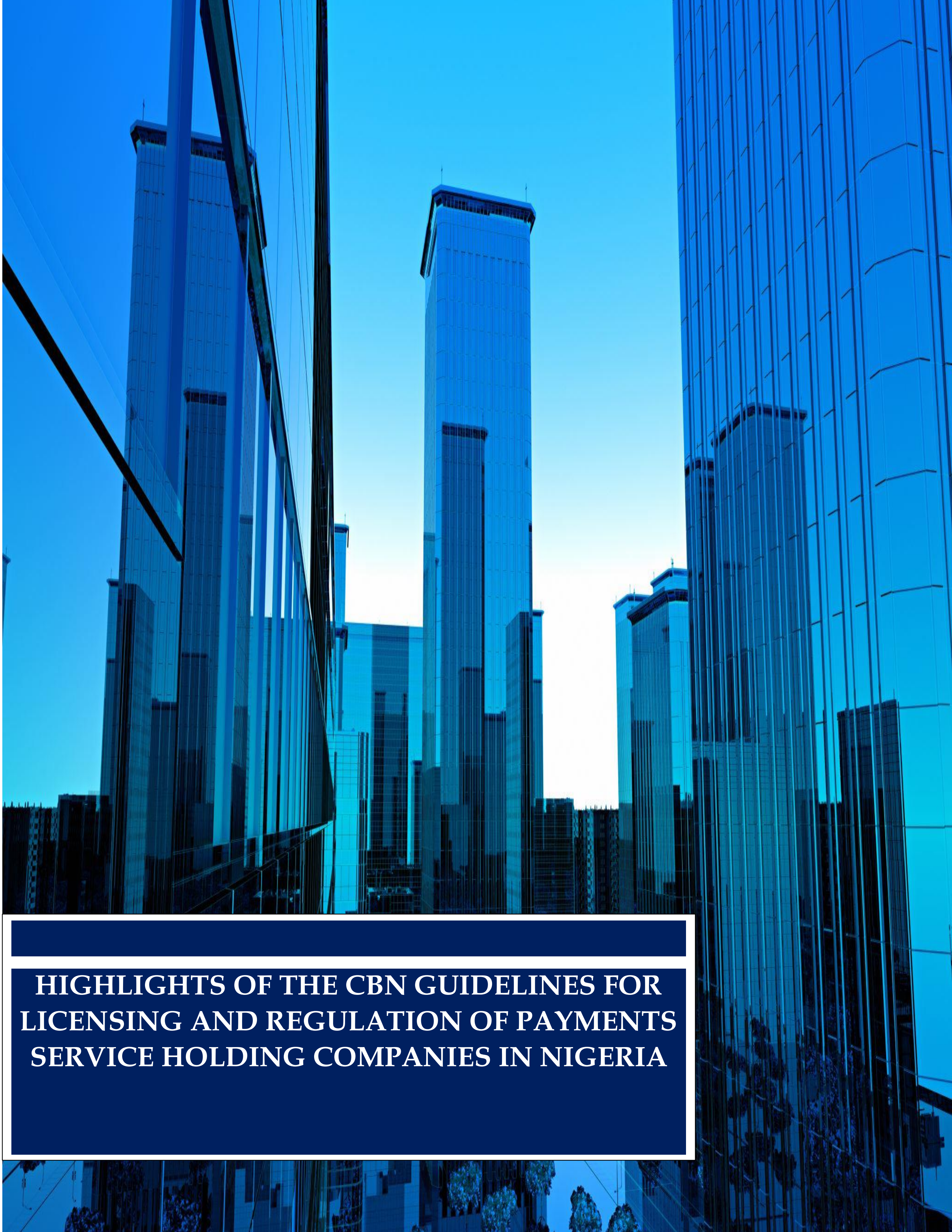

HIGHLIGHTS OF THE CBN GUIDELINES FOR LICENSING AND REGULATION OF PAYMENTS SERVICE HOLDING COMPANIES IN NIGERIA

In exercise of its powers under the Central Bank of Nigeria Act, ("CBN") issued the Guidelines for Licensing and Regulation of Payments Service Holding Companies in Nigeria (the "Guidelines"). This is a follow up to the approved new licence categorizations for participants in the payments system, issued by the CBN on 24 May 2021 which requires companies desirous of operating more than one licence category to set up a Payments Service Holding Company (PSHC), clearly delineating the activities of its subsidiaries. The rationale behind this arrangement is *to prevent commingling of activities, facilitate management of risks and enable the CBN exercise adequate regulatory oversight on all companies operating within the group.*

We shall in this review highlight the salient provisions of the Guidelines and the overall implications for industry players.

2. <u>The Corporate Structure of a PSHC</u>

A PSHC is defined in the Guidelines as a company whose principal object clause include the business of a holding company set up for the purposes of making and managing equity investment in two or more companies, being its subsidiaries, which are payments service providers across Mobile Money Operations (MMO), Switching and Processing operations and Payment Solution Services.

Understandably, a PSHC though a corporate body registered with the Corporate Affairs Commission ("CAC") is not allowed to operate any business. However, it may invest in its subsidiaries without engaging in their management and regular businesses. The composition of its board must be between 5 to 10 or as may be determined by applicable CBN Corporate Governance Guidelines.

As a holding company, it must have a minimum of two subsidiaries, which include a MMO and a switching company. Where the PSHC decides to focus on just one line of payment service, it is obligated to obtain the prior approval of the CBN. It may also acquire the controlling interest in any permissible financial and or technological company, provided that where the controlling interest is equivalent to a minimum of 51% of the issued share capital of the company, the prior approval of the CBN must be obtained.

The CBN, in exercise of its regulatory functions, may also direct a PSHC to divest from a subsidiary if the PSHC is being run in a manner that is detrimental to the subsidiary and or the stability of the financial system. There are no stated objective parameters for determining whether the PSHC is being managed in a manner that is detrimental to the subsidiary and or the stability of the financial system. The Guidelines expressly empowers the CBN to take a subjective opinion in such situations. Our view is that this is subject to abuse and may in the long run be counterproductive.

