

# *Analytical Speaking*

## **New set of RBI Directions for Overseas Investment by Core Investment Companies (CICs)**

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The RBI in the year 2011 had issued Non-Banking Financial Companies (Opening of Branch/Subsidiary/Joint Venture/Representative Office or Undertaking Investment Abroad by NBFCs) Directions, 2011 (“**Directions**”) through which norms on Overseas Direct Investment (ODI) by NBFCs were made more stringent compared to other companies. It was presumed that the Core Investment Companies (“**CICs**”), a kind of NBFCs will also be governed by the Directions until such time when the Reserve Bank of India (“**RBI**”) issued draft directions for CICs vide its Notification 2011-2012/1794 dated May 11, 2012.

Until now, CICs (with asset size of less than Rs 100 crores) have been exempted from the regulatory framework and have been kept out of the purview of registration requirements of the RBI. In spite of being a kind of NBFC, the key reason for issuing a separate set of guidelines for CICs can be attributed to the very nature of business of CICs. Simply understood, CICs are NBFCs which invest exclusively in group companies – both financial and non-financial sector, mainly for holding purposes. However, CICs having a total asset size (including assets of other CICs in the group) of Rs. 100 crores or more and raising public funds have been further classified as systematically important CICs (**‘CICs-SI’**) and require registration with the RBI.

Under the present regulatory regime, NBFCs are not permitted to make overseas direct investments (“**ODIs**”). However, considering that CICs are only the group holding companies and as such, do not carry on any other business, a need was felt to liberalize the regime in relation to ODI by a CIC. After a wait of 6 months from the date of issue of draft directions in this regard, the RBI vide its Notification RBI/2012-13/314 dated December 6, 2012 has notified the Core Investment Companies - Overseas Investment (Reserve Bank) Directions, 2012<sup>1</sup> (**‘CIC ODI Directions’**), Thereby allowing CICs to invest overseas up to 400% of their owned funds, subject to the restriction that out of this 400%, not more than 200% of the owned funds should be invested in financial sector. Unlike NBFCs who are prohibited from investing in non-financial sectors, CICs have been allowed to invest in non-financial sector subject to specified conditions.

### **Eligibility Conditions**

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<sup>1</sup> <http://rbidocs.rbi.org.in/rdocs/notification/PDFs/CCN311061212.pdf>



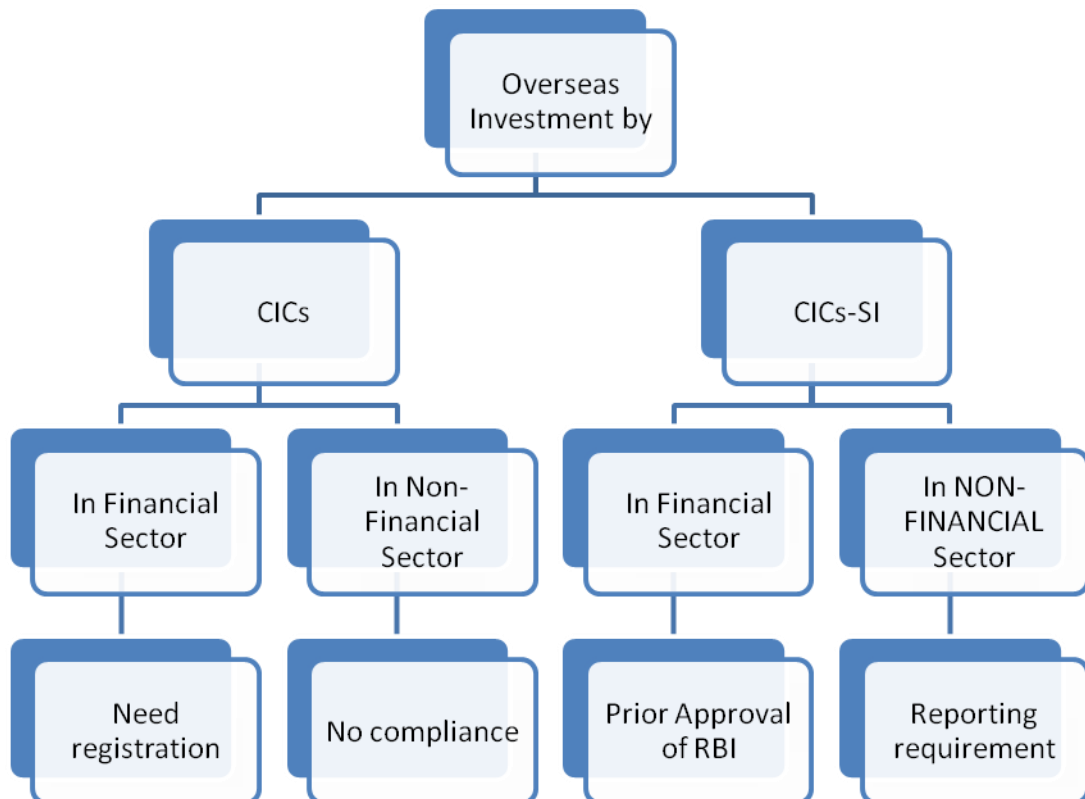
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Every CIC, whether CIC or CIC-SI, is eligible to invest overseas if it is complying with the following eligibility criteria:

1. Maintenance of a minimum adjusted networth to 30% of its aggregate risk weighted assets on balance sheet and risk adjusted value of off-balance sheet items as on the date of the last audited balance sheet as at the end of the financial year;
2. The non performing assets (NPAs) should not be more than 1% of the net advances as on the date of the last audited balance sheet; and
3. CIC should generally be earning profit continuously for the last three years and its performance should be satisfactory during the period of its existence.

### Compliance requirements

The diagram below gives an overview of the CIC ODI Directions:





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### **Investments and Compliances required by CICs**

#### **In financial sector**

Under the CIC ODI Directions, both the CICs and CICs-SI have been treated at par for the purpose of making overseas investments in financial sector. CICs investing in financial sector will be required to hold a certificate of registration (CoR) with the RBI and all regulatory provisions applicable to a CIC-SI including maintaining of Capital Adequacy Ratio (CAR) and leverage ratio will be applicable to such CICs. Apart from this, CICs are also required to comply with general and specific conditions as mentioned in the later part.

#### **In non financial sector**

CICs are free to make investments of any amount in non financial sector without any compliance as these CIC ODI Directions will not be applicable to CICs making investments in non financial sector. Hence, there is no need to comply with any general or specific conditions as laid down in the Directions for making investment in these sectors.

### **Investment and compliances required by CICs-SI**

#### **In financial sector**

The CIC ODI Directions are silent on compliances required by CICs-SI for making investments in financial sector. It would mean compliance with specific / general conditions will be sufficient.

#### **In non-financial sector**

CICs-SI is required to report to the Regional Office of DNBS where it is registered within 30 days of such investment in the stipulated format of quarterly return and also continue to submit the return quarterly.

### **Compliances by 'ALL' CICs Investing Overseas**

All the CICs (whether CIC or CIC-SI) are required to comply with other general and specific requirements as laid down in the CIC ODI Directions, irrespective of registration with RBI and their asset size:



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### **General Conditions:**

In order to make an ODI, CICs would be required to comply with the following general conditions:-

1. Direct investment in activities prohibited under ODI Directions or in sectoral funds will not be permitted.
2. The aggregate overseas investment by any CIC should be < 400% of its net owned funds. Further, the aggregate overseas investment of any CIC in the financial sector should be < 200% of its net owned funds.
3. Investment in financial sector shall be only in regulated entities abroad.
4. Overseas investments by a CIC in financial /non-financial sector would be restricted to its financial commitment. However, a guarantee/comfort letter can be issued only to the overseas subsidiary engaged in non-financial activity
5. CIC which already have non-operating holding companies in existence overseas will need to report the same to the Reserve Bank for a review.
6. SPVs set up abroad or acquisition abroad shall be treated as subsidiary (ies)/joint venture(s) abroad, depending upon percentage of investment in overseas entity.
7. An annual certificate from statutory auditors shall be submitted by the CIC to the Regional Offices certifying compliance of the guidelines.
8. A quarterly return containing the general information of the JV/WOS such as:
  - (a) their financial details,
  - (b) returns obtained during the quarter,
  - (c) aggregate overseas investment of the CIC,
  - (d) net profit of the CIC as per the last audited balance sheet,
  - (e) adjusted net worth, etc,shall be submitted by the CIC to the Regional Office of DNBS and also Department of Statistics and Information Management (DSIM), RBI within 15 days of the close of the quarter.



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9. CICs shall comply with the regulations issued under FEMA, 1999 from time to time.

