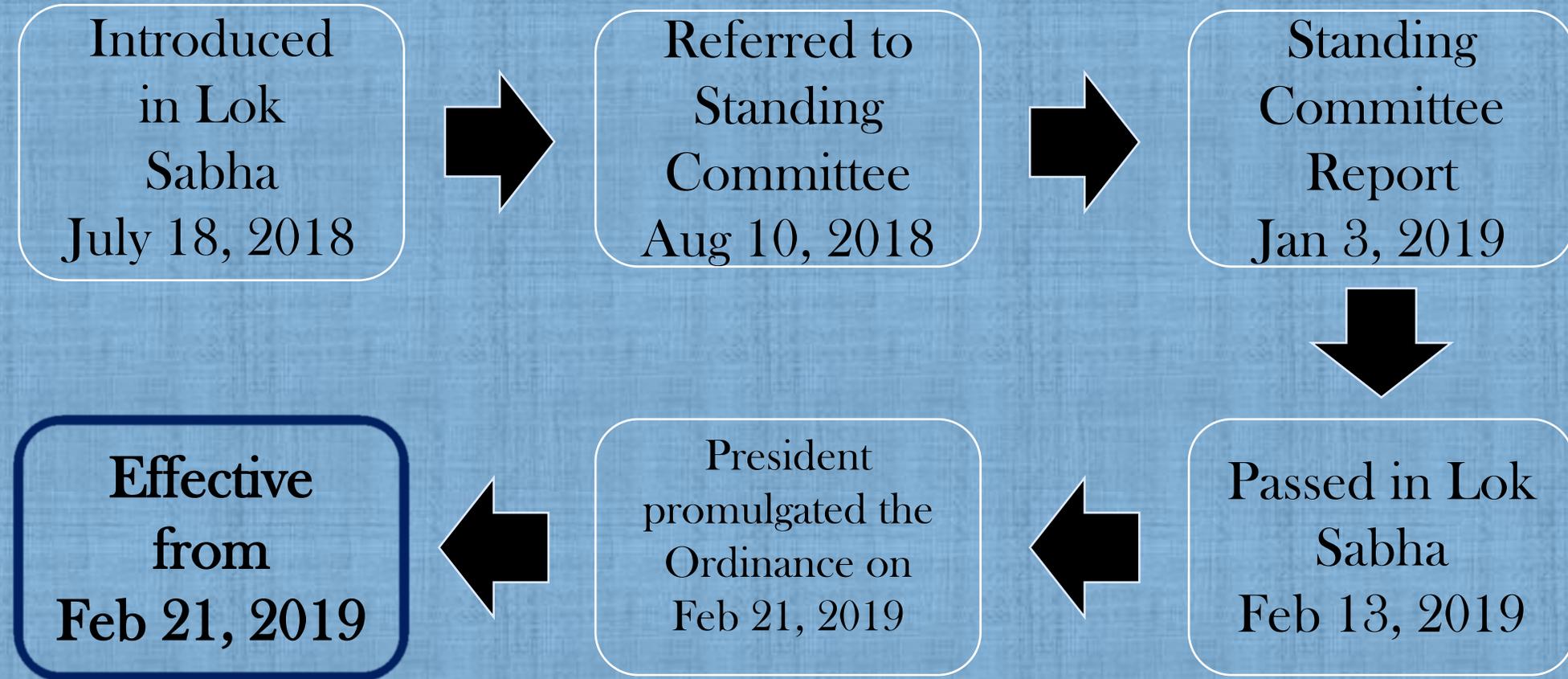


**THE BANNING OF
UNREGULATED DEPOSIT
SCHEMES ORDINANCE, 2019
(BUDS 2019)**

Disclaimer

- The following presentation is given for general informational purposes only and meant for private circulation only.
- You should obtain your own independent advice on the Interpretation outlined in this Presentation.

Almanac of events



Act Vs Ordinance

- An act is a 'Law' which is passed by parliament and has also received the assent of President.
- An ordinance is also a 'Law' but without being subject to the discussion and deliberation in both or one of the houses of the Parliament.
- Ordinance is temporary law passed by the President till its expiry or till it is repealed or till it is approved by the legislature.

