



**THE INSTITUTE OF
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Ref: ICAI/TRD/JUNE2018

Dated: 28.06.2018

To,
Shri Pravin Rawal,
Director (Tax Policy and Legislation)
North Block,
New Delhi 110001.

Dear Sir,

Re: Empowering the members of the Institute of Cost Accountants of India (ICAI) for Valuation and certification thereof – Proposal for amendment in Income Tax Rules

Income Tax Rule 11UA deals with Valuation of jewellery, archaeological collections and shares and securities for the purpose of Section 56. Erstwhile as per Clause (b) of Sub-Rule 2 of Rule 11UA earlier merchant banker and Chartered Accountant were allowed to do valuation of unquoted equity shares under Discounted Free Cash Flow method but vide Notification No. 23/2018 dated 24th May, 2018 it is provided that now only merchant banker can only carry out the valuation of unquoted equity shares under Discounted Free Cash Flow method.

The Institute of Cost Accountants of India (ICAI) is a premier Professional Education Institute constituted under an Act of the Parliament. The Institute is the pioneer in the Cost and Management Accounting profession in the country and member of all the Global Institution in the area of accounting, management accounting etc. The Institute actively taking part in several initiatives of the Government and CBDT towards bringing in reforms in the taxation statute in the country including the new Direct Tax Code. The institute is also actively participating from time to time on various issues faced by the assesseees in respect of Tax matters be it Direct Tax as well as Indirect taxes.

The Institute would like to draw the attention of the Government and highlighting the issues and concerns in respect of Notification No. 23/2018, dated 24th May, 2018 amending Rule 11UA omitting reference to the term 'Accountant' thereby permitting only a merchant banker to determine the FMV of unquoted equity shares as per the Discounted Free Cash Flow Method. The Institute of Cost Accountants of India (ICAI) would like to place before the Government it's professional expertise and experiences in the area of valuation and towards bringing in greater transparency in the methods of valuation and the general interest of all the stake holders and



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assesses, to include the members of The Institute of Cost Accountants of India (ICAI) and to carry out the assignment of valuation.

In relation to this notification, we would like to present detailed submissions in respect of initiatives/concerns of ICAI. **The detailed submissions are placed in the annexure to this letter.**

This submission has detailed about the:

Initiatives taken by The Institute of Cost Accountants of India (ICAI) on Valuation Standards - as a background material for Valuation Practices. Professional competence of Cost Accountants - Recognition by the commercial world including Bankers in connection with stock audit and valuation.

Section 247 of the Companies Act, 2013 recognizes cost accountant (membership in ICAI) to be eligible for registering as a valuer. The statute says "membership of a professional institute set up under an Act of Parliament and at least five years' experience after such membership.

Valuation Standards being formulated by the Cost Accounting standard Board of ICAI - Focus on activities performed by Cost Accountants in respect of valuation by setting up RVO in the Institute. The Institute would like to place on record that limited availability of the merchant bankers would further lead to increase in cost to the assesses for determining the FMV of unquoted equity shares. This, for sure, is neither the intent of the Government nor the same is in line with the objective of the Government of "ease of doing business". Such a situation can be easily avoided if the notification is recognized and a status quo before the notification is maintained.

In view of the above, ICAI would like to place its concern about the effective and transparent way of valuation and ensuring appropriate declaration of value and sincerely place it's request for inclusion of the ICAI and its members within the definition and ambit of valuation under this provision of the Act. In view of all the facts, and considering that ICAI is putting in all out efforts to ensure that the members of ICAI to efficiently and effectively perform their role as a valuer, it is strongly proposed to amendment the Rule 11UA to incorporate and include the members of the Institute of Cost Accountants of India (ICAI) as the authorized valuer under the provisions of Direct Tax.

Regards,

CMA Niranjan Mishra
Chairman – Taxation Committee and Central Council Member



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Encl: Detailed submission as Annexure

Copy shared with:

1. Shri Arun Jaitley, Hon'ble Minister of Finance, Govt. of India, North Block, New Delhi
2. Shri P P Chaudhary, Hon'ble Union Minister of State, Ministry of Law and Justice, and Ministry of Corporate Affairs
3. Shri Shiv Pratap Shukla, Hon'ble Minister of State for Finance.
4. Chairman, Central Board of Direct Taxes



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Annexure to the Representation

ISSUES OF CONCERN OF ICAI ON AMENDED RULE 11U AND RULE 11UA VIDE NOTIFICATION NO. 23/2018, Dated 24th MAY, 2018 ISSUED BY THE CBDT AND THE REQUEST THAT ARE PLACED BEFORE CBDT.

The change has been brought in Rule 11UA of the Income Tax Rules which deals with the valuation of various assets for the purpose of sections 56(2)(viib) or 56(2)(x) of the Income Tax Act. While section 56(2) (x) deals with charging of income tax under the head other sources where there is a gain due to difference in fair value of an asset and the transaction value of an asset transferred, section 56(viib) provides for charging of tax under the head other sources, where any closely held company issues shares at more than fair value of the asset.

