IOV RVF THE VALUER Bi- Monthly Journal, Vol. 02 , Issue-03 May - June 2023, PP. 22- 29

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Valuation of Companies under the Companies Act, 2013: Related Issues

ABSTRACT:

The introduction of Section 247 in the company's act, 2013 recognizes valuation job and the valuation profession in a different dimension. This brings a new area in the valuation professional opportunity in the country. This paper will narrate laws, rules and regulations that are at play, in relation to the valuation of companies after the enactment of companies' act, 2013.

Key words: Valuation, assets & liabilities, shares & debentures, securities, regulations.

INTRODUCTION

It is the Companies Act, 2013 which recognizes that the valuers play an important role inthe corporate world. Once, the valuation job was done the Chartered Accountants or other professionals or experts as specified under the various acts and rules: FEMA, 1999 or regulation under the Income Tax Act, 1961 etc. Later, the concept & rationale behind introducing the registered valuers arise on account of the following:

1. Lay down the criteria for registration, rights & duties of the valuer,
2. Approach and methods to be used by the registered valuers,
3. The style & contents of the Valuation Report,

4. Set the valuation standards,
5. Regulation for the profession required bring to maintain transparency and better governance principles during a valuation exercise.

The following action opens a new area in the valuation profession.

1. Introduction of Section 247 of Chapter VXII of the Companies act, 2013 for the matters requires valuation, and
2. Introduction of the Companies (Registered Valuers & Valuation) Rules, 2017.

Section 247 of the said act provides that only the registered valuers with the requisite qualifications & experience are authorized to do valuation work in respect of any property i.e., shares, stocks, debentures, securities, goodwill or any other assets of a company under the provisions of the act, and in such a manner and terms and conditions etc. and as specified and as may be prescribed by and appointed by the audit committee or by the board of directors of that company. The prescribed guidelines are as follows:

a. Qualifications & experiences as prescribed for the registered valuers for different classes of assets valuation under the Companies Act, 2013,

b. Prescribed rules under the Insolvency and Bankruptcy Code, 2016, and

1. For example,

In respect of valuation of land & building, the registered valuers must be either a graduate or a post graduate in civil engineering, architecture or town planning with minimum of 3 to 5 years of
2. experience,

In respect of valuation of plant & Machineries, the registered valuers must be either a graduate or a post graduate in Mechanical or Electrical engineering, with mini-
3. mum of 3 to 5 years of experience,

In respect of valuation of securities & financial asserts etc. the registered valuers must be either a Chartered Accountants, or a Cost Accountants or a Company Secretaries or an MBA(Finance) with minimum of 3 to 5 years of experience after acquiring the qualification. [1]

1Companies act-2013, Companies (Registered Valuers and Valuation) Rules, 2014

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IMPORTANCE OF VALUATION OF ASSETS

The issue and transfer of both equity shares and the other related securities involves the valuation of the respective company.

The principles and rules relating to valuation of companies involves various laws, rules and accounting etc. The valuation job of a company invites compliance of various statutes, regulations and many other critical activities like:

a. The law ensures that companies do not short-change their existing shareholders by issuing securities below their fair market value,
b. The Reserve Bank of India (RBI) has issued a number of rules and regulations in order to regulate the inflow and outflow of funds,
c. Foreign Exchange Management Act, 1999(FEMA) regulates the non-residents 's outflow/ inflow of foreign exchange on account of the following reasons so that:

1. Non-residents underpay for the Indian securities, or
2. Non -residents do not sell the Indian securities to Indian residents at a price exceeding their fair market value.

d. The Securities and Exchange Board of India (SEBI) is entrusted to prevent investors, especially retail investors, from being offered securities at a value higher than the applicable fair market value,
e. Income tax authorities is entrusted to ensure the fair valuation of securities that are issued or bought orsold in order to prevent evasion of tax.
f. Provisions under the Insolvency & Bankruptcy Code, 2016 prescribes valuation report from a registered valuer.

VALUER: VALUE & VALUATION

It is imperative to study the valuation report of the particular organisation / company before investing in the said company and the valuation task involves the analysis of the following while valuing the company:

a. Economic worth of the company's business,
b. Asset's base of the company, c .
Current financial health,
d. Prospect and future of the company,
e. The industry scenario and the economy of the country

Valuation is essential not only for the company itself but also it is also essential to its investors.

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Valuation helps a company to track its progress, to measure its performance and finally helps to take steps against its competitors. Valuations helps the investors to determine the worth of potential and current investments.
Investors will try to sell their high valued securities and buy the low valued instruments in order to earn more out of their investments in securities.

Valuation of a public company is more convenient than a private company because the data and information readily available for a listed company than for a private company because the private companies do not publish their report on their financial statements.
Moreover, there is no standardized stock exchange for private companies. Therefore, it isn't easy to ascertain the market price and capitalization of the company in respect of private companies.

Section 247 of the Companies Act provides that:
"(1) Where a valuation is required to be made in respect of any property, stocks, shares, debentures, securities or goodwill or any other assets (herein referred to as the assets) or net worth of a company or its liabilities under the provision of this Act, it shall be valued by a person having such qualifications and experience, registered as a valuer and being a member of an organisation recognised, in such manner, on such terms and conditions as may be prescribed and appointed by the audit committee or in its absence by the Board of Directors of that company."2

Hence, a registered valuer in the valuation process ensures that the value as determined is accurate and reliable.

Valuation report under the Companies Act, 2013 The Companies Act, 2013 requires a valuation report from a registered valuer in the following situations:

a. Section 42 of the Companies Act, 2013:

In respect of the private placement of securities, Rule 12(5) of the Companies (Prospectus and Allotment of Securities) Rules, 2014 prescribes that the valuation

2Companies (Registered Valuers and Valuation) Rules, 2017

Section 62(1) (c) of the Companies Act, 2013:

In respect of the issues of preferential shares, Rule 13 of the Companies (Share Capital and Debentures) Rules, 2014 prescribes that if the consideration for the securities being issued is not in cash, then as per Rule 2(d)(xii) of the Share Capital and Debentures Rules, a valuation report for such consideration is also required.