Ordinance (Power of President and Parliament)

- If the ordinance is not approved by both the houses of Parliament?
 - As per Article 123 of the Constitution of India the ordinance shall cease to operate at the expiration of six weeks from the reassembly of Parliament, or, of before the expiration of that period resolutions disapproving it are passed by both Houses.
 - May be withdrawn at any time by the President.

Scope

- Extends to whole of India except the state of Jammu and Kashmir.
- It shall come in force at once : Immediate Repercussion - Anything which falls under the definition of deposit and which is unregulated is banned with immediate effect.
- The ban is not only on acceptance but also on solicitation.

What is a Ponzi scheme?

- **A Ponzi scheme** is a form of fraud that lures investors and pays profits to earlier investors with funds from more recent investors. The scheme leads victims to believe that profits are coming from product sales or other means, and they remain unaware that other investors are the source of funds. A Ponzi scheme can maintain the illusion of a sustainable business as long as new investors contribute new funds, and as long as most of the investors do not demand full repayment and still believe in the non-existent assets they are purported to own.

Background of Ponzi Scheme

- The scheme is named after **Charles Ponzi** who became notorious for using the technique in the **1920s**.
- The idea had already been carried out by **Sarah Howe** in **Boston** in the **1880s** through the "**Ladies Deposit**".
- Ponzi carried out this scheme and became well known throughout the **United States** because of the huge amount of money that he took in. His original scheme was based on the legitimate arbitrage of international reply coupons for postage stamps, but he soon began diverting new investors' money to make payments to earlier investors and to himself.

Saradha Group financial scandal

- The Saradha Group financial scandal was a major financial scam and alleged political scandal caused by the collapse of a Ponzi scheme run by Saradha Group, a consortium of over 200 private companies that was believed to be running collective investment schemes popularly but incorrectly referred to as chit funds in Eastern India.
- The group collected around Rs. 200 to Rs. 300 billion from over 1.7 million depositors before it collapsed in April 2013. The State government also set up a fund of Rs. 5 billion to ensure that low-income investors were not bankrupted.
- The key people involved were Sudipto Sen and Debjani Mukherjee.

Regulation of money lending business

- The power to regulate the business of money lending is delegated to the States under entry no. 30 of the State List , Schedule VII to the Constitution of India: *“Money-lending and money-lenders; relief of agricultural indebtedness.”*
- **The Bombay Money Lenders Act 1946 in Maharashtra:** It is compulsory to get a License if any person engages in the business of money lending.

Meaning of business of money lending as per the Bombay Money Lenders Act, 1946

- “Business of money-lending” means the business of advancing loans whether in cash or kind whether or not in connection with or in addition to any other business. [Sec 2 (2)]
- “Loan” means an advance at interest whether of money or in kind, but does not include deposits/loans as prescribed. [Sec 2 (9)]

Meaning of Deposit – Sec 2 (4)

- **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**
 - whether after a specified period or otherwise,
 - either in cash or in kind or
 - in the form of a specified service,
- with or without any benefit in the form of interest, bonus, profit or in any other form.

Analysis of the words in definition of Deposit Sec - 2 (4)

- **Analysis of the word “Promise to return”**

The definitions provide a condition as to promise to return, hence donation to trusts or other similar institutions will not be covered.

- **Analysis of the word “Return”**

By ‘returns’ of course we mean the promise to pay more than what was contributed initially.

Exclusions from the meaning of Deposit - Sec 2 (4)

- Loans/ financial assistance from banks, PFIs or any registered NBFCs, Regional Financial Institutions and Insurance companies;
- Amount received from or guaranteed by appropriate Government or statutory authority (Govt Securities, REC NHAH Bonds etc);
- Amounts received from foreign government, foreign banks, foreign authorities etc or person resident outside India as per provisions of FEMA Act, 1999;
- Capital contributions by partners of partnership firm or LLP; (Only by way of capital, Not by way of loan)
- Loans received by an individual from his relatives;
- Loans received by a firm from relatives of partners; (Firm doesn't include LLP)
- Any credit given by a seller to a buyer on the sale of any property (whether movable or immovable);
- Amounts received by a registered ARC under RBI and SARFAESI;

Exclusions from the meaning of Deposit - Sec 2 (4) ...Contd.

