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Opinion on Transaction at Arm's Length – Ambuja Cements Limited

January 20, 2025

SHAILESH HARIBHAKTI & ASSOCIATES

CHARTERED ACCOUNTANTS

SHA/PCIL/2024-25/004

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For the kind attention of,

The Board of Directors

Ambuja Cements Limited

Adani Corporate House,
Shantigram, Near Vaishnav Devi Circle,
S. G. Highway, Khodiyar,
Ahmedabad, Gujarat 382421

Dear Board Members,

Re: Opinion on compliance with arm's length compliance for transaction between related parties for FY 2025-26

At the outset we would like to thank you for providing us this opportunity. Our mandate is to provide an opinion on whether the transaction entered between Ambuja Cements Limited ('ACL' or 'Ambuja' or 'the Company'), a Company listed on the NSE & BSE, and Penna Cement Industries Limited ('PCIL'), detailed below, is at arm's length.

1 Background of the Transaction

ACL on June 13, 2024, announced the 100% acquisition of PCIL from its existing promoter group P Pratap Reddy and family. In line with this acquisition, PCIL becomes a part of the Adani Group. ACL is an established player in the Indian cement industry, primarily engaged in the manufacturing, selling, and distribution of various types of cement and related products. ACL leverages its extensive network of cement manufacturing facilities across the country to deliver their products.

PCIL, before its acquisition by ACL, was one of the largest privately held cement companies in India, with an installed cement capacity of 10 million tonnes per annum. Founded in 1991, Penna Cement has established itself as one of the most trusted cement brands, with significant footprints in southern and western India. Their clientele ranges from small house owners to organised real estate developers and from various state governments to global construction majors.

In order to achieve synergies and economies of scale, reduce operational costs, strengthen the sustainability of the businesses including environmental sustainability, and conserve natural resources, ACL & PCIL are proposing to enter into a Master Service Agreement ('MSA' or 'agreement') for purchase and sale of materials and services.



2 Scope of Opinion

We, Shailesh Haribhakti & Associates ('SHA') have been appointed by the Company to provide an opinion on whether the proposed agreement for supply of materials and services by ACL and PCIL is at arm's length.

Our scope will be restricted to the following:

- a. Companies Act, 2013 and read with Rules thereunder ('Companies Act')
- b. Securities and Exchange Board of India ('SEBI') (Listing Obligations and Disclosure Requirements) ('LODR') Regulations, 2015 ('Listing Regulations') applicable as on date
- c. Indian Accounting Standard (Ind AS) 24 – Related party disclosures notified under the Companies (Indian Accounting Standards) Rules, 2015 ('Ind AS')
- d. References to other laws that we feel are appropriate.

3 Scope Limitations

This opinion is confidential for use and reliance of the parties involved in the transaction along with their respective consultants, representatives and to whom it is issued and may be produced before regulatory authorities, as may be required, in connection with the purpose as outlined above.

Our opinion is subject to the scope limitations detailed hereinafter. As such the opinion is to be read in totality, and not in parts, in conjunction with the relevant documents referred to in this opinion. Our work does not constitute an audit or due diligence. Accordingly, we are unable to and do not express an opinion on the accuracy of any financial information referred to in this opinion.

This opinion is issued on the understanding that the Client has drawn our attention to all the matters, which it is aware of concerning the financial position of the Company and any other matter, which may have an impact on our opinion, on the value of the subject transaction, including any significant changes that have taken place or are likely to take place in the value of the assets of the Company.

In the course of the assignment, we were provided with both written and verbal information. We have evaluated the information provided to us by the Client through broad inquiry, analysis and review (but have not carried out a due diligence or audit of the Company for the purpose of this engagement, nor have we independently investigated or otherwise verified the data provided). The terms of our engagement were such that we were entitled to rely upon the information provided by the Client without detailed enquiry. Also, we have been given to understand by the Client that it has not omitted any relevant and material factors. Accordingly, we do not express any opinion or offer any form of assurance regarding its accuracy and completeness. We assume no responsibility for any errors in the above information furnished by the Client and their impact on the present exercise.