Rule 11UA has been divided into two sub rules which provide as follows:

1. Sub rule (1) of Rule 11UA determines the fair market value of a property, other than immovable property
2. Sub rule (2) of Rule 11UA determines the fair market value of unquoted shares for the purpose of section 56 (2)(viib) of the I.T Act, 1961

Clause (a) of sub rule (2) of Rule 11UA deals with adjusted net asset value (NAV) method. Certification of such valuation is silent in the Rules. Clause (b) of sub rule (2) of Rule 11UA deals with the discounted cash flow (DCF) approach DCF model indicates the fair market value of a business based on the value of projected cash flows that the business is expected to generate in future.

Central Board of Direct Taxes (CBDT) vide its Notification no –

23/2018/F.No.370142/5/2018-TPL dated 24th May, 2018 has made alterations in Rule 11UA(2)(b), which allowed merchant bankers and chartered accountants for carrying out valuation of the equity shares using discounted cash flow method. The notification has withdrawn the power assigned to CAs for determining fair market value of unquoted shares under Discounted cash flow (DCF) method for the purpose of section 56(2)(viib). The said notification has been made effective from 24th May, 2018.



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The notification has also removed the definition of the term 'accountant' as defined under Rule 11U, which defines the meaning of expression used in determination of fair market value for Rule 11UA.

Therefore, if a closely held company is desirous of issuing further shares and wants to get it valued under DCF, then it will have to get it done by merchant bankers only.

Valuation of business, financial instruments and other assets has been gaining importance over the period of time and is considered as one of the most critical areas in finance, in particular after the implementation of Ind-AS and it plays a key role in financial reporting and in other areas of finance such as buy/sell, solvency, merger and acquisition.

The Institute of Cost Accountants of India (ICAI) is extremely concerned about this notification and the rationale of this notification, which may not be in the interest of the assessee and all the stakeholders. The pioneer institute / profession of Cost Accountancy qualification is a blend of financial management, strategic management and financial reporting which provides a focused understanding and concentrate on valuation and is adequately equipped to independently undertake Valuation Assignments.

ICAI place on record the competencies of the Cost Accountants in the field of Accounting, Auditing, Management Accounting and as Valuer under section 247 of the Companies Act, 2013 including the initiatives taken and its concerns regarding this amendment. With this representation, we also want to put forward our eligibility towards consideration of the ICAI Professional for valuation related functions:

1. Initiatives taken by The Institute of Cost Accountants of India (ICAI) on Valuation Standards - as a background material for Valuation Practices.

Towards bringing in transparency in the valuation methods and towards appropriately determining the value of the assets, it is felt important to have the consistent, uniform and transparent valuation policies and harmonize the diverse practices in use in India; the Institute is in the process of issuance of valuation practices Standards. This is one of the best initiatives of its kind that has been taken up in India by The Institute of Cost Accountants of India (ICAI).



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The Institute of Cost Accountants of India (ICAI) issues Cost Accounting Standards on the various elements and segments of cost which forms an integral part in the process of preparing and issuance of Valuation Standards in line with the best practices and within legal framework to ensure transparency in the principles, procedures and quality of valuation output. The standards include methods and procedure of classification of cost, deriving cost of different overheads and direct/indirect elements of cost of a business. These standards form the basis of Valuation of any business. ICAI, being the pioneer in cost accounting possesses the expertise and is in the process of preparing the framework for Valuation thereby using the Cost Accounting Standards to ascertain Business Valuation including valuation of assets and financial instruments.

While preparing the Valuation Standards International Best practices are being taken into consideration keeping in background the unique conditions of Indian Economy and Best Practices prevailing in India.

These formulated standards on valuation would require the member and the valuers to properly value the assets in a standard determined manner and recognizes the manner of valuation provided for in specific legislations including the legislation relating to Companies Act. The valuation standards forming part of the Cost Accounting Standard Board is being formulated with specific reference to the provisions of Income Tax Act; Companies Act 2013, SEBI Regulations; and The Insolvency and Bankruptcy Code.

In view of the above, the members of The Institute of Cost Accountants of India (ICAI) and should be considered as the authorized valuer in Rule 11UA (2) (b) and the necessary amendment should be incorporated.

2. Knowledge base and Professional competence of The Institute of Cost Accountants of India (ICAI) in the area of accounting, management accounting , valuation, auditing taxation etc

As discussed, the ICAI is pioneer in the field of imparting professional knowledge on Accounting, standards, Statutory legislations, Valuation , management and strategic management etc and authorized to carry out the responsibility of various certifications under the provisions of VAT Act, GST Act, Companies Act, Customs Law & Practice, and several other provisions as applicable in the Country.