- Amounts received by a political party under the Representation of the People Act, 1951;
- Any periodic payment made by the members of the self-help groups as per the ceiling prescribed by State/ Union Territory Government;
- Amount received in the course of, or for the purpose of, business and bearing a genuine connection to such business for following and which has not become refundable including:
 - Payment, advance or part payment for supply/ hire of goods / services;
 - Advance received in connection with and adjusted towards consideration of an immovable property under an agreement or arrangement;
 - Security deposit;
 - Advance under long-term projects for supply of capital goods;

Provided that if the above amounts received become refundable, such amounts shall be deemed to be deposits on the expiry of fifteen days from the date on which they become due for refund.

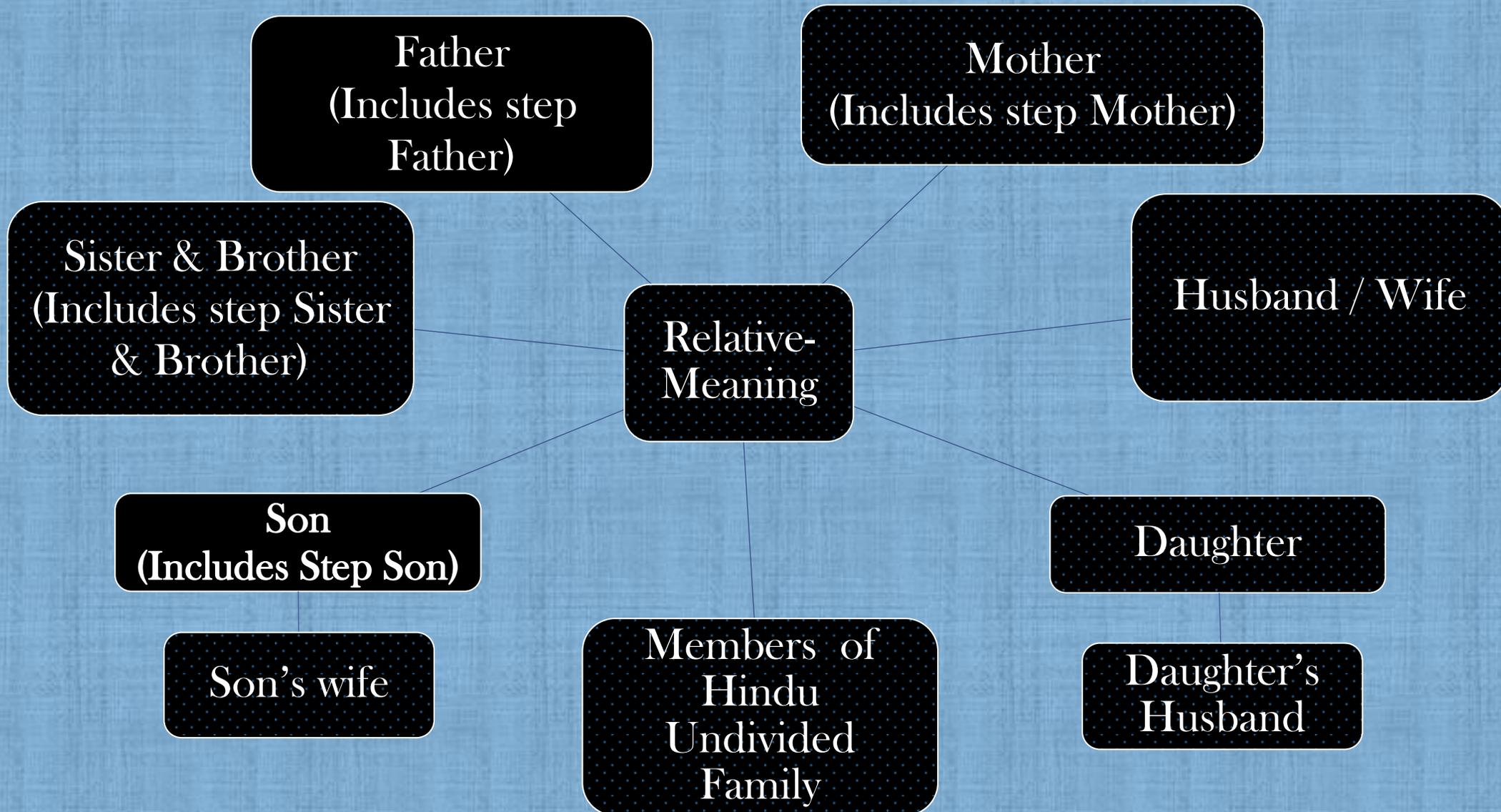
Analysis - “In the course of / purpose of / bearing a genuine connection to business” - Sec 2 (4) (l)

