April, 2023 on which the shareholders have approved the Plan by way of a special resolution and shall continue to be in force until earlier of:

i. 31st March, 2026; or

ii. The date all the options reserved under the Plan are granted and exercised; or

iii. The date of termination, if any, of the Plan.

2. Grant and Acceptance of Grant

2.1 **Grant of Options**: Each grant under this ESOP 2023 shall be made in writing by the Company to the eligible employees fulfilling the eligibility criteria in a Letter of Grant as may be approved under the ESOP 2023 from time to time.

2.2 **Acceptance of the Grant**: Any employee who wishes to accept the Grant made under ESOP 2023 must deliver to the Company a duly signed acceptance of the Letter of Grant on or before the date (Closing Date) which shall not be more than 60 (Sixty) days from the date of the grant, as specified in the letter of Grant.

3. Vesting Schedule and Vesting Conditions:

Options granted under ESOP 2023 would vest as the company achieves its targets. The shares will vest at the end of

- First year- if the company's earnings is 15%;
- Second year- if the company's earnings is 23% over the two-year period;
- Third year- if the entity's earnings is 29% over the three-year period.

4. Fair value of option: The fair value per share at the grant date is ₹ 122.

Annexure: 2

Raj Malhotra/ Managing Director / JayZee Ltd.

From: "Raj Malhotra" < rajmalhotra@jayzee.com >

Sent: 15th April 2024 10:00

To: "Sanjay Kumar" < sanjay@jayzee.com >

Cc: "Manik Paul" < paul@jayzee.com >

Subject: Custom baggage's related

Attachments:

CA. Sanjay,

Trust you are doing well!

After a productive 4 months business tour in the USA, I am now preparing to return to India. During my stay abroad, I have acquired a few personal items, and as a responsible citizen, I want to ensure that I comply with all customs regulations upon my arrival.

The following are the items I will be bringing back with me:

- Personal Effects items: ₹59,000
- 13-Inch Laptop: ₹37,000
- Jewellery (15 grams, purchased in the USA): ₹67,000
- Music System: ₹1,25,000

I would appreciate it if you could kindly guide me on the proper procedures and any applicable customs duties or exemptions, I should be aware of regarding these items.

Your expertise in finance and taxation matters would be greatly helpful in ensuring everything is in order for a smooth entry into India.

Thank you for your time and assistance. Looking forward to hearing from you soon.

Best regards,

Raj Malhotra

I. Multiple Choice Questions

3.1 JayZee Ltd. has previously intended to use the building for its business operations. However, due to changes in the business environment, the company leased the property to ABC Industries. Determine the value at which the investment property should be recognized and calculate the gain or loss to be recognised from the reclassification of the asset on 1st April, 2024.

(a) ₹ 10 million and no gain or loss

(b) ₹ 8 million and gain of 2 million

(c) ₹ 4 million and loss of 2 million

(d) ₹ 6 million and no gain or loss

3.2 You are required to compute the customs duty payable by Mr. Raj Malhotra with reference to the Baggage Rules, 2016, Assuming if the effective rate of customs duty is 38.50% inclusive of social welfare surcharge, while ignoring the Agriculture Infrastructure and Development cess.

(a) ₹ 67,875

(b) ₹ 43,320

(c) ₹ 38,500

(d) ₹ 54,670

3.3 Determine the amount of expenses to be recognized in the Statement of Profit and Loss at the end of second year in respect of options granted to employees under “ESOP plan 2023” as approved by the shareholders of JayZee Ltd.

(a) ₹ 6,78,750

(b) ₹ 7,23,867

(c) ₹ 8,94,667

(d) ₹ 7,46,703

3.4 JayZee Ltd aims to enhance its manufacturing efficiency and productivity by reducing breakdown losses and defective products. To achieve this, management seeks to assess Overall Equipment Effectiveness (OEE), a key metric for evaluating the performance of the manufacturing process. You are required to calculate 'OEE'.

(a) 83.65%

(b) 81.03%

(c) 81.87%

(d) 83.14%

3.5 Whether JayZee Ltd. was required to pass resolution with respect to appointment of Mrs. Sunita in SPL considering it to be a related party transaction?

(a) No, as such appointment did not amount to appointment of Mrs. Sunita to an office or place of profit in SPL.

(b) Yes, as Mrs. Sunita was a related party to JayZee Ltd. and she would be drawing a monthly remuneration exceeding ₹2.5 lakhs in its subsidiary company.

(c) No, as even though Mrs. Sunita was a related party to JayZee Ltd., she would be drawing remuneration from SPL, its subsidiary company and not JayZee Ltd., itself.

(d) No, as such provisions with respect to related party are not applicable in relation to a foreign subsidiary company.

II. Descriptive Questions

3.6 You are required to analyse whether the situation relating to constructive obligation for payment of bonus is an error requiring retrospective restatement of comparatives, considering that the amount is material.

3.7 (A) Referring to the merger transaction with BM Autos Ltd. in the case study, answer the following questions:

(i) Determine the number of shares of JayZee Ltd, will be issued to the shareholders of BM Auto Ltd. as per the arrangement entered.

(ii) Suppose if BM Autos Ltd.'s P/E ratio is 6.4, then what will be its current market price and what will be exchange ratio on this basis. Also determine JayZee Ltd.'s post-acquisition EPS.

(iii) What should be the exchange ratio if JayZee Ltd.'s shareholders desire that pre-acquisition and post-acquisition EPS should remain the same?

Note: - Round off your calculations upto 2 decimal points.

(B) What is take over by reverse bid?

3.8 How should auditors deal with the issues in the audit report of JayZee Ltd.?

ANSWERS TO THE CASE STUDY 3

I. Answers to the Multiple Choice Questions

3.1 (d) ₹ 6 million and no gain or loss

Reason: As per Ind AS 40, Initial recognition of an owned investment property should be at cost only. As per para 59 of Ind AS 40, "Investment Property" Transfers between investment property, owner-occupied property and inventories do not change the carrying amount of the property transferred and they do not change the cost of that property for measurement or disclosure purposes. Hence if a property which was previously used for business operations, is subsequently reclassified as an investment property, and the company follows the cost model, the investment property should be recognized at its carrying amount at the date of reclassification.

In this case, the property was purchased for ₹ 10 million on April 1, 2020. After 4 years, the carrying amount is ₹ 6 million, after accounting for depreciation. Since as per Ind AS 40, the company has to follow the cost model, the fair value is relevant only for disclosure and not for the recognition of the asset in the balance sheet. Therefore, the investment property should be recognized at the carrying amount of ₹ 6 million, as that is the value at which it is currently held on the books and there will be no gain or loss on such reclassification.

3.2 (d) ₹ 54,670

Reason: Computation of customs duty payable by Mr. Raj Malhotra

Particulars	₹
Personal effects [Duty free clearance is allowed]	Nil
Laptop computer [One laptop computer is exempt when imported into India by a passenger ≥ 18 years of age]	Nil
Jewellery [Duty free jewellery allowance is not available to Mr. Raj since he did not reside abroad for more than 1 year]	67,000
Music system	1,25,000
Total value	1,92,000
Less: General duty-free baggage allowance of ₹ 50,000	50,000
Value of baggage liable to customs duty	1,42,000
Rate of Duty	38.50%
Customs duty @ 38.50% (including social welfare surcharge)	54,670

3.3 (b) ₹ 7,23,867

Reason: Expense for F.Y. 2023-24 = Expected number of employees at the end of the vesting period x Shares per

employee x Fair value of a share x Proportionate vesting period

= 440 employees x 100 shares x ₹ 122 x 1/2 = ₹ 26,84,000

Expense for F.Y. 2024-25 = (Expected number of employees at the end of the vesting period x Shares per employee x Fair value of a share x Proportionate vesting period) - Expense recognized in the year 2023-2024

= (419 employees x 100 shares x ₹ 122 x 2/3) – ₹ 26,84,000

= ₹ 7,23,867

3.4 (c) 81.87%

Reason: Calculation of Shifts:

Total Shifts = Days per week × Shifts per week × Total Weeks

= 6 × 2 × 4 = 48 Shifts

Calculation of Un-Planned Downtime:

Un Planned Loss of minutes per shift	= Total unplanned loss in minutes/Total shifts
	= 1440/48 = 30 mins
Total Loss	= Breakdown Maintenance (in mins) + Set up Changes (in mins) + Power Failure (in mins)
	= 360 + 840 + 240
	= 1440 mins

Calculation of Planned Production time

Planned Production minutes per shift	= Total Time – Planned Downtime
	= 540 - 60
	= 480 mins
Total Time	= 9 hrs × 60 mins

= 540 mins

Planned Downtime = Lunch Break + Miscellaneous Breaks + Preventive Maintenance

= 30 + 15 + 15 = 60

Availability Ratio = {(480 min-30 min)/480 min} = 93.75%

Actual Production = 140 units per shift

Standard Time = 3 minutes

Standard Time Required = 140 units x 3 minutes = 420 minutes

Actual Time Taken = 480 mins - 30 mins. = 450 minutes

Performance Ratio = (420 min/450 min) x 100

= 93.33%

Quality Ratio = (131/140) x 100 = 93.57%

Thus, OEE 0.9375 × 0.9333×0.9357 = 81.87%

3.5 (a) No, as such appointment did not amount to appointment of Mrs. Sunita to an office or place of profit in SPL.

Section 188 of the Companies Act, 2013, along with Rule 15 of the Companies (Meetings of Board and its Powers) Rules, 2014 contain provisions which regulate 'related party transactions'.

