



# Detailed analysis of Banning of Unregulated Deposit Schemes Ordinance, 2019

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## Introduction

The Hon'ble President of India, on the aid and advice of the Union Government, on February 21, 2019 has promulgated '*The Banning of Unregulated Deposit Schemes Ordinance, 2019*' (hereinafter referred to as 'Ordinance'). While the Union Government called it a landmark law that will help fighting the menace of illicit deposits and Ponzi schemes which loot hard earned money of public, the Ordinance has received a lukewarm reception from the professional community which feels that the law has gone far beyond its mandate and would gravely impact legitimate business transactions.

Through this article, an attempt has been made to understand the implication of Banning of Unregulated Deposit Schemes Ordinance, 2019. For the sake of better understanding, the author has divided the article into four parts comprising of the definition, the substantive law and the sanctions imposed.

## PART 1 : Important definitions

The objective of the Ordinance is to ban Unregulated Deposit Scheme. Thus, at the outset, it will be important to analyse the definition of 'Unregulated Deposit Scheme'

### I. Unregulated Deposit Scheme

As per section 2(17) of the Ordinance, the term '*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

such deposits are not a Regulated Deposit Scheme.

Thus, prerequisite for any deposit to qualify as an '*Unregulated Deposit Scheme*' is

#### **1. Must be a 'Deposit'**

The amount accepted / solicited by must qualify to be a 'deposit' within the definition prescribed under section 2(4) of the Ordinance.

## **2. Accepted by way of business**

Such deposits must have been accepted or solicited by any deposit taker by way of business. Thus, the cases where deposits are accepted for purposes other than business are outside the ambit of 'Unregulated Deposit Scheme' and thus, are not hit by the provisions of 'The Banning of Unregulated Deposit Schemes Ordinance, 2019'.

Example:

a. In case Mr. X accepts deposits from his friend Mr. Y for his personal use, such deposits shall be outside the purview of the Ordinance

b. In case Mr. X accepts deposits from his friend Mr. Y for his business use, such deposits shall be within the purview of the Ordinance

## **3. Not Regulated Deposit Scheme**

Such deposits are not a Regulated Deposit Scheme

## **II. DEPOSIT**

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Section 2(4) of the Ordinance defines the term '*deposit*'. As per the scheme of Ordinance, the definition of term '*deposit*' shall have different meaning for different category of persons.

### **1. Category 1 - Meaning of 'Deposit' in case of Companies**

In respect of a company, the expression '*deposit*' shall have the same meaning as assigned to it under the Companies Act, 2013;

### **2. Category 2 - Meaning of 'Deposit' in case of Non-Banking Financial Companies**

In respect of a non-banking financial company registered under the Reserve Bank of India Act, 1934, the expression '*Deposit*' shall have the same meaning as assigned to it in clause (bb) of the section 45-I of the said Act;

### **3. Category 3- Meaning of 'Deposit' in case of persons other than Companies and Non-Banking Financial Companies**

In such cases, a deposit means any money received as loan or advance by a deposit taker with a promise to return the same, 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.

Exclusions from the definition of Deposits

The definition of '*deposit*' shall exclude :

- a. Loans received from banks (including cooperative banks)
- b. Loan or financial assistance from Public Financial Institutions / NBFCs / Insurance Companies;
- c. Amounts received from the Government or Statutory Authority or from any other source whose repayment is guaranteed by Government
- d. Amount received from foreign sources like
  - i. Foreign Governments
  - ii. Foreign or international banks, multilateral financial institutions
  - iii. Foreign Government owned development financial institutions
  - iv. Foreign export credit collaborators
  - v. Foreign bodies corporate
  - vi. Foreign citizens
  - vii. Foreign authorities or person resident outside India
- e. Amount received by way of capital contribution by partner in partnership firms / LLP
- f. In case of individual, amounts received by way of loan from his relatives