- “An amount received” is subject to two conditions, viz: In the course of business; or For the purpose of business; and Bearing a genuine connection to such business.
- The amount so received may or may not be used for the purpose of the business. Such an amount must bear a genuine connection to such business.

Meaning of Deposit Taker - Sec 2 (6)

- “Deposit taker” means any individual or group of individuals; a proprietorship concern; a partnership firm; an LLP; a company; an association of persons; a trust; a co-operative society or a multi-State cooperative society; or any other arrangement of whatsoever nature, receiving or soliciting deposits,
- but does not include— as specified

Meaning of Relative - Sec 2 (4) (Expln V)



Analysis of the meaning Relative

- The definition of relative doesn't include grandfather and grandmother; and doesn't specifically mention about step daughter, hence advance from them is not exempt under this ordinance.
- Nothing specifically has been mentioned about the lineal ascendants and descendants other than the relatives mentioned. Hence, any loans/deposits from them are prohibited.

Unregulated Deposit Scheme - Sec 2 (17)

“Unregulated Deposit Scheme” means a Scheme or an arrangement under which

- deposits are accepted or solicited by any deposit taker
- by way of business and
- which is not a Regulated Deposit Scheme

Regulated Deposit Scheme (RDS) (First Schedule)

RDS means the schemes/arrangements listed below by:

- SEBI: Collective Investment Scheme, Alternative Investment Funds, Funds managed by a portfolio manager, ESOP, Mutual Funds etc
- RBI: Deposits accepted by NBFCs; authorized payment system under the Payment and Settlement Systems Act , 2007
- IRDA: Contract of Insurance
- National Housing Bank Deposits
- State Government or Union Territory Government: Prize chit or money circulation scheme under the Prize Chits and Money Circulation Scheme (Banning) Act,1978
- Pension Fund Regulatory and Development Authority
- Employee Provident Fund Organization
- Central Registrar, Multi-State Co- operative Societies
- MCA, Government of India

Analysis - By way of Business

Does business includes Profession?

Question arises whether the word “business” includes a “profession”.

Banning of Unregulated Deposit Schemes – Sec 3

- On and from the date of commencement of this Ordinance (21st Feb 2019),
 - (a) the Unregulated Deposit Schemes shall be banned; and
 - (b) no deposit taker shall, directly or indirectly, promote, operate, issue any advertisement soliciting participation or enrolment in or accept deposits in pursuance of an Unregulated Deposit Scheme.

Fraudulent default in Regulated Deposit Schemes – Sec 4

- No deposit taker, under such scheme, should commit any fraudulent default:
 - (a) in the repayment or return of deposit on maturity;
 - (b) in rendering any specified service promised against such deposit.

Not only the ordinance bans Unregulated Deposit Schemes but also makes it an offence to do a fraudulent default in Regulated Deposit schemes.

Explanation - Fraudulent Default

- As per Explanation (i) to Section 21 of the Ordinance, the expression “fraudulently” shall have the same meaning as assigned to it in section 25 of the Indian Penal Code.
- As per Section 25 of the Indian Penal Code, a person is said to do a thing “fraudulently” if he does that thing with intent to defraud but not otherwise.

Wrong Inducement in relation to UDS - Sec 5

- No person should knowingly make any misleading statement, or promise or forecast which is false or deceptive, misleading in material facts or deliberately conceal any material facts, to induce any other person to invest in, or become a member or participant of any UDS.

