

VALUATION PROFESSION IN INDIA: ORGANISATIONAL EVOLUTION, INSTITUTIONAL IMPORTANCE AND WAY FORWARD

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*‘Not everything that can be counted counts, and not everything
that counts can be counted’*

-William Bruce Cameron

INSTITUTIONS AND ECONOMIC GROWTH

The emergence of market society across the globe, increased trade of goods and services. It was accompanied by an exchange of ideas, movement of people that drove political, economic and social changes. Rapid increase in economic activity with market transitions, altered the mechanisms of existing institutions. The need for formalised and accountable institutions was created. Historical examination of the role of institutions in determining market outcomes highlights the pivotal role that institutions play in the larger economic growth trajectory of a country. European colonisation, division of Korea and evolution of these countries thereafter are evidence to the fact that ‘institutions matter’. Colonies that were subject to extractive and exploitative institutions at the hands of their colonisers, still struggle to drive a progressive institutional change. Consider the case of Africa. Vested interests, high levels of corruption and exploitation which were passed down from their colonisers have defined the current political and economic outcomes to a large extent. The growth trajectories post division of Korea into North and South is a quintessential historical event

that provides evidence on role of institutions. The two parts have very different economic, political and social institutions. It reaffirms that less-restrictive, market oriented, and efficient institutions are foundations of nation growth and prosperity.¹

The study of role of institutions in economic growth has assumed greater significance owing to globalisation and increased interdependence between countries. Institutions that uphold property rights and ensure that contracts are enforced are pre-requisites to strong nation building. Studies² have arrived at a classification of institutions into four categories. The first is ‘market-creating’ institutions. These institutions allow for the development of a market economy, one that allows free trade and in absence of which markets cease to exist. The second is ‘market-regulating’ institutions. These institutions are concerned with externalities that arise from market failure. Excess market power, inefficient resource allocation typically accounts for market failure. Regulatory agencies in sectors such as telecommunications, transport and financial services form a part of market regulating institutions. Third category is ‘market-stabilising’ institutions. These comprise of institutions that reduce macroeconomic volatility and risks associated with financial crises- inflationary pressures, monitoring exchange rate fluctuations etc. The fourth category of ‘market-legitimising’ institutions are those that provide social protection and involve redistribution of resources. It includes social protection mechanisms such as pension schemes and unemployment insurance schemes³. By virtue of its inclusive nature, ‘market-legitimising’ institutions also manage to avert conflict.

Valuation Profession as an Institution

A market-oriented economy with increased firm activity engages a large number of stakeholders who may have conflicting interests. Competition is an essential characteristic of a free market economy, which at times can lead to abuse of market power and aggravation of conflicts.⁴ To balance individual interests, the law mandates a set of governance norms ensuring societal interests are best protected over individual benefit. This has given rise to the age of ‘professionals’.⁵ Professionals possess specialised knowledge and expertise in their area of operation. In the absence of formal institutions, the market forces of demand and supply acted as clearing agents and arrived at the equilibrium price of assets and commodities. However, while this may be the invisible hand that Adam Smith discussed in his *laissez-faire* economic policies, market prices in the current complicated political and economic structures may not serve as a useful metric to quantify the worth of assets and commodities. One such institutional framework where market price may not be a useful guide is the institution for Valuation Profession. A market-regulating, market-legitimising institution, it is fundamental in developing a sub-system of professionals. They act as economic agents that take several financial decisions on the basis of value of an asset.

Prior to developing a case for the need of an institution of Valuation Profession, it is imperative to understand the essence of this institution.

