IN THE HIGH COURT OF JUDICATURE AT BOMBAY

CRIMINAL APPELLATE JURISDICTION

CRIMINAL BAIL APPLICATION NO.1263 of 2014

JIGNESH PRAKASH SHAH .. APPLICANT

Versus

THE STATE OF MAHARASHTRA .. RESPONDENT

Mr.Mahesh Jethmalani, Senior Advocate with Mr.Ameet Naik, Mr.Aniket U. Nikam and Ms.Gunjan Mangala i/b Mr.Aniket Nikam, Advocate for the applicant.

Mr.A.B. Avhad, Special Public Prosecutor.

Mr.V.B.Konde Deshmukh, APP for the Respondent State.

Mr.Sandeep R. Karnik, Advocate for the Intervenor.

CORAM : ABHAY M. THIPSAY, J.

DATED : 22nd AUGUST, 2014.

ORAL ORDER :

1 The applicant is the Accused no.10 in C.R.No.89 of 2013 registered by the Economic Offences Wing (EOW). The crime was initially registered vide C.R.No.216/13 of MRA Marg Police Station on the basis of a report dated 30th September 2013 lodged by one Pankaj Saraf, in respect of offences punishable under sections 120B IPC, 409 IPC, 465 IPC, 467 IPC, 468 IPC, 471 IPC, 474 IPC, 477-A of the IPC. Later on, investigation of the case was transferred to EOW, whereafter

the provisions of the Maharashtra Protection of Interest of Depositors Act (for short 'MPID Act'), were applied to the facts of the case.

2 The applicant was arrested on 7th May 2014. Before his arrest, a number of other accused in this case were arrested from time to time, and were released on bail. The applicant was arrested after charge-sheet had already been filed against some of the arrested accused.

3 When this application was made, investigation as regards the present applicant was proceeding, and no charge-sheet against him had been filed. The hearing of the Bail Application consumed quite some time, and when the hearing concluded, the applicant had already been in custody for about 85 days. It was, therefore, thought proper to defer the decision on the Bail Application till the filing of the charge-sheet, which was anyway expected to be filed within 90 days from the detention of the applicant in custody. On 90th day from the day on which applicant's detention in custody was first authorized, a charge-sheet came to be filed against him, whereafter, a copy thereof was provided to this Court, and also to the learned counsel for the applicant. Though the matter had already been argued fully by the learned Special Public Prosecutor and the learned counsel for the applicant, in view of

the filing of the charge-sheet, the learned counsel were permitted to advance further arguments, if so desired, and accordingly, concise oral arguments were advanced by the learned Special Public Prosecutor as also the learned counsel for the applicant after the filing of the charge-sheet. Intervention of the First Informant - Pankaj Saraf - in the matter was permitted and the Intervenor has, apart from advancing oral arguments through his counsel, filed written arguments in the matter.

4 I have heard Mr.Mahesh Jethmalani, learned counsel for the applicant. I have heard Mr. A.B.Avhad, Special Public Prosecutor. I have heard Mr.Sandeep Karnik, learned counsel for the First Informant at length. I have also heard one Ketan Shah who claimed to be an 'investor', and expressed a desire to make submissions on behalf of the 'investors', a number of whom were crowding the Court hall during the hearing of the bail application.

5 The case relates to the alleged scam that is said to have taken place in the activities and working of National Spot Exchange Ltd (for short 'NSEL'), a Company incorporated under the Companies Act, 1956, in May 2005.

6 It will be appropriate to examine what is the allegation in the First Information Report lodged by the Intervenor. The First Informant Pankaj Saraf is a Director of a Private Limited Company doing the business of 'investment, trading and financing'. That, he had been 'investing' in the traders contracts offered by the NSEL through his brokers – M/s.Capital Financial Commodities Ltd and Way to Wealth Pvt.Ltd. Mr.Pankaj Saraf had entered into a client-broker agreement with his brokers, and had submitted the necessary documents to them. The brokers were members of the NSEL. Pankaj Saraf was primarily transacting in T + 2 and T + 25 contracts. His grievance is that during the period from October 2008 to July 2013, NSEL allowed 25 members (who are named as accused) to trade on the exchange as sellers. It is alleged that in admitting these companies as members, due diligence was not observed. It is also alleged that these 25 members (sellers) had conspired with the applicant and the senior management of NSEL and in connivance with NSEL, traded fictitious stocks on the exchange by raising fake documents. That, the applicant and other senior officers of the NSEL were hand in glove with the defaulting parties, and have, in collusion with them, defrauded the First Informant. Though, during the initial contracts between these member companies as sellers and buyers, the Company squared off the contracts on the date of maturity but later, when the investment in these companies grew substantially, they did not

honor their commitments and caused a wrongful loss to the tune of Rs.2.2 crores to the First Informant. It is alleged that a loss of about 5600 crores was caused to the other '*investors',* numbering more than 13000.

