2021

Findings of the Peer Review of the Valuation Reports

Based on Workshop on Peer Review of Valuation Reports conducted on 17th February, 2021.

Preamble

A peer review workshop was organised by ICAI Registered Valuers Organisation in association with Insolvency and Bankruptcy Board of India (IBBI) to share findings of Peer Review of Valuation Report for the three Asset Classes, i.e., Securities or Financial Assets, Land & Building and Plant and Machinery as per Companies (Registered Valuers and Valuation) Rules, 2017. The workshop was held through video conferencing on 17th February, 2021.

A similar Workshop was organised by ICAI RVO in association with IBBI on 14th February, 2020 and the outcome of which was published on the website of IBBI and RVOs.

The workshop was addressed by Dr. Navrang Saini Whole Time Member, IBBI, Mr. Ashok Haldia, Independent Director ICAI RVO and Mr. Debajyoti Ray Chaudhuri, Chief General Manager, IBBI. CA. Ms Sarika Singhal of ICAI RVO moderated the proceedings.

MD/CEOs of thirteen RVOs participated in the workshop and 9 RVOs made presentations on key findings emerging out of the peer review undertaken by them. Others did not have RVs for the period under review.

The peer review also examined compliance with the Guidelines on Use of Caveats, Limitations and Disclaimers by the Registered Valuers in Valuation Reports and it was noted that most Registered Valuers have welcomed the guidelines, however, its implementation needs to be monitored closely.

In general, the RVOs were of the opinion that quality of valuation reports had improved compared to the previous year and most of the shortcomings observed in the previous year's peer review were not observed in the current peer review.

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Summary of findings during the peer review of valuation reports are provided below:

1. Significant improvement from previous year's peer review, however there is scope for further improvement.

2. Scope of work was vague and relevant details were not incorporated (This was there in previous year's peer review as well).

3. Appointing Authority was not stated.

4. Report stated that the valuer takes no responsibility for the data presented in the report.

5. Adherence/Compliance with valuation standards used was not specifically stated in the Report.

6. Absence of supporting evidence and analysis (This was there in previous year's peer review as well).

7. General lack of understanding of concepts and definitions.

8. Structure and formatting of the report was not as per Rule 8(3) of the Companies (Registered Valuers & Valuation) Rules, 2017.

9. Valuation Report only mentions 'The fee for the engagement is not contingent upon the results reported.' It does not specifically cover independence or conflict of interest covered in the Engagement Letter.

10. Important definitions were not there in the report.

11. Date of appointment was not mentioned in the Valuation Report. Valuation Date was also not mentioned in the Valuation Report.

12. While the nature and sources of the information used or relied upon was stated in the Valuation Report, the financial projections were not included in the sources of information.

13. Limitations in the form of non-availability of projections were addressed by ignoring the income approach for valuation. Some more justification for the same should have been incorporated.

14. Limiting Conditions that directly affect the Valuation were not clearly stated.

15. Valuation Approach- Management Certified Projections were used by the Valuers. It is advisable to provide information on:

    - procedures performed by the valuer especially with respect to projections provided by management;
    - reason for not considering certain methodologies;
    - current state of operations of the Company; and
    - financials as at the valuation date.

16. Valuers have considered full year cash flows for FY 2019-20 while the valuation date is in February e.g. 15th February, 2020.

17. Valuers have not mentioned COP number.

18. The purpose of valuation was not clearly stated.

19. Valuers have not clearly stated the face value of the instrument which was being valued.

20. Full disclosure of valuer's interest or conflict, if any, was not provided.

21. Nature and sources of information were not properly stated at one place.

22. Conclusion was not under a separate heading.

23. Assumptions and limitations were not justified and pertinent to the valuation in hand.

24. Significant uncertainty was not put under separate heading.

25. The extent of investigation undertaken including the limitation on that investigation set out in the scope of work were not disclosed.

26. Due diligence done, if any, was not separately described and discussed in detail.

27. The Premise, Assumptions were not stated under separate headings.

28. Executive Summary was not there in some reports.

29. There were number of typographical errors in the report.

30. Intended user of the Report was not stated.

31. Valuers did not state the reasoning for adoption of a particular valuation approach(es) in the valuation report.

32. While using DCF method, a disclaimer clarifying whether projections used were solely provided by Management or were rationalized subsequently with reasons thereof was not there.

33. Reasons to justify extent of Liquidation Discount applied were not recorded.

34. Some RPs insist on recording Realisable value instead of Liquidation Value.

35. The letters of engagement issued by IPs were not comprehensive.

36. Declaration on restriction on use, distribution and publication of report was not there.

37. Appropriate and suitable methodology was not used for valuation of lease hold property.

38. Any material uncertainty in relation to valuation was not commented upon.

39. While reviewing Plant & Machinery Valuation Reports certain deficiencies were observed such as:

- erroneous report headings;
- details of investigations conducted not provided; and
- technical specifications of some machines not provided.

40. While reviewing Land & Building Valuation Reports certain deficiencies were observed such as:

- lack of evidence for market survey of prices; and
- non-authentication of physical measurements.

41. While reviewing Securities and Financial Valuation Reports certain deficiencies were observed such as:

- due weightage not given to COVID-19 crisis;
- steady growth of business presumed during pandemic;
- non-inclusion of intangible related to IT enabled services;
- the method of valuing subsidiaries was not provided; and
- adoption of tangible asset valuation from the books of accounts.

42. Other Issues:

- Appointment of Single Valuer (representing one class of asset) as an umbrella valuation engagement involving valuations under other classes of asset.
- Fair Value of Financial Assets (ICDs, Receivables etc.) of companies under Insolvency/ resolution plan.
- Liquidation Value – sometimes misused for lower bids under bankruptcy/ insolvency auctions.
- Importance of rationale in valuer's report

Recommendations/Suggestions:

1. Valuation report stated that since the projections were price sensitive information, the income approach has not been used. The confidentiality agreement entered by the company with the valuer should not deter the valuer from using financial projections. If it is still not possible, valuer should provide a cogent rationale for not using the projections.

