**Re : Representation for amending reference of “merchant banker” in Income-tax rules relating to valuation by adding “registered valuer” or “accountant” pursuant to SEBI’s decision to prohibit Merchant Bankers from valuation activities**

The Income-tax Rules 1961 provide for valuation of shares and other assets by Category I Merchant Banker regulated under SEBI Guidelines in various circumstances like ESOP perquisites, indirect transfer u/s. 9(1)(i), gift taxation u/s. 56(2)(x), etc. For this purpose, “merchant banker” is defined to mean Category I merchant banker registered with Securities and Exchange Board of India established under section 3 of the Securities and Exchange Board of India Act, 1992 (15 of 1992) (Refer, for instance, Rule 11U(c))

In this regard, we would like to bring to your kind attention that recently SEBI in its 208th Board Meeting held on 18 December 2024 has approved amendments to SEBI (Merchant Bankers) Regulations, 1992. As per SEBI’s Press Release No. 36/2024, following are the main features of the amendments as relevant to valuation activity by merchant bankers :-

*“3.1 Merchant Bankers, other than Banks, Public Financial Institution and their subsidiaries, shall undertake only permitted activities. MBs may carry out other regulated activities as a separate business unit after obtaining registration/ confirmation from the respective regulatory authority.*

*3.1.1 Permitted activities which come under the purview of SEBI have been specified.*

*3.1.2 Activities other than permitted activities by MB shall be hived off to a separate legal entity with a separate brand name, within a period of two years. MBs which have to hive off activities and the hived off entity, shall abide by such code of conduct as may be specified by SEBI from time to time.*

*3.1.3 The separate entity may be allowed to carry out activities other than the permitted activities by sharing the resources with the MB on an arm’s length basis without casting any legal liability in respect of the same, on the MB.*

***3.2 MBs shall not undertake fresh valuation activities as part of its MB Registration. However, existing valuation assignments taken up by MBs may be completed. If an MB wishes to take up valuation activities, it shall obtain registration from the concerned regulator or authority, within a period of nine months****.”*

The above referred amendments may be notified any time soon by SEBI. Upon such amendment becoming effective, Merchant Bankers will need to cease undertaking any fresh valuation assignments. Any new valuation assignment will need to be undertaken by obtaining registration from concerned regulator or authority, within a period of nine months. Such concerned regulatory authority could be Insolvency and Bankruptcy Board of India (IBBI), Institute of Chartered Accountants of India (ICAI), etc

This development has immediate and significant impact on income tax compliances concerning valuation by Category I Merchant Banker under various Income-tax rules. This is because for all new valuation assignments accepted after the effective date of amendment, the valuation will not be in the capacity as Category I Merchant Banker and therefore, there could be litigation on whether it is valid for income tax purposes.

Since this amendment has immediate and significant impact for taxpayers in general in relation to compliances involving valuation by Category I Merchant Banker , we request for an immediate amendment to the Income-tax Rules which refer to valuation by “merchant banker” by adding an appropriate category of valuers who can carry out such valuations. A list of such rules is annexed herewith as **Annexure A** for your ready reference.

We suggest that the reference to “merchant banker” may be amended to add registered valuer referred in section 247 of the Companies Act, 2013 (18 of 2013) or an accountant (wherever accountant is not already covered therein). The recommendation to add instead of substituting “merchant banker” with registered valuer is in view of transitional period post notification of SEBI amendment where existing valuation assignments can be executed by merchant bankers.

The reason for recommending registered valuer referred in s.247 of Cos Act 2013 is that the said section read with Companies (Registered Valuers and Valuation) Rules, 2017 provides for a comprehensive regulatory framework for recognition of registered valuers organisations, eligibility & qualifications of the valuers, registration of the valuer with IBBI, valuation standards, model code of conduct, penalty and punishment for violations, etc which regulates the professional practice of valuation. Such is also the basis for SEBI’s decision to discontinue valuation activity by merchant bankers in their capacity as merchant bankers. SEBI has also prescribed valuation by registered valuers u/s. 247 of Cos Act 2013 only under various SEBI Regulations such as SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 (“ICDR, 2018), SEBI (Delisting of Equity Shares) Regulations, 2021, SEBI (Buy-back of Securities) Regulations, 2018 (Refer, para 9 of SEBI’s Consultation Paper dated 28 August 2024)

Needless to say, immediate action of CBDT by amending the relevant rules will clear any ambiguity, lead to certainty & better compliance by taxpayers and avoid any unwarranted litigation on valuation aspect.

**Annexure A**

**List of Income-tax rules which refer to valuation by merchant banker**

| **Rule** | **Context** | **Eligible valuer** |
| --- | --- | --- |
| ***Valuation by merchant banker or accountant*** | | |
| **Gift taxation u/s. 56(2)(x) and 50CA** | | |
| Rule 11UA | Value of unquoted shares and securities (other than equity shares) for S.56(2)(x) and 50CA | Open market value determined by ***merchant banker*** or accountant |
| **Indirect transfer u/s. 9(1)(i)** | | |
| Rule 11UB(3) | Value of unlisted shares of Indian company held by foreign entity deriving substantial value from assets situated in India | FMV determined by ***merchant banker*** or accountant |
| Rule 11UB(4) | Value of interest in partnership firm or AOP held by foreign entity deriving substantial value from assets situated in India | FMV determined by ***merchant banker*** or accountant |
| Rule 11UB(5) | Value of any other asset held by foreign entity deriving substantial value from assets situated in India | Open market value determined by ***merchant banker*** or accountant |
| Rule 11UB(6)(i) | Share of or interest in foreign entity where transfer is between non-connected persons- Market capitalisation based on the full value of consideration for transfer+ liabilities | Book value of liabilities as certified by ***merchant banker*** or accountant |
| Rule 11UB(6)(ii)(b) | Share of or interest in foreign entity where transfer is between connected persons and shares of such foreign entity are not listed on recognised stock exchange | FMV of shares/interest in foreign entity and liabilities considered in FMV is determined by ***merchant banker*** or accountant |
| **Exit tax for charity** | | |
| Rule 17CB- Exit taxation for charitable entities registered S.12AA, 10(23C), S.12AB | Value of any other share or securities (other than equity shares) by specified charitable institution u/s. 115TD | Open market value determined by ***merchant banker*** and accountant |
| ***Valuation by merchant banker*** | | |
| **ESOP perquisite taxation** | | |
| Rule 3(8) | Value of unlisted shares issued under ESOP scheme | FMV to be determined by ***merchant banker*** only |
| **“Angel tax” u/s. 56(2)(viib) applicable upto 31 March 2024** | | |
| Rule 11UA(2) | Value of unquoted equity/preference shares for determining excess premium | FMV to be determined by ***merchant banker*** only under Discounted Free Cash Flow or other methods |
| **Buyback distribution tax for buybacks till 30 September 2024** | | |
| Rule 40BB(8) | Determining amount received for shares bought back where shares are allotted as part consideration for acquisition of any asset or settlement of any liability, amount received shall be determined based on the formulary approach- (value of assets or liabilities/ number of shares) | While determining amount received- FMV of assets and liabilities to be determined by ***merchant banker*** only |