Section 55 of the Companies Act, 2013:

In respect of the issue of preferential shares by a listed company, the price of the shares needs to be determined by the valuation report but for repeat issue which is as per the second provision to the Rule 13(1) of the Share Capital and Debentures Rules, no further valuation report is required.

Section 52 of the Companies Act, 2013:

While issuing the sweat equity shares to directors/ employees at a discount or for consideration other than cash, as per Section 52 of the Companies Act read with Rule 8 of the Share Capital and Debentures Rules, a valuation report is required for the intellectual property rights or of know how or value additions for which the sweat equity shares are to be issued.

Rule 16(1)(c) of the Companies (Share capital & Debentures) Rule, 2014:

While buy back of shares, where the shares of companies are not listed on a recognised stock exchange, when the valuation of shares are to be purchased, the same requires valuation by the registered valuer.

Rule 2 (c) (ix) & Rule 6(1) of the Companies (Acceptance of Deposit) Rule, 2014:

The secured debentures once valued by the registered valuer will be excluded from the definition of deposits.

Section 177 (4)(vi) of the company's act, 2013:

The vigil mechanism shall provide for adequate safeguards and provide for direct access to the Chairperson of the Audit Committee or the Director nominated to play the role ofAudit Committee, as the case may be. The valuation of assets with reference to Audit Committee shall be done by the registered valuer.

Rule 6 of the Companies (Acceptance of Deposits) Rules, 2014:

The amount of such deposits and the interest payable thereon shall not exceed the market value of such assets as assessed by a registered valuer.

Section 192 of the Companies Act:
No company can enter into an arrangement with a director or any director of a holding or subsidiary or associate company, in terms of the following situations:

1. Such person acquires or is to acquire assets for consideration other than cash from the company, or
2. When a company acquires or is to acquire assets for consideration other than cash from such person

Section 230 of the Companies Act, 2013:
While any corporate debt restructuring under the said Act is proposed, then a valuation report of the company by the registered valuer is essential in respect of the shares and all the assets and the properties whether the same are tangible or intangible, movable or immovable etc.

Section 232 of the Companies Act, 2013:

In case of any merger or amalgamation of any two or more companies under the said act. Section 232(2) of the said act provides that a report of the expert with regard to valuation is required to be circulated where an order has been made by the Tribunal under section 232(1) of the act, merging companies or the companies in respect of which a division is proposed.

Section 281 (1) (a) of the company's act, 2013:

In case of liquidation case of winding up of a company, the valuation of assets to be done by the registered valuer for submission to the liquidator. For the acquisition of any stake held by minority shareholders and for a Company Liquidator appointed by the National Company Law Tribunal (NCLT) pursuant to or in connection with the winding up of a company to submit a report to the NCLT regarding the assets of the company, under Section 281 of the Companies Act

Section 236(2) of the Companies Act:

In case of acquisition of shares of a company and the acquirer is a person, or group of persons under section 236(1) shall offer to the minority shareholders of the company for buying the equity shares held by such shareholders at a price determined on the basis of valuation by a registered valuer in accordance with the rules as may be prescribed.

Section 305(2)(d) of the company's act, 2013:

During declaration of insolvency and proposal of voluntary winding up has been made by the company, the same must be accompanied by the valuation report by the registered valuer.

Section 319(3)(b) of the company's act, 2013:

In case of sale of property of the company in consideration of shares by the liquidators, any member of the transferor company who did not vote in favour of the special resolution and expresses his dissent in writing to the company liquidator, may require the liquidator to purchase his interest at a price to be assessed by the agreement or by the registered valuer.[3]

VALUATION REPORT

a. The details of the company under valuation;
b. Background information of the asset under valuation;
c. Purpose & object of valuation; Appointing authority for the appointment of valuer;
e. Detail's identity of the valuer;
f. Specify that any other experts are involved in the valuation process;
g. Disclosure of the valuer's details i.e., any interest/conflict, if any in relation to the company;
h. Date of appointment of the valuer;
i. The date of valuation completed and date of the report submitted;
j. Sources of information and other details in connection with valuation process;
k. Methodology and Procedures adopted while carrying out the valuation process;
l. Assumptions;
m. Valuation standards followed;
n. Major factors which influenced the valuation process;
o. Caveats, limitations and disclaimers etc.[4]

CONCLUSION

The role of valuers in the business valuation process plays a very vital rolenot only to the management of a organisation but also to the investors and other various authorities. Hence, the valuers act either negligently or failed to consider all the required criteria / formalities as per the Companies Act,2013 while determining the value of shares, then the related person and the authorities has the right to sue the valuer for any losses caused by the wrong valuation of shares. In normal practice, the Tribunal does not intervene with the act of expert valuers. Once, the value is contested, there must be sufficient evidence in order to establish that is required to prove that the valuation is incorrect.5 Hence, for valuation purposes, the registered valuers with requisite qualifications & experience are needed for a fair and accurate assessment of the assets.

The law states that the Valuer should exercise due diligence while performing the task of valuation. The due diligence should be categorically and specifically defined in terms of additionalsteps a valuer needs to follow before taking up the valuation task of a company. Although, the due diligence is a very broad term and imply various types of due diligence e.g., tax matters,financial issues or commercial issues etc which need specific expertise and the valuer requires to build up qualifications, knowledge and expertise before taking up the aluation task of a business enterprise.

4 Companies (registered valuers and valuation) rules, 2017