

# Primer

## Applying for New Banking Licenses: A Guide to Non-Operative Financial Holding Companies

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**Vinod Kothari**

[vinod@vinodkothari.com](mailto:vinod@vinodkothari.com)

**Nidhi Ladha**

[nidhiladha@vinodkothari.com](mailto:nidhiladha@vinodkothari.com)

Vinod Kothari & Company

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## *Primer*

This Note discusses the non-operative financial holding companies (NOFHC) required for the purpose of new banking licenses in India.

The background for the note is the Guidelines of the RBI (“Banking License Guidelines”) for issuance of new banking licenses in India<sup>1</sup> and clarifications issued by the RBI in this regard (“RBI Clarification”)<sup>2</sup>. This Note incorporates the provisions of the Banking License Guidelines, NBFC regulations, and other applicable laws.

The concept of non-operating financial holding companies has been discussed elaborately in an RBI working paper<sup>3</sup>. The holding company model has been historically followed in the USA pursuant to the Graham-Leach-Bliley Act, and has subsequently been adopted in several other countries too.

This note, for easy guidance of readers, is written in an FAQ format.

### ***Applicable Law/ Regulations to NOFHCs***

#### **1. Is the NOFHC a “holding company” of the bank as per the common understanding of the term “holding company”?**

The common understanding of the term “holding company” is an entity that holds more than 50% of the voting capital of the subsidiary. In this sense, the NOFHC may not be a holding company, and over period of time, cannot be a holding company. The Guidelines require that over a period of 3 years, the holding, will have to be brought down to 40% and thereafter, successively, to 20%, and ultimately, 15%, of course, over a long period of 12 years from the commencement of business.

#### **2. Under what law is an NOFHC incorporated/regulated?**

An NOFHC will be a company incorporated under Companies Act, 1956 and shall require registration as an NBFC with the RBI. RBI’s Directions issued in this behalf shall regulate the NOFHC.

It is clear from the Guidelines that a separate set of directions will be issued by the RBI for non-operative financial holding companies.

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<sup>1</sup> <http://rbidocs.rbi.org.in/rdocs/Content/PDFs/GFLNB2222013.pdf>

<sup>2</sup> <http://downloaddoc3.rbi.org.in/FPRCQPS030613.pdf>

<sup>3</sup> <http://rbidocs.rbi.org.in/rdocs/content/PDFs/79486.pdf>

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### **3. At what stage do we need to form the NOFHC?**

New private sector banks can be opened through a NOFHC only. However, the nature of the NOFHC is that of a shareholding company. On reading of the Guidelines, our view is that NOFHC is not required at the time of applying for a banking license and the NOFHC can be set up after getting the in-principle approval from RBI<sup>4</sup>. However, at the time of making application, the Promoters have to indicate the source of funds. Our reading of the Banking Regulation (Companies) Rules is that the application is made in the name of the banking company, not the holding company. However, it will be handy to have the holding company incorporated.

### **4. Are there any special features at the time of incorporation of NOFHC? Any special requirements in the MoA/ AoA of the NOFHC?**

Yes, the MoA of the NOFHC must limit the business of the holding company only to hold shares in financial companies. The NOFHC is a limited purpose vehicle - hence, it should not ideally contain any other objects.

The AOA of NOFHC may contain restrictions on directorship and change in control of NOFHC as provided in the guidelines.

### **5. Is it better to use an existing company to serve as NOFHC or to float a new one?**

Most likely, going by the asset size of the NOFHC, it appears that the company will need registration with the RBI as an NBFC. This is even more obvious by the references to the to-be-issued guidelines/directions of the RBI for NOFHCs. In order to minimise the loss of time for incorporation/RBI registration, promoter groups may consider using existing CICs under their control.

It is quite clear, looking at the complicated requirements for shareholdings of the NOFHC (see the graph below) that even if existing entities within the group are used, there will have to be massive realignment of holdings within the group. The amendments to the Indian Stamp Act made by the Banking Laws (Amendment) Act 2012 have resolved the stamp duty applicable in case of realignment of holding of a bank, but the same does not apply in case of bank holding companies. In addition,

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<sup>4</sup> Clarification issued by RBI (Q. 16-31)

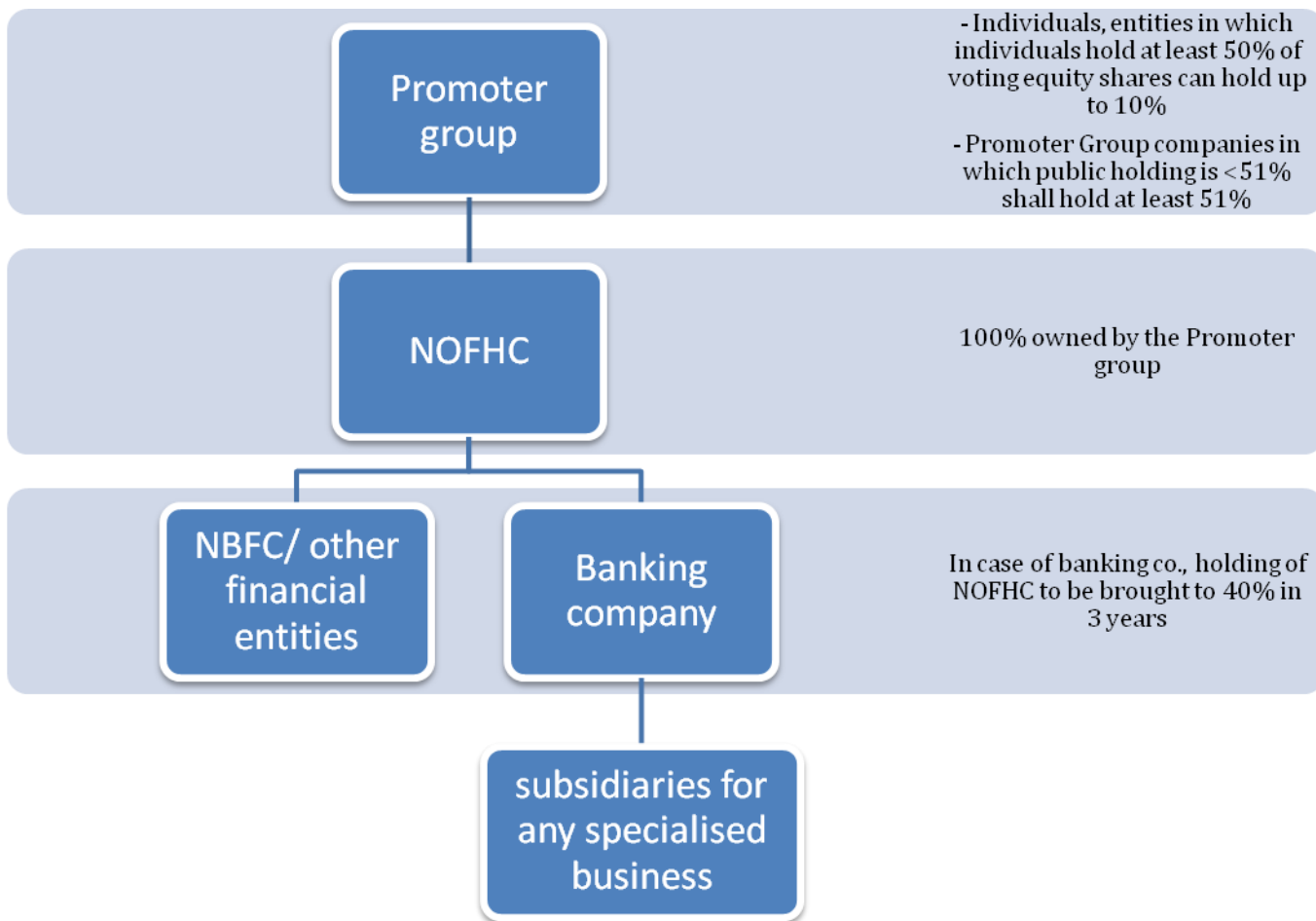


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there may be consequences of capital gains tax, SAST Regulations, etc. One has to very carefully plan the matrix of shareholdings in the NOFHC.

