

BAN ON UNREGULATED DEPOSIT SCHEMES

(C A P N SHAH)

1. BACK GROUND:

The Lok Sabha passed the “Banning of Unregulated Deposit Schemes Bill, 2019”, on 13.02.2019. As the said Bill could not be passed by Rajya Sabha before the Parliament was dissolved, the Hon’ble President has issued an Ordinance called “The Banning of Unregulated Deposit Schemes Ordinance, 2019”, on 21.02.2019. This has come into force on 21.02.2019. The main objective of the Ordinance is to provide for a comprehensive mechanism to ban the unregulated deposit schemes and to protect the interest of depositors. The Ordinance contains a substantive banning clause which bans deposit takers from promoting, operating issuing advertisements or accepting deposits in any unregulated deposit scheme. It creates three different types of offences viz., Running Unregulated Deposit Schemes, Fraudulent default in Regulated Deposit Schemes and Wrongful inducement in relation to Unregulated Deposit schemes. There are adequate provisions for disgorgement or repayment of deposits in cases where such schemes have managed to raise deposits illegally. The Ordinance provides for attachment of properties/ assets of deposit taker by the Competent Authority and subsequent realization of assets for repayment to the depositors. However, there are some controversial provisions in the Ordinance which have created some practical issues. In this article an attempt is made to discuss some of the important provisions of this Ordinance.

2. UNREGULATED DEPOSIT SCHEME:

(i) Section 2(17) of the Ordinance states the an “Unregulated Deposit Scheme” shall mean a Scheme or an arrangement under which deposits are accepted or solicited by any deposit taker by way of business. However, this term does not include a deposit taken under the Regulated Deposit Scheme as stated in the First Schedule to the Ordinance.

(ii) Section 3 of the Ordinance bans any Unregulated Deposit Schemes effective from 21.02.2019. In other words, no deposit taker can directly or indirectly promote or issue any advertisement soliciting participation or enrolment in such Scheme. Further, the deposit taker cannot accept any deposits in pursuance of an Unregulated Deposit Scheme.

(iii) Section 5 of the ordinance provides that no person shall knowingly make any statement, promise or forecast which is false, deceptive or misleading in material facts or deliberately conceal any material facts to induce another person to invest in, or become a member or participant of any Unregulated Deposit Scheme.

(iv) Further Section 6 of the Ordinance states that a Prize Chit or Money Circulation Scheme which is banned under the provisions of the Prize Chits and Money Circulation Scheme (Banning) Act, 1978, shall be deemed to be an Unregulated Deposit Scheme under this Ordinance.

3. **REGULATED DEPOSIT SCHEMES:**

(i). The ordinance does not apply to Regulated Deposit Schemes as mentioned in the First Schedule to the Ordinance. These Schemes are as under:

S.No	Schemes Prescribed by	Regulated Deposit Scheme
(a)	Securities and Exchange Board of India	: Collective Investment Scheme : Alternative Investment Funds : Funds managed by Portfolio Managers : Share Based Employee Benefits : Any other scheme registered under SEBI : Amounts received by Mutual Funds
(b)	Reserve Bank of India	: Deposits accepted by NBFC : Any other scheme registered / regulated with RBI. : Amounts received by Business Correspondents and Facilitators : Amounts received by Authorized Payment System.
(c)	Insurance Regulatory and Development Authority	: Contract of Insurance :
(d)	State Government or Union Territory Government	: Scheme by Co-operative Society : Chit Business under Chief Funds Act, 1982. : Scheme regulated by enactment relating to money lending : Any scheme of prize chit or money circulation scheme ::
(e)	National Housing Bank	: Scheme for accepting deposits under NHB Act, 1987 :
(f)	Pension Fund Regulatory and Development Authority	: Scheme under PFRDA :
(g)	Employees P. F. Organization	: Scheme under EPFMP Act, 1952
(h)	Central Registrar, Multi-State Corporative Society	: Scheme from accepting deposits from voting members
(i)	Ministry of Corporate Affairs	: Deposits under Chapter V of Companies Act, 2013 : Nidhi or Mutual Benefit Society under Section 406 of Companies Act 2013.