In case of any firm, amounts received by way of loan from the relatives of any of its partners;

'*Relative*' for this clause has the same meaning assigned to it in the Companies Act, 2013, which includes the following :

- i. Members of a Hindu undivided family
- ii. Husband and wife
- iii. Father
- iv. Mother
- v. Son
- vi. Son's wife
- vii. Daughter
- viii. Daughter's husband.
- ix. Brother

x. Sister

It may be pertinent to mention that only loans received by partnership firm from relative of a partner is out of the definition of '*Deposit*' and not loans received by LLP from relative of a partner. This is because the definition of the term '*firm*' does not extend to LLP.

g. Amounts received as credit by a buyer from a seller on the sale of any property (whether movable or immovable);

h. Amounts received by an asset re-construction company

i. Voluntary contributions received by a political party or deposit made under section 34 of Representation of People Act, 1951

j. Periodic payment made by the members of the self-help groups

k. Amount collected for such purpose as may be prescribed by the State Government

#### I. Business Receipts

Any amount received in the course of, or for the purpose of business and bearing a genuine connection to such business.

This clause is inclusive and provides an illustrative list of receipts that shall always fall outside the purview of 'deposit'. These are :

i. Advance for the supply or hire of goods or provision of services.

ii. Advance received as a consideration of an immovable property under an agreement or arrangement

iii. Security or dealership deposited for the performance of the contract for supply of goods or provision of services

iv. Advance under the long-term projects for supply of capital goods except those specified in item (ii):

#### **Note:**

i. When amounts received under items (i) to (iv) 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:

ii. However, in case amount become refundable, because deposit taker could not obtain necessary permission under the law, to deal in the goods or properties or services for which money is taken, such amounts shall be deemed to be deposits.

### **III. Regulated Deposit Scheme**

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As per section 2(14) of the Ordinance, the term '*Regulated Deposit Scheme*' means the Schemes specified under column (3) of the First Schedule, which are –

### **1. Schemes regulated by Securities and Exchange Board of India**

- i. Collective Investment Schemes
- ii. Alternative Investment Funds
- iii. Funds are managed by a portfolio manager
- iv. Schemes under Securities and Exchange Board of India (Share Based Employee Benefits) Regulations, 2014
- v. Amount received as subscriptions to a mutual fund
- vi. Any other scheme or an arrangement registered under SEBI Act, 1992

### **2. Schemes regulated by Reserve Bank of India**

- i. Scheme under which deposits are accepted by NBFCs
- ii. Scheme or an arrangement under which funds are accepted by Business Correspondents and Facilitators of banks
- iii. Scheme or an arrangement under Payment and Settlement Systems Act, 2007 (51 of 2007).
- iv. Any other scheme or an arrangement regulated under the Reserve Bank of India Act, 1934

### **3. Schemes under the Insurance Regulatory and Development Authority of India**

A contract of insurance

### **4. Schemes of State Government or Union territory Government**

- i. Scheme or an arrangement made by a co-operative society
- ii. Scheme or an arrangement conducted as a chit business with the previous sanction of the State Government.
- iii. Scheme or an arrangement regulated by any enactment relating to money lending which is for the time being in force in any State or Union territory.
- iv. Scheme or an arrangement by a prize chit or money circulation scheme under section 11 of the Prize Chits and Money Circulation Schemes (Banning) Act, 1978

5. Scheme or an arrangement for acceptance of deposits registered under the National Housing Bank Act, 1987
6. Any scheme or an arrangement under the Pension Fund Regulatory and Development Authority Act, 2013
7. Any scheme, Pension Scheme or Insurance Scheme framed under the Employees' Provident Fund and Miscellaneous Provisions Act, 1952
8. Any scheme or an arrangement for acceptance of deposits under the Multi-State Co-operative Societies Act, 2002 (39 of 2002)

### **9. Schemes of Ministry of Corporate Affairs, Government of India**

- i. Deposits accepted or permitted under the Companies Act, 2013
  - ii. Deposits accepted by a company declared as a Nidhi or a Mutual Benefit Society under section 406 of the Companies Act, 2013
10. Deposits accepted under any scheme or an arrangement registered with any regulatory body in India constituted or established under a statute; and
- 11 Any other scheme as may be notified by the Central Government under this Ordinance.