An institution for Valuation Profession as the name suggests is an entity that deals with business valuation. The entity consists of experts- Valuer or Valuation Professionals who carry out the task

of valuation and arrive at an estimate or worth of the asset which is called a value. This value is not the market price. It can be significantly different and in most cases is context specific.⁶ This value is determined after evaluating all aspects of the business and through use of other objective measures. The field of business valuation encompasses a wide array of variables that jointly and severally impact the value.⁷

Imperatives for Institutionalising Valuation Profession

The need for an institution of Valuation Profession stems from the wealth maximisation strategy. Business valuation process generally arises when an entity considers to sell all or a portion of its operations or even merge with / acquire another entity. Downside risks of incorrect valuation include deterioration in the value of assets or in the extreme case, complete loss of value.⁸ Financial risks are heightened in cases where values are not genuine. Both over and undervaluation of assets can leave either party worse-off and discourage a mutually beneficial exchange, stalling economic growth. Valuations are an essential part of business decisions. In order to facilitate smoother transactions in the market, a valuation of assets is required. An ever-growing market with expanding innovations and businesses are bound to render traditional methods, resources, technologies and entities redundant. This process of replacement of the old with new, coined as ‘creative destruction’ by the economist Joseph Schumpeter⁹ creates a need for an institution that achieves this with minimum erosion of value. Valuation services are used not only by corporate houses but also other financial institutions such as banks. Individual persons also seek valuation services. The values serve as a guide for evaluating alternatives and help arrive at an informed decision. The ultimate purpose of any firm is the creation of value for its stakeholders.

Focusing on the Indian context, post 1991, India has been on the path to become a market driven economy. The liberalisation, privatisation and globalisation (LPG) policies adopted in 1991, set India at the centre stage of international trade in goods and services. Early developments included diversification in manufacturing sector, emergence of a strong service sector and expansion of the financial sector. The role of institutions in further developing and sustaining economic growth cannot be negated.¹⁰ India continues to experience several political and economic changes. In this process, the resource stock of the country and its value also change. Thus, building a strong and efficient institution of Valuation Profession is of supreme significance. For long run growth of any profession, existence of institutions matters. The next section explores the evolution of the framework for institution of Valuation Profession in India.

ORGANISATIONAL EVOLUTION OF THE FRAMEWORK OF VALUATION PROFESSION

The valuation profession is a vital institution of the market economies, it directly or indirectly affects everyone. Valuation services are required in almost all parts of our globally financial system; it is needed for several market-based transactions such as mergers, acquisitions, take over, liquidation,

issue of securities etc. India in particular, being one of the fastest growing economies in the world, has a strong vested interest in high quality standards for valuation, both domestically and globally.¹¹

For long, in absence of any statutory provisions and rules in place, the valuation services have been delivered by the auditors, merchant bankers, company secretaries and chartered accountants. The services delivered were largely based on subjective opinions and not on any universal standard or established frameworks. Regulation of this profession is important to ascertain standardisation of practices and reduction in commercial uncertainties. However, the valuation profession and the services provided by it are not regulated, which creates a risky situation for the stakeholders.¹²

In 2005, the J.J. Irani Expert Committee report emphasised on recognition of the valuation profession and the necessity of regulating it. The Government of India, with the intention of regulating the valuation professionals and valuation professional organisations, introduced the concept of Registered Valuer (RV) under section 247 of the Companies Act, 2013 (Companies Act).¹³ Section 247 makes it mandatory to be a RV in order to carry out all valuations under the Companies Act. Even before this, the Government had been taking incremental steps for quite some time to bring the profession under some kind of structured framework. To overcome lacuna of absence of such a framework, following steps were taken by the Government in the recent past to establish an effective framework for promoting and recognising the valuation profession in India;

(a) The Companies Bill, 2008: The Companies Bill, 2008 (2008 Companies Bill) was a step forward towards the introduction of RVs to come into existence. The 2008 Companies Bill emphasised on the need to have a RV. Section 218 of the Bill provided that: ¹⁴

where valuation is required to be made in respect of any property, stocks, shares, debentures, securities, goodwill or net worth of a company or its assets, it shall be valued by a RV appointed by the Audit Committee or in its absence by the Board of Directors of the company.

