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Highlights of the Central Bank of Nigeria (CBN) Guidelines for Licensing and Regularisation of Payments Service Holding Companies in Nigeria

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Introduction

Following the New Licence Categorisations[1] within the Nigerian Payments System (NPS), The Central Bank of Nigeria (CBN) on 3rd August 2021 released a circular on the new guidelines for the licensing and regulation of Payments Service Holding Companies in Nigeria (the "Guidelines").

1. What does the CBN hope to achieve with the Guidelines?

The Guidelines mandate companies that wish to operate more than one licence category to set up a Payments Service Holding Company ("PSHC") and distinctly separate each of its subsidiaries.

According to the CBN, this will better aid the regulator in managing potential and risks and achieve adequate regulatory oversight of the companies operating within the Group structure.

2. What kind of companies do the Guidelines apply to?

The Guidelines are directly applicable to companies in the regulated payment sectors, and more specifically; Mobile Money Operations, Switching and Processing, Payment Solution Services and any other activity as may be approved by the CBN.

3. What is a PSHC?

A PSHC is a company whose, in accordance with the Guidelines, main objective shall be operating as a "holding company[2]" to make, hold and manage equity investment in two or more companies, as its subsidiaries[3], that carry on business as payment service providers[4] (the **"Subsidiaries"**). In the CBN Circular dated 9th December 2020 on the new license categorization for the Nigerian payments systems, the CBN has streamlined payments system licensing, in accordance with permissible activities, into the following four broad categories: Switching and Processing (**"S & P"**), Mobile Money Operations (**"MMOs"**), Payment Solution Services (**"PSS"**), and Regulatory Sandbox (the **"Streamline"**). In accordance with the Streamline, the Guidelines have provided that the payment service activities affected are MMOs, S & P, PSS. The Guideline, therefore, provides that for the PSHC to emerge, there shall be at least 2 (two) Subsidiaries engaged in MMO (**"Mobile Money Operator"**) and S & P (**"Switching Company"**).

4. About the PSHC structure

The Guidelines stipulate that a PSHC shall be a non-operating corporate entity registered at the Corporate Affairs Commission (CAC) and licensed by the CBN formed solely to hold investment in the Subsidiaries via a "parent-subsidiary" structure, and which PSHC shall not interfere in the day-to-day operations of the Subsidiaries.

A PSHC shall have a minimum of two Subsidiaries, which Subsidiaries shall be at least a Mobile Money Operator and a Switching company. The PSHC shall have board size of between 5 (five) and 10 (ten) board members or as prescribed by the CBN Corporate Governance Guidelines[5].

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[1] (ref: PSM/CIR/GEN/CIR/01/22)
[2] Which is as defined by Section 381 of the Company and Allied Matters Act, No. 3 2020
[3] Ibid.
[4] Which is as defined in Section 131 of the Banking and Other Financial Institution Act 2020 as an entity licensed by the CBN to provide technical or technology infrastructure, software solutions or services or facilitating end-to-end electronic payment to third parties and such other services as the CBN Governor may by regulation designate.
[5] In constituting the Board of Directors of a PSHC, consideration shall be given to core competencies in the areas of operation of the subsidiaries.

A PSHC is permitted to have only two hierarchies which makes it permissible for it to have a Subsidiary which is a parent to another Subsidiary (intermediate company). It may acquire controlling interest in any permissible financial and/or technological company, subject to prior approval of the CBN, where controlling interest represents a minimum of 51% of authorised share capital of the entity.

If a PSHC elects to change to mono-line payments service provider, it shall seek the prior approval of CBN and submit along with its request for approval the following:

a. Annual audited financial statements of the immediate past three years under the arrangement/structure it seeks to discontinue;

b. Divestment plan from Subsidiaries; and

c. Any other requirements as may be determined by the CBN from time to time.

5. How to obtain a PSHC Licence

A formal application addressed to the Director, Payments System Management Department is required to be submitted by the promoters of a PSHC for the grant of a licence which is processed in two phases; **Approval-In-Principle**[6] and **Final Licence**[7].

It is important to note that a Financial Holding Company[8], with a payment service provider as a Subsidiary, that had been licensed prior to the issuance of these Guidelines, needs not apply for a PSHC licence.

6. CBN's expectations of a PSHC

Upon commencement of the PSHC's operations, the CBN primarily expects a PSHC to comply with relevant guidelines and regulations issued by the CBN, relevant extant laws and the provisions of the Securities and Exchange Commission ("SEC"), Corporate Governance Guidelines for publicly quoted companies and listed entities in Nigeria (where applicable), maintain adequate accounting systems, keep records that capture all information which reflect the financial condition of the PSHC and ensure that it and all its Subsidiaries are adequately capitalised at all times and render returns to the Payments System Management Department of the CBN on a quarterly basis, or in frequency and format, as may be prescribed from time to time on the information requested in the Guidelines.

