

Suggestions and Comments on Report of the Internal Working Group of RBI to Review Extant Ownership Guidelines and Corporate Structure for Indian Private Sector Banks by the Bombay Chamber of Commerce and Industry

15 January, 2021

We thank the Reserve Bank of India (the “RBI”) for this opportunity to present our views and suggestions on the Report of the Internal Working Group to Review Extant Ownership Guidelines and Corporate Structure for Indian Private Sector Banks’ issued on November 20, 2020 (“IWG Report”). The RBI had released the report a little while back and invited suggestions and feedback from various stakeholders. Set out below are our inputs on certain specific recommendations in the discussion paper.

Sl. No	Subject	Rationale / Recommendations
1.	Dilution thresholds and timelines for Promoter shareholding in Banks	<p><u>IWG Report Recommendation:</u></p> <p>The Report recommends that where Large Corporate Houses (“LCH”) intend to convert existing NBFC’s to banks, the promoter/promoter group should dilute their holding in such NBFC to 49% immediately prior to the application for a license and subsequently dilute the promoter stake in the bank to 26% along a more expeditious timeline of 10 years compared to the 15 year time period provided to non – LCHs.</p> <p><u>Concern:</u></p> <p>Several LCHs and Promoter Groups have significantly more than a 49% holding in their respective NBFCs. Requiring an upfront dilution will be onerous and punitive.</p> <p><u>Recommendation:</u></p> <ul style="list-style-type: none"> • The promoting entity of the LCH and the proposed banking entity are required to pass the RBI’s stringent, robust eligibility criteria in order to be considered for a banking license. Such criteria will ensure the high degree of compliance and suitability required by the RBI. • Requiring an LCH to dilute to 49% up front would effectively be a “forced sale” and therefore too onerous and potentially punitive. The focus has to be to ensure adequate capacity for risk capital infusion

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		<p>and on setting up the banking business and accelerated divestment, requirements will detract from focusing on the core banking business.</p> <ul style="list-style-type: none"> As such, maintaining a uniform standard among all applicants would provide a level playing field and, as provided in the 2013 and 2016 guidelines, promoter shareholding in banks may start with 100% and be diluted to 40% within 5 years from the commencement of banking business and 26% within 15 years for all applicants including LCHs as opposed to having different requirements between LCHs and other banking license applicants.
2.	<p>Promoter Shareholding in Non-Operating Financial Holding Company (NOFHC)</p>	<p><u>IWG Report Recommendation:</u></p> <p>The promoting entity shareholding in NOHFC be as per the 2013 guidelines i.e. the NOHFC must be 100% owned by the promoting entity.</p> <p><u>Concern:</u></p> <p>The above is inconsistent with the August 1 2016 RBI Guidelines for 'on tap' Licensing of Universal Banks in the Private Sector wherein the promoting entity's minimum shareholding in NOHFC was established at 51%. Further, in line with 2016 guidelines, a few LCH's had promoted Core Investment Companies (CICs) (that could subsequently be designated as NOFHCs), where the promoting entity shareholding was maintained over 51%, some of which are listed with public shareholding. Hence reverting to the 2013 guidelines where the promoting entity owns 100% of the NOFHC is both inconsistent with the 2016 guidelines and entails significant restructuring challenges, especially for listed CICs.</p> <p><u>Recommendations:</u></p> <ul style="list-style-type: none"> In view of the above, it is requested that the RBI clarify and reconfirm the 2016 guidelines on this topic i.e. existing CICs owned by LCHs may be designated as an NOFHC, if the promoting entity holds at least 51% in such CICs.

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		<ul style="list-style-type: none"> Furthermore, in the event that an LCH has to undertake restructuring in order to comply with the NOFHC structure guidelines, we recommend that the Government should allow for tax neutral restructuring such that the taxation implications of a restructuring do not become prohibitively onerous for an LCH that otherwise is eligible.
3.	<p>Restriction and conflict of interest on Group's exposure to entities under the NOFHC</p>	<p><u>IWG Report Recommendation:</u></p> <p>The NOFHC and the entities held under it shall not have any exposure to the Promoter Group except for the exposure of NOFHC to the entities held under it. In addition, the bank shall not take any exposure on the Promoters / Promoter Group entities or individuals associated with the Promoter Group or the NOFHC, including any financial entities held by the NOFHC.</p> <p><u>Concern:</u></p> <p>It is understood and necessary that the bank be adequately ring-fenced from the promoter and promoter group to restrict conflicts of interest. However, the 2013 NOFHC guidelines require all financial services businesses of the promoter group be housed under the NOFHC. Hence, there could be exposures between such financial services businesses (such as asset management companies / insurance companies) and the promoter group entities. Encompassing other financial services entities, already required to be compliant by their respective government regulators, to additional RBI restrictions is too onerous and duplicative.</p> <p><u>Recommendations:</u></p> <ul style="list-style-type: none"> Exposures to the promoter/promoter group entities by non-bank entities under the NOFHC are well regulated today and are covered under the exposure norms defined by the respective regulators and hence may be permitted to continue within such prudential norms. Further, treasury investments by promoter group entities in products and offering of non-bank entities held under NOFHC (viz. schemes by the asset management company and other products by

