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**IMPORTANT REGULATORY UPDATE ON VALUATIONS FOR ISSUE OF SHARES**

Vide its Notification No. 23/2018/F.No.370142/5/2018-TPL dated 24th May, 2018 the Central Board of Direct Taxes (CBDT) (Income Tax Department) has barred all chartered accountants (CA) from valuing equity shares wherein fresh issue of such shares in a closely held company is taking place. With this change, now only the Merchant Bankers (registered with Securities and Exchange Board of India - SEBI) are authorised to determine the fair market value of unquoted equity shares for fresh issue of such shares in order to determine the gift tax liability, if any in the hands of such company.

**Prefatory Note:** Under the Income Tax Act, 1961, there are provisions relating to taxability of issue of unquoted shares wherein if the shares have been issued (allotted) at below their fair market value, the difference amount between the fair market value of such shares and the price at which they have been issued is taxable in the hands of the company which issues such shares as income from other sources. Section 56(2)(viib) deals with this provision and the valuation formula and conditions have been explained in Rule 11UA(2) of the Income Tax Rules, 1962. The value so obtained becomes the maximum price for issue of such shares under the Income Tax provisions.

The valuation methodology for the same has been unchanged as per the Discounted Cash Flow (DCF) method or adjusted Book Value method or value as may be substantiated by the company to the satisfaction of the AO based on the value of its assets including intangible assets.

**Changes made:** Now only the Merchant Bankers are authorised under the Income Tax Law for valuation of issue of equity shares under section 56(2)(viib) of the Income Tax Act, 1961 read with Rule 11UA(2) of the Income Tax Rules, 1962. This is in line with the valuation requirements for exercise of specified security (equity shares) or sweat common stock (ESOP) under section 17(2)(vi) of the Income Tax Act, 1961 read with Rule 3 of the Income Tax Rules, 1962 wherein only Merchant Banker are authorised to value such Shares/Options.

Another change in the provisions of section 56(2)(viib) of the Income Tax Act, 1961 is that like this section does not apply where consideration for issue of shares is received by a venture capital undertaking from a venture capital company or a venture capital fund, now vide CBDT Notification No. 24/2018/F.No.370142/5/2018-TPL(Pt) dated 24th May, 2018, similar exemption has been extended to the Angel funds as well provided that the consideration has been received for issue of shares from an investor in accordance with the approval granted by the Inter-Ministerial Board of Certification under clause (i) of sub-para (3) of para 4 of the notification number G.S.R. 364(E), dated 11th April, 2018 issued by the Department of Industrial Policy and Promotion. It is clarified that this notification shall be deemed to have come into force retrospectively from the 11th April, 2018 itself.

*All companies and advisors are expected to take note of this change in Income Tax law to be compliant with the regulatory provisions.*