Further, Section 2(76) of the Act defines who is a 'related party. As per Section 2(76), 'related party', with reference to a company, means a director or his relative;

Where the transaction or transactions to be entered into as contract or arrangement is for appointment to any office or place of profit in the company, its subsidiary company or associate company at a monthly remuneration exceeding ₹ 2.5 lakh as mentioned in clause (f) of subsection (1) of Section 188, approval by an ordinary resolution is required.

The expression “office or place of profit” means any office or place −

(1) where such office or place is held by a director - if the director holding it receives from the company anything by way of remuneration over and above the remuneration to which he is entitled as director, by way of salary, fee, commission, perquisites, any rent-free accommodation, or otherwise;

(2) where such office or place is held by an individual other than a director or by any firm, private company or other body corporate - if the individual, firm, private company or body corporate holding it receives from the company anything by way of remuneration, salary, fee, commission, perquisites, any rent-free accommodation, or otherwise.

Mrs. Sunita, a relative of a JayZee Ltd.’s director, was appointed as a director in JayZee Ltd.'s subsidiary, SPL, for a monthly salary of ₹ 3 lakhs in the F.Y. 2024-25. This compensation, received as a related party holding a director position in SPL, constitutes her sole remuneration. Consequently, her appointment does not create an 'office or place of profit' with respect to JayZee Ltd. Therefore, JayZee Ltd. was not required to obtain shareholder approval via an ordinary resolution for her SPL directorship.

II. Answers to the Descriptive Questions

3.6 As per paragraph 41 of Ind AS 8, errors can arise in respect of the recognition, measurement, presentation or disclosure of elements of financial statements. Financial statements do not comply with Ind AS if they contain either material errors or immaterial errors made intentionally to achieve a particular presentation of an entity’s financial position, financial performance or cash flows. Potential

current period errors discovered in that period are corrected before the financial statements are approved for issue. However, material errors are sometimes not discovered until a subsequent period, and these prior period errors are corrected in the comparative information presented in the financial statements for that subsequent period.

As per paragraph 40A of Ind AS 1, an entity shall present a third balance sheet as at the beginning of the preceding period in addition to the minimum comparative financial statements if, inter alia, retrospective restatement has a material effect on the information in the balance sheet at the beginning of the preceding period.

In the given case, expenses for the year ended 31st March, 2023 and liabilities as at 31st March, 2023 were understated because of non-recognition of bonus expense and related provision. Expenses for the year ended 31st March, 2024, on the other hand, were overstated to the same extent because of recognition of the aforesaid bonus as expense for the year. To correct the above errors in the annual financial statements for the year ended 31st March, 2025, the entity should:

(a) restate the comparative amounts (i.e., those for the year ended 31st March, 2024) in the statement of profit and loss; and

(b) present a third balance sheet as at the beginning of the preceding period (i.e., as at 1st April, 2023) wherein it should recognise the provision for bonus and restate the retained earnings.

3.7 (A) (i) No. of Shares to be issued to the shareholders of BM Auto:

= (10/20) × 12,50,000 = 6,25,000

(ii) Revised P/E ratio of BM Autos Ltd.

EPS of BM Auto = ₹ 12,50,000/ 12,50,000 = ₹ 1

Market Price = EPS × P/E Ratio

Revised Market Price of BM Autos Ltd. = ₹ 1 × 6.4

= ₹ 6.40

Exchange Ratio

New Exchange Ratio = ₹ 6.40 / ₹ 20 = 0.32 or i.e 0.32 shares of JayZee Ltd. for one share of BM Autos Ltd.

Post-acquisition EPS of JayZee Ltd.

Post-acquisition EPS of JayZee Ltd.

= (₹ 50,00,000 + ₹ 12,50,000) / (25,00,000 + 12,50,000 × 0.32)

= ₹ 62,50,000/ 29,00,000 = ₹ 2.16

(iii) Desired Exchange Ratio

Post-acquisition total number of shares =

Post-Acquisition Earnings / Pre-Acquisition EPS of JayZee Ltd. = ₹ 62,50,000 / ₹ 2 = 31,25,000

Number of Shares Required to be Issued = 31,25,000 - 25,00,000 = 6,25,000

Thus, exchange ratio should be:

Exchange Ratio = 6,25,000 / 12,50,000 = 0.50

(B) In ordinary cases, the company taken over is the smaller company. The concept of takeover by reverse bid, or of reverse merger, is thus not the usual case of amalgamation of a sick unit which is non-viable with a healthy or prosperous unit. Instead, it is a case whereby the entire undertaking of the healthy and prosperous company is to be merged and vested in the sick company, which is non-viable. A company becomes a sick industrial company when there is erosion in its net worth. This alternative is also known as taking over by reverse

bid. The three tests to be fulfilled before an arrangement can be termed as a reverse takeover are specified as follows:

1. The assets of the transferor company are greater than the transferee company.
2. Equity capital to be issued by the transferee company pursuant to the acquisition exceeds its original issued capital.
3. The change of control in the transferee company through the introduction of a minority holder or group of holders.

3.8 In the present case, auditors are **unable to obtain sufficient and appropriate audit evidence** with respect to inventory of the company, neither the physical verification has been done by the management nor adequate inventory records are being maintained by JayZee Ltd. The audit team is also unable to undertake the physical inventory count and as such the value of inventory could not be verified. Further, inventory constitutes **30%** of the total assets of JayZee Ltd., which is significant.

In the above case, the auditor is unable to obtain sufficient appropriate audit evidence on which to base the opinion, and the possible effects on the financial statements of undetected misstatements, if any, **could be both material and pervasive**. Thus, auditors should give a **Disclaimer of Opinion**.

As per Companies Auditors' Report Order 2020 (CARO 2020) dated 25th Feb 2020, the audit report shall include a statement on the following matter:

Whether the physical verification of the inventory has been conducted at reasonable intervals by the management and whether, in the opinion of the auditor, the coverage and procedure of such verification by the management is appropriate. In view of the above the auditor should give a qualification in his report narrating the situation.

CASE STUDY 4

Agriculture and allied industries have been one of the vital sectors of the Indian economy. The crop protection industry refers to companies that manufacture fertilizers, pesticides, fungicides etc. This has a direct connection with agriculture. Allied industries of the agricultural sector include the animal husbandry industry, which is a branch of agriculture. It includes dairy farming, poultry farming, apiculture, aquaculture among others.

Mr. Karnal Singh, the founder of VEN Private Limited, founded the company in Hoshiarpur, Punjab in the year 1965. During the 1960s, the "Green Revolution" development program in India enhanced the productivity of crops. VEN Private Limited became one of the many companies manufacturing crop protection solutions. It focused on the manufacture of pesticides and insecticides.

During 1970s, "White Revolution", another landmark development program, transformed India from a milk deficient nation into the world's largest producer of milk. This popular movement prompted Mr. Karnal Singh to branch out into dairy farming, focusing on milk production and other dairy products. The crop protection business and dairy farm business turned out to be profitable ventures. Over the years, the need for animal feed products especially for livestock increased multifold. Animal feed refers to fodder like compressed and pelleted feed, grains and legumes made specifically to feed livestock cattle. Seeking this opportunity, Mr. Karnal Singh established the animal feed business in the 1990s.

Thus, VEN Private Limited became a diversified agri-business company having three different business verticals - Dairy, Animal Feed and Crop Protection.

Their vision statement reads: ***"Providing sustained value that nourish people and the planet"***

Over the years, each of these divisions has operated with the above vision in mind, aligned with what the company aspires to achieve. Although operations have been wholly contained within Punjab, the business has thrived and become profitable over the years. Management of the company in recent years has been handled by the family members, headed by Mr. Karnal Singh's son Mr. Kunal Singh.

The current management is exploring various opportunities to expand its business across different verticals. As a first step, it intends to assess the performance of each of its divisions as they currently stand in FY 2024–25 within Hoshiarpur, Punjab.

Divisional performance evaluation (Hoshiarpur, Punjab):

At VEN, the performance of each division is assessed independently, and staff members are rewarded based on the division's outcomes. For the financial year ending 31st March 2025, the financial performance of each division is as follows:

- The Dairy Division (DD) reported revenue of ₹ 6,80,00,000 and a profit before interest and tax (PBIT) of ₹ 60,10,000. The netbook value of plant and equipment stood at ₹ 5,65,25,000, and net current assets amounted to ₹ 1,04,75,000.
- The Animal Feed Division (AFD) achieved the highest revenue of ₹ 10,62,50,000 and the highest PBIT of ₹ 63,77,500. The netbook value of its plant and equipment was ₹ 7,43,75,000, and net current assets totaled ₹ 1,51,25,000.
- The Crop Protection Division (CPD) generated revenue of ₹ ,00,00,000, with a PBIT of ₹ 57,66,000. The netbook value of plant and equipment stood at ₹ 2,62,50,000, while the net current assets were ₹ 60,00,000.

It is noted that the PBIT for each division includes a deduction for head office expenses, which have been allocated 2% of the respective division's revenue. The company's cost of capital is 9% per annum, and depreciation on plant and equipment is charged at 15% per annum on cost.

VEN evaluates divisional performance using both Return on Investment (ROI) and Residual Income (RI), calculated based on the controllable profits and using the net book value of plant and equipment at the reporting date as the investment base. These metrics also serve as the basis for the company's performance-linked reward system. In this context, the manager of the Animal Feed Division has claimed that his division is the best-performing unit in the company.

It is proposed to expand the operations of the Dairy Division by venturing into the manufacturing of frozen desserts, as part of the strategic growth initiatives led by the management. For further details, refer to Annexure 1.