Subsequently, the Government also proposed a formal and regulatory framework for the valuation professionals by introducing a Valuation Professional Bill, 2008, *‘which provided for the constitution of the Council of Valuation Professionals inter alia for development, regulation, certification of qualification and quality of the valuation professional engaged in providing valuation services.’* The Valuation Professional Bill, 2008, adopted a two-tier statutory self-regulated model where the Council of Valuation Professionals acted as the principal regulator and the recognised institutes as the frontline regulators.¹⁵

The 2008 Companies Bill further provided for the Government to maintain a record of RV to keep a track of all the active valuers. It laid the eligibility criteria for the professionals to become a RV, their roles and responsibilities etc. However, due to some technicalities, it was not introduced in the Indian parliament. Later, it was introduced as the Companies Bill, 2009 with further recommendations from the Standing Committee on Finance which increased the extent of the RV.¹⁶

(b) The Companies Act, 2013: The Ministry of Corporate Affairs (MCA) vide its notification dated

October 18, 2017, introduced RV as a new profession under section 247 of the Companies Act which states that the valuation, where required, in respect of any property, stocks, shares, debentures, securities or goodwill or any other asset or net worth of a company or its liabilities, is to 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.'*¹⁷ Prior to this notification, this profession was not regulated by any regulatory body. Perhaps this is the reason as to why the valuation profession has not achieved the heights which it deserves, in parallel to other existing professions such as Chartered Accountants, Company Secretaries, Cost Accountants. Subsequently, vide notification dated 23rd October, 2017, the Central Government delegated its powers and functions vested in it under section 247 of the Companies Act, 2013 to the Insolvency and Bankruptcy Board of India.

In pursuance of provisions of section 247 of the Companies Act, the MCA placed the Draft Companies Rules, 2017 and invited comments/ suggestions from the general public in order to understand the requirements and concerns of various stakeholders. After considering the comments/ suggestions, the Companies (Registered Valuers & Valuation) Rules, 2017 (Valuation Rules) were notified under the Companies Act by the MCA on October 18, 2017 as a response to the arising needs of the market of valuation services. These rules laid down various valuation standards and policies to be followed by the companies and the RVs.¹⁸ It also laid down the eligibility criteria for an organisation to be registered as a Registered Valuers Organisation (RVO), thus, sealing the existence and functioning of the RVOs.

(c) The Companies (Removal of Difficulties) Second Order, 2017: After section 247 of the Companies Act came into existence, a difficulty was observed when various different organisations dealing with various distinct group of assets such as land and building, machinery and equipment, and having different set of valuers for valuation were functioning without being recognised. It was imperative to recognise these organisations by registering them in order to ensure the required level of regulation on the RVs as well as on these organisations. Further, it was essential to recognise the internal procedures and conducts of these organisations to improve the standards in valuations and workings of the valuers. This order, as notified by MCA, highlighted;

And, whereas, although the said section provides for valuation to be made 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, there is a need to provide clarity and remove the difficulty of having no reference to an organisation to which the valuer may belong...¹⁹

Thus, this order amended the definition of RV specified under section 247 of the Companies Act and bestowed identity to various valuation organisation and recognised their existence.²⁰

The first RVO, namely, RVO Estate Manager and Appraisers Foundations, was registered in 2018. At present, there are more than 4300 RVs and 16 RVOs registered with IBBI. RVs are permitted to form an entity i.e., Registered Valuer Entity (RVE) (Partnership / Company) for rendering valuation services. There are currently 43 RVEs registered as RVs as of June 30, 2021.²¹

As per Valuation Rules, societies and trusts were also allowed to be registered as RVOs, however, for societies and trusts to be registered as RVOs, it was mandatory for them to be converted into or register themselves as a company under section 8 of the Companies Act²² within one year of the date of commencement of valuation rules.

