RBI releases Guidelines for 'on tap' Licensing of Universal Banks in the Private Sector

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In brief

The Reserve Bank of India (RBI) has released the final guidelines (2016 guidelines) for 'on tap' licensing of Universal Banks in the Private Sector on 1 August 2016. The licensing policy is a change from the current 'Stop and Go' policy, where RBI opens the window for bank licences for a limited period. As full-fledged bank licensing will now be on-tap, applications can be submitted to RBI at any time - applicants not found suitable for grant of approval under the 2016 guidelines, however, will not be eligible to apply for three years from the date of the RBI decision.

The 2016 guidelines, mostly in line with the draft guidelines issued in May 2016, lay down the rules for eligible promoters, corporate and holding structure requirements for setting up the bank, corporate governance, prudential and exposure norms, and the process that will be followed by RBI for taking the decision on the applications submitted to it. Unlike the previous guidelines issued in February 2013, for licenses of Universal Banks (2013 guidelines), the RBI has now permitted the Non-operating Financial Holding Company (NOFHC) structure as an option for individual promoters and standalone promoting/ converting entities, instead of making it mandatory.

This insight provides a summary of the 2016 guidelines and a comparison chart of key changes between the 2013 and 2016 guidelines.

In detail

Eligible Promoters

- Individuals/ professionals who are residents[1] and having 10 years of senior level banking and finance experience.
- Entity/ group in private sector that is 'owned and controlled by residents' and having a successful track record of at least 10 years provided that -
  - Non-financial business of such entity/ group should not account for 40% or more in cases where total assets of the entity/ group is more than INR 50 billion.
- Existing Non-Banking Financial Companies (NBFCs) that are 'owned and controlled by residents' and have a successful track record for at least 10 years.

'Fit and Proper' criterion

The Promoter/ Promoter Groups should be 'fit and proper', which would be assessed by RBI on the basis of the following:

- Having a past record of sound credentials and integrity
- Should be financially sound and should have a successful track record for at least 10 years
- In case of individuals – to have minimum 10 years of senior level experience in banking and finance

[1] As defined in FEMA Regulations

- In case of entities/ NBFCs – to have minimum 10 years of experience in running its/ their businesses, financially sound, etc.

Preference will be given to promoting entities having diversified shareholding.

The terms 'Promoter' and 'Promoter Group' have been defined in the guidelines.

Corporate structure

- Structure without NOFHC
  - NOFHC is not mandatory where individuals or standalone promoting/ converting entities do not have any other group entities, and do not propose to establish any other entity after the bank is incorporated
  - In case of setting up or conversion to a bank, any change in shareholding of 5% or more within the promoting entity/ converting entity from date of application has to be reported to RBI.
- Structure with NOFHC
  - NOFHC to be registered with RBI as an NBFC
  - NOFHC to be held only by individuals, non-financial services entities and Core Investment Companies/ investment companies in the group
  - Promoter/ promoter group to hold at least 51% of the total voting equity shares of the NOFHC
  - In case of individuals (belonging to promoter group) holding more than 51% of the shareholding of NOFHC - shareholding by each such individual along with his relatives and entities in which promoters/ relatives hold greater than 50% shares, is capped at 15%
  - Non-promoter holding restricted to 49% of the total voting equity shares of NOFHC
    - In case of individuals (not being a promoter) - shareholding by each such individual along with his relatives and entities in which such individual/ relatives hold greater than 50% shares, is capped at 10%
  - Only promoters/ promoter group should have significant influence and control[2] in the NOFHC
  - NOFHC should hold the bank as well as other regulated financial services entities of the group (in which individual promoters/ group has significant influence or control)
  - NOFHC shall not be permitted to set up new financial services entity for 3 years, except where Subsidiary/ Joint Venture/ Associate of bank is legally required or permitted by RBI
  - Activities that can be conducted departmentally by the bank or through separate structure, *viz.*, Subsidiary/ Joint Venture/ Associate (as required by RBI) may be carried out through separate financial entities under NOFHC. However, promoters desiring to continue existing specialised activities from a separate entity proposed to be held under NOFHC, can do so, with prior RBI approval
  - Activities not permitted to the bank would also not be permitted to be undertaken by entities under the NOFHC
  - Corporate structure should not impede ring-fencing of the financial services entities held by the NOFHC
  - Entities held by NOFHC should be regulated by respective regulators on solo basis
  - Any change in shareholding within the NOFHC that results in acquisition/ transfer of equity capital in excess of 5% of NOFHC will need prior RBI approval