In the specific area of valuation and valuation management The Institute of Cost Accountants of India (ICAI) is once again a pioneer since it is having a full length paper at the Final Level of



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examination of the examination of the Institute called as "Valuation Management". The area of valuation of unquoted equity shares, it is also noteworthy to mention in that syllabus of paper 8 of the Final Examination wherein the theory of valuation, discount rate selection in relation to cash flows and different approaches to valuation of equity shares are being extensively dealt with. Other important papers of the final level syllabus like Financial Management, cost management are few examples of the core papers of the Final Course, wherein higher level skills of evaluation and synthesis of aspiring Cost accountants are evaluated. It is very important to note that the manner of valuation provided by Rule 11UA(2)(b) predominantly mentions application of discounted cash flow method. A member of The Institute of Cost Accountants of India (ICAI) has the desired level of professional competence as also the understanding of the business and cash flow projections, is well equipped to, inter alia, undertake valuation of shares.

3. Provisions of Section 247 of the Companies Act, 2013 recognizes members of The Institute of Cost Accountants of India (ICAI) to be eligible for registering as valuer.

Chapter XVII of the Companies Act, 2013 deals with Registered Valuers. Section 247 (**Valuation by registered valuers**) 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 and registered as a valuer 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.* The provision speaks like:

Qualifications and experience

An individual shall have the following qualifications to be eligible for registration under Rule 5

- (i) A Post -Graduate degree, in the specified discipline, from a University established, recognized or incorporated by law in India and at least three years of experience in the discipline thereafter; or
- (ii) A Bachelor's degree, in the specified discipline, from a university established, recognized or incorporated by law in India and at least five years of experience in the discipline thereafter; or



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- (iii) **Membership of a professional institute set up under an Act of Parliament and at least five years' experience** after such membership.

Accordingly, Rules in this regard are issued by the Government (Companies (Registered Valuers and Valuation) Rules, 2017). In accordance with these Rules, The Institute of Cost Accountants of India (ICAI) has formed ICAI Registered Valuers Organization (RVO). This is a section 8 Company formed to enroll and regulate registered valuers as its members. This organization carries out the functions of the Registered Valuers Organization under the Companies (Registered Valuers and Valuation) Rules, 2018, and functions incidental thereto. These Rules recognize the qualification of the member of ICAI (Cost Accountants) as eligible to be registered as a valuer for the course on valuation conducted by Registered Valuers Organization, examination of which is conducted by Insolvency and Bankruptcy Board of India (set up under the Insolvency and Bankruptcy Code, 2016).

The 50 hours educational course for ICAI Registered Valuers' Organization (a Section 8 company formed by ICAI) has commenced. It is an extensive training covering all aspects of valuation, case studies, finance, financial statement analysis, judicial pronouncements etc.

The qualifying education, experience and examination or training for various asset classes, is given in an indicative matrix in Companies (Registered Valuers and valuation) Rules, 2017. Since the Companies Act, 2013 allows a member of ICAI to act as valuer of assets including, shares and securities, such a member should also be permitted to act as a valuer of equity shares for income tax purposes as per the Income-tax Act, 1961.

4. Requirement of more professionals and greater reach of professionals.

The Institute of Cost Accountants of India (ICAI) is having a huge base of members who are scattered in all over India including metros and second tier or third tier cities. This will enable to a greater reach to the professionals that are required for the Valuation purpose. On the contrary as per SEBI, as on date, there are only 195 Intermediaries (Merchant Bankers) (Source: <https://www.sebi.gov.in/sebiweb/other/OtherAction.do?doRecognisedFpi=yes&intmld=9>). Who are generally concentrated in metro cities.

With the enablement of the members of The Institute of Cost Accountants of India (ICAI) to execute the assignment of valuation, scarcity of the merchant bankers would be reduced and the government could extend the services to the remotest corner of the country. This approach



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would reduce the cost to the assessee for determining the FMV of unquoted equity shares and thereby would be benefitted by all the stakeholders. This, for sure, is neither the intent of the Government nor the same is in line with the objective of the Government of "ease of doing business". Hence, in all possibility, the valuations would be prepared by The Institute of Cost Accountants of India (ICAI) Members on behalf of the bankers and the cost would increase.

5. Initiatives of ICAI- relating to the activities performed by Cost Accountants in respect of valuation

ICAI, in its regular activities, is engaged in enhancing knowledge base of its members to improve the efficiencies and capabilities of its members in practice. ICAI has focused in the field of valuation with the introduction of IBC. ICAI has formed RVO as a separate entity within the Institute to enable its members to enhance their capabilities for performing their function more effectively and efficiently as valuers. And in relation to the same to the same, your attention is drawn to the following issue:

ICAI conducted Certificate Course on Valuation for its members, wherein it imparts training and expertise in taking up Valuation assignments. The participants undergo a written examination before being awarded the certificate for Valuation. The course is case study based and all the participants are exposed to undergo virtual stimulation exercise.

ICAI has successfully trained most of their members in practice through the course on Valuation. It is to be noted that valuation required under the Companies Act, 2013 and the Income-tax Act, 1961 is entirely in the nature of financial valuation, involving application of accounting and finance. Hence the members of ICAI are best suited to be the Registered Valuers in cases involving financial valuation.

In view of all the facts, and considering that ICAI is putting in all out efforts to ensure that the members of ICAI to efficiently and effectively perform their role as a valuer, it is strongly proposed to amend the Rule 11UA to incorporate and include the members of ICAI as the authorized valuer under the provisions of Direct Tax.