

A globe showing the Americas, with financial data overlays like '100%' and '10%' on a blue background.

RBI comes out with draft guidelines for licensing of new banks in private sector

In his 2011 budget speech, Hon'ble Finance Minister had announced that Reserve Bank of India (RBI) would issue guidelines for banking licences before the close of this financial year. Consequently, RBI has on 29th August, 2011 issued the draft "Guidelines for Licensing of New Banks in the Private Sector" (the Guidelines). The draft Guidelines have been issued for comments from banks, non-banking financial institutions, industrial houses and public. After the comments are received and reviewed, the Guidelines would be finalized and issued. The Guidelines specify various requirements for obtaining banking license, viz., eligible promoters, corporate structure, new bank to be under a non-operative holding company, minimum capital requirements and shareholding structure, foreign shareholding, corporate governance, etc.

The following is a brief summary of the Guidelines:

- ⇒ **Eligible promoters** - Entities/groups, in the private sector, which are owned and controlled by residents, shall be the eligible promoters. Besides, eligible promoters should have diversified ownership, sound credentials, integrity and 10 years' successful track record of running businesses. The entities/groups with 10% or more income or assets or both in the last three years from activities, which are inherently risky and misaligned with banking model, such as, real estate construction and broking activities, shall not be eligible to promote new banks.
- ⇒ **Corporate structure** – A non-operative holding company (NOHC) shall be required to be set up to hold the new bank and other financial services companies of the promoter group. NOHC would act only as the holding company. Individual/entities of the group engaged in non-financial services would only be permitted to hold shares in NOHC. NOHC would be set up as a non banking finance company (NBFC) to be governed by a separate set of prudential guidelines, and would not be allowed to borrow money to invest in companies held by it.
- ⇒ **Minimum capital requirement, etc.** – Minimum initial capital required for new bank is Rs. 500 crore. NOHC shall hold at least 40% paid-up capital for a period of initial five years. Holding in excess of 40% shall be required to be diluted in two years. NOHC's shareholding shall be brought

down to 20% and then to 15% within 10 years and 12 years respectively from the date of licensing.

- ⇒ **Foreign shareholding** – A cap of 49% has been prescribed for foreign holding (FDI, NRI and FII) for first five years. Foreign holding in the bank thereafter shall be as per the prevailing FDI policy. A non-resident shareholder, whether individually or in groups, cannot hold 5% or more of paid-up capital.
- ⇒ **Corporate governance** – At least 50% directors of NOHC should be totally independent of promoters, promoter group entities, their business associates, customers and suppliers. Ownership and management should be separate and distinct in the promoter / promoter group entities that own or control NOHC. Promoter’s funding should be from transparent and verifiable sources. A financial service entity under NOHC shall not be allowed to undertake such activities which are permitted to be undertaken departmentally by the bank.
- ⇒ **Business model** - The proposed business model of the new bank should be viable, realistic and address as to how the bank proposes to achieve financial inclusion.
- ⇒ **Other conditions** - Prior RBI approval shall be required for 5% or more shareholding in the bank by individuals/entities/groups. No entity except NOHC can hold more than 10% shares in the bank. Bank’s exposure to entities in promoter group has been capped at 10% and 20% of its paid-up capital and reserves at individual and aggregate level respectively. Listing of the bank in two years of licensing is mandatory. At least one out of four branches has to be opened in unbanked rural areas.
- ⇒ The Guidelines prescribe conditions for conversion of existing NBFC into bank and additional conditions for promoters having 40% or more of their assets/income from non-financial business.

As the Guidelines are at draft level, final version of the same would be issued by RBI once it receives and deals with the comments from various stakeholders.
