



DEL ITAT: Rejection Of DCF Valuation Report Merely Due To Disclaimer Clause Is Untenable, Addition U/S 56(2)(VIIB) Deleted

Facts and Issues

The Assessee issued equity shares at a premium to various shareholders during the AY 2016-17. The equity shares were allotted to one of the shareholders at a significantly higher premium based on a valuation report prepared under the Discounted Cash Flow (DCF) method by a Chartered Accountant.

During assessment proceedings u/s 143(3), the Assessing Officer (AO) questioned the justification for the share premium and rejected the valuation report primarily on the ground that it contained a disclaimer stating that the valuation was based on management-provided projections and estimates, without independent verification. The AO further observed that the actual financial performance of the Assessee did not match the projections used in the DCF valuation.

Accordingly, the AO rejected the DCF valuation, adopted the Net Asset Value (NAV) method under Rule 11UA, and made an addition of Rs. 8.39 crore u/s 56(2)(viib) of the Act. The addition was upheld by the CIT(A).

Contentions of the Assessee before the ITAT

The Assessee contended that the shares were valued by an approved valuer using the DCF method, which is a recognized method under Rule 11UA. The valuer had appeared before the AO pursuant to summons u/s 131 and confirmed the valuation methodology and assumptions. Assessee contended that the disclaimer clauses relied by AO are a standard feature of valuation reports, as valuers rely on management projections and do not conduct in-depth verification or statutory audits. Assessee had also filed a valuation report issued by a merchant banker before the CIT(A), who had also endorsed the valuation report submitted by the Chartered Accountant.

Contentions of the Revenue before the ITAT

The Revenue contended that the valuation was entirely based on management projections without any scientific or verifiable basis. The disclaimer in the valuation report showed that the valuer did not vouch for the correctness or accuracy of the data. Also, the projected turnover was not achieved, thus, the DCF valuation was unreliable and the AO was justified in adopting the NAV method to determine fair market value of shares. Revenue relied on the decision of Delhi ITAT in the case of Agra Portfolio Private Limited v. ITO (ITA No. 2189 /Del/ 2018).

Observations and Ruling of the ITAT

The ITAT noted that the Assessee had obtained a valuation report from an approved valuer using the DCF method, which is expressly recognized under Rule 11UA. If the AO had any doubt regarding the valuation, then AO ought to have referred the matter to the Valuation Officer, which was not done in the instant case.

ITAT observed that the ITAT decision relied by AO has been reversed by the jurisdictional High Court which is reported in 464 ITR 348. Further, the issue was squarely covered by the Delhi High Court judgment in PCIT v. Cinestaan Entertainment Pvt. Ltd. (433 ITR 82), wherein it was held that DCF valuation could not be rejected on the grounds relied upon by the AO. Accordingly, the ITAT deleted the addition made u/s 56(2)(viib) and allowed the appeal of the Assessee.

Citation

Intermesh Shopping Network Pvt. Ltd. [TS-1597-ITAT-2025 (DEL)]



Our Comments

This ruling reinforces the settled principle that valuation under the DCF method must be examined as on the valuation date, without the benefit of hindsight. The ITAT has correctly recognized that disclaimer clauses are intrinsic to valuation exercises and cannot be a standalone reason to reject a valuation report.

The decision reiterates that where the Revenue disputes valuation, the statutory mechanism of reference to the Valuation Officer must be followed, instead of arbitrarily substituting valuation methods.

Needless to say, the assumptions based on which the DCF valuation is made should be bonafide and must have some basis and must not be adhoc or arbitrary.