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No investigation of the Company's claim to title of assets has been made for the purpose of this opinion and the Company's claim to such rights has been assumed to be valid. Therefore, no responsibility is assumed for matters of a legal nature.

All the assumptions made in order to verify the value of the assets was based on information and / or report(s) obtained from the Company. Nothing has come to our attention to cause us to believe that the facts and the data set forth in this data are not true or incorrect. Therefore, no responsibility is assumed for information furnished and believed to be reliable. Our opinion is not to be construed as us opining or certifying the compliance with the provisions of any law, other than those covered in our scope.

In expressing our opinion, we have relied on the financial and other information provided to us by the management of the Company. Our reliance on and use of such audited and unaudited information should not be considered as an expression of our opinion on it, and we do not accept any responsibility or liability for the impact of any inaccuracies in it as a result of its use in expressing our opinion.

This opinion has been prepared solely for the purposes of opining on the arm's length compliance of the subject transaction. You shall indemnify and hold us harmless against any expenses (including reasonable fees and disbursements of counsel), loss, damage, harm or injury (collectively "Losses") that may be suffered or incurred by us arising out of or relating to disclosing our opinion.

4 Laws on Transactions with Related Parties

A. Related Party

A.1. Companies Act

The term 'related party' has been defined under section 2(76) of the Companies Act as:

- i. a director or his relative;
- ii. a key managerial personnel or his relative;
- iii. a firm, in which a director, manager or his relative is a partner;
- iv. a private company in which a director or manager or his relative is a member or director;
- v. a public company in which a director or manager is a director and holds along with his relatives, more than two per cent (2%) of its paid-up share capital;
- vi. any body corporate whose Board of Directors, Managing Director or Manager is accustomed to act in accordance with the advice, directions or instructions of a director or manager;
- vii. any person on whose advice, directions or instructions a director or manager is accustomed to act;

Provided that nothing in sub-clauses (vi) and (vii) shall apply to the advice, directions or instructions given in a professional capacity;



- viii. any body corporate which is
 - a. a holding, subsidiary or an associate company of such company;
 - b. a subsidiary of a holding company to which it is also a subsidiary; or
 - c. an investing company or the venturer of the company.
- ix. a director other than independent director or key managerial personnel of the holding company or his relative with reference to a company, shall be deemed to be a related party.

A.2. Listing Regulations

Regulation 2(1)(zb) of the Listing Regulations define 'related party' as defined under sub-section (76) of section 2 of the Companies Act or under the applicable accounting standards. In other words, the Listing Regulations refer and include the definition of related party quoted above.

In addition, by way of a proviso it provides that the following shall also be deemed to be a related party:

- a. any person or entity forming a part of the promoter or promoter group of the listed entity; or
- b. any person or any entity, holding equity shares of ten per cent (10%) or more, with effect from April 1, 2023; in the listed entity either directly or on a beneficial interest basis as provided under section 89 of the Companies Act, at any time, during the immediate preceding financial year.

Ambuja is the holding company and holds a controlling ownership interest (100%) in PCIL, making them related parties.

B. Related Party Transactions

B.1. Companies Act

As per section 188 of Companies Act, except with the approval of the Board by way of a board resolution, no company shall enter into contracts or arrangement with a related party with respect to the following:

- a. sale, purchase or supply of any goods or materials;
- b. selling or otherwise disposing of, or buying, property of any kind;
- c. leasing of property of any kind;
- d. availing or rendering of any services;
- e. appointment of any agent for purchase or sale of goods, materials, services or property;
- f. such related party's appointment to any office or place of profit in the company, its subsidiary company or associate company; and
- g. underwriting the subscription of any securities or derivatives thereof, of the company



We understand that the Company is entering into a transaction for supply of materials and services from a related party. Accordingly, the said transaction should be covered above.

Further, the Companies Act by way of third proviso to the section 188(1) of Companies Act provides that such approval by the Board of Directors will not be required for transactions entered in the **ordinary course of business** and on **an arm's length basis** (*discussed in detail in following paragraphs*).

