



# **“Valuation, Valuation Standards and Valuation Profession”**

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# Agenda

## **VALUATION**

- History of Business Valuation in India
- Guiding Principles of Valuation
- Why Valuation
- Valuation Approaches & Methodologies
- Valuation across Business Cycle

## **VALUATION STANDARDS**

- Valuation without Standards
- Ethical Standards
- Need for Uniformity
- Valuation Resources and Practice Guidance
- Comparison of International Valuation Standards
- Mandatory Performance Framework
- Regulatory Valuations in India

## **VALUATION PROFESSION**

- New Regulations and Opportunities
- CoE 2020 Report - Key Recommendations

# 'History of Business Valuation in India'

Since **SEBI Act** came into force in 1992, companies are **free to price** their issues in consultation with the Merchant Bankers

**ICAI issued Valuation Guide on Share Valuation in 1994 and 1999**

**SEBI brought Fairness Opinion on Valuation** in scheme of Arrangement of Listed Cos in 2008

Income Tax prescribed **Valuation for Transfer of Shares in 2009**

**ESOP FBT of 2007** changed to **Perquisite Tax in 2009**

**DCF Method** prescribed by RBI in **2010** for all **FDI Valuations** (later changed to any Internationally accepted method)

Income Tax prescribed **Valuation for Issue of Shares in 2012**

From 2016, "**Fair Value Standard**" came into force (Ind AS 113)

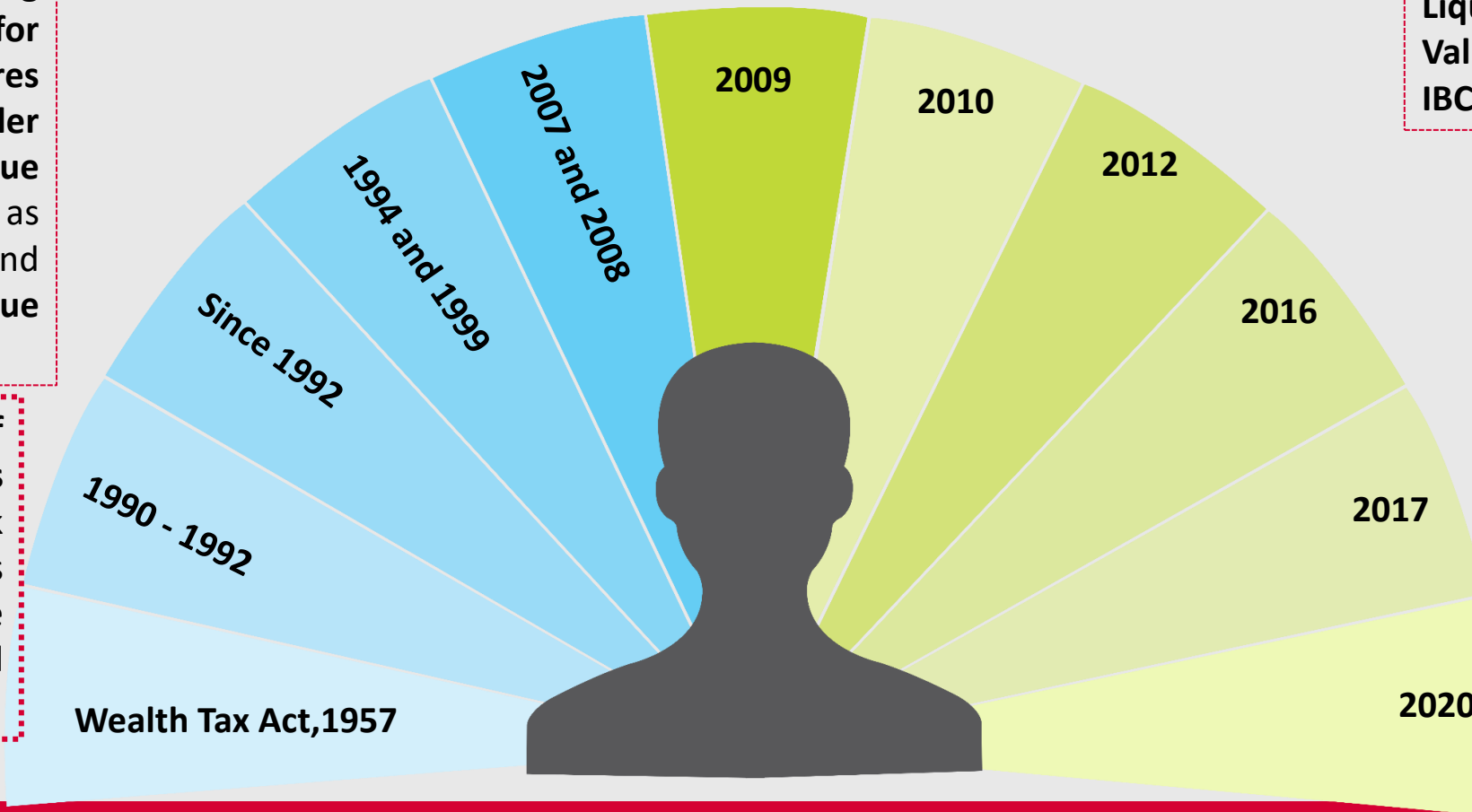
**Liquidation Value and Fair Value of "Assets"** came in IBC w.e.f Dec 2016.