(j)	Any Regulatory Body	:	Deposits accepted under any scheme registered with regulatory body
(k)	Central Government	:	Any other scheme as notified by the Government under this ordinance.

(ii) Section 4 of the Ordinance provides that while accepting deposits pursuant to a “Regulated Deposit Scheme” no deposit taker shall commit any fraudulent default in the repayment or return of the deposit on maturity or in rendering any specified services promised against such deposit.

(iii) From the above provisions for Unregulated Deposit Scheme it is evident that the terms (a) Deposit and (b) Deposit Taker are important. It may be noted that merely because a person is covered by the term “Deposit Taker” or loan or advance is covered by the term “Deposit”, it does not mean that such deposit taken by a deposit taker is prohibited by the Ordinance. These two terms defined in the Ordinance are explained in the following paragraphs.

4. **DEFINITION OF “DEPOSIT”:**

The term “Deposit” is defined in section 2(4) of the Ordinance as under:

(i) **Deposit:**

Deposit means an amount of money received by way of an Advance or Loan or in any other form by any Deposit Taker with a promise to return the money after a specified period or otherwise, either in cash or kind or in the form of a specified service. This may be with or without any benefit in the form of interest, bonus, and profit or in any other form.

(ii) **Exclusions:**

However, the following transactions are excluded from the definition of Deposit.

(a) Loan from a Scheduled Bank, Co-operative Bank or any other Banking Company as defined in the Banking Regulation Act, 1949.

(b) Loan or financial assistance received from a notified Public Financial Institution, Regional Financial Institution or Insurance Companies.

(c) Amount received from a State or Central Government or from any other source if it is guaranteed by the Government or from a Statutory Authority.

(d) Amounts received from any Foreign Government, Foreign Bank, Multilateral Financial Institution, Foreign Government owned Development Financial Institutions, Foreign Export Collaborators, Foreign Corporate Bodies, Foreign Citizens, Foreign Authorities or person resident outside India (subject to provisions of Fema, 1999) etc.,

(e) Amounts received as Credit by a buyer from a seller on the sale of any movable or immovable property.

(f) Amounts received by a recognized Asset Re-Construction Company

(g) Any deposit made u/s 34 or an amount accepted by a Political Party u/s 29B of the Representation of People Act, 1951.

(h) Any periodic payment made by the members of the self-help groups recognized by the State Government.

(i) Any amount collected for such purpose as is authorized by the State Government.

(j) An amount received in the course of or for the purpose of business and bearing a genuine connection to such business. This includes the following receipts.

- (i) Payment or Advance for supply or hire of Goods or services.
- (ii) Advance received in connection with consideration of an immovable property
- (iii) Security or Dealership Deposit for contract for supply of Goods or Services.
- (iv) Advance received under Long-term projects for supply of Capital Goods.

The above receipts are subject to the following conditions.

- If the above amounts become refundable, such amount shall be deemed to be Deposits on the expiry of 15 days, if not refunded, within 15 days.

- If the above amount becomes refundable due to the Deposit Taker not obtaining necessary permission or approval under the law to deal in goods or properties or services for which money is taken, it will be treated as a 'Deposit'

(k) Amount received as contribution towards the capital by partner of any Partnership Firm or LLP.

(l) Amounts received by an Individual by way of Loan from Relatives or amounts received by a firm by way of loan from relatives of any of its partners.

For the above purpose the term "Relative" is defined to mean any one who is related to another if they are members of HUF, or is husband, wife, father, mother, son, son's wife, daughter, daughter's husband, brother, or sister of the individual.