B.2. Listing Regulations

Regulation 2(1)(zc) of the Listing Regulations define 'related party transactions' as a transaction involving a transfer of resources, services or obligations between:

- (i) a listed entity or any of its subsidiaries on one hand and a related party of the listed entity or any of its subsidiaries on the other hand; or
- (ii) a listed entity or any of its subsidiaries on one hand, and any other person or entity on the other hand, the purpose and effect of which is to benefit a related party of the listed entity or any of its subsidiaries, with effect from April 1, 2023;

regardless of whether a price is charged and a "transaction" with a related party shall be construed to include a single transaction or a group of transactions in a contract.

Since the transaction for supply of materials and services between Ambuja and PCIL (it's 100% subsidiary), the same will be a related party transaction as per the Listing Regulations.

C. Ordinary Course of Business

The phrase 'ordinary course of business' is not defined under the Companies Act or the rules prescribed thereunder. The ordinary meaning of the expression 'in the ordinary course of business' in dictionaries is 'part of doing regular business; the regular or customary condition or course of things; as things usually happen'. Black's Law Dictionary defines 'ordinary course of business' as the 'normal routine in managing trade and business'.

In common parlance, 'ordinary course of business' would include transactions which are entered into in the normal course of the business pursuant to or for promoting or in furtherance of the company's business objectives, as per the charter documents of the company.

An assessment of whether a transaction is in 'ordinary course of business' may be very subjective, judgmental and can vary on case-to-case basis. The purpose of making such assessment is to determine whether the transaction is usual or customary to the Company and / or its line of business.

The Company would, therefore, be required to exercise its judgment to conclude whether a transaction which the Company enters into can be considered to be in the ordinary course of its business.



Tests for determining whether a contract / activity falls within the ordinary course of business:

The courts have *inter alia* laid down the following principles in this regard:

- a. the objects of the company permit such activity;
- b. it is a historical practice and there is a pattern of frequency (and not an isolated transaction);
- c. it has a connection with the normal business carried on by the company;
- d. the income, if any, earned from such activity/transaction is assessed as business income in the company's books of accounts and hence, is a 'business activity'; and
- e. it is a common commercial practice.

The above list is not exhaustive. Individually, none of the above parameters can amount to the transactions being in the ordinary course of business.

Both Ambuja and PCIL are engaged principally in the business of manufacturing, selling and dealing in cement of all kinds and other cement related products, hence, the proposed agreement should fall under the ordinary course of business.

D. Arm's Length Transaction

Explanation to sub-section (1) of Section 188 of the Companies Act defines the term 'arm's length transaction' as a transaction between two related parties that is conducted as if they were unrelated, so that there is no conflict of interest.

Arm's length basis does not mean arm's length price as price is just one of the components of the terms of dealing with the other party and there are several other matters which need to be considered. The transaction as a whole and the entire bundle of the terms and conditions needs to be considered for determining whether the transaction is on an arm's length basis.

In the absence of any information/methodology/approach for determining the "arm's length transaction" in the Companies Act, such methodologies/approaches existing under Transfer Pricing Guidelines contained in the Income-tax Act, 1961 ('IT Act') can be adopted.

In the case of *Iljin Automotive Private Limited v. Asst. Commissioner of Income Tax*¹, the Court opined that "the determination of 'arm's length price' seeks answer to the question – What would have been the price if the transactions were between two unrelated parties, similarly placed as the related parties in so far as nature of product, and terms and conditions of the transactions are concerned?"

¹(2011) 16 Taxmann.com 225



The Bangalore Bench of the Income Tax Appellate Tribunal in the case of *Filtrex Technologies Pvt Ltd v. Asst. Commissioner of Income Tax IT(TP)*² held that acceptance of arm's length price declared by one party cannot preclude the Revenue from examining arm's length price in the hands of the other party to the same transaction.

In terms of section 92F of the IT Act, "arm's length price" means a price which is applied or proposed to be applied in a transaction between persons other than associated enterprises, in uncontrolled conditions.