Non-promoters holding in the bank

- No single entity or group of related entities is permitted to have shareholding or control, directly or indirectly, in excess of 10% during the first 5 years of bank's operations
- Large industrial houses[3] are permitted to only own equity up to 10% of the bank on an aggregate basis (without any controlling interest).

Capital requirements

- Minimum capital of INR 5 billion; minimum net worth of INR 5 billion at all times (also applicable to NBFCs converting into banks)

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[2] As defined under Accounting Standards 21 and 23

[3] Means a group with assets of INR 50 billion or more with the non-financial business of the group accounting for 40% or more in terms of total assets/ in terms of gross income.

- 40% of the paid up capital should be held by the NOFHC, and this shall be locked in for 5 years; NOFHC to continue its holding at 40% for any increase in capital within 5 years.
- Shareholding in excess of 40% should be brought down to 40% within 5 years, to 30% within 10 years and to 15% within 15 years
- Bank should maintain a minimum capital adequacy ratio of 13% of its risk-weighted assets for at least 3 years, subject to upward revision by RBI
- On a consolidated basis, NOFHC should maintain a minimum capital adequacy as per Basel norms applicable to the entity
- The bank should be publicly listed within 6 years of commencement of business

Foreign shareholding

- Governed by existing Foreign Direct Investment (FDI) policy subject to minimum promoter shareholding indicated in these guidelines
- Aggregate foreign shareholding should not exceed 74% (under automatic route up to 49%)

Other key considerations

- 25% of new branches should be in unbanked rural areas with a population of less than 9,999 as per the latest census
- Corporate governance, cross-holding norms, prudential and exposure norms, including Priority Sector Lending (PSL) targets as applicable shall need to be adhered to
- The bank has to maintain arm's length relationship with Promoter/ Promoter Group entities as also with major suppliers[4] and major customers of these entities
- Prior approval required for any acquisition of shares/ compulsorily convertible debentures/ bonds/ voting rights where holding aggregates to 5% or more of paid-up equity capital or voting rights of the bank

Procedure for application and RBI decision

- The licensing window will be open on-tap
- A realistic and viable business plan (addressing how the bank proposes to achieve financial inclusion) should be submitted along with application
- After initial screening by RBI, the applications will be referred to a Standing External Advisory Committee (SEAC)
- SEAC will submit its recommendations to the Internal Screening Committee (ISC), consisting of the Governor and the Deputy Governors
- ISC will submit its recommendations to the Committee of the Central Board of the RBI for final decision to issue in-principle approval (valid for 18 months)
- Applicants aggrieved by the RBI decision may appeal within one month from the date of receipt of communication
- Applicants not found suitable for grant of approval will not be eligible to make an application for 3 years from the date of the RBI decision.

Comparison between 2016 and 2013 guidelines

Parameter	2016 Guidelines	2013 Guidelines
Eligible Promoters	• Individuals/ professionals (residents) with 10 years of senior level experience in banking and finance • Entities/ group in private sector (that are resident owned and controlled) with successful track record of at least 10 years; Non-financial business of such entity/ group should not account for 40% or more in cases where total assets of the entity/ group is more than INR 50 billion • Existing NBFCs (that are resident-owned and controlled) with successful track record for at	• Entities/ group in private sector (that are resident owned and controlled) and entities in public sector • Promoter/Promoter group with existing NBFC

[4] Major suppliers and major customers of the promoter group would mean dealings with whom constitute 10% or more of annual purchases or sales or both taken together.