If an existing company is being used as an NOFHC, a transition period of 18 months from the date of getting in-principle approval from RBI or before commencement of banking business, whichever is earlier, will be given to such an NOFHC to restructure its shareholding, realignment of business among the entities under the NOFHC, re-organization of the Promoter Group entities to bring the regulated financial services entities under the NOFHC etc in terms of the Guidelines<sup>5</sup>.

Graph showing structure of bank and shareholding in NOHFC



<sup>5</sup> Clarification issued by RBI (Q. 16-31)



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**6. Can an existing financial service company be converted into NOFHC?**

Yes. An existing financial service company can be used as an NOFHC. However, such financial service company shall be required to transfer all its regulated services to a new company and shares of that new company shall be held by the NOFHC. Listed financial service companies can also be converted into NOFHC provided it meets the requirement of para(C)(ii)(b) of the Guidelines i.e. the public hold at least 51% voting equity shares in the company.<sup>6</sup>

**7. Whether documents like MOA/AOA, latest financial statements etc are required to be submitted by all the group companies while making application for in-principle approval?**

No. The entities/individuals belonging to the Promoters/ Promoter Group, which would participate in the voting equity shares of the NOFHC, would have to provide the MOA and AOA, financial statements for past ten years and IT returns for last three years, as appropriate, at the time of submission of their application. However, last available financial results in respect of group companies which are not participating in voting equity of NOFHC would also required to be submitted with the application.<sup>7</sup>

**8. Whether one of the eligibility conditions of having sound track record for 10 years as is required in respect of only financial entities of the Group or every entity forming promoter group will have to have such record?**

The overall track record of the Promoters/Promoter Group for at least 10 years will be seen in all its activities both financial and non-financial. If some, but not all, companies forming part of the Promoter Group have been in existence for less than 10 years, the track record of such companies will be seen for the period they are in existence. Further, if the Promoters/Promoter Group incorporates a new CIC for the purpose of holding shares in the NOFHC, the track record of the Promoters/Promoter Group setting up the CIC will be seen.<sup>8</sup>

### ***Merits/Economics of the Holding Company Structure:***

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<sup>6</sup> Clarification issued by RBI (Q. 32-37)

<sup>7</sup> Clarification issued by RBI (Q. 40-41)

<sup>8</sup> Clarification issued by RBI (Q. 49, 54)



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### **9. What are the merits/demerits of having control of group financial entities under the NOFHC?**

The Banking License Guidelines provide that promoter shall be permitted to set up a bank only through NOFHC structure - hence, the structure is mandatory for banks. Reading Para 2 C (iii) of the Banking License Guidelines seems to also make it mandatory for all other regulated financial services companies within the group to be held only by the NOFHC. The Guidelines also say that this is being done to ring-fence the regulated financial services providers within the group from the rest of the entities within the group.

While it is apparent that it is mandatory to have the holdings of the non-banking financial entities in the group under the umbrella of the NOFHC, one must realise that there are serious limitations that apply in case of entities under the NOFHC umbrella. One of the most serious limitations is the provision in Para 2 C (iv) of the Guidelines. This says that the other entities under the NOFHC shall not do the business that the bank is entitled to do. The exceptions to this are leasing, hire purchase, factoring, or other specialised activities such as insurance, infrastructure debt funds, mutual funds, stock broking, etc. The most important implication of this restriction is that most of the NBFC business currently being done by NBFCs will have to be transferred from NBFCs to banks. This includes secured lending, asset financing, loans against properties, loans against shares, working capital financing, etc. There will be major portfolio transfers that will have to happen as the business gets transferred to the banking company.

All this will amount to major corporate restructuring exercise for NBFCs wanting to set up banks. A mere transfer of business from NBFCs to banks will surely not work, as the shareholders of NBFCs may simply not comfortably allowing major part of NBFC business being transferred to the bank. The answer may lie in schemes of arrangement whereby shareholders of existing NBFCs are offered shares in the bank, through schemes under sections 391, 393 of the Companies Act.

Also, Para 2 C (vi) puts a 3 year embargo on any new financial services entity being put up under the NOFHC structure.

Another implication of regulated financial businesses coming under the NOFHC umbrella is that the exposure norms for exposure in a single borrower/group of borrowers shall apply on a consolidated basis.

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While all financial sector entities under either “control” or “significant influence” of the promoter group must be under the NOFHC, there is no bar on the promoter group holding minority stakes in financial services companies - this will usually be limited to 20%. This is based on our interpretation of a combined reading of para 2 C (vii) and 2 C (viii), and para 2 (I) (ii) (b). This point is also separately discussed in this Note.

While there are considerable limitations in case of entities under an NOFHC, the only possible merit seems to be that banks may undertake exposure in entities under the NOFHC - see a later question on this.

### **10. What all entities will be covered by “regulated financial services entities”?**

All banking companies, NBFCs, housing finance companies, SEBI-regulated entities. In our view, it does not seem to be the intent of the Guidelines to include CICs/holding companies to be included within the purview of “regulated financial services entities”. If that were the case, CICs holding non-financial entities within the group will also come under the umbrella of the NOFHC, which could not be the intent. Similarly, the part of the Guidelines that says financial services entities should not be holding shares of NOFHC should not include CICs.

Further, any subsidiary or associate of such financial entities providing financial services regulated by RBI, SEBI, IRDA or any other regulator shall also come within the purview of ‘regulated financial entities’ irrespective of the fact whether such companies are providing services to the Group Companies, whether financial or non financial, only or not.<sup>9</sup>

### **11. Is it mandatory that promoter shareholding in existing financial companies within the group is transferred to the NOFHC?**

Yes, in terms of para 2(C)(viii), promoters (including Group entities and individuals associated with promoters) can hold the shares in bank and in financial companies only through NOFHC, hence, shares of existing financial companies, whether promoting the NOFHC/bank or not, shall necessarily be transferred to NOFHC. However, the unregulated financial services activities/ entities of the Promoter Group may not come under the NOFHC.<sup>10</sup>

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<sup>9</sup> Clarification issued by RBI (Q. 66)

<sup>10</sup> Clarification issued by RBI (Q. 47)



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- 12. A financial service company, say A has two subsidiaries, say B and C in financial services sector. Will it be sufficient if the NOFHC holds the equity of A and therefore indirectly holds the equity of B and C?**

The NOFHC shall directly hold the bank as well as all the other regulated financial services entities of the Group in which a Promoter Group has significant influence or control and therefore, all the three companies will have to directly come under the NOFHC and Company A, Company B and Company C cannot make investment in equity / debt capital instruments amongst themselves. However, such financial entities under the NOFHC can set up subsidiaries if so required under any law subject to RBI's and concerned financial regulator's approval.

