

Time to institutionalise valuation profession

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The market usually discovers the price of an asset, reflecting its worth. However, it is often neither feasible nor desirable to conduct a market test for every asset. In such cases, the worth of an asset needs to be estimated with reliable accuracy. The person who estimates the worth is a 'valuer'; the process of estimation is 'valuation', and the worth so estimated is 'value'.

If the value of an asset is what the price ought to be in the given context, the valuation is perfect. Similarly, the price of an asset is authentic if it converges with the valuation. Value and price compete to reflect the true worth of an asset.

Inventing the right worth

An economy requires valuations of assets to facilitate a variety of transactions. A corporate insolvency proceeding envisages estimation of 'fair value' and 'liquidation value' of the assets. These values serve as reference for evaluation of choices, including liquidation, and selection of the choice that decides the fate of the corporate and its stakeholders.

A wrong valuation may liquidate a viable company or rescue an unviable one. A banker determines the amount of loan that can be sanctioned against security or guarantee. It may not have adequate protection, where it sanctions a loan against the security of an asset/guarantee of a guarantor whose worth is overestimated.

A company issues shares on preferential basis based on valuation. An erroneous valuation may result in one set of shareholders getting shares either too cheap or too expensive. Government divests its stake in public sector units based on valuation of the enterprise. An inaccurate valuation may either fail the divestment or rip off the exchequer. Decisions based on sub-optimal valuations, in addition to causing unfair gain/loss to parties, have the potential to distort market and misallocate resources which may impinge upon economic growth.

The valuation profession

Given its growing importance, the valuation profession has emerged as a key institution. This profession has a long history in India. It acquired considerable recognition in the late 20th century in sync with its progressive evolution after Independence. Different statutes — banking, securities, tax, company, insolvency — require valuation for a variety of purposes.

Each statute, in isolation, focusses on what needs to be valued, who can render valuation services and the manner of such valuation. Though the users often demanded quality, they did not focus on building capacity for valuation services. Several self-regulating organisations came up to build the expertise of their members to meet the immediate needs of specific classes of users and to promote members' interests. Different statutes thus created separate islands to meet their immediate needs but failed to engender holistic development of the profession.

An estimated 50,000 individuals practise this profession today. They do not enjoy the same respect as members of professions like medical science or chartered accountancy. The users of valuation services do not have either the assurance of quality services or an effective remedy for deficiency of service. For want of valuation standards (akin to accounting standards), a valuer finds it difficult to defend his valuation, while the market may doubt the ability of the valuer and the integrity of the valuation process. There is no agency to address market failure in this area.

The institutional arrangement for any profession is a statutory body with twin responsibility of development and regulation of the profession. There have been several attempts in the past to provide such an arrangement for valuation profession. Based on recommendations of expert groups, Bills had been introduced in Parliament to strengthen the profession as part of the company law.

The Government even drafted an exclusive legislation (Valuation Professionals Bill, 2008) to provide for a two-tier statutory self-regulation with the Council of Valuation Professionals as the principal regulator and 'recognised institutes' as the frontline regulators.

These attempts, however, did not culminate in any tangible results for various reasons. The Companies Act, 2013, for the first time, provided for valuations under the company law from a registered valuer (RV). This provision, however, could not be operationalised for want of an institutional arrangement for the profession.

IBC and valuation

The Insolvency and Bankruptcy Code entitles certain stakeholders in term of liquidation value.

It envisages certain decisions with reference to fair value and liquidation value. With the operationalisation of the Code in late 2016, the need for an institutional arrangement became acute.

The Government amended the company law by a Removal of Difficulties Order in October 2017 to provide an interim institutional framework comprising the Authority and Registered Valuers Organisations (RVOs). To operationalise this provision, it notified the Companies (Registered Valuers and Valuation) Rules, 2017 (Rules) and designated the IBBI as the Authority.

An individual who has (a) prescribed qualification and experience; (b) is enrolled with an RVO; (c) completed the specified educational course, and (d) passed the examination of the relevant asset class is eligible for registration as an RV.

Currently, there are 16 RVOs with 4,500 RVs registered under the Rules across three asset classes. The remit of the Rules is limited to valuations required under the Code and the company law. However, considering the inherent benefits, government departments, regulators and banks are preferring to use the services of RVs.

A market economy needs a well-functioning institutional framework.

Hence the focus of the institutionalists in 'getting the institutions right'.

A Committee of Experts recently recommended an exclusive statute to provide for the establishment of the National Institute of Valuers to protect the interests of users of valuation services and to promote the development of, and to regulate the profession of valuers and market for valuation services.

Another government committee has recommended the asset class-specific valuation standards to be adopted by valuers. Implementation of these initiatives should put the valuation profession on an institutional pedestal and on a par with other professions, ensuring that valuers enjoy an enviable reputation, while being accountable for the services they render.

This would minimise concerns in valuations at times attributed to the profession, for the overall benefit of the economy.

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