As per section 92C of IT Act, the arm's length price in relation to international transaction or specified domestic transactions be determined by any of the following methods:

Name of method	Reason for selection or rejection
Comparable uncontrolled price method	<p>This method evaluates the "price" charged in a controlled transaction with reference to the "price" charged in comparable uncontrolled transactions, which could be identified either through internal or external comparable companies.</p> <p>The Company is in the business of supplying cement and thus, a comparable uncontrolled transaction is available. Accordingly, we have analysed the related party transaction using this method.</p> <p>The OECD in para 2.15 of its guidelines of 2017, states that: "<i>Where it is possible to locate comparable uncontrolled transactions, the CUP method is the most direct and reliable way to apply the arm's-length principle. Consequently, in such cases the CUP method is preferable over all other methods.</i>"</p> <p>Further, in para 2.3 of such guidelines, OECD gives preference to comparable uncontrolled price method over other methods by providing that "<i>where, taking account of the criteria described at paragraph 2.2, the comparable uncontrolled price method (CUP) and another transfer pricing method can be applied in an equally reliable manner, the Comparable Uncontrolled Price method is to be preferred.</i>"</p>
Resale price method	<p>This method is applicable in a resale situation, where the property or services purchased from an Associated Enterprise ("AE") are sold to unrelated enterprise. The method is applied on either a transactional or a comparable-company basis, and it applies to distributors/ marketers.</p> <p>Since the particular transaction is not a resale situation, this method is not selected.</p>

² Appeal No. 469/Bang/2017



Cost plus method	<p>This method is generally applied in relation to supply of products or provision of services. It is most useful where semi-finished goods are sold between related parties, where related parties have concluded joint facility agreements or long-term buy-and-supply arrangements, or where the controlled transaction is the provision of services.</p> <p>We have selected Comparable Uncontrolled Price Method as the most appropriate method. Accordingly, this method is not selected.</p>
Profit Split method	<p>This method may be applicable mainly in international transactions involving transfer of unique intangibles or in multiple international transactions, which are so interrelated that they cannot be evaluated separately for the purpose of determining the ALP of any one transaction. This method is therefore appropriate for integrated transactions with more than one enterprise.</p> <p>Since there are no unique intangibles or any series of multiple transactions, this method is not selected.</p>
Transactional net margin method	<p>This method is generally appropriate for the provision of services/ sale of goods where Resale Price method (RPM) / Cost Plus method (CPM) cannot be adequately applied.</p> <p>The process of selection involved issue of tender and bidding process. Accordingly, this method may not be appropriate.</p>
Such other method as may be prescribed	<p>Any method that takes into account the price that has been charged or paid, or would have been charged or paid, for the same or similar uncontrolled transaction, with or between non-associated enterprises, under similar circumstances considering all the facts, shall be regarded as one of the recognized methods for determining the ALP.</p> <p>We have selected Comparable Uncontrolled Price Method as the most appropriate method. Accordingly, this method is not selected.</p>

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As per the proposed MSA, materials will be supplied by the entities at the rates given in the table below. Further, our analysis to determine if the same is at arm's length is also given in the below table:

No.	Material / Service	Pricing Formula & Delivery Point	Justification
1	Cement	<p>Price will be as follows:</p> <p>(a) Average Net Selling Price of Previous Month (less 2% Discount) applied in the following manner:</p> <ul style="list-style-type: none"> (i) Weighted Average Market price of ACL for markets, where cement supplies are from PCIL plant. (ii) Markets price reduced by Total Logistics Cost (Primary Freight, Secondary Freight and Handling including rent) (iii) Arm's Length Price will be = Net Market price as per point no (ii) above with further reduction of 2% discount on the net price. <p>(b) Delivery point: "Ex-Delivery": delivered at the Manufacturing Plant gate</p>	<p>Market Benchmark: The pricing uses the previous month's net selling price as a benchmark, reflecting an independent market reference point.</p> <p>Discount at Net Selling Price Rate: The 2% discount could be seen as commercially reasonable, potentially reflecting a bulk purchase agreement or prompt payment incentive commonly offered in arm's length transactions.</p>
2	Clinker	<p>Price will be as follows:</p> <p>(a) Manufacturing Plant's variable Cost of production of previous quarter, plus 35% markup.</p> <p>(b) Delivery point: At the Manufacturing Plant.</p> <p>(c) Any handling and transportation cost to be charged as per 'Actual'</p>	<p>Cost-Plus Pricing with Mark-Up: This approach provides transparency by reflecting the actual variable costs incurred by ACL in producing the clinker.</p> <p>Reasonable Mark-Up: The 35% mark-up could be justified if it aligns with typical industry margins for clinker sales between independent companies.</p>