## **PART 2 : Substantive provisions**

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### **1. Section 3 – Banning of Unregulated Deposit Schemes**

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Section 3 of the Ordinance places a blanket ban on Unregulated Deposit Schemes and prohibits deposit taker from promoting, operating, issuing any advertisement soliciting participation or enrolment in or accepting deposits in pursuance of an Unregulated Deposit Scheme.

### **2. Section 4 – Fraudulent default in Regulated Deposit Schemes**

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Section 4 of the Ordinance prohibits deposit taker, while accepting deposits under a Regulated Deposit Scheme, from commission of fraudulent default in the repayment or return of deposit on maturity or in rendering any specified service promised against such deposit.

Section 4 is not applicable to companies (as per proviso to Section 27 of the Ordinance)

### **3. Section 5 – Wrongful inducement in relation to Unregulated Deposit Schemes**

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Section 5 of the Ordinance prohibits any person from knowingly making 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.

#### **4. Section 6 – Certain scheme to be Unregulated Deposit Scheme**

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Section 6 of the Ordinance provides that prize chit or a money circulation scheme 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.

#### **5. Section 7 – Provisional Attachment**

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The power for provisional attachment in cases of contravention of section 3 has been vested with a Competent Authority. This Competent Authority is an officer appointed by appropriate government who is not below the rank of Secretary to that Government.

As per section 7(3) of the Ordinance, where the Competent Authority, has reason to believe (the reason for such belief to be recorded in writing), on the basis of such information and particulars as may be prescribed that any deposit taker is soliciting deposits in contravention of section 3, he may, by order in writing, provisionally attach the deposits held by the deposit taker and the money or other property acquired either in the name of the deposit taker or in the name of any other person on behalf of the deposit taker.

It is pertinent to mention that section 7(3) of the Ordinance is very poorly drafted and does not provide for giving any show cause notice to the deposit taker prior to provisionally attaching deposits. Not providing an opportunity of being heard prior to provisional attachment constitutes a direct contravention of principles of Natural Justice and vitiates the pre-requisites of a fair trial. As this law will evolve, there is a high possibility that section 7(3) may be read down by Constitutional Courts to the extent it fails in providing a show cause notice prior to provisional attachment.

#### **6. Section 14 and 15 – Confirmation of attachment by Designated Court**

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(i) Section 14 of the Ordinance obliges the Competent Authority to file an application before the Designated Court for making the provisional attachment absolute within a period of thirty days from the date of the order of provisional attachment. This period may be may extend up to sixty days, for reasons to be recorded in writing.

(ii) The Designated Court shall then issue notice to the deposit taker or any person whose property is attached under section 14, to show cause, within a period of thirty days, as to why the order of attachment should not be made absolute and the properties so attached be sold.

(iii) Thereafter, the Designated Court shall proceed to pass an order -

(a) making the provisional order of attachment absolute;

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

(c) cancelling the provisional order of attachment,

## **7. Section 19 - Appeal to High Court**

Any person including the Competent Authority, if aggrieved by any final order of the Designated Court under this Chapter, may appeal to the High Court, within a period of sixty days from the date of such order.

