Liberalisation of FDI Pricing Norms

The Reserve Bank of India ("RBI") has vide its circular dated July 15, 2014, liberalized the pricing guidelines to be followed by an unlisted company for issue and transfer of securities with and without optionality clause. In a nutshell, the pricing of securities is now required to be done as per any internationally accepted pricing methodology for valuation of shares on arm's length basis instead of discounted cash flow method.

The new pricing guidelines stipulated by RBI are as follows:

Issue of Securities: The price of securities issued to person resident outside India shall not be less than the fair value of securities arrived as per *any internationally accepted pricing methodology* for valuation of shares on *arm's length basis*, duly certified by a Chartered Accountant or a SEBI registered Merchant Banker.

Transfer of Securities from Resident to Non-Resident: In case of transfer of securities from Resident to Non-Resident, the transfer consideration shall not be less than fair value worked out as per *any internationally accepted pricing methodology* for valuation of shares on *arm's length basis* which should be duly certified by a Chartered Accountant or a SEBI registered Merchant Banker.

Transfer of Securities from Non-Resident to Resident: In case of transfer of securities from Non-Resident to Resident, the transfer consideration shall not be more than the minimum price at which transfer of shares can be made from a resident to non-resident. The same shall be required to be certified by a Chartered Accountant or a SEBI registered Merchant Banker.

Exit by Non-Resident with Optionality Clause: In case of transfer of shares with optionality clause by a non-resident, the transfer consideration shall not be more than fair value worked out as per *any internationally accepted pricing methodology* for valuation of shares on *arm's length basis* which should be duly certified by a Chartered Accountant or a SEBI registered Merchant Banker.

Other Compliances: The Indian investee company is also required to disclose the following in its balance sheet for the financial year in which the transaction for issuance or transfer of securities has taken place:

- valuation of share or convertible debentures,
- the pricing methodology adopted,
- the agency that has given/certified the valuation

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RBI has now notified its bold policy announcement of April 2014 vide its circular dated July 15, 2014 of liberalizing the pricing norms for foreign investment. RBI has made the pricing norms in line with the internationally accepted principle of valuation instead of specific formulae.

Now, the pricing for methodology would include Earning per Share (EPS), Price to Earnings (P/E), Return on Invested Capital (ROIC), Enterprise Value (EV), etc apart from existing Discounted Cash Flow (DCF) method. Further, the guiding principle set out in the circular prohibits guaranteed assured return by the Indian company to the foreign investor at the time of making investments.