Operational efficiency and integration of supply chain management

In its effort to enhance operational efficiency and integrate supply chain management across its verticals, VEN has obtained consultancy services from an entity based in the USA. These consultancy services are aimed at developing a customised enterprise resource planning (ERP) software solution to optimise procurement, production, logistics, and distribution processes. The service is expected to be completed within three months from now. The consideration of USD 1,000,000 for such consultancy services is required to be paid in foreign currency. It is anticipated that the exchange rate will decline by 4% over the three months period and in order to protect the dollar payments after three months, finance manager has decided to hedge the risk involved in foreign currency transaction. He is looking forward to two options to hedge the transaction risk i.e. either Forward cover or Money market cover. The relevant spot and forward rates are:

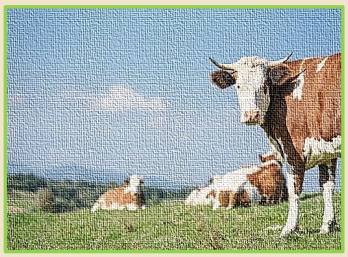
	Spot	**3 Month's Forward**
₹ / $	85.60/ 85.90	87.60/ 87.90

The borrowing rates in India and USA are 8% and 5.5% respectively and deposit rates are 6.5% and 4% respectively.

This ERP implementation has also supported the Crop Protection Division in resolving its warehousing and shipping constraints and enabled integration with Reachme, the e-commerce platform, as further explained in the Annexure 2.

Annexure 1

Diversification Strategy: The Dairy Farm operations for FY 2025–26 at Dhagwar, Kangra district, Himachal Pradesh



VEN perceives that there is an opportunity to grow in the premium milk and dairy product segment. For this it wants to follow a different business operating model than the current one at Hoshiarpur. At Hoshiarpur, raw milk is procured from farmers, which is then used to produce different dairy products. The quality of milk that is used cannot be directly controlled by VEN. The dairy products at the Hoshiarpur unit caters to the wide strata of customers ranging from those preferring economy range products to those wanting premium range products. For premium range products, VEN wants to have complete control over the quality of milk that is the main ingredient of its diary operations. For this reason, it wants to own the breed of cows from which the milk will be procured that will be used to make premium range products. In order to have access to open pastures, where the required conditions can be given to the cows. VEN plans to start a new unit of dairy farm operations at Dhagwar town in Kangra district, Himachal Pradesh. VEN wants to procure high milk-yielding breeds of cows that will provide high quality milk to be used to make premium range products. They will be bred, raised, fed and managed in order to produce milk and other dairy products. Cows will be milked every day. Milk thus obtained will be stored in cold storage and sold to retail distributors on a weekly basis. The milk will be fresh milk and concentrated or sweetened or otherwise altered in any way. Milk production will be the primary focus of this newly developed milk farm. Work for this new dairy farm began in FY 2025-26.

On April 1st, 2025, VEN purchased land for ₹ 3 crores at Dhagwar town for this new dairy farm. On this day, it also purchased 100 cows which had an average age of 3 years. VEN received a non-refundable grant of ₹ 10,00,000 for the acquisition of the cows.

During the financial year 2025-26, VEN incurred the following costs:

(i) ₹ 12,00,000 to raise and feed the animals in terms of taking care of their foods requirements and managing their upkeep to maintain them in healthy condition.

(ii) ₹ 5,00,000 as breeding fee to a local farmer.

On 1st October 2025, 20 calves were born. There were no other changes in the number of animals during the year ended 31st March 2026.

On March 31st, 2026, VEN had 10,000 litres of milk in cold storage, which had not been sold to retail distributors. The milk was sold shortly after the year end at the same market price, which had not changed since the year end.

Information relating to fair value

As of April 1st, 2025, the fair value less cost to sell of the land was ₹ 3 crores. Over the next two valuation dates, the value appreciated to ₹ 3.10 crores on October 1st, 2025, and further to ₹ 3.15 crores by March 31st, 2026. For milk, the fair value per litre stood

at ₹ 40 on April 1st, 2025, increasing to ₹ 42 by October 1st, 2025, and further to ₹ 45 as of March 31st, 2026. Regarding livestock, the fair value of a newborn calf rose from ₹ 30,000 per calf on April 1st, 2025, to ₹ 35,000 on October 1st, 2025, and reached ₹ 40,000 by March 31st, 2026. A 6-month-old calf was valued at ₹ 32,000 on April 1st, 2025, ₹ 38,000 on October 1st, 2025, and ₹ 44,000 by March 31st, 2026. The fair value of a 3-year-old cow increased from ₹ 42,000 per cow on April 1st, 2025, to ₹ 47,000 on October 1st, 2025, and reached ₹ 50,000 by the end of the financial year. Similarly, a 4-year-old cow was valued at ₹ 42,000 per cow on April 1st, 2025, ₹ 48,000 on October 1st, 2025, and ₹ 52,000 on March 31st, 2026.

Product Development Strategy: Introduction of frozen dessert products at Hoshiarpur, Punjab within the Dairy Division

It has been proposed to expand the business of Dairy Division at Hoshiarpur, Punjab by venturing into manufacture of frozen desserts. This would require additional investment in plant and equipment of ₹ 1,75,00,000 which will generate a contribution of ₹ 95,00,000 per annum. The annual fixed cost of the division will increase by ₹ 8,50,000 (excluding depreciation). Net current assets of this division will increase by ₹ 25,00,000 due to the acceptance of this proposal.

Annexure 2: Expansion plans for Crop Protection Division for FY 2025-26



Crop Protection Division primarily sells pesticides and insecticides. The main market for the company has been Punjab. Recently, Mrs. Gunjan Wadhwa, the head of the CPD informed the management at VEN that there is a growing demand for these products from the nearby states of Haryana and Uttar Pradesh. These are from small pockets of rural towns, comprising farmers who have small landholdings and do not have direct access to VEN's distributors in Punjab. Therefore, they buy these products from agents, who charge a hefty commission, which reduces their profit margins. The CPD in the meantime is looking to expand its market presence outside Punjab. Mrs. Wadhwa sees an opportunity to expand in rural towns rather than in larger semi-urban cities where competition is stiff. An additional hurdle that the company faces is the lack of warehousing and shipping facilities, since VEN has had its operations only within Punjab. While VEN's newly implemented ERP system has significantly improved internal efficiencies across procurement, production, logistics, and distribution, it does not substitute for the physical infrastructure and external network required to penetrate new rural markets. Since the project is still at a nascent stage, Mrs. Wadhwa does not recommend investing in warehousing and shipping facilities in these newer markets yet. Hence, she approaches Reachme, an e-commerce company who are willing to connect sellers like VEN with buyers like small farmers in rural areas. The company earns a seller fee for the sales made through the website. Buyers pay a yearly subscription fee in order to access the website services. Further the company is willing to provide VEN warehousing and shipping services for an additional fee.

I. Multiple Choice Questions

4.1 The land on which VEN has its dairy farm operations at Dhagwar, Himachal Pradesh is classified as agricultural land. Which of the following statements is true?

(a) Income from dairy farming can be considered agricultural income and is therefore exempt from tax.

(b) Income from dairy farming can be considered agricultural income as like traditional agricultural activities, it is related to agricultural land.

(c) Income from dairy farming can be considered business income and is non-agricultural income

(d) Income from dairy farming performed on agricultural land can be apportioned between business income and agricultural income based on certain pre-defined ratios.

4.2 The Animal Feed Division, at Hoshiarpur is headed by Gurwinder Singh. He wants to improve the division's Economic Value Added (EVA). Which of the following can help the division achieve this?

(a) Operating profits can be improved without investing more capital

(b) Choose projects where an additional infusion of capital gives a return that is less than the cost of obtaining this additional capital

(c) Discontinue projects where the return on investments yields more than the cost of capital

(d) Change the cost of capital to reflect EVA that is favourable

4.3 What type of business model does Reachme follow?

(a) Hypermarket model

(b) Digital Platform model

(c) Freemium model

(d) Service Ecosystem model

4.4 Suppose if after 3 months ₹ / $ Spot Rate happens to be 89.00/ 89.34 the expected loss of……..is likely to be avoided by company if it takes forward cover.

(a) ₹ 11,00,000

(b) ₹ 14,00,000

(c) ₹ 14,40,000

(d) ₹ 17,40,000

Note: Consider all calculations **up to 2 decimal points** for accuracy.

4.5. The compliance officer of VEN Private Limited, Mrs. Nikita, is unsure whether prior RBI approval is applicable for the foreign exchange remittance for the purpose of obtaining such consultancy services from abroad.

Advise Mrs. Nikita on whether prior approval from the Reserve Bank of India (RBI) is required for remitting foreign exchange:

(a) Yes, prior RBI approval is required because the amount exceeds the permissible limit under FEMA regulations.

(b) No, prior RBI approval is not required because the amount is within the permissible limit under FEMA regulations.

(c) Yes, RBI approval is mandatory for all payments to foreign entities irrespective of the amount involved.

(d) No, prior RBI approval is not required since the company is engaged in agricultural activities.

II. Descriptive Questions

4.6 To EVALUATE divisional performance and support strategic decisions on expansion and performance measurement, answer the following:

(i) **Compute** the Return on Investment (ROI) and Residual Income (RI) for each division. **Assess** the validity of the claim made by the manager of the Animal Feed Division based on these performance measures.

(ii) **Evaluate** the proposal to expand the Dairy Division for a one-year period. Based on ROI and RI analysis, **advise** management on whether the project should be accepted.