## **PART 3 : OFFENCES AND PUNISHMENTS**

<b>Offence</b>	<b>Imprisonment</b>	<b>Fine</b>	<b>Type of offence</b>
<b><u>Section 21</u></b> (1) <u>Solicits</u> deposits in contravention of section 3	1 year to 5 years	Rs. 2 Lakhs to Rs. 10Lakhs	Cognizable & non-bailable
(2) <u>Accepts</u> deposits in contravention of section 3	2 year to 7 years	Rs. 3 Lakhs to Rs. 10 Lakhs	Cognizable & non-bailable
(3) Accepts deposits in contravention of section 3 AND fraudulently defaults in repayment	3 year to 10 years	Rs. 5 Lakhs to 2 times funds collected	Cognizable & non-bailable
<b><u>Section 22</u></b> Contravention of section 4	Upto 7 years	Rs. 5 Lakhs to Higher of - Rs. 25 Crores or 3 times of profits	Non-Cognizable bailable



<b>Section 23</b> Contravention of section 4	1 year to 5 years	Upto Rs. 10 Lakhs	Cognizable & non- bailable
<b>Section 24</b> Subsequent conviction	5 year to 10 years	Rs. 10 Lakhs to Rs. 25 Crores	Cognizable & non- bailable

## **PART 4 : MISCELLANEOUS PROVISIONS**

### **1. Section 12 – Priority of depositors’ claim**

Section 12 of the Ordinance provides that 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.

This provision is subject to the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 or the Insolvency and Bankruptcy Code, 2016.

### **2. Section 13 – Precedence of attachment**

Section 13 of the Ordinance provides that an order of provisional attachment passed by the Competent Authority, shall have precedence and priority, to the extent of the claims of the depositors, over any other attachment by any authority competent to attach property for repayment of any debts, revenues, taxes, cesses and other rates payable to the appropriate Government or the local authority.

This provision is subject to the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 or the Insolvency and Bankruptcy Code, 2016.

### **3. Section 9 – Creation of Central database**

Section 9 of the Ordinance empowers Central Government to designate an authority, which shall create, maintain and operate an online database for information on deposit takers operating in India.

### **4. Section 10 – Intimation of business by deposit taker**

Section 10 of the Ordinance provides that every deposit taker which commences or carries on its business as such on or after the commencement of this Ordinance shall intimate the Competent Authority about its business.

Contravention of Section 10 – Fine upto Rs. 10 lakhs (as per section 26)

## **5. Section 11 – Sharing of information**

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- i. Section 11 of the Ordinance obliges the Competent Authority to share all information with the Central Bureau of Investigation and with the authority which may be designated by the Central Government under section 9.
- ii. Appropriate Government, any Regulator, income-tax authorities or any other investigation agency, having any information or documents in respect of the offence investigated under this Ordinance by the police or the Central Bureau of Investigation, shall share all such information or documents with the police or the Central Bureau of Investigation.
- iii. Principal officer of any banking company having reason to believe that any client is a deposit taker and is acting in contravention to the provisions of this Ordinance, he shall forthwith inform the same to the Competent Authority.

## **6. Section 34 – Ordinance to have overriding effect**

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Section 34 of the Ordinance provides that the provisions of this Ordinance shall have effect notwithstanding anything contained in any other law for the time being in force, including any law made by any State or Union territory.

## **7. Section 35 – Application of other laws not barred**

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Section 35 of the Ordinance provides that the provisions of this Ordinance shall be in addition to, and not in derogation of, the provisions of any other law for the time being in force.

## **Conclusion**

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The Banning of Unregulated Deposit Schemes Ordinance, 2019 has ushered in a new regime for regulation of Unregulated Deposit Schemes. By ensuring stringent consequences in cases of contravention, this ordinance will help in safeguarding the interest of general public who are fooled by illicit deposit schemes run by unscrupulous elements of society.

However, given the wide definition of the term '*deposit*', coupled with the fact that most of the offences under this Ordinance are cognisable and non-bailable, misuse of the provisions of this Ordinance against legitimate businesses cannot be ruled out. Various provisions of this Ordinance have been vaguely worded and drafted without considering the consequences on legitimate businesses. It is suggested that the Ordinance be vetted by a team of experts having wide representation from people of all walks of life.

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