"The Hon'ble Special Court passed an order on 21.07.1994 in MA 269 of Court criticized the dishonest conduct of SCB." 1993 filed by Custodian for recovery of 50 lakhs Units from SCB. The Hon'ble Special

IN THE SPECIAL COURT (TRIAL OF OFFENCES RELATING TO TRANSACTIONS IN SECURITIES) AT BOMBAY

MISC. APPLICATION NO. 269 OF 1993

A. K. Menon, Custodian ...Applicant

Vs.

1. Standard Chartered Bank
2. Harshad S. Mehta
3. Growmore Research and Assets Management Co. Ltd. ...Respondents

Mr. A. M. Setalvad with Mr. G. R. Joshi i/b. M/s.P. M. Mithi & Co. for the Applicant

Mr. D. D. Madon with Mr. T. K. Cooper i/b. M/s. Gagrat & Co. for Respondent No. 1.

Mr. Anand Desai i/b. M/s. Mahimtura & Co. for Respondent Nos. 2 and 3.

CORAM: S. N. VARIAVA J.

21ST JULY 1994

ORAL ORDER:

1. This Application is by the Custodian for recovery of 50 lac units from Respondent No. 1. The Custodian claims that these belong to Respondent Nos. 2 and/or 3.

2. Day before yesterday i.e. 19th July 1994 when this Application reached hearing Mr. Madon applied for an adjournment on the ground that the 1st Respondent wanted to challenge the virus of

Section 16 of the Securities Contract (Regulation) Act, 1956 and a Notification dated 27th June 1969 issued thereunder. It must be mentioned by way of clarification that this Court has, by a Joint Order dated 14th December 1993 in Misc. Application No. 11 of 1993 and Misc. Petition No. 23 of 1993 held that all ready-forward transactions are illegal by virtue inter alia of the provisions of Section 16 of the Securities Contract (Regulation) Act, 1956 and by virtue of the Notification mentioned above. Before this Court, there are a number of matters where the transactions are ready-forward transactions. All matters had been adjourned from time to time in order to enable parties to have the Order dated 14th December 1993 tested in the Supreme Court and/or to take such steps as they may be advised. This matter has also been adjourned on 18th January 1993, 15th March 1993, 30th March 1993, 19th April 1994, 26th April 1994, 14th June 1994 and 22nd June 1994 on this very ground. The Court has been making it clear to parties that these matters would now not be adjourned any further. Therefore, on 19th July 1994, as in spite of so many adjournments no steps had been taken by the 1st Respondent, this Court refused to adjourn the matter any further. At the request of Mr. Madon it was however kept back

till the 20th July 1994. This matter was then argued on 20th July 1994. As one of the contentions raised by Mr. Madon was covered by an Order of this Court and Mr. Madon wanted to study that Order, the matter was kept back till today.

3. The facts are as follows:

On 13th February 1992, 1st Respondent entered into a Contract. Under this the 2nd Respondent bought for the 1st Respondent 50 lac Units at the rate of Rs.14.18000 per Unit. On the same day it was also agreed that these Units would be resold on 12th May 1992 at the rate of Rs. 14.76430. Thus, on 13th February 1992 there was a Contract to purchase at a particular rate with a commitment to re-sale on 12th May 1992 at a fixed rate.

4. Mr. Madon has submitted that in the Order dated 14th December 1993, the Court has not defined a ready-forward transaction. But apart from this submission there is no denial that a Contract to purchase or sell with a firm commitment to re-sell or re-purchase on a fixed date and at a fixed price would be a ready-forward transaction. Thus, it has not been explained to this Court how according to the 1st Respondent, this was not a ready-forward transaction.

5. The 2nd and 3rd Respondents were

notified on 8th June 1992. Normally it would be expected that all parties particularly a major Financial Institution like the 1st Respondent would honestly and immediately intimate to the Custodian all transactions which they have had entered into with the 2nd or 3rd Respondents. The 1st Respondent do nothing. The 2nd Respondent by his letter dated 5th March 1993 informed the Custodian about this transaction. He informed the Custodian that the 1st Respondent had failed to reverse the transactions. He requested the Custodian to therefore raise an appropriate claim on the 1st Respondent. A copy of this letter was also sent by the 2nd Respondent to the 1st Respondent.