(iii) **Analyse**, with the help of **calculations** from the Dairy Division's proposal, how ROI can improve over time with the aging of assets.

(iv) Recognizing the limitations of purely financial metrics, the management of VEN Ltd. intends to incorporate Non-Financial Performance Indicators (NFPIs) for the following functional areas:

(a) Human Resource Management

(b) Product and Service Quality

(c) Brand Awareness and Company Profile

Explain the relevance and scope of NFPIs in evaluating performance in each of these areas.

Note- Compute ROI and RI by considering "Net Current Assets" along with "Net Book Value of Plant and Equipment".

4.7 Hari Singh, the head of the Dairy Division at Dhagwar, Himachal Pradesh. He has done his masters in dairy farming (specialization). Financial performance will be one of the metrics that is used to assess his performance for the year. Since he does not have a background in finance or commerce, he wishes to understand the impact of the above transactions on the financial reports that are being prepared for his division for the year 2025-26.

As the Chief Accountant, guide him about how the above information has been accounted for in the financial reports prepared

as per Indian Accounting Standards for the year ended March 31st, 2026.

PREPARE an extract of the profit and loss account and the Balance Sheet to show how these transactions will be reflected for FY 2025-26.

Note: VEN uses the cost model to account for land acquisitions.

4.8 Advise the VEN whether it should adopt Forward Cover or Money Market Cover? Consider all calculations up to 2 decimal points for accuracy.

ANSWERS TO THE CASE STUDY 4

I. Answers to the Multiple Choice Questions

4.1 (c) Income from dairy farming can be considered business income and is non-agricultural income

Reason: The correct answer is (c) Income from dairy farming can be considered business income and is non-agricultural income. Dairy farm operations are being performed on agricultural land, hence there is an indirect connection to agricultural land. However, it is not correct to classify income derived from dairy farm operations to agricultural income merely on account of this connection. In dairy farm operations, it is the livestock like cows, sheep and buffalo which are the main component.

4.2 (a) Operating profits can be improved without investing more capital

Reason: The correct answer is (a) EVA can be improved when operating profits can be improved without investing more capital. This can be achieved if more efficiency is built into the business operations, revenue can be boosted by introducing more products or expanding market share, reducing costs etc.

In statement (b), the return on capital infused should be more than the cost of additional capital. In statement (c), projects where return is less than cost of capital need to be discontinued. Statement (d) implies that the cost of capital should be manipulated to reflect a favourable EVA, which is not ethical.

4.3 (b) Digital Platform model

Reason: The correct answer is (b) Digital Platform model.

More specifically Reachme follows the Business to Consumer digital platform model. Reachme is a digital platform that connects business to retail consumers.

4.4 (c) ₹ 14,40,000

Reason: Correct Option C = ₹ 14,40,000

Do not take forward Cover	Take forward Cover
Present Cost: $ 10,00,000 × ₹ 85.90 = ₹ 8,59,00,000 After three months $10,00,000 × ₹ 89.34 = ₹ 8,93,40,000	Take forward Cover at 87.90 Expected Cost after three months: $10,00,000 × ₹ 87.90 = ₹ 8,79,00,000
Difference in cost between two options = ₹ 8,93,40,000 - ₹ 8,79,00,000 = 14,40,000	

4.5 (b) No, prior RBI approval is not required because the amount is within the permissible limit under FEMA regulations.

Reason: Correct option is (b).

The following remittance by person other than individual shall require prior approval of the Reserve Bank of India:

Remittances **exceeding** USD 10,000,000 per project for any consultancy services in respect of infrastructure projects and

USD 1,000,000 per project, for other consultancy services procured from outside India.

II. Answers to the Descriptive Questions

4.6 (i) Calculation of ROI (Return on Investment)/ RI (Residual Income) for FY 2024-25 for the divisions at Hoshiarpur, Punjab (Amount in ₹)

Particulars	Dairy Division	Animal Feed Division	Crop Protection Division
a. Profit before interest and tax	60,10,000	63,77,500	57,66,000
b. Revenue	6,80,00,000	10,62,50,000	6,00,00,000
c. Head office expenses [@2% of (b)]	13,60,000	21,25,000	12,00,000
d. Controllable operating profit (a)+(c)	73,70,000	85,02,500	69,66,000
e. Net book value of plant and equipment	5,65,25,000	7,43,75,000	2,62,50,000
f. Net current assets	1,04,75,000	1,51,25,000	60,00,000
g. Investment (e)+(f)	6,70,00,000	8,95,00,000	3,22,50,000
h. ROI [(d)/(g) × 100]	11%	9.50%	21.6%
i. Required return [@9% of (g)]	60,30,000	80,55,000	29,02,500
j. RI [(d)-(i)]	13,40,000	4,47,500	40,63,500

The claim made by the manager of the Animal Feed Division is **invalid** because it registered worst performance among the three divisions under both the criteria. The ROI of Animal Feed Division is 9.50%, which is less than (11.00% and 21.60%) other two divisions, whereas RI is ₹ 4,47,500 which is also less than (₹ 13,40,000 and ₹ 40,63,500) both other divisions.

It is important to note that the Animal Feed Division earns the highest profit, however **since its investment is high** the ROI and RI are the lowest compared to the other divisions.

(ii) Evaluation of Expansion Proposal for frozen desserts – Dairy Division, Hoshiarpur, Punjab

ROI/ RI for proposed expansion (for first year)

Particulars	Amount in ₹
a. Additional investment in plant and equipment	1,75,00,000
b. Depreciation for first year on the above investment (15%)	26,25,000
c. Net book value of additional investment in plant and equipment at reporting date (a-b)	1,48,75,000
d. Additional net current assets	25,00,000
e. Total additional investment (c)+(d)	1,73,75,000
f. Additional contribution	95,00,000
g. Additional fixed cost	8,50,000
h. Net addition to earning (f)-(g)-(b)	60,25,000
i. ROI [(h)/(e)×100]	34.68%
j. Required return [9% of (e)]	15,63,750
k. RI [(h)-(j)]	44,61,250

Advise

ROI Criteria – Management of VEN private limited **must expand** the business of Dairy Division by venturing into manufacturing of frozen desserts, because the proposed expansion expected to generate ROI at rate of **34.68%, which is not only more than existing ROI of Dairy Division (11%) but also more than overall ROI as well** (because among the three division the maximum ROI generated by Crop Protection Division i.e., 21.6%).

RI Criteria – Management of VEN private limited **must expand** the business of Dairy Division by venturing into manufacturing of frozen desserts, because the proposed expansion expected to generate additional RI of **₹ 44,61,250**.

(iii) ROI improves with age of the assets

Since ROI is rate of earning as percentage of investment, hence while assets getting older the amount of investment reduced; resultantly **if same productivity or efficiency is maintained** then ROI improves. Same can be seen through calculations below that ROI improves from 34.68% in first year to 40.85%, and 49.69% respectively in second and third year.

ROI for proposed expansion over years (Amount in ₹, round off to nearest rupee)

Particulars	Second Year	Third Year
a. Plant and equipment at beginning of year	1,48,75,000	1,22,50,000
b. Depreciation for year on the above plant and equipment (15%)	26,25,000	26,25,000
c. Net book value of plant and equipment at reporting date (a)-(b)	1,22,50,000	96,25,000
d. Net current assets (assumed to be constant)	25,00,000	25,00,000
e. Total relevant investment (c)+(d)	1,47,50,000	1,21,25,000
f. Contribution (assumed to be constant)	95,00,000	95,00,000
g. Fixed cost (assumed to be constant)	8,50,000	8,50,000
h. Net addition to earning (f)-(g)-(b)	60,25,000	60,25,000
i. ROI [(h)/(e)×100]	40.85%	49.69%

(iv) Non-Financial Performance Indicators (NFPIs) are sustainable action-based indicators. For example, employee training will increase the profit & let them feel empowered, putting effort in research and development will result in a high brand image & high intellectual property rights. Hence for being sustainable rather being only profitable an organisation needs to include NFPIs as part of performance matrix in addition to financial performance Indicators. Although the scope of NFPIs substantially depends upon width and depth of organisation's objective, operations and strategies, but generically VEN Private Limited can consider–

Human resources management

Superior performance comes from superior processes. Who actually devise and execute superior processes to build an organisation with competitive advantage? It is the people (human resources) and their efforts. Hence human resources are a significant element for success of any organisation. If they performance well, then entire organisation automatically performs well; hence measures such as staff turnover, absenteeism, job satisfaction, and offer letter accepted shall be part of performance metrics.

Product and service quality

What make any business **distinct from others**, what are the sources of competitive advantage? It is substantially the value which its products or services capable to create for the users; and quality is important determinant of value. Simply saying quality is conformance to need to user. Hence the following performance measures, owning to quality shall be part of performance metrics.

1. What are the functions that product or service offers and how much value these are capable to generate?

2. Where do our product stand in market in comparison that of competitors, especially rivals?

3. Is product capable to generate further superior performance and scope of innovation?

Brand awareness and company profile (brand equity)

Non-financial performance measures consider the **brand equity (value of the brand)** as one of the significant performance measures. Brand value is largely based upon factors like **customer's awareness & loyalty** which includes consumer behaviour also perceived quality, stakeholder's expectation and organisation ability to meet them, and factors like patents and trademarks etc.

