

Legal Update

Eligibility criteria for Public Financial Institutions made stringent by MCA

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Legal Update

Section 4A was inserted in the Companies Act, 1956 vide Companies (Amendment) Act, 1974 with effect from 1st February 1975 defining Public Financial Institutions (PFIs) for the first time. As per section 4A(2) of the Act, any institution, which is established or constituted by or under any Central Act or not less than 51% of the paid-up share capital of such institution is held or controlled by the Central Government, would become a PFI, if so notified by the Central Government. However, to bring more clarity and to make stringent criteria for a PFI, Ministry of Corporate Affairs vide circular dated **2nd June 2011** had prescribed some additional parameters for an institution to be recognised as a PFI. The conditions as mentioned in the said Circular were as follows:

- A company or corporation should be established under a special Act or the Companies Act, 1956 being a Central Act;
- The main business of the company should be industrial/infrastructural financing;
- The company must be in existence for at least 3 years and their financial statements should show that their income from industrial/infrastructural financing exceeds 50% of their income;
- The net worth of the company should be Rupees One Thousand Crores;
- The company is registered as an Infrastructure Finance Company (IFC) with the RBI or as a Housing Finance Company (HFC) with the National Housing Bank,

It was clarified that Central Public Sector Undertakings and State Sector Undertakings are not required to satisfy the conditions relating to income and net worth stated above.

Further, vide another circular no. **10/2012** dated **21st May 2012**, the Ministry has added the following two points to the existing eligibility criteria of a PFI.:

- NOC from RBI/NHB, in the case of IFC/HFC, with regard to supervisory concerns, if any, must be obtained and enclosed with the application, and
- Such IFCs/HFCs, after being declared as PFI are required to disclose in their audited Financial Statements that they are complying with the directions and conditions laid down by the Ministry.

The above conditions introduced vide the said Circulars in 2011 and 2012 were in addition to what was prescribed under Section 4A of the Companies Act, 1956. The PFIs enjoy various benefits under the Companies Act, the Income Tax Act, Recovery of Debts Due to Banks and Financial Institutions Act among others. Moreover, the PFI can raise funds from insurance companies, mutual funds, provident funds and R-NBCs. Hence, to protect the interest of investors and public at large, it was necessary to control such institutions and some stringent eligibility to be defined. Previously in the absence of strict and defined norms in this regard, various companies were granted status of PFI and were enjoying the above benefits, but surely, after the above circular the companies applying for the PFI status will have to fulfill the above conditions.

It is pertinent to note that the conditions mentioned in both the circulars are applicable to an institution making an application to Central Government for declaring as a PFI and not to the existing PFIs. Even if the existing PFIs do not satisfy the income and net worth criteria, these will continue to enjoy such status and therefore the conditions mentioned in the circulars are to be complied with by the new applicants only.