It may be noted that this is a very restricted definition as brother's wife, sister's husband, nephew, niece, mother-in-law, father-in-law or near relatives of Spouse are not considered as relatives. Therefore, any loan or advance received from such persons will be treated as a deposit.

5. **DEPOSIT TAKER:**

Section 2(5) of the Ordinance States that a "Deposit Taker" means (i) An Individual or a Group of Individuals, (ii) A proprietorship Concern, (iii) A Partnership Firm, (iv) A LLP (v) A company, (vi) AOP, (vii) A Trust – Private Trust or Public Trust (viii) Co-operative Society or a Multi – State Co-operative Society. (ix) Any other arrangement of whatsoever nature. However, this term does not include (a) A Corporation incorporated under an Act of Parliament or a State Legislature or (b) a Banking Company, SBI, a Subsidiary Bank, a Regional Rural Bank, a Co-operative Bank, or a Multi- State Co-operative Bank.

6. **IMPACT OF THE ORDINANCE ON CERTAIN DEPOSITS:**

Some practical issues arise from the above provisions of the Ordinance. As stated above, if any Loan, Advance or Deposit is taken by a person which falls in the list of Regulated Deposit Schemes the provisions of the Ordinance will not apply. Further, merely because a Loan, Advance or Deposit falls within the definition of 'Deposit' given in the Ordinance it does not mean that it is to be considered as a deposit under the Unregulated Deposit Scheme. What is prohibited under the Ordinance is a loan, advance or deposit taken under the "Unregulated Deposit Scheme" as defined in Section 2(17) of the Ordinance. In other words, if the deposit

taker is not operating any scheme under which deposits are accepted by way of business, such deposit will not be considered as deposit under Unregulated Deposit Scheme. Accepting deposit by way business would mean that the business of the deposit taker is to accept deposits and give the money as loans to others (i.e. Money Lending or Finance business). In the light of the above, some of the practical issues are discussed below:

(i) If an Individual takes a loan of ₹50 Lakhs from his friends for construction of his house, such loan is not prohibited by the ordinance although such loan is considered as a Deposit u/s 2(4) of the Ordinance. This is because under the definition of the term “Unregulated Deposit Scheme” only such deposit which the deposit taker takes by way of business is prohibited. In other words, if the deposit taker is taking loans, advances or deposits for his money lending or finance business and such business is not covered by the definition of Regulated Deposit Schemes, it will be considered as a deposit under the Unregulated Deposit Scheme.

(ii) If an Individual, Firm or LLP takes any Loan, advance or deposit of Rs. One Crore from any person (including a partner of the firm or LLP or a non-relative of such partner) as working capital for the manufacturing or trading business it is not prohibited by the Ordinance. The reasoning is the same as stated in (i) above as the person taking such Loan, advance or deposit is not taking the same for the business of taking deposits. Further, the Deposit taker cannot be considered as having advertised or solicited for taking Loans, advances or deposits. Such receipt is in the course of, or for the purpose of, business and bearing a genuine connection to such business and therefore will not be considered as a ‘Deposit’ u/s 2(4) of the Ordinance.

(iii) If a LLP engaged in construction of residential flats takes an advance from the prospective customers against promise to allot residential flats after construction, the said advance cannot be considered as a deposit taken under the Unregulated Deposit Scheme. This is because the advance is not taken for the purpose of business of taking deposits as stated in (i) above.

(iv) If an individual carrying on business of Money Lending has taken loans, advances or deposits from relatives he will not be considered as having contravened the provisions of the Ordinance since such loans, advances or deposits do not come within the definition of ‘Deposit’ u/s 2(4) of the Ordinance. The same will be the position if such loans, advances or deposits are taken from relatives of a partner of a partnership firm. However, if such loans, advances or deposits are taken from relatives of any partner of a LLP carrying on money lending business, which is not falling within the definition of Regulated Deposit Scheme, the LLP will be considered as violating the provisions of the Ordinance. This is because deposits from relative of a partner of a LLP is not excluded from the definition of a Deposit under the Ordinance.