A PSHC is also expected to maintain financial flexibility and capital-raising capabilities to support its Subsidiaries and also be able to provide and use its available resources to augment the capital of its Subsidiaries, in the event of financial stress or adverse conditions. However, a PSHC shall not be allowed to borrow from the Nigerian banking system for the purpose of capitalizing itself or any of its subsidiaries.

[6] Promoters of a proposed PSHC shall not incorporate the company until an Approval-in-Principle has been obtained from the CBN, a copy of which shall be presented to the CAC for that purpose. Subsequent to the issuance of the Approval-in-Principle, the promoters may proceed to carry out the activities stated in the Approval-in Principle.

[7] PSHC licences shall be granted for an indefinite period of time or such period as the CBN deems necessary and shall not be transferable.

[8] Pursuant to Extraordinary Gazette No. 38 of December 29, 2011, a financial holding company is a company whose principal object includes the business of a holding company set up for the purpose of making and managing equity investment in two or more companies, being its subsidiaries, engaged in the provision of financial services, one of which must be a bank. Bank means commercial, merchant or specialized bank

7. Ownership and Control

In the event that there is an ownership of 5% and above or any change which results in the change of control of the PSHC, the prior approval of CBN must be obtained.

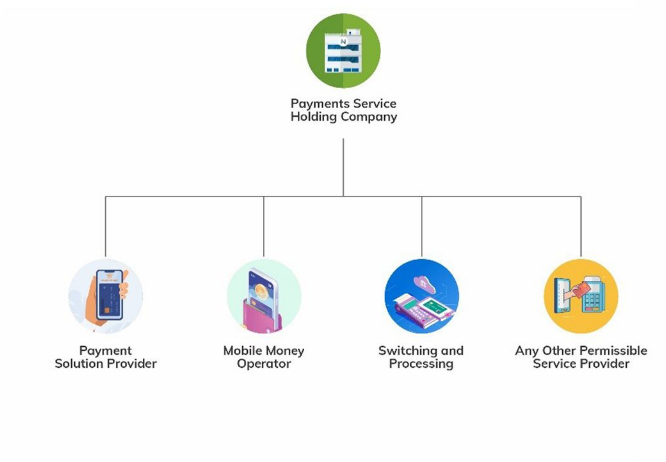
The Subsidiaries are prohibited from acquiring shares in the PSHC and from acquiring shares of other Subsidiaries of their parent PSHC.

8. What are the Possible PSHC Structures?

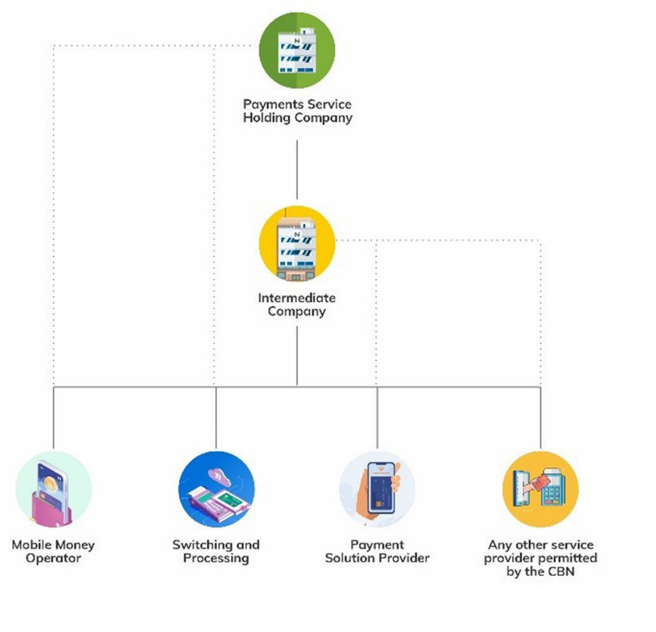
As highlighted above, the PSHC Structure is triggered where the PSHC has a minimum of two Subsidiaries, which must include a Mobile Money Operator and a Switching Company See Diagram 1.

A PSHC is only permitted to have only two hierarchies where there is an intermediate company which is a subsidiary to the PSHC (the "**Primary Subsidiary**"), which Primary Subsidiary is in turn parent company to another Subsidiary(ies). See Diagram 2

CORPORATE STRUCTURE 1



CORPORATE STRUCTURE 2



9. What is the Minimum Capital Requirement for a PSHC?

The Guidelines provide that where a PSHC owns 100% of its Subsidiaries, it will be required to have a minimum paid-up capital which exceeds the minimum regulatory share capital/ total equity of all its Subsidiaries, as may be prescribed from time to time by the Central Bank of Nigeria.

Where, however, the PSHC owns less than 100% of its Subsidiaries, its minimum paid-up capital must exceed the aggregate of its proportionate holding in the Subsidiaries.

10. Change in ownership structure

Should a PSHC lose control of any of its two Subsidiaries (either MMO or Switching company) for a period exceeding six (6) consecutive months, the PSHC shall cease to be a PSHC and will be required to return its licence to the CBN for cancellation. Subsequent to the cancellation of its licence, the PSHC shall divest wholly and completely from that Subsidiary within a period of six (6) months or any other period as may be determined by the CBN, to enable the Subsidiary continue operations as an independent entity.