**Registered Valuer provisions** of Companies Act, 2013 Implemented **Companies (Registered Valuers and Valuation) Rules, 2017**

**CG appointed Committee of Experts** submitted report with **Draft Valuer Bill, 2020**

**Fixed Pricing Guidelines** for valuation of shares erstwhile **Controller of Capital Issue (CCI)** guidelines as per NAV, PECV and **Market Value** method.

**Valuation of unquoted shares** on adjusted Book Value Method as per Balance Sheet (repealed w.e.f. 1.4.1989)



# 'Guiding Principles of Valuation'

## Return on Capital Employed and Growth

Companies create value when their ROCE exceeds WACC.

- competitive advantages
- industry structure
- market trends

## Conservation of Value

The valuation of business is directly linked with its underlying cash flows and value from Operations.

- Accounting numbers may be misleading

## Demand, Supply and Equilibrium

The transactions in real life take place at the equilibrium of demand and supply at a particular point of time.

- Value is fundamental; Price is market driven

## Economies of Scale

Higher Growth brings benefits to business but not where the business model itself is questionable.

- Positive Cash Flows essential even though in longer run for start-up's

# 'Why Valuation'

## Transactions

- Mergers / Acquisitions
- Investment
- Fund Raising
- Sale of Businesses
- Voluntary Assessment
- Dispute Resolution

## Regulatory

- RBI
- Income Tax
- SEBI
- Companies Act
- IBC

## Financial Reporting

- ESOP
- Purchase Price Allocation
- Impairment / Diminution
- Fair Value (Ind AS)

