Chit Funds Amendment Bill, 2019

December 6, 2019
Source: *Economic Times*

Manifest pedagogy: Chit Funds and other forms of alternative investment schemes have been a gateway to financial savings and thus, are required to be a fail safe for people to meet exigencies, in light of such arguments, it is expedient to have proper legal and institutional regulations for these products.

In news: The Parliament has passed the Chit Funds (Amendment) Bill, 2019.

Placing it in syllabus: Micro finance institutions (explicitly mentioned)

Static dimensions:

- What is a chit fund?
- What are alternative investment schemes?
- Regulation of chit funds in india

Current dimensions: Scams in chit funds & Chit funds amendment bill

Content:

What is a chit fund?

- Chit fund is **defined as per Section 2(b) of the Chit Fund Act, 1982.**
- Chit funds are often **microfinance institutions.**
- Chit Funds are also known as the Chitty, Kuree, chit.
- It is a type of rotating savings and agreement among **different persons to subscribe a certain sum of money**

for a **specified period** of time.

- After specified period the **amount is returned to the subscribers** with interest.
- Chit fund helps in **collecting the small savings** of the individuals.
- It **helps small traders and businessmen** save excess cash on a daily or monthly basis.
- Chit companies are **more active in rural and town areas.**

What are alternative investment funds (AIFs)?

- Alternative investment funds are defined in **Regulation 2(1)(b) of the SEBI (Alternative Investment Funds) Regulations, 2012.**
- It refers to any **privately pooled investment fund, (whether from Indian or foreign sources)**, in the form of a trust or a company or a body corporate or a Limited Liability Partnership (LLP).
- Hence AIFs are private funds which **are otherwise not coming under the jurisdiction of any regulatory agency** in India.
- AIFs shall seek registration in one of the **three categories**
- **Category I:** Mainly invests in **start- ups, SMEs or any other sector which Government considers economically and socially viable.**
- **Category II:** These include **private equity funds or debt funds** for which **no** specific incentives or **concessions are given by the government** or any other Regulator. Category I and II are **close ended,** tenure shall be for a **minimum of three years.**
- **Category III: Hedge funds or funds which trade with a view to make short term returns** or such other funds which are open ended. They may also be close ended.

Regulation of chit funds in India:

- The Chit Funds in India are **regulated by the Chit Fund**

Act, 1982.

- Under this law, **registration** of the chit fund business can be **done only by the respective state governments.**
- The **Chit Registrar is appointed by the Government** under **section 61** of Chit Fund Act, 1982.
- If the **chit is not registered** with the registrar of chits then **neither it is legal nor bound to pay the deposited amount** of the subscribers.
- The **approval of a chit scheme may be refused** by the registrar if
  - the chit organiser has been convicted of any offence under the Act or
  - has defaulted in the payment of fees or
  - has been convicted of any offence and sentenced to imprisonment and a period of 5 years has not been lapsed since the release.
- **All the banks** (including co-operative banks) are **prohibited from conducting chit business** as per **Section 86** of the Chit Fund Act, 1982.

Scams in chit funds:

Saradha chit fund scam:

- Saradha Group chit fund scandal **duped 1.4 million investors in West Bengal and neighbouring states.**
- As much as **Rs 1,200 crore** was raised through its **illicit money pooling schemes** before the **company collapsed in April 2013.**
- The group used **collections from new investors to make payments to the previously-enrolled members,** rather than from income generated through investments.
- The activities of these companies were found to be in serious **violations of the Companies Act, SEBI Act** and several provisions of the **Indian Penal Code.**
- It was alleged that the **Mamata Banerjee led West Bengal government had a direct link with Sudipta Sen**, the Chairman of the chit fund group.

- Following the unearthing of the scam in April 2013, Mamata Banerjee-led **West Bengal government set up a Rs 500 crore relief fund for small investors** who had put money in the scheme.
- **Of the list of 87 such companies presented in Parliament**, against whom complaints had been received for indulging in Ponzi schemes, **seventy-three were from West Bengal.**
- **On April 23, 2013, Sudipta Sen, along with Debjani Mukherjee and Arvind Singh Chauhan, were arrested from Kashmir.**
- After serious allegations of international money laundering, the **case was transferred to the CBI by the Supreme Court of India in 2014.**
- By the time the CBI took over the case, the **Special Investigation team (SIT)** had arrested 11 people, traced 224 immovable properties, seized 54 vehicles and had filed chargesheets in nearly 300 cases.

Rose Valley chit fund scam:

- Rose Valley scam is the financial fraud which rocked state of **West Bengal in 2013.**
- As per **Enforcement Directorate (ED)** estimates **Rs 17,520 crore** was reportedly raised from investors across India.
- The **All India Small Depositors Association pegged the amount at Rs 40,000 crore.**
- The Rose Valley **group had allegedly floated a total of 27 companies** for running the alleged chit fund operations of which **only half a dozen were active.**
- It is alleged that the **company had made "cross investments" in its various sister firms** to suppress its liabilities towards investors.
- According to ED, a portion of the money was also used to **bribe politicians so that the scam could run smoothly.**
- In 2015, Rose Valley **chairman Gautam Kundu was arrested.**
- The **government froze all the 2,600 bank accounts of the**

Rose Valley Group, which held around Rs 800 to 1,000 crore.
- On January 25, 2019, CBI arrested Bengali film producer Srikant mohta for duping rose Valley group by Rs 25 crore.

Chit funds amendment bill:

-> The Act specifies various **names to refer to a chit fund** such as chit, kuri. The bill additionally **inserts 'fraternity fund' and 'rotating savings and credit institution'** to this list.

-> The Bill changes the names of the terms 'chit amount', 'dividend', 'prize amount' mentioned in the Act to **'gross chit amount', 'share of discount' and 'net chit amount',** respectively.

-> The Act specifies that a chit will be drawn in the presence of at least two subscribers. The Bill seeks to **allow these subscribers to join via video-conferencing.**

-> The Bill seeks to increase the **commission of foreman from 5% to 7%** and allows the foreman a **right to a lien against the credit balance** from subscribers. (*Lien is right to keep possession of property belonging to another person until a debt owed by that person is discharged).*

-> The Act specifies the **maximum amount of chit funds** as

(i) **one lakh rupees** for chits conducted by individuals and for every individual in a firm with less than four partners

(ii) **six lakh rupees** for firms with four or more partners.

The **Bill increases these limits to three lakh rupees and 18 lakh rupees, respectively.**

-> The Act does not apply to:

(i) any chit started before it was enacted

(ii) any chit where the amount is less than Rs 100

The Bill **removes the limit of Rs 100** and allows the **state governments to specify the base amount** over which the provisions of the Act will apply.