

# ***RBI amends pricing guidelines- Valuation of shares as per internationally accepted pricing methodology on arm's length basis***

14 July 2014

## ***In brief***

The Reserve Bank of India (RBI) has replaced existing pricing guidelines for valuation of equity instruments with internationally accepted pricing methodology for valuation on arm's length basis.

## ***In detail***

The existing pricing guidelines under Foreign Exchange Management (Transfer or Issue of Security) Regulations (FEMA 20) prescribe Discounted Cash Flow (DCF) / Return on Equity (ROE) valuation method for the purpose of issue/ transfer of unlisted shares to non-residents by an Indian company.

The RBI has now done away with these methods.

Henceforth, in following cases the issue/ transfer price of unlisted equity instrument shall be determined as per internationally accepted pricing methodology for valuation of shares on arm's length basis, duly certified by a Chartered Accountant or a Securities and Exchange Board of India Registered Merchant Banker:

- Issue under Foreign Direct Investment Route under Schedule 1 of FEMA 20

- Transfer of Unlisted Equity Shares (with call/ put option) under Foreign Direct Investment Route under Schedule 1 of FEMA 20
- Issue under Portfolio Investment Scheme for Private Placement under Schedule 2 of FEMA 20
- Issue under Foreign Portfolio Investment Scheme under Schedule 2A of FEMA 20

## ***The takeaways***

The RBI has withdrawn all existing guidelines relating to valuation in case of any acquisition/ sale of shares and accordingly, such transactions will henceforth be based on internationally accepted pricing methodology.

Separately, as per extant FEMA Regulations, transfer of unlisted equity instrument (without call/ put option) are required to follow the "prescribed RBI guidelines" which in turn refer to DCF method. This notification does

not prescribe any change in this regard. Hopefully, the RBI circular which would be issued in connection with this notification would clarify that even in this case, internationally accepted pricing methodology should be adopted.

*Source: Notification No. FEMA 306/ 2014 notified vide G.S.R No. 435(E) dated May 23, 2014*

## ***Let's talk***

For a deeper discussion of how this issue might affect your business, please contact:

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