7 In what manner NSEL was supposed to act, how the trading transactions were to take place, and how the offences came to be committed, can be best gathered from the relevant details given in column no.16 of the *printed prescribed proforma* of the police report/charge-sheet.

> "National Spot Exchange Limited (NSEL) is a spot exchange which was originally conceptualized by Jignesh Shah in the year in the year 2006. NSEL is meant to be an electronic platform that facilitated trading in 52 commodities throughout the country."

8 In order to understand the nature of the transactions in question, it would be necessary to understand *how* the business of the NSEL was to be transacted, and this has been explained in the police report/charge-sheet as follows:-

> Commodity spot trading is about buying and selling a commodity, paying cash for and receiving your goods on the 'spot'. This is called 'ready delivery contract' under FC(R) Act,

1952, which signifies that the buyer and seller agree on a price and 'deliver' their side of the contract immediately. NSEL is a spot exchange designed to help this activity, with the added feature of being electronic (so buyers and sellers can be in different locations) and anonymous (the buyer and seller don't know who the other side is). The important feature of any such exchange is that the exchange has to stand guarantee subject to its bye-laws to either party that it will ensure that the contract is settled. If the buyer can't bring in the money for any reason, the exchange should then sell the goods to someone else and recover the money (and make up the difference). And a similar exercise if the seller defaults. Now, when the seller and buyer are far away from each other, how does the exchange guarantee delivery ? The idea is that the seller must come to an exchange-designated warehouse and give his goods, which are then tested and verified for quality and weight. He then gets a warehouse receipt (WR) that is used for electronic trading. When he sells on the exchange, the warehouse receipt is transferred to the buyer; this receipt entitles the buyer to take the goods out of the warehouse, or if he chooses, to retain the goods there (to sell them later) by paying the warehouse rental charges.

9 How the traders' contracts were to work, has been explained as follows :-

The seller was required to deposit his stocks in warehouses which were approved and designated by NSEL on or before T, with T being the 'trade date'. NSEL was responsible for checking and verifying the quality and

quantity of he underlying commodities and goods are required to be compulsorily weighed at the designated weigh bridge/weigh scale and will be monitored and certified by the warehouse supervisor. Upon NSEL certifying the same, NSEL issued a warehouse receipt which was evidencing proof of ownership of a stated quantity of commodities of a stated grade and quality by the beneficial owner or the holder of the certified warehouse receipt. The depositor receives the photo / scanned copy of the warehouse receipt and the original is retained by the Exchange to transfer to the buyer upon the onward sale by the depositor. Additionally, a delivery margin of around 10% of the value of the goods was to be paid by the depositor to the Exchange.

On T, the investor enter into a contract to buy the commodities with T + 2 delivery cycle. Simultaneously, he would also enter into a contract to sell the commodities with a T + 25 delivery cycle. On T+2, NSEL would issue a delivery allocation report in which the quantity and location of the commodities purchased would be mentioned. The allocation report contained details of the end client, warehouse receipt No, Lot/QC No. and warehouse location. Further, it included a confirmation from NSEL that the original warehouse receipts were in it's custody.

As the original warehouse receipts were 1n the custody of the Exchange, NSEL vide its policy asked the investors (who were the sellers in the T+25 contract) to retain the goods in the Exchange certified and designated warehouse until 25 days passed as pre pay-in through warehouse receipts against

sale obligation. On the 25th day, the Exchange would then collect the money for the investor and would then release the goods to the buyer. NSEL was therefore the custodian of the goods from the time of purchase under the T+2 contract till the time of its sale and was responsible for its safe custody.

As is usually the norm in any electronic exchange, when a client trades on the anonymous order driven trading system on the Exchange, the buyer does not know the seller and in the same way, the seller does not know the buyer. But in case of the paired contracts, always the counter party is known through invoices.

