Divya Jyoti Foundation
Registered Valuers Organisation

CHALLENGES FACED IN CIRP ASSIGNMENTS AND SOLUTIONS

As directed by authority (IBBI), we had requested our Registered Valuer Members to send us case studies in CIRP assignments. We have received a write-up about the challenges faced and solutions from our registered valuer members and the same is published for your reference.

Kind of valuations assignments encountered and success story behind the said assignments in SFA (Securities or Financial Assets)

1. Preferential allotment
2. IBC liquidation and going concern value

To say, getting valuation assignment in India is a challenge and with such competitive environment and in times of covid, successful competition of the valuation engagement is by itself a big challenge. We have tried to put up few challenges and how have we faced the same and possible solutions from our side.

CIRP assignments

Challenge 1 (Valuation of receivables)

While doing CIRP assignment, acknowledgment from the balances outstanding (in favor of the party appearing in the balance sheet) is difficult to receive!

Solution and suggestions

In general, at time of CIRP valuation, we value the asset side of the balance and try to estimate both liquidation and going concern value for said assets. Any company that is under CIRP, primary reason is that it is not receiving cash from its debtors and hence outstanding balance of that will always be the main line item under valuation. Question comes how do we value it as we cannot reply on the book value of the assets and mostly debtors will not reply to balance confirmations sent via email or post. Under such scenario comfort is drawn only on the basis of the accounting tool extracts but what we need to do here is go beyond the accounting tools and check in other substantive method like ageing, court cases, counter party
standing in creditors, management view (shared via IP), last year audit documents and certain open market search on existence of such debtors.

In case of any related party, one needs to notify the same in her / his valuation report also.

**Challenge 2**

Data received is ambiguous/ vague

*Solution and suggestions*

Under such circumstances and due to continuous learning, it is now learned that any data received from the concerned party should be first authenticated/ certified by IP and then needs to be evaluated further. It is also important to counter check the data from multiple sources, like audit balance sheet can be cross checked with ROC data, current year data provided can be cross checked with accounting data. If we don’t verify the data and start the engagement at times it has been seen that there is lot of duplication of work.

**Challenge 3**

Proper definition of liquidation value

*Solution and suggestions*

Until the time, we go in the live wire situation, speaking about Liquidation Value is just like a theoretical term which has been read in multiple times under IBC. But the actual value which comprises the various figures of individual line items of Assets collectively is difficult to be arrived at. Also making notions/perception on such can lead to mis-representation of facts and statements and may even impact the Valuation derived. Hence its very important to attend sessions on IBC and Valuations related to IBC.

**Challenge 4**

RV is unaware of the Corporate Debtor until the completion of the assignment and IP is also learning about the corporate debtor and noncooperation by corporate debtor

*Solution and suggestions*

Appointment of RV done via the IP and RV does not have any direct interaction with the management of company. Now biggest questions comes is that does IP
know about every possible thing about the balances of company that she/ he can provide adequate answer as our valuation is depended on the answers given by IP. Whatever knowledge he/she i.e. IP possesses is shared with the RV. In such cases, knowing about the in and outs of the CD becomes a challenge in itself. A continuous feedback from the RP and constant questions of the RV provides the better understanding about the business of the CD. Don’t feel shy to ask simplest of question also, as you never know it can win you a good assignment.

**Under other assignments**

**Challenge 1:**

**Calculation of Ke under CAPM**

\[ Ke = R_f + B \times (R_m - R_f) \]

All the factors in the formula are important and needs a through understanding of macro and micro economic factors about the company and industry in which it operates

**Calculation of BETA:**

While calculating beta of different sector/industry for a company, we do not find an appropriate guidance on from where to fetch the data regarding the same. The biggest challenge we face is should we use BETA as per Damodaran sir website or calculate ourself. Damodaran sir website data is also statis and not dynamic to date, so challenge comes what to do.

**Solution:**

With less guidance received on the same, sites quoting global betas are picked up for consideration, and further values are derived. Better is to choose few comparable companies and calculate the beta of those companies compared to the SENSEX and unlevered the same. Data for debt is easily available on sites like moneycontrol. Incase we are unable to find comparable company, we can pick the data of comparable industry and do the same to calculate the unlevered beta and use the same for calculation of levered beta basis debt equity ratio of the company under valuation.

**Calculation of market return (Rm):**

Confusion regarding calculation of market return; several opinions have been received on drawing conclusion for the same.

**Solution**
Under the guidance of merchant banker, who have been in this field for long much before IBC came into existence, has suggested to take market return on the basis of historical data of S&P 500 return taken on daily basis adding the dividend yield as on the date of valuation.

**Calculation of growth rate:**

What are the possible Growth rate assumptions? How do we determine that?

**Solution**

Growth rate is generally considered less that then current GDP if the country as its inferred that no company can grow more than the country in perpetuity, its advisable to check the industry trend of the comparable companies that how have to grown and basis that a assumption should be taken and not just a random number.

**Challenge 2:**

**Calculation of DLOM and DLOC:**

In respect to DLOM and DLOC, what reasons are there to use, what %age can be applied and in which scenario?

**Solution and suggestions**

I think we should talk more about this topic, how control premium needs to be calculated and how DLOC and DLOM needs to be calculated. RVO’s should organize more sessions on this topic as its completely a grey area and no one has a concrete answer to these questions.

**Challenge 3:**

**Quality of projections (specially for startups)**

We get assignments of 2 months old start up looking for valuation in crores and not having any control on the projections and current nos of the startup, biggest challenge comes how do we trust these entrepreneurs and how do we use these projections.

**Solution and suggestions**

Spend some time more with the founder and the finance guy of the company to understand the projections as that will help you to understand the fundament of the company better, also it will help you to understand the industry. Also, try and google the past history of the promoters and founders of the company. At the end of
the day, we have to relay on the data, but if we are finding it grossly misleading, we can always request the client to work on it freshly and resubmit.

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