VALUATION AND THE CODE

Valuation plays a critical role in the corporate insolvency resolution process under the Insolvency and Bankruptcy Code, 2016 (Code). Throughout the entire corporate insolvency resolution process (CIRP), the practical and strategic implications of valuation play key roles. Each player in the process makes decisions based on the value of the corporate debtor (CD) and its assets. Some of the most important areas in which valuation plays an important role during insolvency resolution process are adequate protection of value of the CD; determination of claims; call for resolution plans by resolution applicants, approval of resolution plan by committee of creditors (CoC) and realisations by creditors. Role of valuation ranges from asset collateral valuation matters, to disputes as to the value of the CD as a whole, to fairness and equity issues related to the valuation of securities and distribution of proceeds to settle the claims of various stakeholders.

Framework established under the Code

Transparent and credible value of the assets of a CD is an important parameter for commercial decisions in a CIRP. It determines the entitlement of some stakeholders under the resolution plan. The Code read with regulations assign the task of such valuation to RVs.

The Valuation Rules provide a comprehensive unified framework for development and regulation of the profession of valuers, though its remit is limited to valuations required under the Code and the Companies Act. This framework, however, does not affect the conduct of valuations under any law other than the Companies Act and the Code. With effect from February 01, 2019, only a RV will be appointed by an IP to conduct any valuation under the Code or any of the regulations made thereunder.

The approach followed for regulation and development of the valuation profession is quite distinct as compared to other professions in the country. Only fit and proper persons are eligible for registration as RVs, given the responsibilities they discharge. For determining if a person is fit and proper, the IBBI considers various aspects, including (i) integrity, reputation and character, (ii) absence of convictions and restraint orders, and (iii) competence and financial solvency.

The Valuation Rules broadly follow the model of insolvency profession for regulation of RVs. Valuers are subject to a two-tier, regulated self-regulation where they are enrolled with an RVO as a member, and thereafter registered with the IBBI as a valuer. This combines the benefits of statutory regulation and self-regulation and promotes competition among the RVOs. Similar to the role played by IPAs for IPs, Registered Valuer Organisations act as frontline regulators for RVs.

They provide an institutional arrangement for the oversight, development, and regulation of RVs. They grant membership to valuers who comply with the eligibility norms provided in the Valuation Rules, conduct educational courses in valuation and provide training for the individual members before a CoP is issued. They also lay down standards of professional conduct and monitor their members for adherence to standards. They may take appropriate action to ensure that compliance with the Valuation Rules is strictly adhered to by their members.

The Valuation Rules envisage a competitive industry of RVOs, where they compete with one another to provide better valuation services through their professional members, in the interest of the users, and other stakeholders of valuation services. These also envisage that a member may shift membership from one RVO to another, subject to prior permission of the Authority for the same. The Valuation Rules require an RVO to employ fair, reasonable, just and non-discriminatory practices for enrolment and regulation of its members. It was, however, observed that a few RVOs were restricting transfer of membership by using dilatory tactics, charging unreasonable transfer fee, etc.

Role of Valuers under the Code

As opposed to other professions in India like Chartered Accountants, Company Secretaries, Cost Accountants, Advocates and medical professionals, there is no legislation as such which provides for the development and regulation of the profession of valuers exclusively. Over time, several laws or subordinate legislation framed thereunder recognised and demanded valuation services provided by valuers. For example, under the SARFAESI Act, 2002 in case of sale of immovable assets, before effecting the sale of immovable property, the authorised officer is required to obtain valuation of the property from an approved valuer, the latter being a person registered as a valuer under section 34AB of the Wealth Tax Act, 1957 and approved by the Board of Directors or Board of Trustees of the secured creditor. Similarly, the Foreign Exchange Management (Transfer of Issue of Security by a Person Resident Outside India) Regulations, 2017 provides for the valuation of capital instruments. Further, under Schedule 6 of these Regulations, the investment in a Limited Liability Partnership either through capital contribution or acquisition/ transfer of profit shares, cannot be less than fair price worked out as per any valuation norm which is internationally accepted/adopted as per market practice. There are other statutes such as the Banking Regulations Act, 1949; Income Tax Act, 1961 etc. that also have provisions that require valuations to be done for various purposes.