- 13. Whether an overseas subsidiary of promoter group company engaged in financial services is also required to be come under NOFHC?**

Yes, all financial service entities in which promoters have 'significant influence' or 'control' will be required to under NOFHC.<sup>11</sup>

- 14. Whether 'unregulated financial service companies' are also to be included under the umbrella of NOFHC?**

No, unregulated financial service companies need not compulsorily to come under the NOFHC umbrella.<sup>12</sup>

- 15. Can an NOFHC make investments within the Group?**

NOFHC are allowed to make investments in capital instruments issued by unconsolidated financial and insurance entities within the Group and such investment should not exceed 10% of its consolidated capital funds. Consolidated capital funds would mean the Capital, Reserves and Surplus of the NOFHC determined on the consolidation of its subsidiaries, associates and joint ventures.

- 16. Can the NOFHC make investments outside the Group as well?**

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<sup>11</sup> Clarification issued by RBI (Q. 254)

<sup>12</sup> Clarification issued by RBI (Q. 65)





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This point has been already been discussed in this Note. As per para 2 (I) (ii) (b) of the Guidelines, the NOFHC, including all its consolidated entities, may make investments in other financial entities (which are not consolidated), to a limit of 10% of aggregate capital funds of the group. Needless to say, the aggregate capital funds of the Group will be counted after elimination of any cross holdings.

**17. What are other businesses/activities that the NOFHC may carry?**

Practically, none. However, the NOFHC may have to maintain liquidity depending on the nature of its liabilities. The NOFHC can make investment in bank deposits, money market instruments (debt mutual funds are not covered), government securities and actively traded bonds and debentures besides lending to or investing in entities that are held under it. So, on the asset side of the NOFHC, the only assets one may expect to have are - investments in the Group, investments outside the Group, and liquid balances.<sup>13</sup>

**18. Can an NOFHC carry on the housing finance business or any other business which was carried on by the regulated financial service company under the NOFHC?**

No, all such lending activities and other para banking activities are to be carried on from inside the bank, its subsidiaries, associates or joint ventures. NOFHC cannot do such business activities.

**19. If the Promoter Group has a housing finance company which is primarily hold by other regulated financial service companies, can such HFC continue its business or should it be required to come under NOFHC umbrella?**

Lending activities must be conducted from inside the bank. Therefore, the housing finance activity of the HFC should be transferred to the bank under the NOFHC. The financial sector regulated entity which holds the HFC substantially will have to come under the NOFHC.<sup>14</sup>

**20. Can an NOFHC set up new business through a newly incorporated financial service company?**

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<sup>13</sup> Clarification issued by RBI (Q. 78)

<sup>14</sup> Clarification issued by RBI (Q. 101-102)



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An NOFHC cannot start any new financial business in any way within 3 years from the date of commencement of business. However, a foreign subsidiary can be set up by a financial services entity already under the NOFHC framework provided the setting up of such an entity is necessary under the regulation in that foreign jurisdiction.

### **21. Can the NOFHC acquire any new business pursuant to any scheme of arrangement?**

Yes, as the restriction on setting up of new financial services entity within the first three years would not apply to restructuring of the existing business / demergers or any other restructuring of existing business mandated by the sectoral regulators. However, any such restructuring or scheme of arrangement will have to be undertaken with RBI's approval.<sup>15</sup>

### **22. Can the financial entities under the NOFHC carry on non financial activities?**

Once the financial group (that is, the banking company, and other financial activities which necessarily have to come under the NOFHC umbrella) has a banking company in terms of the Guidelines, surely enough, the banking company can only carry such activities which are regarded as para-banking activities by the RBI. For other regulated financial activities, the group has the liberty of carrying them under other entities within the NOFHC umbrella. But then, can any of the entities under the NOFHC umbrella carry non-financial activities? For example, trading, or consulting? Surely, there is a restriction against a bank carrying non-banking activity under the Banking Regulation Act, but surely, there should not be any such restriction in case of other financial entities under the NOFHC umbrella.

However, the mood of the RBI seems to be that entities under the NOFHC umbrella cannot engage in any non-financial activities. There is, therefore, an obvious bar on any unregulated activity, clearly ruling out any non-financial activity.<sup>16</sup>

## ***Shareholding of the NOFHC:***

### **23. Who can be the shareholders of the NOFHC?**

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<sup>15</sup> Clarification issued by RBI (Q. 297)

<sup>16</sup> Clarification issued by RBI (Q. 47)



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First, it should be clear that the NOFHC is 100% owned/controlled by the promoter group - this comes clear from repeated references to “wholly owned NOFHC”. However, there are some limitations to the extent of concentration, and limits on publicly-owned holding companies.

In case of holdings of individuals, there is a cap of 10% of “voting equity shares” (the term voting equity shares seems like over-stressing on “voting”, since equity shares are always, by presumption, voting shares, unless the company has issued non-voting equity shares, which is a rarity. However, for the purpose of the Guidelines, only ‘voting equity’ is to be reckoned if there are non-voting shares also.<sup>17</sup>). This cap seems to be in line with section 12 (2) of the Banking Regulation Act. The cap on individual holding includes holdings of relatives, and companies in which individual/relatives hold 50% or more voting capital. Since the cap includes holdings of “relatives” (as defined in Companies Act), this effectively limits the holdings of the “family”.

It is to be noted that it is not mandatory that the individuals, along with their relatives and/ or entities in which they hold at least 50% voting equity, should hold voting equity in NOFHC. The cap of 10% as discussed in preceding para applies when an individual chooses to be a promoter of the NOFHC<sup>18</sup>.

The second condition is what is a little intriguing and seems to suggest that there are holding companies behind the holding company as well. It says, the holding of companies, in which public holding is at least 51%, must be at least 51% in the NOFHC. This seems like going contra to the essential principle that the NOHFC itself is 100% owned/controlled by the promoter group. With public holding of 51% and above, no promoter group can really be sure of sustained control over such “widely held companies”. However, this is a prime condition to be fulfilled by the promoters of NOFHC.<sup>19</sup> Further, it is not necessary that all Group companies in which public shareholding is more than 51% should be shareholders of the NOFHC.<sup>20</sup> It has been further clarified that while considering this percentage shareholding, any convertible instruments held by the promoters, whether compulsorily or optionally convertible into voting equity shares, will be considered as voting equity shares.<sup>21</sup>

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<sup>17</sup> Clarification issued by RBI (Q. 39, 61-62)

<sup>18</sup> Clarification issued by RBI (Q. 1-4)

<sup>19</sup> Clarification issued by RBI (Q. 15)

<sup>20</sup> Clarification issued by RBI (Q. 43)

<sup>21</sup> Clarification issued by RBI (Q. 300)



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What is the meaning of “public” holding in this context? In our view, holding of shares other than with the promoter group should be regarded as public shareholding. Public shareholding here cannot be taken to mean shares offered to public either by prospectus or letter of offer, as that would go against the idea of full ownership of the holding company by the promoter group. As also clarified by RBI, for the purpose of the Guidelines, ‘public shareholding’ implies that no person along with his relatives and entities in which he and / or his relatives hold not less than 50% of the voting equity shares, by virtue of his shareholding or otherwise, exercises ‘significant influence’ or ‘control’ (as defined in Accounting Standard 23) over the company<sup>22</sup>.