(v) Amounts received by way of contributions towards the capital by partners of any partnership firm or a LLP are not considered as ‘Deposit’ u/s 2(4) of the Ordinance. A Partnership

deed of any partnership firm or LLP specifies the initial contribution to be made by partners towards capital. Further, the deed also provides that further contribution of money shall be made by the Partners in such manner as may be mutually agreed upon by the partners. Therefore, it is possible to take the view that any further funds brought in by the partners in the partnership firm or LLP will be considered as contribution towards capital by partners. Further, even if the amount received from a partner is considered as a Deposit u/s 2(4) of the Ordinance, it will not be considered as a deposit under Unregulated Deposit Scheme if the partnership firm or LLP is not carrying on money lending or finance business.

(vi) If a company is accepting deposits from public and is complying with Chapter V (Acceptance of Deposits by Companies) of the Companies Act, 2013, such deposits will not be considered as deposits under Unregulated Deposit Scheme.

(vii) If a LLP engaged in manufacturing business takes a loan of ₹2 Cr., from a partnership firm carrying on Money Lending Business, the provisions of the Ordinance will not apply. This for the reason that the term 'Deposit' in section 2(4) of the Ordinance does not include any amount received in the course of or for the purpose of business of LLP and having a genuine connection to the business.

(viii) If a subsidiary company takes a loan from its holding company it will not be contravening the provisions of the Ordinance. This is because u/s 2(4) of the Ordinance 'Deposit' taken by a company is given the same meaning as assigned to it in the Companies Act, 2013. Section 2(31) of the Companies Act read with Rule 2(1) (c) (vi) of the Companies (Acceptance of Deposits) Rules, 2014, provides that "Any amount received by a company from any other Company is not to be considered as a deposit.

(ix) If a buyer of goods receives credit of 45 days from the seller, the same will not be considered as an Unregulated Deposit and the Ordinance will not apply to such credit. This is because such Credit is not considered as a Deposit u/s 2(4) of the Ordinance.

(x) Section 3 of the Ordinance bans the Unregulated Deposit Schemes w.e.f 21.02.2019. It also prohibits, w.e.f. 21.2.2019, any deposit taker from, directly or indirectly, promoting, operating, issuing any advertisement or accepting deposits in pursuance of an Unregulated Deposit Scheme. This will mean that a deposit taker cannot take any fresh deposit under such scheme on or after 21/02/2019. However, it is not clear from this section as to what is the position of the deposits already taken before 21.2.2019 under any Unregulated Deposit Scheme. Whether the deposit taker has to refund such outstanding deposits to the depositor and, if so, within what period. This issue requires clarification from the government.

7. **COMPETENT AUTHORITY:**

(i) The provisions of the Ordinance are to be administered by the State Governments and the Union Territories (Appropriate Governments). Section 7 of the Ordinance authorizes the Appropriate Governments to appoint one or more Officers (not below the rank of Secretary to that Government) as a Competent Authority.

(ii) Where a Competent Authority has reason to believe, on the basis of the information and particulars as prescribed by Rules, that any deposit taker is soliciting deposits in contravention of the provisions of the Ordinance, he may provisionally attach the deposits held by the deposit taker. He may also attach the money or other property acquired by the deposit taker or any other person on his behalf. The procedure for such attachment will be as prescribed by the Rules.

(iii) For the above purpose the Competent Authority is vested with the powers of the Civil Court under the Code of Civil Procedure, 1908. While conducting the investigation or inquiry he can exercise this power for (a) discovery and inspection, (b) enforcing attendance of any person, (c) compelling the production of records, (d) receiving evidence on affidavits, (e) issuing commission for examination of witnesses and documents and (f) any other matter which may be prescribed by the Rules.