Not only did NSEL permit investors to participate in these contracts, but, in fact, NSEL actively encouraged and induced investors to enter into such dual transactions.This active inducement was not just by highlighting the possible benefits available due to the price differential but also by providing economic rationale to investors by waiving storage charges for those members and their constituents who sell the product on the longer duration contract out of delivery receivable against the purchase position of the shorter contract. Accordingly, many members also actively marketed these contracts. Moreover, NSEL retained the warehouse receipts issued by it which were to be used to discharge margin obligations on the trades.

NSEL has 820 members of different categories which are as under:-

TCM - Trading Cum Clearing Member, TM - Trading Member, ITCM - Institutional Trading Cum Trading Member, PCM – Professional Clearing Member, TCM - A - For All Agri-Commodities all Delivery Centres in a State, TCM - B - For Single Agri-Commodity All Delivery Centres in a State, TCM - C - For Single Agri-Commodity Single Delivery Centre in a State, TCM - Pulses - For Pulses in a Particular State .

The members were required to register the client prior to executing trades on their behalf. For this purpose, the members required their clients to submit the duly filled in prescribed 'Know Your Customer' form and execute the member - client agreement with the members. Thereafter, the members would upload the relevant details in the Exchange software in order to generate the Unique Client Code ("UCC"). Once the UCC was generated, the client was permitted to execute trades through the members. There are around 13,000 clients of the above Members of the NSEL.

The trades were generally executed by members on behalf of their clients in the following manner:

i. On the 'Trade Date (T), the following actions take place:

a the trade is executed by the member on behalf of the client

and

b pursuant to execution of the trade, a confirmation E-mail was sent by the member to the client along with the provisional return computation on the trade;

ii. On T+ 1, a contract note is issued by the member to the client for the Buy and Sell side;

iii. On the same day or prior to it, member collects monies from the clients

iv. On T+2, the following actions will take place:

a. pay in of funds by the member on behalf of the client for the trade; and

b. pay out of commodity (the Warehouse Receipt for which is retained by the Exchange as early pay in for the pay in obligations for the T+25 trade);

v. On T+3, client wise delivery allocation report for the executed trade is available on the Exchange interface for download by the member;

vi. On T+25, the trade is settled by way of pay out of funds.

All trades, T+2 and T"T25, are settled in accordance with the Settlement Calendar issued by NSEL for that month.

10 Indeed, it appears that the NSEL deviated from its business model. It also appears there had been no actual physical delivery of commodities, and bogus warehouse receipts were issued. NSEL was actually supposed to trade in commodities, but instead of doing that, it permitted bogus transactions of trading to be introduced and resultantly, in effect, permitted financial transactions of lending and borrowing.

11 I have carefully considered the whole matter in all its perspectives. The contentions advanced on behalf of the applicant, as also the contentions advanced by the learned Special Public Prosecutor, have undergone slight changes when certain aspects of the matter

became clear. Similar is the case with the contentions advanced by the First Informant/Intervenor.

12 The first and foremost contention advanced on behalf of the applicant is that the applicant is not responsible for these illegalities, irregularities and wrongs that have taken place in the affairs of the NSEL. It is submitted that the applicant is a Non-Executive Director in the NSEL. It is submitted that the wrongs of permitting trading in fictitious stocks, issuing warehouse receipts without there being stocks deposited in the warehouse, etc, have taken place at the level of the employees concerned of NSEL, and at the most, at the level of the active Directors of the NSEL. It was contended that there is nothing to show that the applicant was aware of these irregularities/illegallities.

13 In view of this contention, the emphasis of the learned Special Public Prosecutor and the learned counsel for the Intervenor has been on unacceptability of such a contention. It was pointed out that NSEL was promoted and controlled by Financial Technologies (India) Ltd (for short 'FTIL'), and that FTIL owns 99.99% of the shareholding of NSEL. It was contended that the applicant is a Promoter Director of NSEL, and that he and his family hold about 44% of the total shareholding of the FTIL. It is submitted that it was, therefore,

impossible to believe that the applicant was not aware of what was happening in respect of the NSEL transactions. During the pendency of the present application, the statements of some persons came to be recorded, from which certain facts making it clear that the applicant could not have been unaware of the bogus and fictitious transactions of sale and purchase that were taking place on the NSEL platform, have been revealed.