The shareholders in the NOFHC may consist of individuals, non-financial entities of the promoter group, and non-operative financial companies of the group. Non-operative financial companies should be taken to mean core investment companies (CICs)<sup>23</sup>. However, RBI has clarified that a non-operative financial holding company though regulated by RBI will remain outside NOFHC. NBFC (Investment Companies) which hold/deal in equity shares of Promoter Group Companies cannot be under the NOFHC. Therefore, NBFC (Investment Companies), which would include CICs and other non-operative holding companies, would remain outside NOFHC. However, if there are investments in voting equity shares of regulated financial sector entities in which the Group has significant influence or control, such entities will have to be brought under the NOFHC.<sup>24</sup>

Shares of NOFHC cannot be held by any entity outside the Promoter Group or by any financial service entity within the Promoter Group<sup>25</sup>.

It is pertinent to note that the shares of NOFHC can be held by individuals, corporate entities and companies belonging to the Promoter Group. An LLP or trust or other bodies corporate do not fall under any of these categories. Therefore, an LLP or trust or bodies corporate cannot hold voting equity shares directly in the NOFHC but can hold indirectly through a company in the Promoter Group which holds voting equity shares of the NOFHC.<sup>26</sup>

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<sup>22</sup> Clarification issued by RBI (Q. 8-13, 59-60)

<sup>23</sup> For more on CICs, see our page <http://india-financing.com/core-investment-companies.html>

<sup>24</sup> Clarification issued by RBI (Q. 67-68)

<sup>25</sup> Clarification issued by RBI (Q. 45, 82)

<sup>26</sup> Clarification issued by RBI (Q. 52-53)



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**24. Whether the companies which form part of promoters group where public holds not less than 51% of voting capital, have to be listed companies at the time of application for banking license?**

No, a company in which public holds more than 50% need not be a listed company. The requirement under the Guidelines is that companies having public shareholding of at least 51% should hold at least 51% voting capital of NOFHC. Such promoter group companies having public shareholding would include those companies in which promoters, by virtue of his shareholding or otherwise, exercises 'significant influence' or 'control'.<sup>27</sup>

**25. Can a Promoter Group company wherein 100% shareholding is with public promote the NOFHC?**

It is not necessary that there has to be an individual promoter. The company wherein 100% of voting equity shares are held by the public can set up the NOFHC and hold to the extent of 100% of the voting equity shares of the NOFHC if such a company is a non-financial services company or a non-operating financial holding company in the group. Further, the company itself will be deemed to be the Promoter and all the provisions of the guidelines applicable to the Promoter and the Promoter Group will apply to it.<sup>28</sup>

However, with due respect, it is to be noted that RBI has clearly mentioned in its clarifications that only one promoter group can promote the NOFHC. In answers to several questions, the RBI has stated that even a listed company can hold the NOFHC. Is it not strange that a listed company, purportedly having wide-spread ownership interest, can own an NOFHC, but when it comes a promoter, not more than one promoter can own an NOFHC? In fact, the whole idea of a single promoter for an NOFHC is completely self-contradicting and unreasonable.

In several bank-promoter groups, there will be strategic investors, joint-venturers, groups of promoters or associates joining together to put up equity in the NOFHC. The stipulation of a single promoter will only lead to creation of one more layer at the shareholding level of the NOFHC. That is, if 2 or more promoters of strategic investors want to come together to own an NOFHC, they will together have to form a shareholding company (a CIC), which in turn will own the NOFHC. The entire

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<sup>27</sup> Clarification issued by RBI (Q. 8-13)

<sup>28</sup> Clarification issued by RBI (Q. 79)



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ownership structure arising as a result of the Guidelines will lead to proliferation of entities, thereby making the ownership structure of banking companies highly opaque.

**26. Can 10 or more unrelated individuals act as promoters each holding not more than 10% shares in NOFHC or whether companies under different management and belonging to different groups can be the promoters?**

No. The requirement is that not less than 51% of the voting equity shares of the NOFHC shall be held by companies in the Promoter Group, in which the public hold not less than 51% of the voting equity of such companies. If 10 independent individuals form a Group, then such a Group cannot satisfy the above criteria laid down for holding the NOFHC.

Additionally, such newly formed Promoter Group would not be able to meet one of the 'Fit and Proper' criteria, which requires Promoters/Promoter Groups to have a successful track record of running their business for at least 10 years. Hence, individuals belonging to the Promoter Group only can participate in the voting equity shares of NOFHC.<sup>29</sup>

The NOFHC has to be wholly owned by a single Promoter/Promoter Group, hence, two or more separate Groups cannot combine together to set up a NOFHC.<sup>30</sup>

**27. Can a strategic partner in one the holding company of NOFHC would be deemed as promoter/promoter group and would be required to bring its existing financial services businesses also under the NOFHC set-up by the promoters?**

Two or more separate groups cannot combine together to set up a NOFHC. A strategic shareholder not being a part of the Promoter Group, can be a shareholder in a company belonging to the Promoter Group holding the NOFHC. Further, it is also to be noted that if the strategic partner is in control of the company and is not a resident, then such company cannot hold shares in the NOFHC, as NOFHC has to be owned and controlled by residents.<sup>31</sup>

**28. CICs, which are not systematically important, are not required to be registered with the RBI currently. Can such CICs be shareholders of the NOFHC?**

<sup>29</sup> Clarification issued by RBI (Q. 5-7)

<sup>30</sup> Clarification issued by RBI (Q. 42)

<sup>31</sup> Clarification issued by RBI (Q. 114)



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CICs holding the non-financial sector companies of the Promoter Group can be the shareholders of NOFHC.

**29. Whether the CICs promoting the NOFHC and holding investments in unregulated financial sector entities and non-financial sector entities, would be required to be registered as a CIC-SI with the RBI and would come under the purview of the NOFHC?**

If such a CIC fulfills the twin conditions of: a) having asset size of more than 100 crores including the assets of other CICs in Group and; b) holds public funds, as provided in CIC Directions, registration as CIC-SI with the RBI will be mandatory.

Further, a CIC that holds shares only in non-financial companies of the Promoter Group would not be considered as a financial services company and would be held outside the purview of the NOFHC.<sup>32</sup>

**30. Can a Multi-State Cooperative Society be a promoter of bank as per the NOFHC?**

There is no bar as such in the guidelines. Hence, in our view, such a society can promote a bank if it meets the shareholding requirements as provided in the Guidelines.

**31. Can there be foreign shareholders in the NOFHC?**

There are elaborate references in the Guidelines about foreign shareholdings in banks. However, there is no mention about foreign shareholdings in the NOFHC.

Going by the general provisions of the extant FDI policy, FDI is not allowed in case of investment vehicles, except in case of infrastructure SPVs. Since the NOFHC is an investment company, it may be presumed that foreign shareholding will not be allowed in NOFHC.