4.7 Extract from Balance Sheet

Non-Current Asset	**Note Reference**	**Amount (₹)**
Property, Plant and Equipment		
Land	Note C	3,00,00,000
Biological assets other than bearer plants		
Dairy Cows	Note A (iii)	52,00,000
Calves	Note B	8,80,000
Inventory		
Milk	Note E	4,50,000

Extract from the Statement of Profit & Loss

	Note Reference	**Amount (₹)**
Income		
Change in fair value of purchased dairy cow	Note (A) (iii)	10,00,000

Change in fair value of newly born calves	Note B	8,80,000
Grant received	Note D	10,00,000
Fair value of milk	Note E	4,50,000
Total Income		**33,30,000**
Expenses		
Maintenance	Note A (iv)	12,00,000
Breeding fee	Note A (iv)	5,00,000
Total Expense		**17,00,000**
Net Income		**16,30,000**

Working Note

The impact of various transactions mentioned in Annexture 1, as regards dairy operations at Dhagwar, Himachal Pradesh for FY 2025-26 in the financial reports, of FY 2025-26 are as below:

(A) Acquisition of Dairy Cows: The herd of cows are biological assets as per Ind AS 41 that covers reporting requirements for the agricultural sector. It mentions that agricultural activity includes the management of the transformation of biological assets (living plants and animals) into agricultural produce (harvested product of the entity's biological assets). Here dairy cows (animals) are used to produce dairy products like milk (harvested produce). Dairy cows, that represent the biological asset will be recorded as Separate line item "Biological Asset other than bearer plants" under non-current asset in the Balance Sheet using the fair value model laid down in Ind AS 41.

Accordingly, the 100 cows which had an average age of 3 years that were purchased on April 1st, 2025, had a fair value of ₹ 42,000 per cow. As of year end, there has been an increase in the value of this biological asset. This is on account of 2 factors:

(i) Increase in the price of a 3-year-old cow from ₹ 42,000 per cow to ₹ 50,000 per cow. This represents an increase of ₹ 8,00,000 on account of the increase in price (₹ 50,000 per cow - ₹ 42,000 per cow = ₹ 8,000 per cow × 100 cows = ₹ 8,00,000). This will be recognized in the profit and loss account for FY 2025-26.

(ii) Physical change in cow, due to the passage of 1 year increases the average age of cows from 3 years to 4 years. On account of this on March 31st, 2026, while a 3-year-old cow is valued at ₹ 50,000 per cow; the cows that now have an average age of 4 years as of this date are valued at ₹ 52,000 per cow. Therefore, each cow has had its market value increase by ₹ 2,000 per cow as of March 31st, 2026. This increase in the value of the biological asset due to physical change works out to ₹ 2,00,000 (₹ 52,000 per cow - ₹ 50,000 per cow) ×100 cows). This will be recognized in the profit and loss account for FY 2025-26.

(iii) Accordingly, as of March 31st, 2026, the Balance Sheet will reflect ₹ 52,00,000 as the value of 100 cows with an average age of 4 years (100 cows × ₹ 52,000 per cow). The profit and loss account will show an income of ₹ 10,00,000 on account of (a) price increase in the value of biological asset ₹ 8,00,000 (refer point (i) above) and (b) increase in value due to physical change of the biological asset ₹ 2,00,000 (refer point (ii) above).

(iv) Corresponding expenses, of ₹ 5,00,000 breeding fees paid to the local farmer and ₹ 12,00,000 various herd maintenance expenses will be considered as expenses in the profit and loss account for the year.

(B) Calves born during FY 2025-26: These biological assets have been acquired on account of breeding the cows. It is not possible to calculate the “cost of acquisition” of such calves

and hence they will be shown as an asset in the Balance Sheet valued at fair value as on March 31st 2026, and this value will be credited to the profit and loss as income for the year.

It is given that 20 calves were born on October 1st, 2025. Therefore, their age, as on March 31st 2026, will be 6 months. The fair value net of any cost to sell of these calves as on March 31st, 2026, is ₹ 44,000 per calf. Hence the value of 20 calves at the year end will be ₹ 8,80,000, in the balance sheet as well as considered as income in the profit and loss for the year.

(C) Land acquisition: The purchase of land is not covered under Ind AS 41. The relevant standard would be Ind AS 16 "Property, Plant and Equipment". According to it land would be considered as an asset, valued at cost in the Balance Sheet as of March 31st 2026. Since the useful economic life of the land is infinite, no depreciation can be charged against it. Therefore, the value of land as shown in the Balance Sheet as of March 31st 2026, will be at the cost of acquisition which is ₹ 3 crores. Any subsequent change in market value post-acquisition is ignored under the cost model. ***(Please note that the allowed alternative corresponding treatment under revaluation model permits the land to be revalued to market value with the revaluation surplus taken to other comprehensive income).***

(D) Grant received: VEN received a non-refundable grant of ₹ 10,00,000 for acquisition of cows. It is not subject to any conditions or requirements to be satisfied; hence it is an unconditional grant. As per Ind AS 20, this grant needs to be considered as income of the company and credited to the profit and loss account.

(E) Inventory of milk: Milk is an agricultural produce and will be measured on the same basis as biological assets. As of March 31st, 2026, VEN has 10,000 litres of milk in cold storage, the

fair value of which is ₹ 45 per litre. Therefore, milk would be valued at ₹ 4,50,000. This will be reflected as part of Inventory in the Balance Sheet. This is regarded as "cost" for future application of Ind AS 2 to the unsold milk. The fair value of milk is also considered as income in the profit and loss account.

8. Forward Cover

Amount Payable under Forward Cover ($10,00,000 × ₹ 87.90) = ₹ 8,79,00,000

Money Market Hedge

To pay $ after 3 months' company shall require borrowing in ₹ and translate to $ and then deposit in $.

For payment of $10,00,000 in 3 months @ 4.00% interest p.a. the amount required to be deposited now ($10,00,000/1.01) = $9,90,099.01

With a spot rate of 85.90 the ₹ loan needed will be = ₹ 8,50,49,504.96

Loan repayable after 3 months @ 8.00% p.a. interest will be ₹ 8,50,49,504.96 (1.02) = ₹ 8,67,50,495.06

Advise

Since outflow of cash shall be least in case of Money Market Hedge hence it should be opted for.

CASE STUDY 5

Safe and Wise Advisory Limited (SWAL) is well established financial planning & risk advisory firm of the country with nation-wide presence. SWAL is engaged in selling third party products be it financial products or insurance products (life assurance only). Financial advisory business of SWAL is doing well and contributing to the half of gross revenue of group and two-third of overall group's bottom line, but insurance brokerage business is not performing as per expectation. 'Independent and impartial advice' to client is unique selling point of SWAL.



SWAL was established by Mr. Ravi Verma around two decade ago (when life-assurance business goes private), at then it was one division business i.e. assurance brokerage business. Mr. Ravi Verma is dynamic leader and presently leading the company as CEO, apart from being major shareholder of the company.

SWAL is widely acknowledged in market for two distinct features, first being presence wide across the nation, in form of 'sub-agency offices' equipped with professionally trained sale staff headed by financial planner or advisor, where customer can take advise and discuss opinion prior to investing/ buying any insurance or financial product. SWAL has 'sub-agency offices' in 580 cities, towns and blocks. Locations are semi-commercial in nature but prominent. SWAL has practice to sign 30-year lease, when so ever taking and 'sub-agency office' on lease in order to reduce the lease cost and bring stability.

Secondly, SWAL sold product of all third parties, hence provide a range of products to its client to choose from. In 2010, SWAL signed a 15 year's agency agreement with all 23 life insurance companies recognised then. SWAL's tagline is also depicting the same 'we are ethically committed to

understand and deliver your needs'. SWAL believes in organic growth and listed on stock market 3 years back to float additional capital to fund more 'sub-agency offices'.

22 out of these 23 life assurance companies are private and registered themselves with regulatory between the year 2000-2009 for a period of 25 years. Considering the default by few insurance firms and increasing customer complaints, regulator of insurance business in country tighten the registration criteria and harden the norms.

Typically each of 'sub-agency office' comprises three regular and one contractual employee. One being financial planner/ advisor, 2 sales and relationship officer and contractual worker in role of support staff and vested with miscellaneous clerical responsibilities. The on-roll number of employees engaged in assurance brokerage business has been increased to 1,564 from 720 five year ago (up-till 3 year ago number was 845 but since expansion of 'sub-agency' office division it is around 1,500).

Market trend is changing, since the SWAL commence the business. Each of such insurance company, now has their own network of branch offices to sale their insurance product directly; that too at more prominent locations. SWAL counter this step by highlighting its 'independence and impartial advice' practice, although SWAL managed to retain the revenue at same level, but this result in low profitability of 'sub-agency office' business. Now these insurance companies are not authorising any new agent.

Safe and Wise Advisory Limited (SWAL), a service-oriented company, sought to expand its market reach. To achieve this, SWAL established a dedicated 'E-platform' division, 'Policy at Your Click,' staffed by 50 professionals. Giganet is a service provider offering broadband and voice call services. SWAL intends to obtain broadband connectivity from Giganet to support the operational needs of its E-platform. For data security reasons, SWAL also wants to retain the right to procure the modem from any vendor of its choice at any time. So, SWAL has entered

into an agreement (Annexure1) with Giganet for Broadband Services and for Modem procurement on 15th June 2024.

SWAL Ltd. requires a robust data management software to store, manage, and secure its valuable data against unauthorized access and malware threats. In pursuit of a reliable solution, SWAL engaged with DBMS Ltd., a renowned and experienced leader in data security solutions. After extensive negotiations spanning over a month, both parties have reached an agreement under which DBMS Ltd. shall provide SWAL with a license to use its proprietary data management software ("Software"). DBMS Ltd. is the sole owner and developer of the Software and agrees to grant SWAL a license under the terms and conditions set forth in Annexure 2.