(iv) Except for the offences u/s4 (fraudulent default under Regulated Deposit Schemes) and intimation to be given about accepting deposits u/s10, all other offences under the Ordinance shall be cognizable and not-bailable. In other words, for these offences any Police Officer can book a case on receipt of FIR without waiting for a Magistrate's Order. The Police Officer has, then, to inform the Competent Authority. On receipt of such information, the Competent Authority shall refer the matter to CBI if the offence relates to a deposit scheme involving depositors or properties located in more than one State or Union Territory or outside India and the amount involved is of such magnitude as to significantly affect public interest.

(v) The proceedings before the Competent Authority shall be deemed to be judicial proceedings under section 193 and 288 of the Indian Penal Code. In other words, the Competent Authority will have to conduct the proceedings as per the Rules to be prescribed and on the basis of principles of natural justice.

(vi) Under section 9(1) the Central Government is required to designate Authority to maintain and operate an online database for information on Deposit Takers operating in India. This Authority may require any Regulator (SEBI, RBI, IRDA, State Government, Union Territory etc.,) or the Competent Authority to share such information about Deposit Takers as may be

prescribed. Similarly, Section 11 of the Ordinance Provides that all other authorities such as Income tax authorities, Banks, Regulators or any Investigating Agency has to share information about any offence by a Deposit Taker with the Competent Authority, CBI, Police etc.

(vii) Section 10 of the Ordinance provides that every Deposit Taker who commences or carries on its business as such on or after 21.02.2019 shall intimate the Authority appointed by the Central Government u/s 9(1) of the Ordinance about its business in the prescribed Form. It may be noted that this Form is required to be filed by any deposit taker who accepts or solicits deposit as defined u/s 2(4) of the Ordinance. Further, this Form is to be filed by a Company which accepts Deposit under Chapter V of the Companies Act, 2013. In other words, the Form is required to be filed even if the Deposits taken by the Deposit Taker are under unregulated Deposit Scheme or not.

(viii) It may be noted that the requirement of furnishing information u/s 10 of the Ordinance is going to be onerous as it applies almost to all persons who are carrying on any business of manufacturing goods, trading in goods, money lending, financing, rendering of services etc. The definition of 'Deposit' in 2(4) of the Ordinance includes any loan or advance. Therefore, any person engaged in business or profession receiving loan, advance or deposit, as stated in Para 3 and 4 above, will have to furnish the information in the prescribed form to the Authority appointed u/s 9(1) of the Ordinance. Even a company accepting Fixed Deposits as specified under Chapter V of the Companies Act, 2013, has to comply with this requirement. It is not clear as to whether this information is to be given only once or every year on an ongoing basis. We will have to await the relevant Rule to be prescribed or any clarification from the Government.

8. **DESIGNATED COURTS:**

(i) Section 8 of the Ordinance provides that the Appropriate Government shall constitute one or more Courts which will be called "Designated Courts" to deal with the cases relating to contravention of the provisions of the Ordinance. No other court shall have jurisdiction in respect of matters relating to the provisions of the Ordinance.

(ii) The Competent Authority, within a period of 30 days (which may be extended to 60 days for the reasons to be recorded in writing) from the date of provisional attachment of the property, as stated in Para 7(ii) above, has to file an application to the Designated Court for confirmation of the attachment and for permission to sell the property so attached by public auction or by private sale.

(iii) On receipt of such application the Designated Court has to issue notice to the Deposit Taker, the person whose property has been attached and other concerned persons to show cause within 30 days as to why the attachment should not be confirmed and these properties should not be sold.

(iv) The Designated Court, after adopting the established procedure, has to pass an order confirming the attachment or such other order as it deems fit. The Designated Court can also pass order that, either entire or part of the attached property, may be sold by the Competent Authority by public auction or by private sale.

(v) The Designated Court can pass an order or issue directions, as may be necessary, for equitable distribution amongst the Depositors of money attached or realized from the sale of attached properties.

(vi) When the default relates to one or more Unregulated Deposit Schemes which are investigated by CBI, the Supreme Court can direct that the case be transferred from one designated court to another designated court.