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		<p>insurance companies) may be permissible</p> <ul style="list-style-type: none"> • Retail banking services may be provided by the bank to the promoter group entities as they do not result in creation of any group related exposure for the bank
4.	<p>Eligibility for conversion of LCH backed NBFCs into a bank:</p>	<p><u>IWG Report Recommendation:</u></p> <p>LCHs with NBFCs with AuM of over 50,000 cr and over 10 years of operating history will be eligible for conversion to a bank and also lays down a broad set of other safeguards (referencing to 2013 licensing guidelines) to be considered for eligibility.</p> <p><u>Concern:</u></p> <p>LCHs may have aggregate AuM greater than 50,000 cr spread over more than one entity</p> <p><u>Recommendations:</u></p> <ul style="list-style-type: none"> • The RBI should allow the aggregate AuM for the purposes of eligibility on this aspect subject to required restructuring in order to comply with the guidelines of the banking regulation. • Eligibility criteria should be clearly defined to enable a more objective assessment by the prospective applicant before filing for application.
5.	<p>Voting rights on non-equity share capital and timelines for meeting capital adequacy requirements</p>	<p><u>IWG Report Recommendation:</u></p> <p>The Report references the Banking Regulation Act (2013 as amended), which requires that the capital of a banking company consist of equity shares only (which have voting rights) or equity shares and preference shares (which have no voting rights).</p> <p><u>Concern:</u></p> <p>Restricting the forms of capital that a bank may raise will reduce avenues to access pools of capital than can support the bank's capital and thereby, indirectly exclude such pools of capital from supporting the overall banking system.</p>

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		<p><u>Recommendations:</u></p> <ul style="list-style-type: none"> • Extant regulations may be amended to allow voting rights on preference shares and other forms of equity share capital (such as restricted voting shares) <u>only if</u> the minimum capital requirements of the bank have already been met with equity share capital. • Allow a 3-year timeline, as opposed to an upfront requirement, to comply with the maintenance of statutory reserve requirements (viz CRR, SLR etc.) of a bank.
6.	<p>Diversified ownership of the Promoting entity of NOFHC</p>	<p><u>Concern:</u></p> <p>The IWG report and the 2013 and 2016 guidelines do not define the term “diversified ownership” for a promoting entity that holds stake in the NOFHC. Further, the scope of diversified ownership also seems to extend to promoter group entities that hold shares in the NOFHC.</p> <p><u>Recommendations:</u></p> <p>It is important to define ‘Diversified ownership’. RBI may consider the requirement of ‘diversified ownership’ to have been met by an entity if such entity is listed, i.e., having minimum 25% public shareholding.</p> <p>Further, to the extent one or more promoter group entities combined together hold the minimum threshold for promoters’ stake in NOFHC (51% as stipulated in 2016 guidelines), and such promoter group entities have complied with diversified ownership (i.e., minimum 25% public shareholding), then such LCH will be deemed to have met the diversified ownership criterion and hence remaining promoter entities holding smaller stakes in NOFHC need not to separately comply with this criterion.</p>
7.	<p>Obligations of the Promoting entity and the promoter group entities</p>	<p><u>IWG Report Recommendation:</u></p> <p>In order to prevent any conflict of interest due to interconnected lending and exposure between the bank and the promoter group entities, the definition of the</p>

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		<p>promoter group entities has been kept adequately wide.</p> <p><u>Concern:</u></p> <p>While this is a step in the right direction, the obligations of the promoting entity and the promoter group entities should be distinct since the wide definition could cover many group entities (including listed companies) who are not associated with the banking entity of the group</p> <p><u>Recommendations:</u></p> <p>The desired applicants will benefit with more clarity on this topic, particularly, if the guidelines outline and distinguish between the obligations of the promoting entity and the promoter group entities. This becomes critical as the definition of promoter group entities could extend to other operating and / or listed entities that have neither any exposure to nor any shareholding of the bank / NOFHC – so it may be important to know what obligations to which the promoter group entities may be subjected.</p> <p>While guidelines on inter-connected exposure is definitely right governance and should be adhered to, it may be equally prudent to consider the following:</p> <ol style="list-style-type: none"> a. Define the wider implications on / obligations of / on-going compliances by promoter group entities. b. Restrict the implications / obligations/ on-going compliances to only the promoting entity while inter-connected exposure can be applied more universally.