The role of a valuer under the Code transcends across different processes. For instance, in case of voluntary liquidation of corporate persons the declaration from the majority of the directors of the company regarding its solvency is required to be accompanied by a report of the valuation of the assets of the company, if any, prepared by a RV. Further, while considering an application for avoiding a transaction as undervalue, the Adjudicating Authority may require an independent expert to assess the evidence relating to the value of the transaction. Additionally, regulations framed under the Insolvency and Bankruptcy Code, 2016 also provide for RVs for various services such as determination of fair value and liquidation value at the stage of CIRP of a CD and during Fast

Track Insolvency Resolution Process for corporate persons and valuation of assets intended to be sold during the liquidation process.

The valuation profession under the Companies Act, 2013 and the IBC, in its present form is a regulated profession. This is a good start for creating a credible base of valuers for purposes of these two legislations. The RVs are bound by the Valuation Rules and Code of Conduct contained therein. They are answerable for their actions and misconduct, if any. On the other, valuers operating under other legislations, as discussed above, are not bound by a regulatory framework and are thus not accountable for their actions in case of misconduct. Thus, the current framework under Companies Act, 2013 and the IBC has laid the foundation of institutionalising the profession of valuers. The concept of two-tier regulation, RVOs being frontline regulator and IBBI being the principal regulator, has set the tone for designing a common regulatory framework for all valuers.

WAY FORWARD

There are a large number of individuals and entities practising the valuation profession. At present, there are more than 4300 valuers and 16 RVOs, registered with IBBI under the Valuation Rules. There are also valuers who have registered themselves with other agencies. The market size of this profession is large and the case for an integrated comprehensive institutional framework to regulate the same is thus strong.

To take this profession to the next level and to lay down a roadmap for the future of the profession in India, the Government had constituted a Committee of Experts (CoE) to examine the need for an institutional framework for regulation and development of valuation professionals. The CoE during its deliberations took note of attempts made in the past to provide an institutional framework for the valuation profession, particularly the draft Valuation Professionals Bill, 2008. It studied the progress in implementation and experience with the implementation of the Valuation Rules. It perused the institutional framework for other professions in the country and of the valuation profession in other jurisdictions. It also considered the contemporary thought on regulatory architecture and design and had extensive consultation with stakeholders.

The CoE in its report has, *inter alia*, recommended an institutional framework for valuation profession that envisages an exclusive statute to provide for the establishment of the National Institute of Valuers 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, with a view to ensure that valuers enjoy an enviable reputation of the stakeholders, while being accountable for their services. The CoE has proposed an institutional framework that is least disruptive and builds on the existing resources to ensure that the transition to a new framework is seamless. It has indicated the three objectives that institutional framework should strive for namely, (i) development and regulation of the valuation profession; (ii) development and regulation of market for valuation services; and (iii) protection of interest of the users of valuation services.

The CoE has designed an ecosystem having four elements: (i) National Institute of Valuers, which would be a statutory body primarily responsible for the development and the regulation of the valuation profession in India and registration and regulation of Valuers, Valuer Institutes and VPOs; (ii) Valuers, who would render valuation services, after registration with the Institute; (iii) Valuer Institutes, who would provide educational courses, after registration with the Institute; and (iv) valuation professional organisations (VPOs), who would be front-line regulators primarily responsible for development of the valuation profession, after registration with the Institute. To bring the proposed institutional framework into effect, a statute would need to be enacted that would lay down the basic structure of the institutional framework.