3. <u>Requirements for Obtaining a PSHC Licensing</u>

The process of obtaining a licence is comprised of two phases – Approval-in-Principle ("AIP") and Final Licence. The first phase is commenced by the submission of a formal application (addressed to the Director, Payments System Management Department of the CBN) for the grant of a licence. The Guidelines recognise that financial holding companies with a payment service provider as a subsidiary, that were licensed prior to the issuance of the Guidelines need not apply for a fresh PSHC licence. However, one would assume that save for the issuance of a PSHC licence, the operations of such financial holding companies in relation to the payment service provider subsidiaries will be in accordance with the provisions of the Guidelines.

3.1. Grant of AIP

The Guidelines set out a long list of requirements for the grant of AIP, some of which are:

a. A non-refundable application fee in the sum of N1,000,000.00 (One Million Naira) or such other amount as the CBN may specify from time to time.

b. Evidence of meeting the prescribed minimum paid-up capital of the PSHC. Where the PSHC is the sole shareholder of the subsidiaries, the minimum paid-up capital of the PSHC shall exceed the sum of the minimum regulatory capital/total equity of all its subsidiaries. However, if the PSHC owns less than 100% of the paid-up capital of the subsidiaries, its minimum paid-up capital shall exceed the sum total of the PSHC's proportionate equity holding in the subsidiaries. As a holding company, its capital is applied to the subsidiaries proportionately and excess capital in one subsidiary cannot be applied to cover a deficit in the capital of another subsidiary.

c. Business plan or feasibility report.

d. An undertaking by the promoters that the PSHC shall be adequately capitalized for the volume and character of its business at all times, and that the PSHC shall be under the supervisory authority of the CBN as an Other Financial Institution ("OFI").

e. For regulated foreign institutional investor, a letter of no-objection from the regulatory body in the home country of the investor.

f. Shareholders' agreement executed between the PSHC and its shareholders.

g. Statement of intent to invest in the PSHC by each investor in the PSHC.

h. Technical Services Agreement, where applicable.

i. Draft copy of the Memorandum and Articles of Association of the PSHC.