However, it is pertinent to note that the Guidelines state that entities / groups in the private sector that are 'owned and controlled by residents' [as defined in Department of Industrial Policy and Promotion (DIPP) Press Note 2, 3 and 4 of 2009 / FEMA

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<sup>32</sup> Clarification issued by RBI (Q. 76)



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Regulations as amended from time to time] are eligible to be a promoter of NOFHC. The press notes issued by DIPP under FEMA Regulations define entities ‘owned and controlled by residents’ as Indian companies in which more than 50% of the equity interest is beneficially owned by resident Indian citizens and Indian companies (which are owned and controlled ultimately by resident Indian citizens) **and** wherein the Indian citizen or the Indian companies have the power to appoint a majority of directors of such companies. This would mean that Indian companies in private sector, in which there is less 50% of equity is foreign investment and power to appoint majority directors on the board of such companies is with Indian citizens, can hold shares of NOFHC.<sup>33</sup>

- 32. Where a Group has two or more otherwise unconnected individuals as its promoters, will each individual (along with relatives and entities connected to such individual) be permitted to hold up to 10% of the voting equity shares of the NOFHC or will the 10% limit apply in aggregate to the shares held by all individuals (and connected persons) forming part of the promoter group?**

If there are two or more individuals who are part of the Promoter Group and are not relatives of each other, the limit of 10% would apply individually, and need not be aggregated. However, all such individuals cannot hold more than 49% of the voting equity shares of the NOFHC.<sup>34</sup>

- 33. Can an NOHFC be listed on any stock exchange?**

No, as the NOFHC will be a wholly owned company of promoter/ promoter group having shareholding as specified in the Guidelines, therefore, it can't be a listed on any stock exchange.

- 34. Can residents of India who hold Overseas Citizenship of India hold shares in NOFHC within the limit of 10%?**

No, 10% shareholding in NOFHC can consist of residents, entities owned and controlled by residents only.

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<sup>33</sup> Clarification issued by RBI (Q. 146)

<sup>34</sup> Clarification issued by RBI (Q. 152-153)





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**35. Can a promoter group company having outstanding ADR/GDR be counted as company having more than 50% public shareholding and whether such company can invest in the NOFHC?**

Yes. GDRs / ADRs and their underlying shares would be counted as public shareholding, provided that, by virtue of their shareholding, the holders or their custodians do not have 'significant influence' or 'control' and there are no agreements or other arrangements whereby the GDR / ADR holders or their custodian have undertaken to exercise their voting rights in accordance with the Promoters/management.

**36. Can shares of NOFHC be pledged and transferred to pledgee if pledge is invoked?**

In our view, there is no bar if the promoters pledge their shareholding in NOFHC. However, the same would require prior approval of RBI. In any case, any change in shareholding (by the Promoter Group) with in the NOFHC as a result of which a shareholder acquires 5% or more of the voting equity capital of the NOFHC shall be with the prior approval of RBI.<sup>35</sup>

**37. What happens when existing promoter shareholdings in financial companies is transferred to NOFHC, in respect of the following:**

**a) Stamp duty**

In terms of Banking Laws (Amendment) Act, 2012 as passed by Lok Sabha on December 18, 2012, stamp duty is exempted in case of transfer of holdings in a bank. However, this exemption, in our view, will not be applicable if the company whose shares are transferred is not a banking company. Stamp duty is not a concern in case of demat shares. However, in case of shares in the physical form, stamp duty may become a significant cost.

**b) Capital gains tax**

Presently, capital gain tax will be applicable. Exemption may be announced in the forthcoming Union Budget. However, RBI has clarified that tax on such transfers

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<sup>35</sup> Clarification issued by RBI (Q. 252-253)



## *Primer*

would be applicable as per the extant laws, hence, no relaxation may be expected!<sup>36</sup>

### **c) SEBI SAST Regulations**

Currently, there is no exemption under SAST regulations in case of transfer of shares either in a banking company, or in case of the bank holding company. However, SEBI may eventually grant exemption from SAST regulations in case of reorganisation of the shareholding of NOFHCs as well.

### **38. What is the capital requirement for NOFHC?**

The capital requirements for the NOFHC will, expectedly, be laid down by the Directions that the RBI may be coming up with. At this time, the quick thumb rules on the required resources of the NOFHC will be - assuming that the NOFHC holds 100% capital of the bank, the NOFHC will need resources of Rs 500 crores. This does not entirely have to come by way of equity - as NOFHCs are allowed to leverage on their capital. The required capital will, therefore, be a function of the size of the bank's capital, and the percentage that the NOFHC agrees to hold in the bank.

### **39. What is the minimum holding that the NOFHC must own in the banking company?**

The NOFHC shall hold a minimum of 40% of the paid-up voting equity capital of the bank which shall be locked in for a period of five years from the date of commencement of business of the bank. Holding beyond 40% shall be brought down to 40% within three years from the date of commencement of business of the bank.

The minimum holding of 40% shall be complied with by the NOFHC during first five years, whether the bank raise further funds or not (in case further funds raised, 40% shall be of the increased capital), and thereafter, holding to be brought down to 20% of the paid-up voting equity capital of the bank within a period of 10 years, and to 15% within 12 years from the date of commencement of business of the bank.

### **40. Except NOFHC holding, can any other individual or entity, not related with promoters, hold shares in the banking company?**

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<sup>36</sup> Clarification issued by RBI (Q. 122-130)



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No single entity or the group of the related entities, other than the NOFHC shall have the shareholding or control, directly or indirectly, in excess of 10% of the paid up voting equity capital of the bank and any acquisition of shares which will take the aggregate holding of an individual/entity/group to the equivalent of 5% or more of the paid up voting equity capital of the bank will require prior approval of RBI.

### **41. Can Government of India hold more than 10% in the banks?**

No single entity or group of related entities, other than the NOFHC, shall have shareholding or control, directly or indirectly, in excess of 10% of the paid-up voting equity capital of the bank and this rule applies to Government holding also as in any case, banks would be private sector banks.<sup>37</sup>

### **42. Can a strategic investor of a promoter company of NOFHC, not belonging to Promoter Group hold shares directly in the bank?**

Yes. However, no single entity or group of related entities, other than the NOFHC, shall have shareholding or control, directly or indirectly, in excess of 10% of the voting equity capital of the bank and any acquisition of shares which will take the aggregate holding of an individual / entity / group to the equivalent of 5% or more of the voting equity capital of the bank, will require prior approval of RBI.<sup>38</sup>

### **43. What is the minimum holding that the NOFHC must own in other financial entities within the group?**

Para 2 C (vii) provides that the NOFHC must have “significant influence” over the regulated financial services entity held by it. “Significant influence” is defined in terms of AS 23. It is notable that where there is 20% voting control, there is a presumption as to significant influence. The Guidelines also lay down that all investments of the promoter group in regulated financial businesses will be through the NOFHC. Our interpretation of these Guidelines is that if the promoter group has minority interests, not amounting to significant influence in any regulated financial business, the same may be carried outside the NOFHC.

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<sup>37</sup> Clarification issued by RBI (Q. 136)

<sup>38</sup> Clarification issued by RBI (Q. 115)



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Para 2(D)(vi) says that the NOFHC shall hold such capital in financial entities as may be prescribed by the respective sectoral regulators. This refers to the capital adequacy requirements of each of the regulated financial entities.

#### **44. Can the NOFHC hold non financial entities as its subsidiaries?**

No, unless specifically permitted by the RBI.<sup>39</sup>

#### **45. Can there be foreign shareholding in banking companies?**

While the normal rules about FDI in banking sector are contained in FDI policy, the Guidelines provide a self-contained code for FDI in new private sector banks. The Guidelines override the FDI policy to this extent. The total cap on non-resident shareholding (NRIs, FDI and FIIs) is set at 49% for first 5 years from the date of licensing of the new bank. It is clear that this limitation is applicable only for the first 5 years, after which the extant FDI policy will switch in. There are several specific limits as well:

##### **a) Issue of equity shares to a particular non-resident?**

The holding of any one non-resident (once again, including NRI or FII) shall be limited to less than 5% of voting equity shares. This limit includes shares held directly or indirectly, individually or in groups, or through subsidiary, associate or joint venture for a period of 5 years from the date of commencement of business of the bank. However, after expiry of said 5 years, holding of non residents shall be as per extant FDI Policy.<sup>40</sup> The ‘direct and indirect’ shareholding of non residents here would not include holding in NOFHC.<sup>41</sup>

Also note that the restriction above is for “voting equity shares”. In case of compulsorily convertible preference shares, or compulsorily convertible debentures, which also come under FDI, the above cap of 5% is not applicable. Thus, it is clearly permissible for a foreign shareholder to invest in CCDs convertible after 5 years.

