LEGAL EYE
YOUR PEEK INTO THE INDIAN LEGAL SCENE

Newsflash dated August 19 2010 *SEBI Update*

Guidelines for Core Investment Companies

Brief Background

In the past there has been a lack of clarity whether investment holding companies are considered as Non-Banking Financial Companies (" **NBFCs**") and whether the laws, rules and regulations applicable to NBFCs are applicable to the investment holding companies as well. The Reserve Bank of India (" **RBI**") decided to bring the investment holding companies under its regulatory framework in view of the implications of access to public funds, directly or indirectly, by such companies. RBI on April 21, 2010 proposed a regulatory framework for such investment holding companies which were categorized therein as Core Investment Companies (" **CICs**"). The draft guidelines were open to comments from experts. The RBI vide its Notification RBI/2010-11/168 dated August 12, 2010 (" **said Notification**") has released the regulatory guidelines for CICs.

Definition of CIC

CICs have been defined via the said Notification.

A CIC has been defined in the said Notification as a NBFC carrying on the business of acquisition of shares and securities which satisfies the following conditions:

1. It holds not less than 90 per cent of its Total Assets in the form of investment in equity shares, preference shares, debts or loans in group companies;
2. Its investments in the equity shares (including instruments compulsorily convertible into equity shares within a period not exceeding 10 years from the date of issue) in group companies constitute not less than 60 per cent of its Total Assets;
3. It does not trade in its investments is shares, debt or loans in group companies except through block sale for the purpose of dilution or disinvestment;
4. It does not carry on any other financial activity referred to in Section 45-1(c) and 45-I(f) of the RBI Act, 1934 except investment in bank deposits, money market instruments, government securities, loans to and investments in debt issuances of group companies or guarantees issued on behalf of group companies.

The RBI has thus decided that investments in securities even without an intention to trade in such securities will be regarded as a NBFC activity but at the same time has recognized that CCIs need different treatment as compared to other NBFCs as they are companies which have their assets mainly as investments in shares for holding stake in group companies and do not undertake any financial activity.

Certain parameters like Total Assets have been clearly defined in the said Notification.

Applicability

- CICs having an asset size of Rs.100 crore and above [Systemically Important CICs] (" **CIC-ND-SI**") or
- CICs belonging to a group, where the aggregate assets of all such CICs is more than Rs. 100 crore

shall be regulated by the said Notification and would be required to make an application to RBI within six months of the said Notification to obtain a Certificate of Registration (" **CoR**") under Section 45-1A of the Reserve Bank of India Act, 1934 (irrespective of the fact that such CCI was earlier specifically exempted from seeking a registration by the RBI). Pending disposal by the RBI of such application, CCIs may continue to carry on its existing business.

It has been clarified that the companies to whom the guidelines is applicable will be in contravention of Section 45-IA if it fails to apply to the RBI for the CoR within the stipulated time.

Non-Applicability

CICs having an asset size of less than Rs. 100 crore do not fall within the purview of the said Notification and need not apply for CoR. If the asset size of such CICs equals to Rs. 100 crore then it would be required to apply for CoR within three months of such event.

Requirements

- The Capital Requirements envisaged for a CIC-ND-SI is to maintain a minimum Capital Ratio whereby its Adjusted Net Worth shall not be less than 30% of its aggregate risk weighted assets on balance sheet and risk adjusted value of off-balance sheet items as an the date of the last audited balance sheet as at the end of the financial year.
- Each CIC-ND-SI is to ensure that it' s Leverage Ratio i.e. its outside liabilities at all times shall not exceed 2.5 times its Adjusted Net Worth as on the date of the last audited balance sheet as at the end of the financial year.

A CIC-ND-SI which, is unable to comply with the capital requirements and leverage ratio, may approach the regional office of the RBI in whose jurisdiction it is registered with an action plan for compliance with these conditions. The RBI in such a case may examine the action plan submitted and impose such conditions and / or restrictions, as it deems fit. It is not clear whether the same would be on a case to case basis or whether the RBI would come out with further guidelines on the same.

A CIC-ND-SI which adheres to the requirements regarding capital requirements and leverage ratio, may to the extent necessary, be exempted from compliance with (i) maintenance of statutory minimum Net Owned Fund (NoF) and (ii) requirements of Non-Banking Financial (Non-Deposit Accepting or holding) Companies Prudential Norms (Reserve Bank) Directions, 2007 including requirements of capital adequacy and exposure norms.

Compliance

CIC-ND-SIs are required to submit an annual certificate from their statutory auditors regarding compliance of the guidelines as stipulated in the said Notification within one month from the date of finalization of balance sheet.

Conclusion

The said Notification is a consolidated progressive right regulation. It is a liberal guideline and will help in clearing controversies surrounding CICs in the past. The said Notification will help to bring clarity and certainty in regulation.

For any update please contact our Private Equity Team.

[TOP]

CONTACT US	SUBSCRIBE	UNSUBSCRIBE	DISCLAIMER