Where a PSHC with only two Subsidiaries, loses its controlling interest in either of the Subsidiaries, for a period exceeding six (6) consecutive months, the PSHC shall cease to be a PSHC and will be required to return its licence to the CBN for cancellation.

In the event of either of the afore stated, the former and the latter shall continue to operate independent of one another.

11. What are the permissible activities of a PSHC?

The permissible activities of a PSHC are:

- investment in and hold equities in approved Subsidiaries, provided that the PSHC do not engage in the day-to-day management and operations of the Subsidiaries;

- hold equities in financial and technological subsidiaries that facilitate and/or enhance innovative digital financial services. Hence, the PSHC can invest in other technological companies (such as software and hardware development firms) and financial companies (such as micro-finance banks and finance companies) whose assets and operations can be integrated into the PSHC Structure for the purpose of facilitating and enhancing innovative digital financial services;

- provide broad policy direction, shared services and/or enter into technical or management service contract with any of its Subsidiaries, subject to obtaining the prior written approval of the CBN, in respect of the specified areas. In this regard, the PSHC can provide the following shared services to its Subsidiaries:

  - Human Resources services;
  - Risk Management services;
  - Internal Control services;
  - Compliance services;
  - Information and Communication Technology;
  - Legal services;
  - Facilities (office accommodation including electricity, security, cleaning services in that accommodation); and,
  - Any other services may be approved by the CBN from time to time.

  The above services shall be collectively as **"Shared Services"**.

12. Non-Permissible activities of a PSHC

A PSHC is expressly prohibited from undertaking the establishment, divestment and closure of Subsidiaries, without the prior written approval of the CBN and deriving or receiving income from sources other than as stipulated by the Guidelines.

13. What are the permissible activities of a PSHC?

A PSHC is allowed to generate revenue through:

- dividend from its Subsidiaries;
- income from Shared Services provided to Subsidiariespatents, royalties and copyrights, especially where the intellectual property and proprietary technologies are housed in the PSHC and then licensed to the Subsidiaries via license arrangement. However, the fees payable under the licensing arrangement must reflect an arms' length transaction under the Income Tax (Transfer Pricing) Regulations 2018 ("Transfer Pricing Regulations");
- interest earned from idle funds invested in government securities or placement with licensed financial institutions;
- profit on divestment from Subsidiaries/associates (where such divestment from its subsidiary is approved by the CBN);
- and any other source as may be approved by the CBN.

14. What are the permissible activities of a PSHC?

A PHSC must ensure that it attends to requisite qualifications before it can declare dividends to shareholders. It must ensure that all its operational, preliminary, and organisational expenses and losses incurred and other capitalised expenses, not represented by tangible assets (excluding goodwill), have been completely written off. In addition, it must ensure that adequate provisions have been made to the satisfaction of the CBN for actual and contingent losses. and ensure it has complied with any capital requirements before it can declare dividends.

15. When does a PSHC cease to be Characterized as a PSHC?

A PSHC ceases to be characterized as a PSHC when:

- When it loses control of any of its Subsidiaries being a Mobile Money Operator and a Switch Company for a period exceeding six consecutive months;
- Where a PSHC with only two Subsidiaries, loses its controlling interest in either of the Subsidiaries, for a period exceeding six consecutive months.

Where a PSHC ceases to be characterized as highlighted above, the PSHC shall be required to return its licence to the CBN for cancellation and shall subsequently divest wholly and completely from the relevant Subsidiary within a period of six months or any other period as may be determined by the CBN, to enable the Subsidiary continue operations as an independent entity. Furthermore, where the affected Subsidiaries are a Switching Company and/or a Mobile Money Operator, the affected Subsidiary(ies) shall continue to operate independent of one another.

16. Can there be Cross-Shareholding between a PSHC and the Subsidiaries

No, Subsidiaries including the Intermediate Company of a PSHC cannot acquire shares in the PSHC. Furthermore, Subsidiaries cannot acquire shares in other Subsidiaries including the Intermediate Companies.

17. To What Extent is Cross Directorship between the PSHC and its Subsidiaries Permissible?

The Guidelines emphasizes the need to uphold the extant CBN corporate governance regime. Hence, subject to the written approval of the CBN, a PSHC is not permitted to appoint as director, any person, who at the relevant time is a director of any of its Subsidiaries. Where such an appointment is approved by the CBN, 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. Similarly, subject to the written approval of the CBN, no director of the PSHC is permitted to act as a director of any of the Subsidiaries. Where such an appointment is approved by the CBN, the number of directors from the PSHC, at any point in time, shall not exceed 30% of the membership of each of the Subsidiary.

It is also important to note that a PSHC is also not permitted to appoint a person who has served as a director 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 after the expiration of the tenure of such director, and vice versa.

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