6. The 1st Respondent by their letter dated 11th March 1993 addressed to the Custodian, replied to the letter of the 2nd Respondent dated 5th March 1993. In their reply, they state as follows:

" As you may be aware M/s. Growmore Research & Assets Management Ltd. (GRAM) and/or Harshad S. Mehta (HSM) have defaulted in repurchasing numerous assets sold to Standard Chartered Bank (CCDS) on a Ready Forward Basis. Examples are given on page 51, Para 10.9 (a) of Report No. 4 of the Janakiraman Committee. As a result of this default for an aggregate

maturity value of at least Rs. 95.43 crores, SCB has suffered loss of interest and depreciation of underlying assets.

Indicatively, on 12/5/92 itself, another asset viz. Canpremium of Face value Rs. 11 crores was to be repurchased at the rate of Rs. 11.00 %. Present market value is expected to be about 8.00%. The loss incurred by Standard Chartered Bank on account the depreciation in market value is about Rs. 3.3 crores and in addition an interest loss of Rs. 2.15 crores has been suffered by SCB from 12/5/92 to 15/3/93 @ 21% per annum.

In the circumstances, there is no question of Standard Chartered Bank being liable to pay GRAM/HSM any sum of money whatsoever in respect of unmatured Ready Forwards. On the contrary, GRAM/HSM has caused considerable loss/damage to SCB on account default in repurchasing various assets sold to SCB on R/F basis. "

Thus, to be noticed that the 1st Respondent do not deny the transaction. In fact they admit that there was a firm re-commitment to sell on 12th May 1992. Also to be noted that 1st Respondent do not deny

that the Ready-Forward Contract is with Respondents 2 and 3.

7. As the 1st Respondent was not denying that this transaction had taken place, but was denying that it was liable to return these securities, the Custodian has filed this Application. The claim of the Custodian is that as the transaction is a Ready Forward Transaction, it is illegal under the Securities Contract (Regulation) Act, 1956 and that it is covered by the Order dated 14th December 1993 mentioned above. It is the Custodians claim that under this alleged contract, no rights are created in the Units in favour of the 1st Respondent and the 1st Respondent is bound to return the Units. Alternatively it is claimed that in any case the Units were to be returned on 12th May 1992 and for that reason also the Units should be returned.

8. It would be pertinent to mention, at this stage, that the Reserve Bank of India has also looked into this aspect. After looking into this aspect, the Reserve Bank of India has reported as under :-

" Standard Chartered Bank

- Irregular Investment transaction
- Claims made by Harshad S. Mehta

As per the Central Office note dated 16.4.1993 sale of 50.00 lakh units of UTI for Rs. 7.09 crores made by Harshad S. Mehta (HSM) to the bank on 13.2.1992 was examined. The bank has replied on 11 March 1993 to the Custodian in the matter (copy enclosed). It was observed that Harshad S. Mehta had bought for the bank 50.00 lakh units of 1964 Scheme @ Rs. 14.18 on 13.2.1992 from Growmore Research Management (GRAM) for Rs. 7.09 crores against physical delivery of the units as revealed by deal slip No. 221. On ready forward (R/F) basis reversible on 12.5.1992. The payment for the purchase was made by the bank by way of a bankers cheque favouring State Bank of India. The units so purchases were sold to the Housing Development Finance Corporation Ltd. (HDFC) on the same day for Rs. 1.10 crores on R/F basis reversal being on 13.5.1992 as against the reversal date of 12.5.1992 of purchase from GRAM. On 12 May 1992 the R/F with HDFC was concluded but instead of concluding the Second leg of R/F with GRAM the bank rolled over the contract,

i.e. showed a sale and purchase of 50.00 units simultaneously at even rate of Rs. 14.7709 per unit with GRAM. The authority for/confirmation of the roll over was not traceable by the bank. Further, the bank had sold the Units to GRAM/Harshad Mehta on 13.5.1992 @ Rs. 14.1709 as against the contracted rate of Rs. 14.76430 reportedly due to one day's interest differential. The particulars of the units in question held with the bank were not traceable for identification. Thus, the bank has not rolled over , the second leg of the R/F transaction entered into with H. S. M. on 13.2.1992.