(vii) Section 15 of the Ordinance provides that the Designated Court Shall endeavor to complete the above proceedings within a period of 180 days from the date of receipt of the application from the Competent Authority.

(viii) Any aggrieved person who is not satisfied with the order of the Designated Court can file appeal before the High Court against the said order within 60 days of such order. The High Court may entertain any appeal filed after the above period if sufficient cause for the delay is explained.

9. **PUNISHMENT FOR OFFENCES:**

Sections 21 to 27 of the Ordinance provide for punishment for contravention of the provisions of the Ordinance as under:

SNo.	Nature of Offence	Fine		Imprisonment	
		Minimum	Maximum	Minimum	Maximum
		₹ in Lakhs		(No. Years)	(No. of Years)
(i)	Soliciting for Unregulated Deposits Scheme (Section 3) (This will include advertisement)	2	10	1	5

(ii)	Accepting Deposit under Unregulated Deposits Scheme (Section 3)	3	10	2	7
(iii)	Deposit Taker fraudently defaults in repayment of such deposit or in rendering any specified service (Section 3)	5	200% of Deposit collected	3	10
(iv)	Failure to furnish information under section 10	0	5	---	-----
(v)	Contravention of Section 4	5	25 Crore or 300%, of Profits made whichever is higher	0	7
(vi)	Contravention of section 5	0	10	1	5
(vii)	Second or Subsequent Offence	10	50(Crore)	5	10
(viii)	In case of offences by persons other than Individual, every individual in charge of the affairs of the Deposit Taker shall be deemed to be guilty of the offence and punished as above	-----	-----	-----	-----

10. **TO SUM UP:**

(i) The present Ordinance banning Unregulated Deposits Scheme has been issued after detailed consideration at various levels. Standing Committee on Finance (SCF) presented its Report on the subject of "Efficacy of Regulation of Collective Investment Schemes, Chit Funds etc." in the Lok Sabha. The SCF had issued this Report after consultations with various Ministry Officials and other Stakeholders.

(ii) The Central Government had appointed an Inter-Ministerial Group to identify gaps in the existing regulatory frame work for deposit-taking activities and suggest administrative / legal measures and also to draft a new legislation to cover all aspects of deposit taking.

(iii) The Report of this Inter-Ministerial Group was made public for public comments. After detailed consideration a Bill to ban Unregulated Deposits Schemes was introduced in the Lok Sabha on 18.7.2018. The Bill was referred to SCF on 10.8.2018. It was only after consideration of SCF report that the Bill was passed by the Lok Sabha on 13.02.2019.

(iv) From the above it is evident that lot of thought process has gone into the drafting of this legislation. It is only because Rajya Sabha could not pass this Bill, before the parliament was

dissolved, that the Hon'ble President has issued this Ordinance on 21.02.2019. Let us hope this Ordinance is approved by both Houses of Parliament after the Elections.

(v) Reading the Provisions of the Ordinance it appears to be very harsh. But considering the fact that many ill-informed persons get lured by attractive schemes for Deposits floated by unscrupulous persons, the Government has considered it necessary to enact this legislation in order to protect the interest of small depositors.

(vi) One issue which requires clarification is about the position of such Unregulated Deposits Schemes started before 21.2.2019. There is no specific mention about the same. There is also no provision for refund of money to Depositors of such existing schemes within a particular period. Let us hope that the Government will issue clarification in this matter.

(vii) Section 10 of the Ordinance requiring every person carrying on business or profession receiving loans, advances or deposits to report to the Authority to be appointed by the Government in the prescribed Form is going to be an onerous exercise. Whether the Form is to be filed only once or every year on an ongoing basis is not clear. This requirement and certain other procedural requirements under the Ordinance are dependent on the Rules to be prescribed by the Government. We have to wait for these Rules which are likely to be issued shortly.