Unregulated Deposit Scheme - Sec 6

- Deemed to be Unregulated Deposit Scheme:
 - (a) Prize chit money; and
 - (b) Money circulation scheme
- banned under the provisions of the Prize Chits and Money Circulation Scheme (Banning) Act, 1978. (Also Subject to **Section 11** of the aforesaid act as per Schedule I of BUDS 2019)

Prize Chits and Money Circulation Scheme (Banning) Act, 1978.

- **Conventional Chit Sec 2 (a):** means a transaction whether called chit, chit fund, kuri or by any other name by or under which a person responsible for the conduct of the chit enters into an agreement with a specified number of persons that every one of them shall subscribe a certain sum of money (or certain quantity of grain instead) by way of periodical instalments for a definite period and that each such subscriber shall, in his turn, as determined by lot or by auction or by tender or in such other manner as may be provided for in the chit agreement, be entitled to a prize amount.

Prize Chits and Money Circulation Scheme (Banning) Act, 1978.

- **Money Circulation Scheme Sec 2(c):** Means any scheme, by whatever name called, for the making of quick or easy money, or for the receipt of any money or valuable thing as the consideration for a promise to pay money, on any event or contingency relative or applicable to the enrolment of members into the scheme, whether or not such money or thing is derived from the entrance money of the members of such scheme or periodical subscriptions.

Prize Chits and Money Circulation Scheme (Banning) Act, 1978.

- **Prize Chit - Sec 2 (e):** includes any transaction or arrangement by whatever name called under which a person collects whether as a promoter, foreman, agent or in any other capacity, monies in one lump sum or in instalments by way of contributions or subscriptions or by sale of units, certificates or other instruments or in any other manner or as membership fees or admission fees or service charges to or in respect of any savings, mutual benefit, thrift, or any other scheme or arrangement by whatever name called, and utilises the monies so collected or any part thereof or the income accruing from investment or other use of such monies for all or any of the purposes as specified in Sec 2 (e) - (i) and (ii).

Prize Chits and Money Circulation Scheme (Banning) Act, 1978 - Sec 11

Nothing contained in this Act shall apply to any prize chit or money circulation scheme promoted by-

- (a) a State Government or any officer or authority on its behalf; or
- (b) a company wholly owned by a State Government which does not carry on any business other than the conducting of a prize chit or money circulation scheme whether it is in the nature of a conventional chit or otherwise; or
- (c) a banking company, or a banking institution notified by the Central Government or the State Bank of India or its subsidiary bank or a corresponding new bank constituted under of the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970, or a Regional Rural Bank, or a cooperative bank
- (d) any charitable or educational institution notified in this behalf by the State Government, in consultation with the Reserve Bank.

Transition Provisions - Deposits taken before the date of ordinance

Date of enforcement of this ordinance is 21st February, 2019, If “Deposit” accepted before the date of Ordinance?

Transition provision has not been specifically mentioned in the ordinance.

Applicability in case of Companies

- For companies: the meaning of ‘deposit’ shall be as defined in Companies Act, 2013;
 - **Section 2(31)** of Companies Act, 2013, “deposit” includes any receipt of money by way of depositor loan or in any other form by a company, but does not include such categories of amount as may be prescribed in consultation with the Reserve Bank of India.

Applicability in case of NBFCs-

- For registered NBFCs: definition of 'deposit' shall be as given in Section 45-I (bb) of Reserve Bank of India Act, 1934.

Authorities (Sec - 7)

- Section 2(3) :- “Competent Authority” means an Authority appointed by the appropriate Government under section 7.
- “Appropriate Government” means in respect of matters relating to,—
 - (i) the Union territory without legislature, the Central Government;
 - (ii) the Union territory of Puducherry, the Government of that Union territory;
 - (iii) the Union territory of Delhi, the Government of that Union territory; and
 - (iv) the State, the State Government;

Central Database and Intimation by deposit taker (Sec - 9)

- Creation of Central database of information on deposit takers operating in India. (Sec 9)
- Information to be given if it takes deposits as per sec 2(4) or in case of company as per the Companies Act, 2013.
- All information about URDS to be shared with CBI and other designated authority. (Sec 11)

Intimation of business by deposit taker (Sec 10)

- Every deposit taker which commences or carries on its business as such on or after the commencement of this Ordinance (21.02.2019) shall intimate the authority referred to in subsection (1) of section 9 about its business in such form and manner and within such time, as may be prescribed.