SWAL's **'E-platform'** enables the seamless online sale of life insurance policies, strategically compensating for losses incurred by its sub-agency network. The insurance company has introduced multiple life insurance plans, all of which are available for purchase through SWAL's E-platform. Acting as an intermediary, SWAL facilitates the sale of these policies and earns a commission from the insurance company on each policy sold through its platform. This commission-based model ensures a sustainable revenue stream for SWAL while streamlining the insurance purchasing process for customers.

The insurance company offers a range of life insurance plans, each with distinct premium structures and allocations for investment or savings components. Below is a detailed description of these plans:- **Investment-Linked Policy** – This policy requires an annual premium payment of ₹1,00,000. A portion of ₹60,000 is explicitly allocated towards investment or savings, which is clearly communicated to the policyholder at the time of service supply. The remaining amount covers risk protection and other associated costs. **Single Premium Annuity** – This plan involves a one-time premium payment of ₹ 5,00,000. Unlike investment-linked policies, this plan does not have a separate investment or savings component. The entire premium is utilized to provide annuity benefits, ensuring a steady stream of income for the policyholder.

Regular Life Insurance – Under this policy, the policyholder pays an annual premium of ₹80,000. However, there is no explicit allocation for investment or savings, meaning the distribution of funds between risk coverage and any potential savings component is not clearly defined. **Pure Risk-Cover Policy** – This policy is designed solely for risk coverage, with an annual premium of ₹ 50,000. The entire premium is dedicated to providing financial protection against life risks, without any portion being allocated for investment or savings. These plans cater to different financial and coverage needs, offering flexibility based on the policyholder's preferences and risk appetite.

JS & Associates are at a crossroads regarding their audit approach for SWAL for the financial year ending March 31st, 2025. Historically, they have identified management override of controls and revenue recognition as significant risks. However, their audits in the past 2 financial years yielded clean reports with no issues detected in these areas.

This absence of recent red flags presents a dilemma. On one hand, maintaining a conservative approach suggests continuing to assess these areas as significant risks. This ensures a thorough examination and mitigates the chance of missing potential issues that could arise due to unforeseen circumstances or changes within SWAL.

On the other hand, consistently clean reports raise the question of continued significance. JS & Associates might consider performing a more focused assessment or reducing the emphasis on these risks while still acknowledging their potential impact. This could streamline the audit process without compromising effectiveness. As part of a risk-based audit approach, JS & Associates focus on areas with a higher likelihood of material misstatement.

Supported by revenue figures given below (in '000 Crores), analysts reach to conclusion that growth in the assurance brokerage business is slowing down both for SWAL and industry overall–

Market Size/Year	2024-25	2023-24	2022-23	2021-22	2020-21
SWAL's assurance brokerage business	326	320	312	298	280
Total market size of life assurance	2,240	2,198	2,122	2,004	1,960

Revenue earned by each division of assurance brokerage business (in term of age of the client), is shown in table below for F.Y. 2024-25–

Division/Age	20-30	30-40	40-50	50-60	60+	Total
'Sub-agency office' division	2	25	38	164	51	280
'E-platform' division	8	28	8	2	0	46
Total Business of SWAL						326

Since the profitability of 'sub-agency office' division is declining, hence the strategic review committee of board of directors are concerned about the company's declining profitability due to poor performance of 'sub-agency office' division and suggest that the 'sub-agency office' division should be sold off and that SWAL shall re-position its assurance business as an online solution.

Extract from financial statement for agency office division only (figures in '000 Crores) –

Particulars/Year	2024-25	2023-24	2022-23
Revenue	280	272	250
Profit before interest and tax	18	16	31
Shareholder's' Equity	156	150	150
8% Long term debt	78	64	50
Current Liabilities	455	437	395
Current Assets	605	565	540

Applicable tax rate is 22%. The nature of cost incurred by 'sub-agency office' division is more or less balanced between the variable and fixed. Fixed costs are largely committed in nature.

But the CEO does not agree to the suggestion made by strategic planning committee, because CEO is of belief that SWAL's USP or original business model is 'sub-agency offices' through which they ensure 'independence and impartial advice' to their clients.

On 20/04/2025 – a board meeting of directors was held to discuss on continuance or sale of the 'Sub-Agency Office' division and few other matters, the minutes of which are given in Annexure 3.

Annexure 1

AGREEMENT FOR BROADBAND SERVICES AND MODEM PROCUREMENT

This Agreement is made and entered into on this 15th day of June, 2024, by and between:

First party i.e. **Safe and Wise Advisory Limited (SWAL),** a company duly incorporated and having its registered office at New Delhi, hereinafter referred to as "SWAL"; and Second party i.e. **Giganet Ltd.,** a company duly incorporated and having its registered office at Chandigarh, hereinafter referred to as "Giganet."

Terms of Agreement shall be as follows:

1) Scope of Services

Giganet shall provide broadband and voice call services to SWAL in accordance with the selected service plan for a period agreed as per terms. Additionally, SWAL also reserves the right to opt for any single plan individually, i.e. voice call or broadband services at any time. Giganet offers various plans, including broadband services, voice call services, and a combination of both to its customers.

2) Modem Procurement

Giganet shall provide the Modem device to SWAL. But also, SWAL reserves the right to procure the modem independently from any vendor, and this Agreement shall not impose any restriction in this regard.

3) Term and Termination

The term of this Agreement shall be for a period of three (3) years from the effective date. Upon expiration, the Agreement may be renewed by mutual consent of both parties under terms and conditions agreed upon at the time of renewal.

4) Pricing

The modem shall be sold at a one-time cost of ₹ 10,000. The combined broadband and voice call service plan shall be provided at an annual pricing of ₹ 50,000.

5) Miscellaneous

- Any amendments or modifications to this Agreement shall be made in writing and duly signed by both parties.
- Any dispute arising out of or in connection with this Agreement shall be resolved amicably between the parties. If not resolved, it shall be subject to arbitration under the applicable laws.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date first above written.

Signed for and on behalf	Signed for and on behalf of
of Safe and Wise Advisory Limited (SWAL)	Giganet Ltd.
Ravi Verma	*Mahesh Makhija*
(CEO, Safe and Wise Advisory Limited)	(Managing Director, Giganet Ltd.)

Annexure 2

SOFTWARE LICENSE AGREEMENT

This Software License Agreement ("Agreement") is made and entered into on this 20th day of June, 2024, by and between:

First party i.e. **Safe and Wise Advisory Limited (SWAL),** a company duly incorporated and having its registered office at New Delhi, hereinafter referred to as "SWAL"; and Second party i.e. **DBMS Ltd.,** a company duly incorporated and having its registered office at Bangalore, hereinafter referred to as "DBMS."

WHEREAS:

DBMS Ltd. is the owner and developer of a data management software ("Software"). DBMS Ltd. agrees to grant SWAL a license to use the Software under the terms and conditions set forth herein.

SWAL intends to utilize the Software for its business operations while maintaining operational stability.

NOW, THEREFORE, in consideration of the mutual promises and covenants contained herein, the Parties agree as follows:

a) Grant of License

DBMS Ltd. hereby grants SWAL a non-exclusive, non-transferable license to use its Data Management Software for their internal business operations.

b) Updates and Upgrades

DBMS Ltd. shall provide updates and upgrades to the Software on a when-and-if-available basis. SWAL shall have sole discretion in determining whether to install such updates or upgrades.

c) Software Integrity

DBMS Ltd. shall not engage in any activity that alters the functionality of the Software without SWAL's prior written consent.

d) Term of contract

The term of this Agreement shall be for a period of two (2) years from the effective date.

e) Consideration

SWAL shall pay DBMS Ltd. an annual fee of ₹ 4,00,000 (inclusive of all taxes, surcharges and cess) for the licensed use of the Software.

f) Miscellaneous

- Any modifications or amendments to this Agreement must be made in writing and signed by both parties.
- Any disputes arising out of or related to this Agreement shall be resolved amicably between the parties. If unresolved, the matter shall be subject to arbitration as per applicable laws.

IN WITNESS WHEREOF, the parties hereto have executed this Agreement as of the date first above written.

Signed for and on behalf of SWA Ltd.	Signed for and on behalf of DBMS Ltd.
Ravi Verma	*Jay Soni*
(CEO, Safe and Wise Advisory Limited)	(Managing Director, DBMS Ltd.)

Annexure 3

SWAL

(Safe and Wise Advisory Limited, Reg Address. New Delhi)

Extract of Minutes of the 89th Meeting of the Board held on April 20, 2025 at New Delhi

Item: To discuss the sale or continuance of sub agency division, managerial remuneration and several other matters.

Decision on the 'Sub-Agency Office' Division

The Board deliberated on the continuance or sale of the 'Sub-Agency Office' division. After discussions, it was decided that further evaluation of strategic options would be conducted before making a final decision.

Clarification on Maximum Remuneration

The Company Secretary, Mr. Amit Binoi, was asked about the maximum permissible remuneration for all Directors and the Manager in a financial year. He provided the necessary clarification, confirming that the company follows an annual remuneration

structure while ensuring compliance with statutory limits. The Board noted that the company has Mrs. Jalpa Sen as the Whole-time Director (WTD) and recently appointed Mr. Keyur Valia as the Managing Director (MD). It was emphasized that remuneration must adhere to the prescribed statutory limits for the MD, WTD, and Manager collectively. During the scrutiny of accounts for the financial year 2024-25, it was observed that Mrs. Jalpa Sen, heading the Sub-Agency Office division, had inadvertently drawn remuneration exceeding the statutory limit in the previous financial year due to an oversight. The Board directed corrective action to be taken to ensure future compliance.