# **‘Valuation Approaches, globally’**

**Income  
Approach**



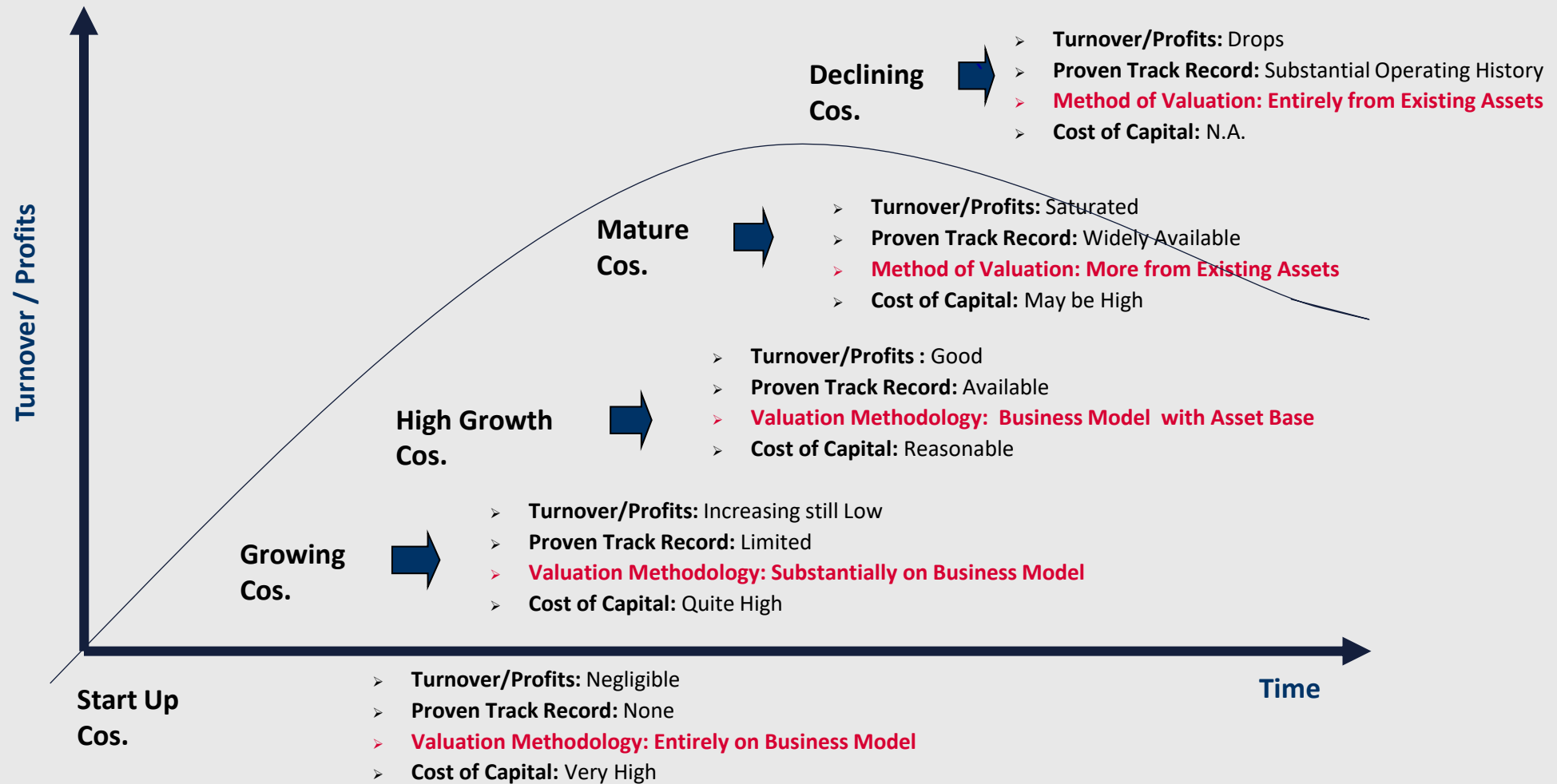
**Asset  
Approach**



**Market  
Approach**



# Valuation across Business Cycle





# **Valuation Standards**



# Valuation without Standards



# Ethical Standards

Fundamental Ethical principles as per the

IVSC Code of Ethical Principles

Integrity

Objectivity

Competence

Confidentiality

Professional Behavior



Integrity & Fairness

Professional Competence

Independence and Disclosure  
of Interest and Confidentiality

Due Care

The model code of conduct for Registered Valuers  
issued by MCA under Companies (Registered  
Valuers and Valuation Rules), 2017

# **Need for Uniformity**

- **International Valuation Standards**
- **Indian Valuation Standards**
- **Ethical Standards**
- **Minimum Performance Framework**

# Valuation Resources and Practice Guidance

## REVENUE RULING 1959-60 (USA)

One of the oldest guidance available on Valuation in the world but still most relevant for Valuation of closely held equity shares. It gives primary guidance on eight basic factors to consider while doing any business /equity valuation.

- **Nature of the Business** and the History of the Enterprise from its inception
- **Economic outlook** in general and outlook of the **specific industry** in particular
- **Book Value** of the stock and the Financial condition of the business
- **Earning Capacity** of the company
- **Dividend-Paying Capacity** of the company
- Goodwill or other **Intangible value**
- **Sales of the stock and the Size of the block of stock to be valued**
- **Market prices** of stock of company engaged in the same or a similar line of business

Guidance w.r.t. valuation from private equity (CONTROL) perspective –

- **INTERNATIONAL PRIVATE EQUITY AND VENTURE CAPITAL (IPEV) VALUATION GUIDELINES (DEC 2015)**

Guidance w.r.t. valuation from MINORITY perspective –

- **AICPA PRACTICE AID VALUATION OF PRIVATELY HELD COMPANY SECURITIES ISSUED AS COMPENSATION (2013)**

Besides, there are Valuation Standards of different countries like U.S., Canada, Indonesia etc. However the IVS issued by IVSC are followed by about 100 countries around the world. The IVS are also complaint with IFRS based on which Ind-AS has been framed.

# Comparison of International Valuation Standards

## Research Paper

<https://cicbv.ca/wp-content/uploads/2014/09/CICBV-2014-Ian-Campbell-Research-Paper-Lobo-Bottomley-Final-April-15.pdf>

The above link provides a research study of differences in the approach to and application of business valuation theory and methodology from different regions around the world

It is concluded in this research that the differences in the approach to and application of business valuation theory and methodology around the world do not relate to the structure of valuation reports. Rather differences emerge in the underlying detail and the overall conceptual approach to valuation – more technical versus more professional judgement based, for example.