14 In the view that I am taking, it is not necessary to discuss such material in depth, and what needs to be observed is that, going by the facts of the case, as reflected from the investigation that has been carried out so far, and judging by the broad probabilities of the case -- as should be done at the stage of bail – it cannot be accepted that the applicant had no knowledge of the illegalities/fraudulent transactions that were taking place in the activities of NSEL.

15 What, however, is significant is that though these illegalities or this 'fictitious trading' is sought to be highlighted as material against the applicant, *the real grievance of the First Informant - and even of the other investors - is not with respect to the fact that such fictitious trading was taking place*. Their grievance is that their money has been lost. A big uproar has been created by them, and for showing the magnitude of

the alleged offences, it is termed as a 'scam of about Rs.5600 crores'. In this connection, certain basic aspects of the matter cannot be lost sight of. The persons whose monies are lost, including the First Informant, are apparently, not the genuine traders for whom NSEL was supposed to provide a platform. The very fact that these persons are, as also the Investigating Agency is, freely using the terms as the '*investors*', 'borrowers', indicates that, that the transactions in question were not genuine transactions of sale or purchase was well known to the so-called buyers also, who now choose to describe themselves as '*investors*'. It is clear that from their point of view, it was only *an investment yielding high returns for their money*. These investors are not middle class or lower class people, but are themselves businessmen. The transactions in question were being entered through brokers who had knowledge of the commercial market. Going by the broad probabilities of the case, it cannot be accepted that the persons who are now crying foul, were not aware of the fact that their transactions were not genuine. They were looking at these transactions clearly as an investment of their monies yielding safe returns. Their estimate or belief about the safety of the transactions has been proved to be wrong, and that is the reason for the uproar which is now being made by pointing out the illegalities in the transactions undertaken by NSEL. Undoubtedly, these wrongs appear to have taken place, and undoubtedly, it cannot be suggested that those

who permitted such fictitious trading have not committed serious offences, still, the fact remains that the persons who are raising the grievance about such fictitious tradings were themselves not genuine traders, and had entered into the transactions purely as financial investments. There is every reason to believe that a sizable number of so-called 'investors' whose transactions were being entered into through brokers, actually did not bother about the fictitious trades, and knowingly participated in such illegal activities, without raising any issue of illegality thereof.

16 There is great substance in the contentions advanced by the learned counsel for the applicant that the brokers through whom the so-called trade transactions were entered into, do have their own legal team and a full knowledge of how the market operates. The legalities of the transactions were quite expected to be known to the brokers and the traders who do not hesitate to term themselves as 'investors', and they were expected to assess the legalities of the transactions. The brokers being quite experienced, and the *investors* being informed persons, it is apparent that the issue of illegality of the transactions raised by them is not out of their concern to adhere to legalities, but in order to project the applicant as the main offender, rather than the defaulting parties.

17 It may be observed in this context, that the legality of the application of the provisions of the MPID Act to this case is not free from doubt. Whether the monies paid by the buyers for purchasing the commodities would amount to 'deposit' as defined in clause (c) of section 2 of the MPID Act, would need serious consideration. Whether NSEL can be termed as a 'financial establishment' as defined under clause (d) of section 2 of the MPID Act, would need equally serious consideration. Since I am dealing only with a Bail Application it would be neither necessary nor proper to go deeper into this aspect, but what needs to be said it that the 'investors' in this case are not the type of persons for whose protection MPID Act has been enacted, as reflected from the statements of objects and reasons behind the said enactment.

18 Though the case has been projected as a 'scam of Rs.5600 crores', it needs to be kept in mind that these amounts have not been received by NSEL. As already observed, it is difficult to accept that the brokers and/or their clients for whom they were working were '*deceived*' by the NSEL inasmuch as in all probability, the brokers and the investors were well aware that they were not entering into a genuine sale and purchase contract. When there is a clear and obvious possibility that these persons knew about the transactions, the 'deception' if any, caused to them cannot be said to have been caused *by the nature of the*

transactions and, at the most, they can be said to have been misled by a propoganda that 'investing' money in those transactions, was safe. The money invested has not come to NSEL, but has gone to the borrowers. i.e. bogus sellers. It is the borrowers who have been benefited by the transactions and the money of '*investors*' has gone to them. The names of 25 different companies who are the defaulters have been mentioned in the FIR itself. Thus, though projected a 'scam of Rs.5600 crores', the ill-gotten amount has not gone to the applicant, or for that matter, to NSEL. In fact, it is not the case of anyone.