Risk Assessment of loan given to – Savya Ltd.

A resolution was passed approving a 10-year amortizing loan of ₹100 crore to Savya Ltd., from surplus funds. The Board reviewed the financial implications, considering:

Probability of Default (PoD): Estimated at 0.5% over the next 12 months at initial recognition.

Loss Given Default (LGD): Assessed at 25% of the balance outstanding.

Credit Risk Assessment: Changes in the 12-month PoD were considered a reasonable approximation for evaluating the lifetime PoD and determining any significant increase in credit risk.

Economic Outlook: Relevant economic factors and credit risk expectations were taken into account. The Board directed that ongoing monitoring of credit risk and financial exposure should be conducted to ensure effective risk management.

Conclusion: There being no further business, the meeting concluded with a vote of thanks to the Chair.

Signed

Ravi Verma

(Chairperson and CEO)

Signed

Amit Binoi

(Company Secretary)

25/04/2025

I. Multiple Choice Questions

5.1 What would have been told by Mr. Amit with respect to maximum remuneration that is allowed in a F.Y. to all such directors and manager taken together?

(a) 3% of net profits.

(b) 5% of net profits.

(c) 10% of net profits.

(d) 11% of net profits.

5.2 Mrs. Jalpa, one of the directors, had drawn remuneration in excess of the limit prescribed by the relevant provisions. As regards recovery of the excess remuneration drawn by him, which of the following options is applicable, if the company has defaulted in paying dues to BDS Bank?

(a) The company shall not waive recovery of excess remuneration paid unless approved by BDS Bank before obtaining approval by a special resolution.

(b) The company shall not waive recovery of excess remuneration paid unless approved by BDS Bank after obtaining approval by a special resolution.

(c) The company shall not waive recovery of excess remuneration paid unless approved by a special resolution. Approval of BDS Bank for such purpose is not required

(d) The company shall not waive recovery of excess remuneration paid unless approved by BDS Bank and if approved by the bank, then company's approval by ordinary resolution is only required.

5.3 How many Performance obligations are there under the Contract with Giganet?

(a) There are 2 separate Performance obligations.

(b) There are 3 separate Performance obligations.

(c) Only 1 Performance obligation is there which encompasses 3 sub contracts.

(d) It depends on the company's choice as to how they want to treat it.

5.4 Which of the following statement is correct w.r.t nature of license as obtained from DBMS Ltd.?

(a) The Software license doesn't provide a right to use the Intellectual Property as the underlying conditions are not satisfied as per the relevant IND-AS.

(b) The Software license doesn't provide a right to use the Intellectual Property as the upgrades will change the functionality of the software.

(c) There is no question of Intellectual Property rights over here in this situation.

(d) The Software license provides a right to use the Intellectual Property that is satisfied at a point in time.

5.5 As part of a risk-based audit approach, JS & Associates focus on areas with a higher likelihood of material misstatement. Which of the following statements best describes the concept of significant auditor attention in the context of scenario given in the case study?

(a) JS & Associates will spend an equal amount of time reviewing all sections of SWAL's financial statements

(b) JS & Associates will prioritize audit procedures for areas with a lower risk of material misstatement.

(c) JS & Associates will design the audit procedures based on their assessment of risks that could potentially cause errors in the financial statements of SWAL.

(d) JS & Associates will rely solely on past audit results to determine the scope of their procedures.

II. Descriptive Questions

5.6 (i) ASSESS the competitive environment of life-assurance business of SWAL (including 'sub-agency office' division). [present only two appropriate points for each phase of assessing the environment]

(ii) EVALUATE the case for holding the 'sub-agency office' division, backed by financial viability among other criteria. [present only two appropriate points for each monetary and the non-monetary issue]

5.7 Calculate the value of supply for GST purposes in each of the plans launched by Insurance company on the E platform of SWAL in the case study.

5.8 Calculate loss allowance for the amortizing loan originated by Savya Ltd.

ANSWERS TO THE CASE STUDY 5

I. Answers to the Multiple Choice Questions

5.1 (c) 10% of net profits

Reason: Part (i) of the Second Proviso to Section 197(1), provides that except with the approval of the company in general meeting by a special resolution, the remuneration payable to any one managing director or whole time director or manager shall not exceed 5% of the net profits of the company and if there is more than one such director then remuneration shall not exceed 10% of the net profits to all such directors and manager taken together.

Here, after the appointment of Mr. Keyur as Managing Director, since the company had both Whole-time Director as well as Managing Director, the company Mr. Amit, the company secretary would have told the maximum remuneration that is allowed in a Financial Year to all such

directors and manager taken together is 10% of net profits, as per the aforesaid provision.

5.2 (a) The company shall not waive recovery of excess remuneration paid unless approved by BDS Bank before obtaining approval by a special resolution.

Reason: Section 197 of the Companies Act, 2013, Where the company has defaulted in payment of dues to any bank or public financial institution or non-convertible debenture holders or any other secured creditor, the prior approval of such person respectively shall be obtained by the company before obtaining approval of such waiver by a special resolution.

Hence, SWAL shall not waive recovery of excess remuneration paid unless approved by BDS Bank before obtaining approval by a special resolution.

5.3 (b) There are 3 separate Performance obligations.

Reason: Promise to provide goods and services is distinct if

- the company can benefit from the good or service either on its own or together with other resources that are readily available to the firm, and
- its promise to transfer the good or service to the company is separately identifiable from other promises in the contract

For broadband and voice call services -

- Broadband and voice services are separately identifiable from other promises as company has various plans to provide the two services separately. These two services are not dependant or interrelated. Also, the company can benefit on its own from the services received.

For sale of modem -

- Company can either buy product from Giganet or third party. No significant customisation or modification is required for selling product.

Based on the evaluation we can say that there are three separate performance obligations: -

- Broadband Service
- Voice Call services
- Modem

5.4 (d) The Software license provides a right to use the Intellectual Property that is satisfied at a point in time.

Reason: Based on the facts given in question, although the updates and upgrades will change the functionality of the software, they are not activities considered in determining the nature of the entity's promise in granting the licence. The activities of DBMS Ltd. to provide updates or upgrades are not considered because they transfer a promised good or service to the company – i.e. updates or upgrades are distinct from the licence. Therefore, the software licence provides a right to use the IP that is satisfied at a point in time.

5.5 (c) JS & Associates will design the audit procedures based on their assessment of risks that could potentially cause errors in the financial statements of SWAL.

Reason: As per SA 701

The concept of significant auditor attention recognizes that an audit is risk-based and focuses on identifying and assessing the risks of material misstatement of the financial statements, designing and performing audit procedures responsive to those risks, and obtaining audit evidence that is sufficient and appropriate to provide a basis for the auditor's opinion. Options (a), (b), and (d) do not accurately represent the emphasis on risk assessment in a significant auditor attention approach.

II. Answers to the Descriptive Questions

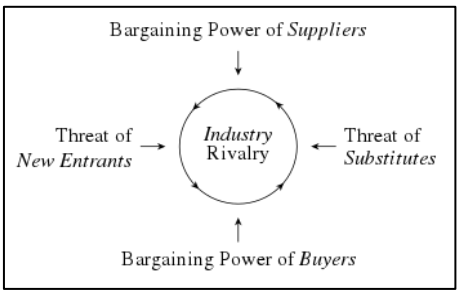
5.6 (i) Michael E Porter, in 1980 in his book "Competitive strategy: Techniques' for analysing industries and competitors"

suggested **five force model** to assess the competitive environment of an industry. The five forces which are enumerated by this model are the bargaining power of suppliers; the bargaining power of customers (buyers); the threat of new entrants; threat of substitute products; and the level of rivalry among current competitors in the industry.

This model is also named as porter's five force analysis. Since each of these five forces affect the competitiveness of business, hence can be used to assess the potential of any organisation or entity; life-assurance business of SWAL (including 'sub-agency office' division) is not an exception to this. **(Any Two Points)**

The bargaining power of suppliers

Number of suppliers will decide the dominance they possess in term of bargaining power regarding the price of good and service they supply to business. In case of 'sub-agency office' division following factors will affect the suppliers' power–



Control over Value Chain – By adopting the strategy of forward integration the insurance companies themselves getting into the direct sale through own network of branch offices in order to enhance their margin or reducing the margin earned by SWAL's 'sub-agency office' division. Since number of insurance companies are neither too less nor too much, hence bargaining power of insurance companies; in terms of percentage brokerage they offered to SWAL is moderate.

Importance of product – SWAL is also dealing in financial product's marketing and advisory, which contribute 50% of group sales and around 67% of group's profit; thus assurance

business which is no doubt significant but only choice (business) available to SWAL. Hence, bargaining power of supplier is moderate.

Substitution among the brand – Life assurance product offers similar utility to client; hence easily substitutes among the brands, means if insurance company 1 charge lesser premium then insurance company 2, client will buy assurance of company 1. No doubt switching is less viable once policy subscribed. Since SWAL's 'sub-agency' division is offering the product from all 23 insurance companies, hence bargaining power of suppliers become low.

Supply of other factors – Other factor such 'sub-agency offices', which are largely on lease, has 30-year lease, this will reduce the lease cost as well as bargaining power of land-lord apart from bringing stability. **(Any Two Points)**

The bargaining power of customers

Whether seller is price taker or makes, this is outcome of bargaining power of customers (true sense competition). If the bargaining power is high seller will become price taker, else he is price maker. Following factors affect the bargaining power of customers of SWAL's 'sub-agency' division–

Number of buyers – In assurance industry the buyers are large (in comparison to few number of suppliers) and diversified, hence their bargaining power is low.

