

# Update

## Investor Protection post Chit funds crisis: MCA acts a day too late; Puts up infructuous affidavit requirement

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## *Update*

### **Introduction:**

MCA vide Circular No.11/2013 dated 29<sup>th</sup> May, 2013 (hereinafter referred to as the “Circular”)<sup>1</sup> has empowered Registrar of Companies (RoCs) to obtain declarations/affidavits from subscribers to the Memorandum & Articles of Association or first Directors at the time of incorporation. Further, whenever a Company changes its objects, RoCs may call for declarations/affidavits from Directors of the Company to the effect that Company or Directors shall not accept deposits unless compliance is ensured with applicable provisions of the Companies Act, 1956, RBI Act, 1934 and SEBI Act, 1992 and rules/directions/regulations made thereunder.

### **Background:**

Against the backdrop of recent Chit Fund controversy in West Bengal and arrest of Amway Officials, Ministry of Corporate Affairs (MCA) tries to save its face and cover up for its inability to trap these fraudulent companies, by coming up with an infructuous Circular.

### **Definition of Deposit:**

The term deposit has been defined under Section 45 I(bb) of the RBI Act, 1934 and under Rule 2 (b) of the Companies (Acceptance of Deposits) Rules, 1975. Further, paragraph 2(1)(xii) of the Non-Banking Financial Companies Acceptance of Public Deposits ( Reserve Bank) Directions, 1998 defines a ‘ public deposit’ as a ‘deposit’ as defined under Section 45 I(bb) of the RBI Act, 1934 and excludes from the definition of public deposit, amount raised from certain set of informed lenders who can make independent decision.

### **Critical Analysis**

The current set of rules and directions needs to be complied only when the Deposits are raised in the truest sense. A Company which raises so called “Deposits” in the form of advance against order of goods, hotel bookings, booking of tour, preference shares, issue of debentures cannot be brought under the purview of this Circular.

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<sup>1</sup> The text of the Circular is available at [http://www.mca.gov.in/Ministry/pdf/General\\_Circular\\_11\\_2013.pdf](http://www.mca.gov.in/Ministry/pdf/General_Circular_11_2013.pdf)



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Further, how will obtaining of an affidavit/ declaration from subscribers/ first Directors or Directors of the Company serve the purpose? Does non serving of an affidavit facilitate undertaking such activities?

In the backdrop of police action against Amway, Corporate Affairs Minister Sachin Pilot had stated in Delhi on 30<sup>th</sup> May, 2013 that the government is looking to remove the legal ambiguities to differentiate between fraudulent ponzi schemes and genuine businesses run by "reputed and law-abiding" entities.

"We (Corporate Affairs Ministry) will work closely with concerned ministries and industries to remove the ambiguity in the law (related to tackling ponzi and other fraudulent schemes) as soon as possible," he had stated.

However, the measures taken by MCA by way of issue of this Circular can hardly do any good in ensuring investor protection and healthy corporate capital market environment.

### **Conclusion**

MCA will not be able to keep a check on so called "deposits" raised by fraudulent companies, with an intent to cheat the investors, merely by empowering RoCs to call for a declaration/affidavit. The Circular will surely prove unfruitful in tackling this grave issue.

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