19 The picture that emerges is as follows. Indeed, illegal and bogus transactions of sale and purchase were shown as having taken place. This has been possible because the NSEL did not stick to its business model. Instead of providing a platform for genuine buyers and traders, this platform was permitted to be used – and actually used – by businessmen who wanted safe investments for their money. These investments were made through brokers who were well experienced with the working of the market. To show bogus sales, bogus documents were created by the bogus sellers/brokers, and this has been possible with the connivance of the officers and directors of NSEL. Though the applicant's contention that he was not aware of the illegalities, or that he being a Non-Executive Director of NSEL was not concerned with the

illegal activities, cannot be accepted, it is also clear that, that the transactions were not genuine, was in all probability, known to the '*investors*' – atleast to a great number of them – and in any case, certainly known to the brokers who were entering into the contracts for their customers – investors. This fact is obvious to the Investigating Agency also, inasmuch the buyers and sellers are freely described as '*investors*' and 'borrowers'. The NSEL, by its improper and wrong working, did provide an opportunity for the unscrupulous 'borrowers' to have huge funds for themselves. However, in the zeal of opposing the applicant's application for bail, it is, perhaps, conveniently ignored that the funds had not come to NSEL, but had gone to such borrowers. Though a number of contentions showing his complicity in the whole matter are raised, on a careful consideration and scrutiny of the matter, the only real allegation against the applicant is that he allowed NSEL to violate the rules and regulations, and its own business model, **which enabled the 'borrowers' to dupe the '*investors*'**.

20 Undoubtedly, an allegation that this has been done by the borrowers in conspiracy with the NSEL – and consequently with the applicant – has been made. However, there is no material to show the same. There is no allegation that the applicant has acquired from the borrowers any part of the ill-gotten money earned by them, as a

consideration for making it possible for them to commit such frauds, or that, any part of the money earned by the borrowers in such a dishonest manner, has been received from them by the applicant. It is almost conceded that there has been no material to show any direct connection or link between the defaulting borrowers and the applicant. When this aspect of the matter was discussed in the course of hearing, a number of contentions showing how the *applicant stood benefited by the fraudulent transactions*, were advanced. It is submitted that these transactions resulted in increasing the turnover of NSEL, improved its market reputation and consequently, benefited the FTIL Group of which the applicant is a major shareholder. It is submitted that the applicant has received benefits from these frauds by way of increase in the income of FTIL and the consequent benefits accruing to the applicant from salaries, commission etc. However, it is obvious, *prima facie,* that had the applicant conspired with the bogus sellers/borrowers/defaulters and had he permitted the illegal activities to take place so that such bogus sellers/borrowers/defaulters should make huge money for themselves, he would never be content with the indirect and incidental benefits, which allegedly accrued to him through FTIL.

21 When this aspect of the matter was discussed, it was suggested that there might be a possibility of some cash through *hawala*

transactions having been passed over to the applicant by the defaulting borrowers. It is submitted that to detect such transactions, indepth investigation is necessary and that, investigation is proceeding in that direction. That, certainly, is *possible*. Such investigation, however, is admittedly, likely to take much time, and it is not possible to hold that the applicant needs to be detained merely because such a possibility exists. It is a fact that as of today, there is no material to show any direct link between the amounts dishonestly earned by the borrowers and the amounts received by the applicant. The benefits which the applicant is said to have gained from these transactions are only indirect benefits such as increase in the volume of business and consequent increase in the profit of FTIL, and are not sufficient, in itself, to support a theory of conspiracy. The very fact that it would take quite some time to investigate whether the proceeds of crime, or a part thereof has been received by the applicant from the defaulting borrowers, (which undoubtedly would support the conspiracy theory) would weigh in favour of granting bail to the applicant, rather than weighing in favour of detaining him in custody till this aspect would be clear. Sufficient time has already been given to the Investigating Agency and in spite of this, no link or connection between the proceeds of crime and the applicant, has been revealed so far.