As per extant FDI Policy, FDI up to 49% of paid up capital is allowed in private sector banks under automatic route and beyond 49% but up to 74% is allowed

<sup>39</sup> Clarification issued by RBI (Q. 140)

<sup>40</sup> Clarification issued by RBI (Q. 44)

<sup>41</sup> Clarification issued by RBI (Q. 168)



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under approval route of RBI. The extant policy restricts the ‘aggregate FDI from all sources’ to 74% of paid up capital of bank and requires, at all times, at least 26% holding by residents.

**b) On transfer of shares to non-residents?**

Same as above. Holding of non-residents should not exceed 5% of voting equity in initial 5 years of operation of bank.

**46. Can there be foreign shareholding in subsidiaries of the bank?**

In the normal course, a bank held under the NOFHC will not be permitted to have subsidiaries. A subsidiary of the bank can be set up only where it is legally required or specifically permitted by RBI. FDI investments in the subsidiary of the bank or in the financial services entities held under the NOFHC would be as per the DIPP guidelines of Government of India/Notifications issued under FEMA.<sup>42</sup>

### ***Minimum Capital Requirements for Bank and the Group***

**47. What is the minimum capital required for the banking company?**

The minimum paid up voting equity capital required for the bank is Rs 500 crores. However, where an NBFC is permitted to convert into a bank, it should have a minimum networth of Rs. 500 crores at all times.<sup>43</sup> It has been clarified by the RBI that initial minimum capital required for banking companies should be infused by way of ‘voting equity shares’ only and depending upon the business plan, additional capital can be brought in by way of any other securities to be issued in terms of applicable laws.<sup>44</sup>

As regards progressive increase in capital requirements, note that the bank needs to maintain Basel II/ Basel III capital requirements.

The Basel III guidelines in India<sup>45</sup> require a minimum Tier 1 capital requirement of 5.5%.

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<sup>42</sup> Clarification issued by RBI (Q. 87)

<sup>43</sup> Clarification issued by RBI (Q. 176-177)

<sup>44</sup> Clarification issued by RBI (Q. 227)

<sup>45</sup> <http://rbi.org.in/scripts/NotificationUser.aspx?Id=7174&Mode=0>



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Basel III capital requirements are slated to be implemented in India in phases from April 1, 2013<sup>46</sup>. Obviously, all new banks will be covered by the Basel III guidelines.

The so-called common equity capital requirement under Basel III and the voting equity capital required under the Guidelines are the same. Hence, the minimum capital required in case of new banks shall be Rs 500 crores, or 5.5% of risk weighted assets, whichever is higher.

Note that the minimum common equity requirement under Basel III is 5.5% based on a minimum capital requirement of 9%. However, the Guidelines put a minimum capital requirement of 13% for a period of 3 years (that is to say, after the initial period of 3 years, the capital requirements will be at par with the regular Basel II/ Basel III requirements. It is not clear, how much of the 13% capital requirement will be in form of Tier 1a common equity. However, going by the commonly-followed 50% norm, it may be logical to hold that the minimum common equity requirement for new banks, for first 3 years, will be 6.5% of the risk weighted assets.

**48. Can the shares of the bank be issued at premium to meet the minimum capital of Rs 500 crores?**

No. The initial minimum capitalization of the bank should be paid-up voting equity capital of Rs. 500 crores.<sup>47</sup>

**49. What are the applicable Basle II/ Basle III norms to NOFHCs?**

The NOFHC shall have such capital so as to meet the requirement of having 40% stake in the bank. The capital requirements for NOFHCs shall be applied on consolidated basis. It does not seem logical to apply any capital norms on stand-alone basis to the NOFHC, since the NOFHC is engaged in no substantial business other than investments in regulated financial businesses, and the investment made by the NOFHC in regulated financial businesses is deducted from its capital as well as assets for computation of risk weighted assets. This leaves with no assets, on which to apply risk weights.

On consolidated basis, the consolidated assets of NOFHC and the entities held by it shall aggregated to apply a minimum capital adequacy of 13% of its consolidated risk

<sup>46</sup> [http://www.rbi.org.in/scripts/BS\\_PressReleaseDisplay.aspx?prid=27862](http://www.rbi.org.in/scripts/BS_PressReleaseDisplay.aspx?prid=27862)

<sup>47</sup> Clarification issued by RBI (Q. 304)



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weighted assets (RWA). The consolidation norms applicable for this purpose are the same as those applicable under accounting standards<sup>48</sup>. There is a 3 year sunset for this requirement too - which should appropriately mean that after 3 years, the capital requirements for each of the regulated entities under the umbrella of the NOFHC will be as applicable under the relevant regulations applicable to each such entity.

### **50. What are the different sources from which the NOFHC can raise resources to fund its investment in the regulated financial entities?**

NOFHCs are allowed to borrow. The Guidelines put a cap of 1.25 times paid up capital and free reserves on “leverage”. Since there is a reference to maintaining the level of debt that may be serviced from dividend income of the NOFHC, the word “leverage” here should mean only interest-bearing redeemable debt. Hence, instruments such as CCDs, or CCPS should not be considered as debt for this purpose.

### ***Dividend Restrictions on NOFHC:***

### **51. What are the dividend restrictions applicable to the bank?**

In terms of section 15 of the Banking Regulation Act, a bank can pay dividend only after writing off of all its capitalized expenditures (including preliminary expenses, organisation expenses, share-selling commission, brokerage, amounts of losses incurred and any other item of expenditure not represented by tangible assets). However, dividend can be paid without writing of depreciation and bad debts in certain situations as provided in section 15(2) of the said Act. Further, section 17 requires transfer of at least 20% of its net profits every year to “reserve fund” before declaration of any dividend.

### **52. What are the dividend restrictions applicable to the NOFHC?**

Since the NOFHC is a financial company under the RBI Act, sec 45IC of the RBI Act applies. This provision requires the NOHFC to transfer at least 20% of its net profits to a “reserve fund”.

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<sup>48</sup> <http://rbi.org.in/scripts/NotificationUser.aspx?Id=1071&Mode=0> . There are minor variations between these norms and those under Basel III consolidation requirements. We are of the view that eventually, Basel III consolidation norms will prevail.

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However, the Guidelines provide for a higher percentage - 25% of profits, every year. The Guidelines also say that if there are any qualifications in the auditors' report which have a bearing on the net profit, the effect of the qualification on net profit must be recognised before any distribution is made.

### ***Exposure Norms Applicable to NOFHC:***

#### **53. What are the exposure norms applicable to the regulated entities under the NOFHC umbrella?**

In order to avoid round tripping of funds and to avoid circular movement of funds in the banking group, the financial entities held by NOFHC shall not have any credit and investments (including investments in the equity/debt capital instruments) exposure to the Promoters / Promoter Group entities or individuals associated with the Promoter Group or the NOFHC. The regulated entities are also prohibited from making investments inter-se in equity/debt instruments of each other. In addition, there is also a bar on these entities to invest in equity instruments of other NOFHCs. Investment in debt instruments of other NOFHCs can be made.