Standardised products – Since the life assurance is the product, which is standard from prospective of core functionality, hence buyers can easily substitute brands and can negotiate to reasonable extent.

Switching – Once policy subscribed can't be easily switched with another, hence due to high switching cost bargaining power reduced to some extent at-least. **(Any Two Points)**

The threat of new entrants

Although entry of a new firm to the industry/ market depends upon the level of entry barriers, but if new entity enters into the industry; it will surely bring additional capacity which enhance the stiffness of competition; hence become a kind of threat. In case of 'sub-agency office' division, there are some major barriers to entry–

Less number of new life-assurance licenses by regulator due to tough regulations – As mentioned in the case that after considering the default by few insurance firms and increasing customer complaints, regulator of insurance business in country has tighten the registration criteria and harden the norms; hence this may act as entry barrier and reduce the threat of new entrants.

Less number of new insurance agent due to no new authorisation by insurance companies – As market is revamping, the agents is becoming competitor to the insurance companies and as mentioned insurance companies stopped authorising new insurance agents, hence this will act an entry barrier for new insurance agents, which is a great positive for SWAL's 'sub-agency office' division and intact the competitive advantage.

Learning curve and economies of scale – Since all the 23 insurance companies dealing in life assurance and SWAL are 10 to 20 years old organisations; hence learning curve and economies of scale (shared services for the 580 offices - presence in 580 cities) which they are enjoying may become entry barriers for new firm. Since new firms require huge capital to be at par to such learning curve and economies of scale. **(Any Two Points)**

Threat of substitution

Substitution means the product from some other industry which can render the same function which life assurance is rending. The threat of substitute product is quiet low.

Competitive rivalry

The level of competition among the players to acquire or retain the market share directly affects the profitability in an industry. Following factor is affecting the competitive rivalry–

Number of competitors and respective market size – Since there are good number of competitors, hence competition will be intense; may cut throat rivalry. Presently SWAL's insurance business represent 14.55% of market share (in 2024-25) in comparison to 14.29% of market share five year ago, without any major variation, hence possibility of gaining new market share is limited that too at high cost (in form of advertisement and more after sale services).

Lack of differentiation – Standardise product results in high rivalry, since the life assurance is standard product hence rivalry may be high on account of easy substitution effect among the different brands.

Slow market growth – If market is growing at high rate, rivalry may be stiffer or may be moderate; because everyone has reasonable opportunity to grow. The moment growth stagnated rivalry become stiffer because no one wish to lose market share. The industry life cycle curve is flatter here, because during last four years overall industry wide CAGR (compounded annual growth rate) of life assurance business is 3.39%, whereas year-on-year growth from 2023-24 to 2024-25 is 1.91%. Although potential is limited, but competition is still high.

Exit barriers – If the exit cost for player to move out of industry is high, it will have to be in industry and fight for survival, which may make competition tougher. Since agency agreement and lease agreement is already signed by SWAL hence, it becomes difficult to exit from the business, hence need to participate in competition to retain the share. **(Any Two Points)**

(ii) Case for holding the 'sub-agency office' division

The strategic review committee suggests that the SWAL's 'sub-agency office' division should be sold off and that SWAL shall re-position its assurance business as an online solution, but the same suggestion firstly needs to be evaluated in terms of financial perspective among the other criteria.

The growth in life assurance business is stagnated and industry is in maturity stage of industry life cycle. This is evident from industry size and growth in the same. During last four years overall industry wide CAGR (compound annual growth rate) of life assurance business is 3.39%, whereas year-on-year growth from 2023-24 to 2024-25 is 1.91%. The moment growth stagnated rivalry become stiffer because no one wish to lose market share. Hence, there is intense competition in market. In cases where market witnesses intense competition, operating efficiently is essential and reduction in cost become key success factor; in order to offer competitive deals to clients and retain market share.

Hence it becomes need of hour, that we review the operating processes followed at 'sub-agency offices' to check whether they are efficient or not, in order to ensure greater profitability rather thinking to sale off the entire 'sub-agency office' division.

Now, move to financial analysis, which suggests it is beneficial to hold back 'sub-agency' division.

Contribution to the group – Insurance business is contributing 50% of top-line of overall group revenue (and 1/3rd of bottom line), and around 86% (280/ 326) of this comes from 'sub-agency office' division and 'E-platform' division contribute only remaining 14%.

Profitability – Margins are positive. There are two major parameters to evaluate profitability further on–

- Operating profit (EBIT/ Revenue) – No doubt, operating profit shrink from 12.4% to 6.43% in three years' time frame. But as earlier quoted, margin is positive and secondly, there is sign of recovery as well. EBIT increased in absolute terms (from 16 to 18).
- Return on capital employed (ROCE) [EBIT / (Equity + Long Term Debt)] – No doubt, ROCE shrink from 15.5% to 7.69% in three years' time frame. But reduction in EBIT is not only a reason, another major reason for decline is also change in capital structure. Long term debt is increased in absolute terms (from 50 to 78).

Liquidity – Current ratio (Current Assets / Current Liabilities) being reasonable measure of liquidity indicates enough liquidity in 'sub-agency office' division to meets it obligation. There is minor decline from 1.367 times to 1.33 times. Component analysis of working capital can be performed for greater insight.

Gearing (Debt / Equity) – Gearing ratio depicts the financial leverage**,** a measure of risk**.** Gearing ratio no doubt increased as result of introduction of debt, from 1/3 to 1/2, but under control. **(Any Two Points)**

Some other quasi-finance and significant factors relevant to the decision of sale of 'sub-agency office' division and full focus on 'E-platform' division–

Client's demography – Clients from all age groups from 20 to 60+ are clients of SWAL's assurance brokerage business. 66.56% (217/326) of revenue coming from clients with 50+ years of age, and 99% (215/217) out of them are associated through 'sub-agency offices', hence holding of 'sub-agency' division become essential. Secondly, clients from all age group may not find it convenient to shift to 'E-platform' 'Policy at you click' and their resistance may result in losing business. Thirdly, they have easily available substitute, because competitors also have branch offices which will give them same feel.

Resistance from employees – Out of 1,564 on-roll employees of assurance brokerage business, only 50 are associated in 'E-platform' division- 'Policy at you click', rest all in 'sub-agency office' division. If SWAL re-structure itself fully as online solution for life assurance then also can't absorb all the employees, many of them need to be retrenched. Resistance will be there in both the cases, because transferred employee may not have requisite skill set, result in poor quality of service and no job satisfaction to employee. Whereas in case of retrenched workers redundancy cost will become additional financial burden. This can be seen as exit barrier.

Legal aspect in term of pre-closure of lease - SWAL has practice to sign 30-year lease, when so ever taking and 'sub-agency office' on lease in order to reduce the lease cost and bring stability. It started the business 2 decades ago and expanded it 3 years ago and many of leases are active right now, in case of pre-closure, it may be possible to bear additional financial burden as per terms of lease agreement.

Loosing USP – 'Independence and impartial advice' with presence wide across the nation, in form of 'sub-agency offices' equipped with professionally trained sale staff headed by financial planner or advisor, where customer can take

advise and discuss opinion prior to investing/ buying any insurance or financial product is USP for SWAL's assurance brokerage business. By disposing the 'sub-agency office' division this central idea, with which SWAL was established may be washed out. **(Any Two Points)**

In nutshell, the life assurance market has matured in recent years, and result in low growth potential and lower profitability but still yielding positive numbers. Hence, sale of 'sub-agency' division will adversely hit the revenue as well as profitability.

5.7 As per Rule 32(4) of the CGST Rules, 2017, the value of supply under GST for each of the plans would be as follows:

Plan 1: Investment-Linked Policy

Rule 32(4)(a): The gross premium is reduced by the amount allocated for investment/savings.

Gross premium: ₹ 1,00,000

Investment/savings allocation: ₹ 60,000

Value of supply: ₹ 1,00,000 - ₹ 60,000 = ₹ 40,000

Plan 2: Single Premium Annuity

Rule 32(4)(b): For single premium annuity policies, the value is 10% of the single premium.

Single premium: ₹ 5,00,000

Value of supply: 10% of ₹ 5,00,000 = ₹ 50,000

Plan 3: Regular Life Insurance

Rule 32(4)(c): For regular policies, the value is 25% of the premium in the first year and 12.5% of the premium charged from the policy holder in subsequent years.

First Year:

Premium: ₹ 80,000

Value of supply: 25% of ₹ 80,000 = ₹ 20,000

Second Year and onward:

Premium: 80,000

Value of supply: 12.5% of ₹ 80,000 = ₹ 10,000

Plan 4: Pure Risk-Cover Policy

Proviso to Rule 32(4): If the entire premium is for risk cover, the rule doesn't apply. The entire premium charged from the policy holder is the taxable value.

Premium: ₹ 50,000 (entirely for risk cover)

Value of supply: ₹ 50,000

5.8 At reporting date, no change in 12-month POD and entity assesses that there is no significant increase in credit risk since initial recognition – therefore lifetime ECL is not required to be recognised.

Particulars	Details
Loan	₹ 100,00,00,000 (A)
LGD	25% (B)
PoD – 12 months	0.5% (C)
Loss allowance (for 12-months ECL)	₹ 12,50,000 (A×B×C)

The suggested answers provided in these Case Studies includes a variety of potential solutions/ alternative points where applicable. This is intended to assist students by offering multiple perspectives and approaches to problem-solving.