Sd/-

Date:14.5.1992 (A. V. Sardesai)

Principal Inspecting Officer

Encl: 10 sheets."

To be noted that this Report is made by the Reserve Bank of India after it had called for explanations from the 1st Respondent. To be noted that before the Reserve Bank of India it is admitted that the Securities were belonging to the 2nd Respondent.

9. The 2nd and 3rd Respondents have supported the Custodian. The 2nd Respondent by his

Affidavit dated 29th March 1994 has placed all the relevant documents before this Court.

10. The 1st Respondent has filed an Affidavit-in-Reply dated 13th April 1994. This Affidavit is after the Affidavit filed by 2nd and 3rd Respondents. In this Affidavit it is inter alia averred as follows :-

"2. At the outset, I respectfully submit that the application is thoroughly misconceived and not maintainable and no reliefs could or should be granted as prayed for against Respondent No. 1. The Units which were purchased by Respondent No. 1 were purchased under a CCDS Scheme on behalf of its clients and were duly paid for by the Respondent No. 1 on behalf of its clients. The said Units sold to Respondent No. 1 were apparently delivered to the Respondent No. 1 in respect of which the Respondent No. 1 issued its Bankers Receipt favouring its client as requested. Thereafter in March 1992 and subsequently further transactions took place under which the Bankers Receipts were returned and fresh Receipts were issued. Ultimately, as a result of subsequent transactions, the

Units were sold by the Respondent No. 1 prior to 31st May 1992 and Respondent No. 1 does not have possession thereof. In fact, it is extremely material to note that the Respondents 2 and 3 are apparently fully aware that the Units were and are not in the possession of the Respondent No. 1 but with another bank, pursuant to which they requested the Custodian to proceed for recovery of these Units from the hands of the said Bank. It is for this reason that the Respondent No. 1 has by its Advocates' letter dated 14th January 1994 called upon the Custodian to furnish particulars of the distinctive numbers of the Units claimed and also to confirm the correctness of what is stated hereinabove. If, as the Custodian; contends, this application is to recover any Units as continuing to be the property of a notified person, there are no such units and there is no such property in the hands of Respondent No. 1. "

In this Affidavit, thereafter it is averred that such a transaction is not illegal and is not in

violation of the Securities Contract (Regulation) Act or any Guidelines of the Reserve Bank of India. To be noted that in this Affidavit also there is no denial that there was a Contract to purchase 50 lac Units at the rate mentioned with a firm commitment to re-sell the same on 12th May 1992. In this Affidavit also there is no denial that the Units belonged to Respondents 2 and/or 3. Therefore, even in this Affidavit, there is no denial of the transaction. All that has been claimed in this Affidavit is that the Units were not now available with the 1st Respondent.

11. On 20th July 1994 after finding that the Court was not adjourning the matter any further, another Affidavit dated 20th July 1994 is filed. In this Affidavit, for the first time, the provision of Section 16 of the Securities Contract Act and the Notification mentioned above are sought to be challenged as ultravirus the Constitution of India. In my view, it is clear that such a challenge cannot be raised in this Court. As stated above, enough opportunity was given to the 1st Respondent to take whatever steps they wanted. Till date, they have done nothing of the sort. The attempt to raise this challenge by this Affidavit is, in my view, just an attempt to further delay this matter.

12. As stated above, the transaction is admitted. The only contention now taken is that the Securities are not available with the 1st Respondent. It is submitted by Mr. Madon that no distinctive numbers have been given. He submitted that the Securities which had been purchased on 13th February 1992 are no longer available with the 1st Respondent and that they have been re-sold by the 1st Respondent. He submitted that, as the exact securities which were delivered were no longer available, the 1st Respondents are not even in a position to deliver those securities. He submitted that the claim of the Custodian for return of the securities does not survive.