Other required information and documents can be accessed here.

4. Grant of Final Licence

The application for grant of final licence must be submitted within six months following the grant of AIP. The application should be accompanied with the following documents:

a. Non-refundable licensing fee in the sum of N5,000,000.00 (Five Million Naira).
b. Evidence of promotion or investment of a payment service company.
c. Evidence of location of head office of the PSHC.
d. Schedule of changes, if any, in the board, management, IT infrastructure and significant shareholding since the grant of AIP.
e. Evidence of ability to meet technical requirements and modern infrastructural facilities required for PSHC operations and meet CBN and other regulatory requirements.
f. Organizational structure of the PSHC
g. Board and staff training programme.

5. Requirements for Commencement of Operations

When the PSHC is ready to commence business, it is required to inform the CBN in writing with the following documents enclosed:

a. Shareholders' register;
b. Share certificate issued to each investor
c. Enterprise Risk Management Framework
d. Internal Control Policy;
e. Minutes of pre-commencement board meeting;
f. Opening statement of affairs signed by the directors and auditors; and
g. Date of commencement of activities.

6. <u>Corporate Governance Compliance</u>

The management of a PSHC is subject to the Corporate Governance Guidelines issued by the CBN from time to time. In addition, appointments to the board and management positions of the PSHC must be in line with the requirements of the Assessment Criteria for Approved Persons' Regime for Financial Institutions or any other applicable regulation issued by the CBN. Similarly, the regulations on the disqualification of board and management, applicable to OFIs will apply to PSHCs. Specifically, the Guidelines require the board of directors of a PSHC to include at least one person with requisite experience in the businesses of the subsidiaries within the group.

7. <u>Ownership and Control of PSHC</u>

The Prior approval of the CBN is required for any shareholding of <u>five (5) percent</u> and above, or any change in ownership which results in change in control of the PSHC.

The subsidiaries of a PSHC are not allowed to acquire shares in the PSHC neither are subsidiaries allowed to acquire shares of other subsidiaries of their parent PSHC. These restrictions are extended to subsidiaries of intermediate companies.

If a PSHC loses control of any of the two payments services subsidiaries (Switching & Processing company or MMO) for more than six consecutive months, the PSHC will be required to return its licence to the CBN for cancellation and henceforth, will cease to be a PSHC. The same consequences will apply in the case of a PSHC with only two subsidiaries which loses its controlling interest in either of the subsidiaries for more than six consecutive months. In both circumstances, the PSHC shall divest completely from that subsidiary within six months or any other period as may be advised by the CBN to enable the subsidiary to continue to operate as an independent entity.

Similarly, the Guidelines, unless with the prior written approval of the CBN, prohibits a director, shareholder, agent, or any instrumentality of a PSHC from entering any agreement or arrangement:

a. that will result in (a) a change in the control of the PSHC and (b) the transfer of shareholding of 5 percent and above in the PSHC. Where such change in control or transfer of shares is effected through the secondary market, the PSHC is required to notify the CBN within seven days following the transfer.

b. for the sale, disposal or transfer of the whole or any part of the business of the PSHC.

c. or the issuance of new shares

d. for the amalgamation or merger or takeover of the PSHC with any other person.

e. for the reconstruction of the PSHC or

f. to employ a management agent or to be managed by or to transfer its business to any such agent.

8. Permissible Activities

The activities of a PSHC are restricted to the holding of equities in financial and technological subsidiaries that facilitate and/or enhance innovative digital financial services. It may, however, with the prior written approval of the CBN, provide policy direction, shared services and/or enter technical or management service contracts with any of its subsidiaries in respect of human resources service; risk management services; internal control services, ICT, legal services; facilities management, and any other services as may be approved by the CBN from time to time.