3	Raw materials for Clinker – fuel on 'as needed basis'	Price will be as follows: (a) Manufacturing Company's landed cost thereof plus carrying cost of 10% per annum for the holding period. (b) Delivery point: At Ex Works Supplier Location, / Manufacturing Company's location.	Cost Recovery with Mark-Up: Similar to clinker, this approach aims to recover the actual cost of raw materials for ACL.
4	Raw materials for Cement – fly-ash, slag, gypsum etc. on 'as needed basis'		
5	Spare parts on 'as needed basis'		
6	Purchase / Sale of Power	Charges related to Renewable energy power; grid power/other power charges shall be charged at the prevailing market prices in the respective consumption areas/location after deduction of actual charges incurred by respective unit which is consuming the said power.	The pricing uses prevailing market price reflecting an independent market reference point.
7	Sale of Cut & Torn Materials	Average selling price of the cut & torn material sold to the third party in the last month.	The pricing uses average selling price to third party as a benchmark, reflecting an independent market reference point.

The agreement is driven by a strategic vision to achieve several key objectives:

- Synergy and Economies of Scale:** By collaborating on material and service procurement, the companies can leverage their combined buying power to negotiate more favorable terms with suppliers. This can lead to significant cost reductions and unlock economies of scale, ultimately benefiting both businesses.
- Operational Cost Optimization:** The proposed agreement fosters operational efficiencies by streamlining processes and potentially consolidating certain activities. This can lead to a reduction in redundant costs associated with independent operations.
- Sustainability Enhancement:** The collaboration presents an opportunity to explore and implement joint initiatives focused on environmental sustainability. This could encompass areas like optimizing resource utilization, exploring alternative fuel sources, and adopting best practices in waste management.

- **Resource Conservation:** By working together, Ambuja and PCIL can more effectively manage, and conserve natural resources used in the cement production process. This aligns with the growing focus on sustainable business practices within the industry.

Overall, this agreement signifies a commitment by Ambuja and PCIL to leverage their combined strengths to enhance their operational performance, optimize costs, and contribute to a more sustainable future for the cement industry.

The markup on the transactions, as stipulated in the proposed MSA, is deemed to be at arm's length. This determination holds true even after adjusting for the specified factors, indicating that the pricing structure in the related party transaction aligns with what would be agreed upon in an uncontrolled transaction. The consideration of these factors ensures that the pricing remains fair, transparent, and reflective of market conditions, reinforcing the arm's length nature of the arrangement.

In conclusion, the Group's decision to engage in a MSA agreement between PCIL and Ambuja is strategic and mutually beneficial. This symbiotic relationship fosters a scenario where both entities stand to gain from a synergistic collaboration.

In a scenario where a willing buyer and a willing seller are involved, the transaction is deemed to be at arm's length due to the principles of fair market value and the presumption that parties, when acting in their own self-interest, engage in negotiations to optimize their respective gains. The concept of arm's length transactions is rooted in the notion that parties, free from any compulsion, are best positioned to determine a fair and equitable value for the assets or services in question. In such instances, market forces drive the negotiation process, and both parties are motivated by their individual objectives. Therefore, the presence of a willing buyer and willing seller serves as a strong indicator that the transaction reflects a fair and market-driven value, aligning with the fundamental principles of arm's length dealings.

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5 Opinion

On consideration of the above analysis, we are of the view that the transaction for supply of materials by ACL and PCIL at above rates, is at arm's length. We undertake no obligation to update this opinion for any subsequent events that may affect the value of the goods / services.

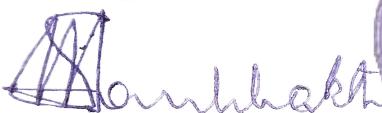
In case of any clarifications required, please feel free to reach out.

Respectfully submitted,

For Shailesh Haribhakti & Associates

Chartered Accountants

Firm Registration No.: 148136W



Shailesh Haribhakti

Proprietor

Membership No.: 030823

Date: January 20, 2025

Place: Mumbai

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