2. The justification for using a discount rate should be provided.

3. Explicit declaration regarding compliance with the Valuation Standards (VS) followed in valuation is required to be stated.

4. COP Number should be stated in the report.

5. Identity of the Valuer with his/her registration number along with identity of other experts involved in the valuation should be provided.

6. While mentioning the purpose of valuation, Valuers should reproduce the sections and related provisions.

7. The Valuer must state the extent of examination and verification made in respect of the information on which his valuation is based. In case any public data is used, the source must be clearly stated with the extent of examination performed by the valuer.

8. Under NAV method, valuers must mention the details of Tangible Assets, Non-Current Assets, Current Assets and Liabilities rather than classifying them under broad heads. This will enable the user to understand the nature of assets or liabilities.

9. An executive summary to understand the valuation report shall be provided, it shall include the methodology used, the value, which is arrived, important dates, valuation standard followed and purpose of valuation etc.

10. The fees structure for the reviewer should be provided like in some other professions.

Compliance with the guidelines issued by IBBI on Caveats, Limitations and Disclaimers (CLD) by the Registered Valuers in Valuation Reports:

1. Caveats, Limitations and Disclaimers were not properly stated.

2. Valuer members now have better understanding that these provide protection to RVs coupled with responsibilities.

3. RVs welcomed the Guidelines issued by IBBI, however, actual implementation was lacking.

4. In some reports, a small list of assumptions was given while no caveats, limitations and disclaimers were given.

5. Only a few Caveats, limitations and disclaimers were captured.

6. In some of the reports, deviation from the Guidelines on Caveats, limitations and disclaimers were observed.

7. Some of the deviations from the Guidelines were that valuer did not state the 'Basis/ Bases of Value' in the Valuation Report, Industry Analysis and Comparison with similar transactions were not done, review of title deeds and assumptions made for internal condition were not specifically stated, no comments were made on the adequacy of information in the report etc.

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Findings of the Peer Review Workshop
(14th February 2020)

PEER REVIEW WORKSHOP

A peer review workshop was conducted by IBBI in association with ICAI RVO. MD/CEOs of eleven RVOs participated and made presentations on key findings emerging out of the peer review undertaken by them. Summary of findings during the peer review of valuation reports are provided below:

GENERAL OBSERVATIONS

1. Scope of work being vague and requisite details were found missing.
2. Insufficient explanation of supporting evidence.
3. An explanation on methodology applied to arrive at specific valuation was not provided.
4. Errors in numerical calculations and mismatch in logical sequencing.
5. Inconsistencies and contradictionswere observed in various parts of the same report.
6. Assumptionswere not clearly articulated.
7. Important sources for land ownership werenot indicated.
8. In some cases, though purpose of valuation was mentioned, however, name of appointing authority was not mentioned.
9. Some references to important dates were missing.
10. There were no mention of caveats, limitations and disclaimers in the valuation report.
11. The major factors that were taken into account during the valuation not fully indicated.
12. Conclusion was not provided.
13. No mention of restrictions on use of the report, if any.
14. Notes to the report are identical across all asset categories.
15. Figures were computed based on provisional balance sheets.
16. The reports do not confirm having ‘Considered’ all three generic approaches to value and do not cite reasons for ‘selection’ of any particular method or for ‘disregarding’ any approach.
17. Valuation Reports do not make reference to outstanding liabilities.

DISCLAIMERS AND DISCLOSURES

1. No standardization in the disclosures observed.
2. Past history of the company should be disclosed in the report to substantiate the professional judgement, especially when the Company is listed and/or is a Multinational Company.
3. In case the company is a wholly Owned Subsidiary (WOS), Valuation Report should mention the layers of shareholding to substantiate the beneficial owner and at least minimum of one layer should be mandatorily mentioned as per Valuation Rules.
4. There should be a para of identity of valuer and other experts (if any) involved or assisted by.
5. Definition of "Fair Value" and "Liquidation Value" should be provided in the Report.
6. Since the corporate debtor is under CIRP, the report should considerLiquidation Value on ‘goingconcern’ basis.

7.Disclosure/disclaimer should not mention "Validity of Report is 3 years from the date of Report", as this provision is the requirement to maintain records for 3 years and not validity of Report or validity of valuation.
8.The valuer shall not disclaim liability for his/its expertise or deny his/its duty of care, except to the extent that the assumptions are based on statements of fact provided by the company or its auditors or consultants or information available in public domain and not generated by the valuer.
9.A statement explicitly restricting the end use of the report to intended user and for intended purpose only was missing in many valuation reports.
10. Statement or disclosure on conflict of interest needs to be specifically mentioned.

VALUATION STANDARDS

1.Most valuation reports lacked an explicit declaration regarding compliance with the specific Valuation Standards.
2. Among the RVOs only ICAI has prescribed valuation standards for the asset class Securities or Financial assets. Some reports do refer to this. However, other RVOs have prescribed International Valuation Standards mostly IVS. Many of the reports do not refer to the valuation standard so adopted.
3.Scope of work was not provided in detail in engagement letter or in the Valuation Report.
4.In a few cases, it was observed that basis of valuation was not as per valuation standards.

CONCLUSION

It was decided that the outcomes of theworkshop, where certain common mistakes/errors by the RVs were identified, must bedisseminated by way of hosting the same on the websites of respective RVOs. Further all the RVs must be sensitize about the common mistakes with a view to stop reoccurrence of such mistakes and thereby improving quality and standard of the valuation reports.

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