22 It was submitted on behalf of the intervenor and also by one Ketan Shah – who claimed to be a representative of the *investors,* and who was permitted to make brief submissions opposing the grant of bail – that the applicant is a monied person and that he should give some offer – of returning the money – to the *investors,* to prove his bonafides. It was submitted that as in the case of Subrata Roy (Sahara Vs. Union of India & ors (Writ Petition (Criminal) No.57 of 2014) decided on 6th May 2014, who has been detained by Their Lordships of the Supreme Court of India, the applicant should also be detained in custody till he gives such offer. This submission and this expectation is not proper. In the first place, though this is termed as a 'scam of Rs.5600 crores by NSEL', it is not that monies have been received by NSEL, but they have gone from one bogus trader (investing) to another bogus trader (borrower). At the cost of repetition, it needs to be observed, that from an analysis of the allegations, it becomes clear that the real and only allegation against NSEL is that it adopted such *modus operandi* that permitted the borrowers to dupe the investors. The benefits received by NSEL and FTIL and consequently, by the applicant from these fraudulent transactions, are only incidental. Therefore, merely because the applicant is a monied person and is likely to be in position to satisfy some investors – as was stated before this Court on behalf of the investor and the investors – he cannot be detained in custody for the purpose of

forcing him to do so. The expectation is not that the money gone in his pocket should be taken out by him, but the expectation is that *he having been instrumental in the duping of investors by the borrowers be made to pay to the investors as he has sufficient means to do so*. Perhaps, the First Informant and the investors feel that by putting the applicant in a difficult situation, it would be easier for them to recover their money. The culpability of the applicant cannot successfully be projected to be of a higher degree than that of the 'borrowers' (bogus sellers) and their brokers, who have actually taken away the money. The example of Subrata Roy is most inappropriate as the facts of that case and the circumstances in which Their Lordships of the Supreme Court directed his detention are entirely different. Moreover, by virtue of Article 142 of the Constitution, the Supreme Court has full power and authority to make any order *for doing complete justice between the parties*. Such power, this Court does not have.

23 There are also some other aspects, a mention of which would be necessary. Though there are direct allegations against the applicant in the FIR itself, the applicant was not put under any arrest. Five other accused were arrested and charge-sheeted. (It is only at about that time that the applicant was arrested). Three of them are the officials of NSEL and two, are the 'borrowers' who have made huge

defaults. Thereafter, without any new material, the applicant came to be arrested. The case of the Investigating Agency earlier was that the co-accused Anjani Sinha, the CEO of NSEL had taken the entire responsibility of the wrongs upon him. Though I am not suggesting that, that should be accepted as a fact and would certify the applicant's innocence, the fact remains that no necessity was felt by the Investigating Agency of arresting and detaining the applicant in custody for the purpose of investigation. In fact, the investigation proceeded ahead and resulted in filing of charge-sheet against the accused persons who had earlier been arrested. Certain property of the arrested accused and also of the applicant, has been attached in the course of investigation. Therefore, it is not that the applicant's detention in custody is essential for further investigation.

24 All said and done, there is no change in the legal principle that pre-trial detention can never be authorized as and by way of infliction of punishment.

25 The applicant is not likely to abscond if released on bail. Appropriate conditions can be imposed upon the applicant to ensure his availability to the Investigating Agency and to the Court.

26 Application is allowed.

27 Applicant is ordered to be released on bail in the sum of Rs.5,00,000/- (Rupees Five lakhs only) with one surety in like amount, on the condition that the applicant shall report to the office of the Investigating Agency on every Monday and every Thursday between 11.00 a.m to 1.00 p.m for a period of two months from today, and thereafter until further orders of the trial court.

28 At this stage, the learned counsel for the applicant prays that as the health of the applicant is deteriorating, and as it would take quite some time to furnish sureties in the amount of bail, the applicant be temporarily released on his depositing cash in lieu of surety. Since I do not think there there is any possibility of the applicant absconding, if permitted to deposit cash in lieu of surety, I am inclined to grant such a prayer.

29 The applicant may deposit cash of Rs.5,00,000/- in lieu of surety, temporarily, for a period of two weeks within which period the applicant is expected to furnish solvent surety in the amount of bail.

30 The counsel for the intervenor prays for the stay of the operation of this order.

31 Prayer rejected.

(ABHAY M.THIPSAY, J)