Case Study-3

Established in 2003, RP Ltd. (RPL), based in Tirupur, Tamil Nadu, India, has established a foothold for itself as a prominent manufacturer, wholesaler and exporter of high-quality T-shirts. Recognised as a prestigious export house, RPL takes pride in its brand, "RK," known for its commitment to style, comfort, and ethical manufacturing practices.

RPL boasts a state-of-the-art manufacturing facility equipped with advanced technology and machinery. Their production process adheres to stringent quality control measures, ensuring every "RK" T-shirt is crafted using premium materials and delivers exceptional durability, comfort, and style. The company's dedication to quality has not only earned them the trust and loyalty of their domestic clientele but has also established them as a reliable and sought-after supplier in the international market.

Understanding the evolving preferences of their customers, RPL offers a diverse range of T-shirts. Their product portfolio encompasses a wide variety of styles, colours, and designs, catering to diverse demographics and fashion trends. They prioritise innovation and constantly update their collections, ensuring their brand stays ahead of the curve and caters to the ever-changing needs of the T-shirt market.

Looking ahead, RPL is committed to sustainable growth and expanding its global footprint. They are actively exploring new markets and forging strategic partnerships to broaden their international reach. Additionally, they are implementing eco-friendly practices throughout their operations, prioritising responsible sourcing and sustainable manufacturing processes. With a focus on continuous improvement, innovation, and ethical practices, RPL strives to solidify its position as a leading player in the global T-shirt industry.

On 23rd April, 2023, RPL enters into a contract with JM Ltd. (JML) to sell T-shirts for Rs. 600 per T-shirt. As per the terms of the contract, if JML purchases more than 2,000 T-shirts till March 2024, the price per T-shirt will be retrospectively reduced to Rs. 540 per unit. Till September 2023, RPL sold 190 T-shirts to JML. RPL estimates that JML's purchases by March 2024 will not exceed the required threshold of 2,000 T-shirts.

In October 2023, JML acquires DC Ltd. (DCL) and from October 2023 to December 2023, RPL sells an additional 1,200 T-shirts to JML. Due to these developments, RPL estimates that purchases of JML will exceed the 2,000 T-shirts threshold for the period and therefore, it will be required to retrospectively reduce the price per T-shirt to Rs. 540.

RPL is analyzing a strategic move – the potential acquisition of JML through a merger. This decision is driven by the potential for significant synergy benefits that could propel RPL's growth and market position.

The synergy between the two companies can be multifaceted. Firstly, combining their manufacturing capabilities could lead to economies of scale. Sharing resources and expertise could optimize production processes, potentially reducing costs and increasing overall efficiency. Additionally, a larger production capacity could allow RPL to cater to a broader range of customer demands and potentially enter new markets.

The following data are available:

Company	After-tax earnings	No. of equity shares	Market price per share
RPL	Rs. 10 crores	10,00,000	Rs. 75
JML	Rs. 3 crores	2,50,000	Rs. 60

It is proposed that certain changes in the shareholding of JML would be made in case of consolidation with RPL, as per the discussion between the management of the two companies, RPL & JML.

During the course of the audit of RPL, CA Devanshi Bisht is verifying export revenues of the company for the F.Y. 2023-24, with her engagement team.

She has verified transactions entered in "Export Sales" account maintained in accounting software from relevant export invoices. The export sales are being made on payment of IGST, for which a refund is automatically credited in the account of the company after the goods are shipped.

On enquiring from internal audit staff regarding the recognition of export revenues, she is told that export sales are recognised for the year on the basis of "Bills of Lading". However, she is not convinced with such a response and feels that the same does not appear to be proper. She finds that four export invoices bearing dates in the month of March 2024 having a total value of Rs. 125 lakhs have not been recognized in export revenue on the ground that bills of lading for these invoices were issued in the month of April 2024.

Further, during audit of current year, CA Devanshi had identified that there was a misstatement also in last year pertaining to export revenues of the company and the same is still not corrected. She had issued unmodified audit report in last year.

In respect of its Japanese exports, on 31^{st} March, 2024, RPL has an export exposure of JPY 10,00,000 receivables. Japanese Yen (JPY) is not directly quoted against Indian Rupee.

The current spot rates are:

INR/US $	Rs. 62.22
JPY/US$	JPY 102.34

It is estimated that Japanese Yen will depreciate to 124 level and Indian Rupee to depreciate against US $ to Rs. 65.

Forward rates for March 2024 are:

INR/US $	Rs. 66.50
JPY/US$	JPY 110.35

CA Devanshi recommended that taking a forward cover in such a situation would be beneficial.

On 31st March, 2024, RPL has an outstanding interest liability of Rs. 1 crore towards loan payable to BFCI Ltd., a public financial institution. On the same date, it issued debentures to BFCI Ltd. in lieu of the outstanding interest and deducted the said interest while computing profits and gains of business of A.Y.2024-25. The Assessing Officer, however, rejected the deduction of interest on loan claimed by RPL.

After the issue of such debentures, the company has a total debt of Rs. 3 crores and surplus funds to the tune of Rs. 5 crores. Further, it has made a gross profit of Rs. 18 crores and incurred indirect expenses of Rs. 4 crores for the financial year.