The shared services are to be provided on arm's length basis and the prior consent of the Board of Directors of the subsidiary must be obtained before the transactions relating to same will be executed.

9. Non-Permissible Activities

A PSHC is prohibited from engaging in the following activities:

a. Establishment, divestment and closure of subsidiaries, without the prior written approval of the CBN.
b. Deriving or receiving income from sources other than as listed in the Guidelines
c. Dividend income from its subsidiaries/associates;
d. Income from shared services, where applicable;
e. Interest earned from idle funds invested in government securities or placement with licensed financial institutions;
f. Patents, royalties and copyrights;
g. Profit on divestment from subsidiaries/associates; and,
h. Any other source as may be approved by the CBN.

Additionally, a PSHC is not allowed to:

a. Arrogate to itself any of the powers or functions of the Board of Directors, or
b. internal management responsibilities and obligations, of any of its subsidiaries or associates of any such subsidiary;
c. Interfere in the day-to-day activities of the subsidiaries;
d. Be involved in the administration and approval process of its subsidiaries, if applicable;
e. Require its subsidiaries or any of its agents to take directives or act on the instructions of the PSHC in its internal decision-making process;
f. Have any of its officers or employees, while in the employment of the PSHC, work for any subsidiary, except employees engaged in shared services arrangements;
g. Engage the services of any employee of any of its subsidiaries;
h. Purchase/dispose assets from/to its subsidiaries, without the prior written approval of the CBN.
i. Engage in any transaction or maintain any business relationship with any of its subsidiaries, except such transaction or business relationship is at arm's length;
j. Borrow from the Nigerian banking system for the purpose of capitalizing itself or any of its subsidiaries;
k. Appoint as a director, any person, who at the relevant time is a director

of any of its subsidiaries, except with the prior written approval of the CBN. However, where such appointment is approved, the aggregate number of directors from the subsidiaries and associates, at any point in time, shall not exceed 30% of the membership of the Board of Directors of the PSHC.

l. appoint a person who has served as a director (executive or non-executive) for the maximum allowable period as stipulated by the CBN, into any subsidiary, or an associate of such a subsidiary until after a minimum period of three (3) years following the expiration of the tenure of such director, and vice versa;

m. appoint a serving director of the PSHC as a director of the subsidiary, except with the written approval of the Central Bank of Nigeria. Where such appointment is approved, the number of directors from the PSHC, at any point in time, shall not exceed 30% of the membership of each of the subsidiaries.

10. Acquisition of Subsidiaries

A PSHC is allowed to acquire subsidiaries. However, for the CBN to give its approval, it must be satisfied that the PSHC has adequate capital resources by way of free funds to carry out the acquisition.

11. Limit on Contingent Liabilities

A PSHC's total exposures on contingent liabilities on behalf of its subsidiaries shall not exceed 20% of the PSHC's shareholders' funds unimpaired by losses.

12. Remarks

The Guidelines is a right step towards achieving the CBN's commitment to promote an efficient payment system in Nigeria and provide a clear direction for operations in that sector. The CBN had on 24th day of May 2021 issued a new regulation which consolidated the requirements for the licensing of payment service providers. Our review of the regulation can be accessed here. The Guidelines provide clarity to players in that space who may be desirous of providing more than one category of payment service. Again, a significant point to note is that PSHC's can, subject to the prior approval of the CBN, acquire (controlling) interests in permissible financial and/or technology companies. The implication of this, which is laudable, is that there would be opportunities for players in the financial and technology sectors to broaden their scope of operations and enhance productivity for overall positive impact on the economy.

<u>NOTE</u>: *No part of this article should be relied upon as legal advice. It is only intended as a general guide on the subject and as such, we advise that you consult a specialist where legal advice is desired. For further information on the subject and any other real estate related questions, kindly contact us at* info@lexsetters.com.

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