### **Specific Conditions:**

1. **Opening of Branch-** CICs are not allowed to open branches under the normal course as they are non-operating entities. In case of CICs already opened branches, they should have within 3 months of the Directions approach RBI for review.
2. **Opening of Subsidiary/Joint Ventures Abroad by CICs-**
  - (a) A subsidiary being established abroad should not be a company which does not have significant assets or operations- i.e. it should not be a shell company.
  - (b) The subsidiary should not be used as a vehicle for raising resources for creating assets in India for the Indian operations.
  - (c) The parent CIC shall obtain reviews of the periodical and audit reports about the business undertaken by the subsidiary abroad and shall make them available to the RBI. If the subsidiary abroad is not undertaking any such activity or the periodical and audit reports are not forthcoming then the approval given for setting up the subsidiary shall be reviewed.
  - (d) The permission granted to any CIC for setting up of overseas subsidiary shall be subject to the condition that it shall make disclosure in its Balance Sheet to the effect that liability of the parent entity in the proposed overseas entity shall be limited to its either equity or fund based commitment to the subsidiary.
  - (e) All the operations of the WOS/JV abroad shall be subject to regulatory prescriptions of the host country
3. **Opening of Representative Offices Abroad by CICs-** CICs will need prior approval from the DNBS for opening representative offices abroad for the purpose of liaison work, undertaking market study and research but not undertaking any activity which involves outlay of funds.



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### A quick comparative glimpse of ODI provisions for NBFCs and CICs:

A comparison between the guidelines issued for ODI by an NBFC and a CIC is briefed in the table below:

<b>PARTICULARS</b>	<b>NBFC</b>	<b>CICs</b>
<b>Overseas investment in non-financial sector</b>	NBFCs are prohibited from making any investment in non-financial sector.	Overseas investment by a CIC is not covered by the CIC ODI Directions and CICs-SI are required to intimate to RBI only for their investments in non-financial sector.
<b>Amount of Investment allowed</b>	The aggregate overseas investment is allowed up to 100% of net owned funds.	The aggregate overseas investment allowed is up to 400% of owned funds and in financial sector, investment should not exceed 200%.
<b>Prior approval of RBI</b>	To take NOC from DNBS prior to making any investment overseas.	CICs to only hold a CoR for making such investments. No clear provision for prior approval in case of financial sector. As regards investment in non-financial sector CICs-SI need not take a prior approval but only intimate within 30 days.
<b>Opening of branches abroad</b>	NBFCs are not allowed to open a branch abroad.	CICs in the normal course are not allowed but in case of CICs already opened branches, they should have within 3 months of the directions approach RBI for review.
<b>Subsidiaries abroad</b>	Subsidiaries can be	Subsidiaries/JV can be



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PARTICULARS	NBFC	CICs
	opened by NBFCs however they cannot extend guarantees to them.	opened and guarantees/letter of comfort can be extended to subsidiaries in non financial sector.
<b>Level of NPAs</b>	Not exceeding 5% of net advances.	Not exceeding 1% of net advances.
<b>CRAR requirements</b>	CRAR requirements to be followed after investment by <ul style="list-style-type: none"> <li>- NBFC-D and NBFC-ND-SI – as prescribed by applicable directions (15%)</li> <li>- Other NBFC-ND- at least 10%</li> </ul>	CRAR of at least 30% to be maintained after investment.
<b>KYC norms</b>	Have to comply with the KYC norms.	No such compliance required.

### Our Analysis

The CIC ODI Directions says that ‘all’ CICs will require prior approval of RBI for making overseas investment. However, a reading of these CIC ODI Directions suggests that prior approval is required for investments in financial sector only. Investments by CICs-SI in non financial sectors can be made without any approval and investment by CICs in this sector has been kept out of purview of these Directions. Further, it is not clear when does the ‘prior approval’ is required, i.e. will it be at the time of each investment in financial sector or will be a one time approval for making investment in a particular company/project.

Though CICs are formed for purpose of making long term investments in group, at some point of time, they might need to disinvest its funds in entities abroad, norms for disinvestments or writing off capital by the CICs have not been prescribed in the CIC ODI Directions.





*RBI allows Overseas Investment by Core Investment Companies (CICs)*

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The CIC ODI Directions provide a great relief to CICs making overseas investment in non-financial sector. However, at the same time, CICs having assets size of less than Rs. 100 crores would require to comply with regulations as prescribed for CICs-SI including registration and other operational requirements if they intend to invest in financial sector. Overall, having a separate set of ODI directions for the group holding companies, big groups may now have relaxing breathe!

To see our more write ups on CICs click here:

<http://india-financing.com/core-investment-companies.html>