It has been further clarified by the RBI that the exposure norms stipulated at paragraph 2 (I) (ii) (a) of the Guidelines refer to third party exposures and capital market exposures of the consolidated NOFHC. As regards the stand alone NOFHC, its exposure to the entities held under it are not subject to single and group borrower exposure limits. The overarching exposure norms of the insurance companies and mutual funds under the NOFHC have been indicated in Paragraph 2 (I) (iv) (a) to (c). Their exposure norms would be as prescribed by IRDA and SEBI respectively.<sup>49</sup>

#### **54. Can financial entities held by the NOFHC have credit exposure inter-se as such companies are not permitted to invest in securities of each other?**

Yes, subject to the intra group transactions and exposure norms in the Guidelines. As regards exposure of entities regulated by other financial sector regulators, to the bank and other entities held under NOFHC, such exposures would be in accordance with the rules/regulations of the respective sectoral regulators.<sup>50</sup>

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<sup>49</sup> Clarification issued by RBI (Q. 218)

<sup>50</sup> Clarification issued by RBI (Q. 261)





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**55. Are all overseas financial service entities also required to be brought under the NOFHC structure?**

Yes, all regulated financial sector entities in which a Promoter Group has significant influence or control will be held under the NOFHC, including the overseas financial entities.<sup>51</sup> However, if such overseas entities are exclusively regulated by foreign regulators, such overseas companies need not come under the NOFHC.

### ***Corporate Governance of NOFHCs:***

**56. What should be the criteria for selection of persons to become directors of NOFHCs?**

The persons to be appointed as directors of NOFHCs shall comply with 'fit and proper' person criteria as applicable to banks to the extent they are appropriate. In addition, no person shall be appointed as director on its Board, if such person is:

- a) a director in any other NOFHC or a bank other than a banking company under it;
- b) a director in any other company (directorships in subsidiary of the NOFHC and section 25 company are excluded)

Apart from above, the qualification, expertise, track record, integrity etc are also other factors which should be taken into consideration while appointing a director of NOFHC.

**57. How many directors shall we need?**

The Board of NOFHC should comprise of optimum number of directors and at least 50% of the directors shall be totally independent of the Promoter or Promoter Group entities and their major customers and major suppliers<sup>52</sup>.

**58. Are the bank and the NOFHC permitted to have common directors? Can they therefore also have some and/or all common independent directors? Similarly,**

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<sup>51</sup> Clarification issued by RBI (Q. 279)

<sup>52</sup> Major customers and major suppliers of the promoter group would mean dealings with whom constitute 10 per cent or more of the annual purchases or sales or both taken together



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**can the NOFHC have some and/or all common independent directors as other regulated financial services entities held by the NOFHC?**

There could be common directors in the NOFHC and the bank. A director of the NOFHC cannot be considered as independent director of the bank. The common directorship between the NOFHC and other regulated financial services entities would be as per the regulations of the sectoral regulators concerned.<sup>53</sup>

**59. Can the bank and/or the NOFHC have foreign directors?**

Yes. There is no bar having eligible individuals who are non resident Indians or foreign nationals on the Boards of the NOFHC and the bank.<sup>54</sup>

**60. Can a person holding directorship in any other company, not related to promoter group, be appointed as director of NOFHC or bank?**

The NOFHC has to be managed by a person who is in whole-time employment and he / she cannot be a director in any other company (other than the bank or a subsidiary of the NOFHC or a Section 25 company) and is not engaged in any other business or vocation.

**61. Are NOFHCs required to constitute any committees also?**

Yes, a Nomination Committee to perform due diligence in respect of its Directors and a Remuneration Committee to decide on the compensation payable to the key management executives shall be constituted by NOHFCs.

The graph below shows the rules about directorships in CIC holding NOHFC, NOFHC and the Bank:

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<sup>53</sup> Clarification issued by RBI (Q. 93)

<sup>54</sup> Clarification issued by RBI (Q. 326)



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### Directors of any CIC holding the NOHFC

- Generally speaking, directors of all registered NBFCs have to be "fit and proper" persons
- Usha Thorat recommendations lay down Clause 49 to be applicable to all NBFCs.
- so if the shareholding CICs in the NOFHC are regulated CICs, they need to abide by the applicable guidelines

### Directors of the NOFHC

- Cannot hold directorship of other company except subsidiary or a sec 25 company
- 'Fit and proper' person criteria applicable as prescribed for banks by Dr Ganguly Group Report
- At least 50% of the Board should comprise of Ids with special knowledge and practical experience
- Undertaking and declarations required from directors

### Directors of Bank

- At least 51% directors to be IDs with special knowledge or practical experience in specified fields
- Directors other than chairman and WTD are restricted to hold office for more than 8 years at a stretch
- Whole time chairman to manage the bank
  - Appointment of part time chairman to be approved by RBI and MD shall be managing the bank
- Director cannot hold directorship of other banking companies
- Board to not to have more than 3 directors who shall be directors of companies exercising 20% or more voting rights in bank
- Undertaking and declarations required from directors
- Not more than one member of family or close relative or should to be on board

### ***Additional Restrictions Applicable to Banks under an NOFHC:***

#### **62. What are the usual investment restrictions applicable to banking entities?**

Para 2.1.3.4 of the Master Circular on 'Exposure Norms' as on July 1, 2012<sup>55</sup> issued by RBI prescribes the rules for investment exposure by banks and accordingly,

<sup>55</sup> [http://www.rbi.org.in/scripts/BS\\_ViewMasCirculardetails.aspx?id=7373#fin](http://www.rbi.org.in/scripts/BS_ViewMasCirculardetails.aspx?id=7373#fin)



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ceilings have been made for investments in (i) shares and debentures of companies, (ii) PSU bonds, (iii) Commercial Papers (CPs). Apart from above, bank's exposure in capital market, venture capital funds, sector wise industry exposure etc are also regulated in terms of said Circular. The banks are required to constitute an investment committee which will be accountable for all investments made by the banks.

### **63. What are the additional investment restrictions applicable to banking entities under an NOFHC?**

There are restrictions on exposure of banks under an NOFHC in respect of companies under the same promoter group. The group entities may be either under the NOFHC, or other promoter group entities.

As far as entities under the promoter group which are not under the NOFHC (which should primarily be non-financial entities), banks have been prohibited from having any credit or capital exposure at all.

In respect of entities are under NOFHC, banks are permitted to have exposure, however, subject to guidelines of the RBI on intra-group exposures. There are draft guidelines on this<sup>56</sup>. The draft guidelines lay a limit of 10% on a single regulated financial entity, and 20% on all regulated financial entities.

### **64. What are the activities/ business the bank can carry on?**

The general principle in this regard is that para-banking activities, such as credit cards, primary dealer, leasing, hire purchase, factoring etc., can be conducted either inside the bank departmentally or outside the bank through subsidiary/ joint venture /associate. Activities such as insurance, stock broking, asset management, asset reconstruction, venture capital funding and infrastructure financing through Infrastructure Development Fund (IDF) sponsored by the bank can be undertaken only outside the bank. Lending activities must be conducted from inside the bank. However, other regulated financial services entities (excluding entities engaged in credit rating and commodity broking) in which the Promoter/Promoter Group has 'significant influence' or 'control' have to be held under the NOFHC and not under the bank unless it is legally required or specifically permitted by RBI.