At present, in the absence of any statutory mandate and local valuation standard issued by any regulatory authority, the valuers generally have been following the International Valuation Standards (IVS) General Standards with or without minor modifications or the RICS Red Book. However, despite the existence of these Standards there is considerable variation in how local standards engage and comply with the accepted principles laid out in the IVS. Recognising the need to have consistent, uniform and transparent valuation policies and harmonise the diverse practices in use in India, uniform valuation standards having international recognition are required. Simultaneously, the valuation standards should be consistent with the Indian institutional framework for valuation profession.

Given the importance of valuation across sectors and different statutes, it is time to bring the valuation profession under a single umbrella framework and valuation standards. This is essential to ensure uniformity and consistency in valuations done by valuers, thereby imparting legitimacy to the valuation profession. Further, continuous professional development of valuers will play a key role in keeping the profession relevant and up-to-date. At the same time the valuers will have to abide by a common code of conduct that lends utmost integrity and professionalism to the profession.

Any attempt to regulate a set of economic agents in a free-market economy set-up is often opposed by many, especially those who will be brought under the umbrella of regulation. A divide is created between those who support the idea of a regulatory regime and those who oppose it. This is the organic process of ushering in a change in an established system. It would not be wrong to say that almost all professions, be it Chartered Accountants, Company Secretary, Cost Accountants etc., have benefitted from a regulatory framework, lending the professions credibility, competence and a space among global professionals. To provide the same legitimacy to the valuation profession, an integrated institutional framework for the valuation profession is the need of the hour.

NOTES

¹ Acemoglu D. et al. (2005), Institutions as a Fundamental Cause of Long-Run Growth, Chapter 6, *Handbook of Economic Growth*, Vol 1A.

² Rodrik D et al. (2004), “Institutions Rule: The Primacy of Institutions Over Geography and Integration in Economic Development”, *Journal of Economic Growth*, Vol 9(2), pp. 131-165.

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³ Rodrik D. and Subramanian A. (2003), “The Primacy of Institutions (and What this Does and Does Not Mean)”, IMF Publications.

⁴ Jauhari A. and Sharma M. (2020), “Institutionalising Valuation Profession in India”, *Insolvency and Bankruptcy Regime in India: A Narrative*, IBBI Annual Publication.

⁵ Report of the Committee of Experts to Examine the Need for An Institutional Framework for Regulation and Development of Valuation Professionals, April 2020, Vol 1, Ministry of Corporate Affairs.

⁶ *Ibid.*

⁷ Valuation: Professionals’ Insight, July 2018, Valuation Standards Board, ICAI.

⁸ Supra Note 5

⁹ Pfarrer M. and Smith K. (2015), “Creative Destruction”, *Wiley Encyclopaedia of Management*.

¹⁰ Supra Note 4

¹¹ Talbot N. (2018), “It’s time to get serious about valuation”, *The Hindu BusinessLine*, 18 July.

¹² Supra Note 5.

¹³ Navrang S. (2019), “Need for Uniform Valuation Standards”, *A Miscellany of Perspectives*, IBBI Annual Publication, p. 172.

¹⁴ Section 218 of the Companies Bill 2008 makes it mandatory for the valuers to be registered under Chapter XVII of this Bill in order to conduct valuation of any property, stocks, shares, debentures, securities or goodwill or net worth of a company or its assets.

¹⁵ *Ibid.*

¹⁶ 21st Report of the Standing Committee of Finance on the Companies Bill, 2009, August, 2010.

¹⁷ Section 247 of the Companies Act, 2013 as notified on October 18, 2017.

¹⁸ Supra Note 4

¹⁹ The Companies (Removal of Difficulties) Second Order, 2017, MCA, October 23, 2017.

²⁰ The Companies (Removal of Difficulties) Second Order, 2017 substituted section 247 (1) of Companies Act, 2013 with ‘a person having such qualifications and experience, registered as a valuer and being a member of an organization recognized, in such manner, on such terms and conditions as may be prescribed’.

²¹ IBBI Quarterly Newsletter, April-June, 2021.

²² Rule 12(3) of the Companies (Registered Valuers & Valuation) Rules, 2017.