Priority of Depositors' Claim and Precedence of Attachment - Sec - 12 & Sec - 13

Sec. 12. any amount due to depositors from a deposit taker shall be paid in priority over all other debts and all revenues, taxes, cesses and other rates payable to the appropriate Government or the local authority.

Sec. 13. Where an Order of provisional attachment has been passed by the competent authority -

- (a) such attachment shall continue until an order is passed under sub-section (3) or sub-section (5) of section 15 by the Designated Court;
- (b) all the attached money or property of the deposit taker and the persons mentioned therein shall vest in the Competent Authority ;

The Competent Authority shall not dispose of or alienate the property or money attached except in accordance with the order of the Designated Court under sub-section (3) or sub-section (5) of section 15.

Application for confirmation of attachment and sale of property Sec -14

(1) The Competent Authority shall, within a period of thirty days, which may extend up to sixty days, for reasons to be recorded in writing, from the date of the order of provisional attachment, file an application with such particulars as may be prescribed, before the Designated Court for making the provisional attachment absolute, and for permission to sell the property so attached by public auction or, if necessary, by private sale.

(2) In case where the money or property has been attached on the permission granted by a Designated Court in another State or Union territory, the application for confirmation of such attachment shall be filed in that Court.

Confirmation of Attachment by designated court Sec - 15

(1) Upon receipt of an application under section 14, the Designated Court shall issue notice to—

(a) the deposit taker; and (b) any person whose property is attached under section 14, to show cause, within a period of thirty days from the date of issue of notice, as to why the order of attachment should not be made absolute and the properties so attached be sold.

(3) The Designated Court shall, after adopting such procedure as may be prescribed, pass an order—

(a) making the provisional order of attachment absolute; or

(b) varying it by releasing a portion of the property from attachment; or

(c) cancelling the provisional order of attachment,

(6) The Designated Court shall endeavor to complete the proceedings under this section within a period of one hundred and eighty days from the date of receipt of the application referred to in sub-section (1).

Payment in lieu of attachment (Sec17) and Appeal to High Court (Sec 19)

- **Sec 17:** Any deposit taker or a person referred to in subsection (1) of section 15, or transferee referred to in section 16 whose property is about to be attached or has been provisionally attached under this Ordinance, may, at any time before the confirmation of attachment, apply to the Designated Court for permission to deposit the fair value of the property in lieu of attachment.
- **Sec 19:** Any person may appeal to HC within a period of sixty days from the date of the order.

Offences and Punishment (Sec 21-27)

PARTICULARS	IMPRISONMENT	FINE
Soliciting deposits under UDS	1 year to 5 years and	INR 2 lakhs to 10 lakhs
Acceptance of deposits under UDS	2 years to 7 years and	INR 3 lakhs to 10 lakhs
Acceptance of deposits under UDS and there is Fraudulent default	3 years to 10 years and	INR 5 lakhs to twice the amount of aggregate funds collected
Fraudulent default in RDS	upto 7 years or	INR 5 lakhs to 25 crores or three times the amount of profit made out of fraudulent default.
Wrongful inducement in relation to UDS	1 year to 5 years and	upto INR 10 lakhs
Repeated offenders	5 year to 10 years and	INR 10 lakhs to 50 crores
Failure to file intimation by deposit taker about its business, to the authority	-	upto 5 lakhs

UDS : Unregulated Deposit Scheme

RDS: Regulated Deposit Scheme

Publication of Advertisement (Sec- 33)

- No newspaper or other publication of any nature can promote any soliciting of deposits or any person to become a member of any Unregulated Deposit Scheme.
- If any publisher promotes such Unregulated Deposit Scheme, the appropriate Government may direct such newspaper or publication to publish a full and fair retraction, free of cost, in the same manner and in the same position in such newspaper or publication as may be prescribed.

A close-up photograph of a hand holding a blue fountain pen, writing the words "Thank you!" in a cursive script on a white surface. The pen is positioned at the end of the word, with the nib touching the paper. The background is a soft, out-of-focus white.

Thank you!