Parameter	2016 Guidelines	2013 Guidelines
	least 10 years; above condition of 40% threshold from non-financial business applicable where NBFC is part of promoter group	
NOFHC shareholding	• NOFHC not mandatory for individuals/ standalone promoters/ converting entities that do not have other group entities • At least 51% shareholding to be held by Promoter/ Promoter group (preferably with diversified shareholding) • Maximum shareholding by each individual belonging to Promoter group in NOFHC - 15%	• Promoter/ Promoter Group to set up bank only through NOFHC • NOFHC to be 100% owned by Promoters/ group (company with 51% public shareholding) • Maximum shareholding of each individual belonging to Promoter group in NOFHC – 10%
'Fit and Proper' criterion	In addition to the conditions stated in the February 2013 guidelines, individual promoters should also have a minimum 10 years of senior level experience in banking and finance	Individual promoters to have a past record of sound credentials and integrity, be financially sound, and have successful track record of running their business for minimum 10 years
Time frame for public listing	Within 6 years of commencement of business	Within 3 years of commencement of business
Dilution of stake	Promoter shareholding to be diluted to: • 30% in 10 years • 15% in 15 years	Promoter shareholding to be diluted to: • 20% in 10 years • 15% in 12 years
Foreign shareholding	As per current FDI regulations (74% in aggregate)	Permitted only up to 49 % in aggregate for the first 5 years from date of licensing
NBFC branches	RBI will consider allowing conversion of all NBFC branches to bank branches, and this can be done only with prior RBI approval	Tier 2 to 6 –Automatic conversion to bank branches Tier 1 – Prior RBI approval required to convert to bank branches
Application screening process	• Application to be reviewed (in given order) by - Initial screening by RBI; - Standing External Advisory Committee; - Internal Screening Committee (consisting of Governor and Deputy Governor); and - Committee of Central Board of RBI • Applicants not found suitable - not eligible to make an application for banking license for 3 years from date of rejection • Aggrieved applicants – Can prefer appeal against RBI's decision to RBI's Central Board of Directors within 1 month of such communication	High Level Advisory to review application

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

Tax & Regulatory Services – Regulatory

Gautam Mehra, *Mumbai*
+91-22 6689 1154
gautam.mehra@in.pwc.com

Akash Gupt, *Gurgaon*
+91-124 330 6509
akash.gupt@in.pwc.com

Bhavin Shah, *Mumbai*
+91-22 6689 1122
bhavin.shah@in.pwc.com

Our Offices

Ahmedabad

1701, 17th Floor, Shapath V,
Opp. Karnavati Club,
S G Highway,
Ahmedabad – 380051
Gujarat
+91-79 3091 7000

Bengaluru

6th Floor
Millenia Tower 'D'
1 & 2, Murphy Road, Ulsoor,
Bengaluru – 560 008
Karnataka
+91-80 4079 7000

Chennai

8th Floor
Prestige Palladium Bayan
129-140 Greams Road
Chennai – 600 006
Tamil Nadu
+91 44 4228 5000

Hyderabad

Plot no. 77/A, 8-2-624/A/1, 4th Floor, Road No. 10, Banjara Hills,
Hyderabad – 500034
Telangana
+91-40 44246000

Kolkata

56 & 57, Block DN.
Ground Floor, A- Wing
Sector - V, Salt Lake
Kolkata – 700 091
West Bengal
+91-033 2357 9101/
4400 1111

Mumbai

PwC House
Plot No. 18A,
Guru Nanak Road(Station Road),
Bandra (West), Mumbai – 400 050
Maharashtra
+91-22 6689 1000

Gurgaon

Building No. 10, Tower - C
17th & 18th Floor,
DLF Cyber City,
Gurgaon – 122002
Haryana
+91-124 330 6000

Pune

7th Floor, Tower A - Wing 1,
Business Bay, Airport Road,
Yerwada, Pune – 411 006
Maharashtra
+91-20 4100 4444

For more information

Contact us at
pwctrs.knowledgemanagement@in.pwc.com

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