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Registered Valuer's role in the scheme of restructuring

Introduction:

The Ministry of Corporate Affairs (MCA) notified Section 230 sub sections 1 to 10 on 07/12/2016 (sub section 11 & 12 were notified on 3rd Feb, 2020) which provided the powers of companies to make arrangements with creditors and members.

In lay man term the section can be described as a scheme of compromise between:
(a) Company and its creditors or any class of them; or
(b) Company and its members or any class of them,
A classic example of such arrangement is a company under financial distress converting its existing debts from Bank or Financial Institutions (FI) into Share Capital (Equity or Preference or a cocktail of both). It basically happens when there is clear signal from the borrower/debtor that they are unable to pay the dues and some sort of compromise or adjustment is required between the parties which are not wholly detrimental to the interest of both of them.

This process can also be termed as a Corporate Debt Restructuring (CDR). In this article we will look at the role of Registered Valuer (RV) under the above-mentioned scheme.

Definition of Section 230 of Companies Act 2013

This scheme of arrangement/ restructuring is generally proposed by a creditor, a member or the liquidator (if the company is under liquidation proceedings) under section 230[3] to the Tribunal. The Tribunal shall on the merit of the proposal, order a meeting of the creditors or class of creditors, or of the members or class of members, as the case may be, to be called, held and conducted in such manner as the Tribunal directs. Section 230 (9) of the Act read with Rule 5 of the Rules inter alia provides that NCLT while hearing the application u/s 230 (1) of the Act can dispense the meetings of the creditors in a case where such creditors or class of creditors having at least ninety percent value, agree and confirm, by way of affidavit, to the scheme of compromise or arrangement.

The role of RV in this scheme

Section 230(2) (v) mandates furnishing of Valuation Report by a RV. The valuation report should consist of valuation in respect of the shares, the property and all assets, whether tangible or intangible, movable or immovable of the company. This may entail engaging of different classes of RV which are:

- Land & Building (L&B),
- Plant & Machinery (P&M) &
- Security or Financial Assets (SFA).

The role of RV becomes crucial here as the entire purpose of engaging a RV is to maintain independence, fairness & objectivity in the report. The valuations given by the valuer shall become the bedrock on which the entire restructuring shall rest upon.

The RV even though appointed by the Proposer of the Scheme is expected to be neutral. There have been multiple cases in the past in which valuation reports by the Valuer has been rejected by the NCLT/NCLAT.

Important Factors to consider for valuation

While preparing the valuation report in such type of schemes it is important to see what will be the status of control over the company after the approval of the scheme because in case of dilution of control of the management the value of shares is ideally expected to increase.

These types of schemes are generally pressure points for RVs as the proposer's insistence would be to complete the assignment as soon as possible. The Tribunal can also reject the scheme if it is of the view that the schemes are beneficial to a selected group of people. The RVs are required to mention in details the method and basis used for valuation. Their reports should help the parties to make an informed judgement.

As in with other types of valuations also a RV is expected to reject appointments if these go against the Professional Ethics set by the Valuation Fraternity. The RV can always step back from the assignment if he finds himself in a position or in a potential situation where his integrity is being compromised because even though the scheme is of arrangement and compromise a RV just simply cannot compromise with ethics!

Deciding on the Valuation Method

The valuation method takes a significant role in the scheme. Sometimes in these situations the commonly used method of Discounted Free Cash Flow cannot be used as it is difficult to gauge the future cash flows of the company as in most cases the company has incurred losses and the immediate future is at best shaky and full of potholes.

Practical Scenario

Many Banks are nowadays empanelling RV and, in such cases, Banks prefer the valuation report from their empanelled RVs only. Such instances can also lead to dispute between if the other parties to the arrangement/ restructuring are not satisfied with the conclusions of the valuation report or they have questions over the integrity of the valuer.

NESL can provide assistance to RV's

RVs cannot simply trust the data provided to them by the management. To ensure accuracy and completeness of data provided to RV, he/she can take the help of an Information Utility (IU). For the said purpose the Insolvency Professional or the Proposer can make an application to the IU. Currently only National E-Governance Services Limited (NESL) has been allowed to act as an IU. An IU is a professional organization (which is registered with Insolvency And Bankruptcy Board of India under Section 210 of IBC, 2016 as per the eligibility criteria prescribed) that will collect financial information, get the same authenticated by other parties connected to the debt & store the same and provide access to the Resolution Professionals, Creditors and other stake holders in the Insolvency Resolution Process, so that all stake holders can make decisions based on the same information.

Current Updates

Recent notification of Section 230(11) of the Act, which provides for takeover in cases of Unlisted Companies) has led to a fear of exploitation of minority shareholders. The provisions allow majority shareholders, holding 3/4th of the shares, in a company to make a takeover offer to acquire any part of the remaining shares, by way of an application before the NCLT. Again, in such a scenario, Valuation reports play an important part in justifying the fair value of the minority shareholders.

Conclusion

The concept of Debt Restructuring is an old concept but the concept of RV is new and as such a RV is required to be cautious while dealing with such assignments and not bow to any coercion or succumb to undue influence.