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<sup>56</sup> [http://rbidocs.rbi.org.in/rbiadmin/scripts/bs\\_viewcontent.aspx?Id=2564](http://rbidocs.rbi.org.in/rbiadmin/scripts/bs_viewcontent.aspx?Id=2564)



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Further, as per the extant instructions, prior permission of RBI is necessary for the banks to invest in the equity of subsidiaries and financial services entities. Accordingly, banks would require RBI's approval for setting up subsidiaries / joint ventures / associates for conducting activities permitted to banks under Section 6 of the Banking Regulation Act, 1949.

**65. Whether new banks are also liable to comply with priority sector lending guidelines as applicable to all existing banks?**

Yes. Priority Sector targets are based on the adjusted net bank credit (ANBC) outstanding as on 31st March of the previous year. Consequently, if a new bank commences on or after April 1, 201X, the advances at the end of the previous financial year will be nil, and hence priority sector targets will be set based upon the advances at March 31, 201X + 1 and this will need to be achieved by March 31, 201X + 2.

### ***Banking Applications by Existing NBFCs:***

**66. What are the options for existing NBFCs for new banking licenses?**

The options for existing NBFCs are as follows:

- a) Start a bank as a separate entity afresh - in this case, all existing banking business being carried by the NBFC will be transferred to the bank.
- b) Convert the NBFC itself into a bank, if the NBFC is carrying on business which may be carried on by banks departmental.
- c) Convert the NBFC into a bank, and if the NBFC is carrying business which may not be carried by the banks departmental - in this case, the business which is not permitted for banks will be divested into the NBFC

In any case, any NBFC, in which public holds more than 51% percent of voting equity shares, converts itself into a bank it must transfer all its regulated financial services business to a separate company/companies and transfer the shareholding in such companies to the NOFHC and the shareholding of the NBFC after such transfer, should be with the NOFHC as specified in para 2 (C) (ii) and (iii) of the Guidelines.<sup>57</sup>

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<sup>57</sup> Clarification issued by RBI (Q. 71)



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### **67. Which of the above options is better?**

There are lots of factors to be evaluated, primarily the reorganisation of shareholdings. A massive reorganisation exercise is required in every case. In case of listed companies, until SEBI grants an exemption under the SAST regulations, it may be a serious issue to carry major transfer of shares as well. Most transformation of existing companies into banks may need schemes u/s 391, 393 of the Companies Act. The assets and liabilities for the purpose of transfer from one entity to another under restructuring of the existing business will be valued as per the relevant provisions of the applicable laws/ regulations.<sup>58</sup>

### ***Miscellaneous***

### **68. Can the new bank use the brand/ logo or tag line of the Promoter Group?**

Yes. The banks can use the promoter group's brand name / logo or taglines in so far they represent and convey the banking function.

### **69. Can a promoter float two NOFHCs: one, holding all financial entities of the group and one, holding the bank solely?**

Two NOFHCs are not envisaged. Only one NOFHC shall hold the bank as well as all the other regulated financial services entities of the Group in which the Promoter Group has 'significant influence' or 'control'.

### **70. Can the bank carry on the commodity broking business of promoter group companies?**

The commodity broking business is not considered to be regulated financial services for the purpose of the Guidelines, and entities in the Promoter Group which are carrying on commodity broking business cannot be held under the NOFHC.<sup>59</sup>

### **71. In case of change in management and ownership of other regulated financial companies within the group by virtue of transfer to NOFHC, whether intimation to concerned regulator will be appropriate or compliance as per the applicable regulation has to be made?**

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<sup>58</sup> Clarification issued by RBI (Q. 206)

<sup>59</sup> Clarification issued by RBI (Q. 162-163)



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Such companies will have to comply with the applicable regulations and decision of the concerned regulator in this regard would prevail.

### **72. Can the NOFHC hold majority stake in insurance ventures of the Group?**

The capital requirements for the regulated financial services entities held by the NOFHC shall be as prescribed by the respective sectoral regulators.

### **73. What kind of business plan is to be submitted along with the application to RBI?**

The period of business plan to be submitted to RBI has not been specified in the Guidelines. However, the business plan should be realistic and viable and should address how the bank proposes to achieve financial inclusion. It would be desirable to give business plan covering three to five years.

### **74. Whether NOFHC, being NBFC-CIC, shall be allowed to sponsor Company C (a newly incorporated IDF-NBFC) in compliance with the Banking Guidelines?**

Yes, but the NOFHC shall not be permitted to set up any new financial services entity for at least three years from the date of commencement of business of the NOFHC.

### **75. Can a financial company under NOFHC set up a subsidiary where it is legally required for that business to do so?**

Yes, subject to RBI approval and subject to the regulations / approvals of the concerned financial sector regulators.

### **76. Certain financial businesses which can be regulated by banks departmentally or through a separate entity (like merchant banking). Whether such a promoter group financial service company has to be transferred its business to bank or can it carry on independently of the bank?**

Any such promoter group company should come under the NOFHC and not under the bank unless it is legally required or specifically permitted by RBI. The merchant banking activities can be conducted from within the bank or outside the bank under the NOFHC.<sup>60</sup>

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<sup>60</sup> Clarification issued by RBI (Q. 247)





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### **77. Can the promoters infuse further funds in financial companies under the NOFHC?**

Yes, but with prior approval of RBI. The objective of such approval from RBI would be to ensure that all the entities including the bank on stand-alone basis as well as the consolidated bank meet the minimum capital adequacy requirement.<sup>61</sup>

### **78. Can bank issue shares under ESOP?**

Yes. ESOP shares can be issued in compliance with SEBI Guidelines in this regard; however, minimum NOFHC holding is to be maintained at all time.<sup>62</sup>

#### **OTHER RELEVANT ARTICLES YOU MAY LIKE TO SEE:**

- See our analysis on clarifications issued by RBI on bank licensing norms in private sector: [http://india-financing.com/New\\_banking\\_licenses\\_confusions\\_galore\\_in\\_RBI\\_clarifications.pdf](http://india-financing.com/New_banking_licenses_confusions_galore_in_RBI_clarifications.pdf)
- See our presentation on bank licensing norms in private sector at: [http://www.india-financing.com/New\\_Licensing\\_Guidelines\\_for\\_Private\\_Sector\\_Banks.pdf](http://www.india-financing.com/New_Licensing_Guidelines_for_Private_Sector_Banks.pdf)
- See our article on bank licensing guidelines in private sector at [http://india-financing.com/Much\\_awaited\\_guidelines\\_for\\_licensing\\_of\\_private\\_sector\\_banks\\_are\\_finally\\_out.pdf](http://india-financing.com/Much_awaited_guidelines_for_licensing_of_private_sector_banks_are_finally_out.pdf)
- See our write ups on other banking regulations at <http://india-financing.com/banking-regulations.html>
- See our all other staff publications at <http://india-financing.com/staff-publications.html>
- For our other write-ups and analysis on SEBI related issues, you can please click: <http://www.india-financing.com/sebi.html>
- For our other write-ups on issues related to corporate laws, you can please click: <http://www.india-financing.com/staff-publications-corporate-law.html>

<sup>61</sup> Clarification issued by RBI (Q. 306)

<sup>62</sup> Clarification issued by RBI (Q. 308-309)