Source – Prepared for the 2014 Ian R. Campbell Research Initiative of The Canadian Institute of Chartered Business Valuators

By Prem M. Lobo and Matt Bottomley

# Mandatory Performance Framework – CEIV credential

The CEIV CREDENTIAL AS TO MANDATORY PERFORMANCE FRAMEWORK ADDRESSED ONE AREA WHERE GAPS IN GUIDANCE ARE BELIEVED TO STILL EXIST RELATES TO PERFORMANCE (that is, addressing the “how much to do” question).

Various terms have been used to describe this topic, such as “level of rigor,” “depth of analysis,” “scope of work,” “level of due diligence,” “extent of documentation,” and “extent of investigation.”

The Certified in Entity and Intangible Valuations (“CEIV”) credential was designed to enhance consistency and transparency in the fair value measurement process and will be issued to valuation professionals who perform fair value measurements for businesses, business interests, intangible assets, certain liabilities, and inventory for financial reporting purposes.

One must be a member of an approved VPO to obtain the CEIV credential. Currently the American Society of Appraisers (ASA), the American Institute of Certified Public Accountants (AICPA) and the Royal Institution of Chartered Surveyors (RICS) are approved to confer this credential.

**Source:**

<https://ceiv-credential.org/mandatory-performance-framework-and-application/>

# Knowing Regulatory Valuations in India under different laws

Fresh Issue of Shares	<ul style="list-style-type: none"> <li>• Reserve Bank of India – FDI</li> <li>• Reserve Bank of India – ODI</li> <li>• Income Tax Law</li> <li>• Company Law</li> <li>• SEBI Law</li> </ul>	<ul style="list-style-type: none"> <li>• Company Law</li> <li>• SEBI Law</li> <li>• Financial Reporting</li> </ul>	Business Combination/ Scheme of Arrangement
Transfer of Shares	<ul style="list-style-type: none"> <li>• Reserve Bank of India – FDI</li> <li>• Reserve Bank of India – ODI</li> <li>• Income Tax Law</li> </ul>	<ul style="list-style-type: none"> <li>• Income Tax Law</li> <li>• Company Law</li> <li>• Financial Reporting</li> </ul>	ESOP/Sweat Equity
Bankruptcy: Insolvency & Bankruptcy Code		Fair Value Accounting : IND-AS	

**Observation :** Valuation Standards permit Departures in order to comply with Legislative, Regulatory and Authoritative requirements. Hence knowledge of applicable Laws and valuation requirements is necessary.

A hand is shown at the top left, placing a smooth, grey, oval-shaped stone onto a stack of five similar stones. The stack is positioned on the left side of the image. The stones are smooth and have a slightly textured surface. The background is white, and the entire image is framed by a thick red border.

# **VALUATION PROFESSION**



# New Era of Valuation in India – Registered Valuers



- Legal Recognition
- Regulated Profession
- Uniform Practice
- Requires Skill set / Capacity Building  
/ Common Education & Training

# New Regulations - Registered Valuers

- Regulating the profession of Valuation in India for Standardization and Transparency. As of now, covers Companies Act and IBC.
- Defined Eligibility, Educational and Exam requirements
- Made 3 Asset classes – Securities or Financial Assets, Land & Building and Plant & Machinery
- Brought in concept of RVO's for education, training and monitoring of Valuers
- Coming up with Indian Valuation Standards
- Prescribed Contents of Valuation Report
- Maintenance of Records for 3+ years

# CoE 2020 Report - Key Recommendations

## Focus on both “Regulation” and “Development” of Valuation Profession

Valuation profession is largely in the self-regulation mode today, except for 3000+ Valuers regulated under the Valuation Rules.

The CoE has recommended enactment of an exclusive statute to provide for the establishment of the National Institute of Valuers (Institute / NIV) to protect the interests of users of valuation services in India and to promote the development of, and to regulate the profession of Valuers and market for valuation services. The Institute shall register and regulate Valuer Institutes, VPOs and Valuers.

**Scope:** The framework should NOT be limited to valuations under the Companies Act, 2013 and the Code, as are presently covered under the Valuation Rules and should cover valuations under other laws in a phased manner in due course, depending on experience and the needs of the time.

**Presumption of *bona fide*:** By definition, divergent views are possible in the field of valuation. If expressions of opinion on the value are lightly interdicted, it would be counterproductive to the objective of developing a vibrant market for the valuation services. Therefore, there should be a presumption of *bona fide* for the valuation conducted by a Valuer.

**Protection of Valuers:** Only the Institute should have authority to take action against a Valuer, after following due process. No court should take cognisance of any offence against a Valuer, save on a complaint made by the Institute or the Central Government.

**Valuation Standards:** The Institute should lay down valuation standards based on the recommendations of the Valuation Standards Committee. It shall be mandatory for Valuers to conduct valuation as per the valuation standards.



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