



INCOME TAX ALERT

N. A. SHAH **BULLETIN**

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Final rules relating to valuation of unquoted equity share

1. The Finance Act, 2017 has introduced new clause (x) in section 56(2) of Income-tax Act, 1961 ('Act') against the existing clause (vii) & (viiia) of section 56(2) of the Act to widen the scope in relation to 'deemed income' on account of receipt of money/property either without consideration or for inadequate consideration by bringing all the assessee under the new clause.
2. Similarly, the Finance Act, 2017, also introduced a new section 50CA of the Act, a deeming provision for computing capital gain on sale of unquoted shares. As per this section, if the consideration received for transfer of unquoted share of a company, is less than the Fair Market Value ('FMV') of such share then the FMV shall be deemed to be the full value of consideration.
3. Both the above provisions are effective from 1st April, 2017.
4. For the existing provisions of section 56(2)(vii)/(viiia) of the Act, FMV of unquoted equity shares is computed as per Rule 11UA of Income Tax -Rules, 1962 ('Rules'). Under the existing provisions, if any immovable property or jewellery is received as underlying assets of unquoted equity shares of a company, the book value of such assets are considered for determining value of shares instead of on the basis of FMV of such underlying assets.
5. In view of the above, the Central Board of Direct Taxes ('CBDT') has prescribed the method of valuation of unquoted equity shares for the purpose of Section 56(2)(x) and Section 50CA of the Act by issuing draft rules vide press release dated 5 May 2017. CBDT has now issued final valuation rules amending Rule 11UA and introducing new rule 11UAA vide notification dated 12 July 2017. The valuation method prescribed for the purpose of section 56(2)(x) & section 50CA of the Act is summarized as under:

The FMV of unquoted equity shares shall be the value, on the valuation date, of such unquoted equity shares as determined in the following manner, namely:—

FMV of unquoted equity shares = $(A+B+C+D - L) \times (PV)/(PE)$ where,

- A= book value of all the assets (other than jewellery, artistic work, shares, securities and immovable property) as reduced by,- (i) any amount of income-tax paid, if any, less the amount of income-tax refund claimed, if any, and (ii) any amount shown as asset including the unamortized amount of deferred expenditure which does not represent the value of any asset

- B = the price which the jewellery and artistic work would fetch if sold in the open market on the basis of the valuation report obtained from a registered valuer
 - C = FMV of shares and securities as determined in the manner provided in this rule
 - D = the value adopted or assessed or assessable by any authority of the Government for the purpose of payment of stamp duty in respect of the immovable property.
 - L= book value of liabilities, but not including the following amounts, namely:—
 - (i) the paid-up capital in respect of equity shares;
 - (ii) the amount set apart for payment of dividends on preference shares and equity shares where such dividends have not been declared before date of transfer at a general meeting of the company;
 - (iii) reserves and surplus, by whatever name called, even if the resulting figure is negative, other than those set apart towards depreciation.
 - (iv) any amount representing provision for taxation, other than amount of income-tax paid, if any, less the amount of income-tax claimed as refund, if any, to the extent of the excess over the tax payable with reference to the book profits in accordance with the law applicable thereto.
 - (v) any amount representing provisions made for meeting liabilities, other than ascertained liabilities.
 - (vi) any amount representing contingent liabilities other than arrears of dividends payable in respect of cumulative preference shares
 - PE = total amount of paid up equity share capital as shown in the balance-sheet
 - PV= the paid up value of such equity shares
6. Further, CBDT has introduced new Rule 11UAA which provides that for the purpose of section 50CA, FMV of unquoted share shall be determined in the manner provided in Rule 11UA and valuation date should be taken as date of transfer of unquoted share.

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