13. I see no substance in this contention. It is a well established practice, which cannot and is not denied, that ~~so far as~~ the Banks/Financial Institutions whilst dealing in securities, very rarely mention distinctive numbers of the securities in the Bankers Receipts or S. G. L's. The Banks/Financial Institutions deal in quantity and ~~or~~ the type of the securities. It is a well established fact that even though there may be a firm commitment to re-sell or re-purchase, those exact securities which had been delivered (under the first part of contract) will never be retained. To do so would be to cause financial loss to an

Institution which would have to hold on to those securities. Therefore, the practice always has been that the Banks/Financial Institutions further deal in those securities. The commitment therefore is to return the same type and quantity of securities on the prescribed date. This question was also considered by this Court and decided by an Order dated 26th July 1993 in Misc. Application No. 53 of 1993. It is to consider this Order that Mr. Madon took time upto today. Today he has made no submissions on this Order. This Order is binding on Respondent No. 1.

14. It is therefore clear that what has to be returned is not the exact same securities (which had been delivered to the 1st Respondent) but an equivalent number of Units at the price which has been fixed. It is therefore, in my view, no defence to say that the exact same Units are not available. What the 1st Respondent has to deliver is 50 lac Units.

15. Mr. Madon next contended that the Contract Notes and Deal Slips disclosed by the 2nd Respondent, show that the 2nd Respondent has merely acted as a Broker in these transactions. He submits that the Units belong to the party described in the Deal Slip as "SBICBRT". He submits that as the 2nd

Respondent has merely acted as a Broker, the Units do not belong to the 2nd Respondent. He submits that there is nothing to show that the Units belong to the 3rd Respondent. He submits that therefore these are not the Units belonging to either the 2nd Respondent or 3rd Respondent and the Custodian can make no claim on these Units.

16. This argument overlooks the fact that in the Application it is specifically claimed that this property belongs to Respondents 2 or 3. In the first Affidavit which is filed, there is no denial of this fact. For the first time, it is only by Affidavit on 20th July 1994, that this fact is sought to be denied. This overlooks the fact that before the Reserve Bank of India and in the enquiry conducted by the Reserve Bank of India, it is admitted by the 1st Respondent that these units belong to the 2nd Respondent. This argument overlooks the fact that in the 1st Respondent's letter dated 11th March 1993, addressed to the Custodian, it is not denied that these belong to the 3rd Respondent. Thus, by an Affidavit filed at the last minute in Court, an attempt is being made to resile from admissions which have been made earlier. This cannot be permitted. This again is merely an attempt to delay.

17. Apart from this, one of the purposes of

the Special Courts Act is to see that all matters come before one Forum. The whole purpose being that this one Forum has an over-all picture of what is happening. It is a fact, which must be judicially noted, that before this Court, it is now clear that the 2nd and 3rd Respondents operated, amongst others, through the medium of the State Bank of India. Through the medium of State Bank of India, the transactions in securities would take place. However, the transactions were really transactions of the 2nd or 3rd Respondents. In fact the wordings on the Deal Slip "SBICBRT" refers to the Current Account of the Respondent No. 2 in the State Bank of India. The monies which have been paid by 1st Respondent were credited into this Account. I therefore see no substance in the contention that these securities did not belong to the 2nd and 3rd Respondent. It is clear and to the knowledge of the 1st Respondent, the transaction was with the 2nd and 3rd Respondent. It is only with a view to get out of admitted liability that such a contention has now been taken up.

18. It is thus clear that the 1st Respondent is bound to return 50 lac units. They have failed to do so. As they have failed to do so, this Court must call upon them to deliver 50 lac Units.

19. On behalf of the 2nd and 3rd Respondents, it is submitted that a Rights Issue had been offered at a concessional and discount price of Rs. 12.80 in the ratio of 2:5 Units. It is claimed that by reason of the 1st Respondent not delivering the Units as per the Contract, the 2nd and 3rd Respondents were unable to take advantage of these Rights Issue. It is submitted that the 2nd and 3rd Respondents would have been able to get 20 lakh more Units under this Rights Issue. It is claimed that the 1st Respondent should now be called upon to deliver additional 20 lakh Units.

20. On behalf of 2nd and 3rd Respondents it is also claimed that dividends had been issued on 30th June 1992. It is claimed that on this account, there has been a loss of Rs. 4,19,10,000/-. It is also claimed that there is a loss of interest on the amount of dividends in a sum of Rs. 1,16,36,160/-. Therefore, according to Respondents 2 and 3, the 1st Respondents should deliver 20 lac more Units and pay damages towards loss in a sum of Rs. 5,35,46,160/-.

21. Mr. Madon opposes this. He rightly points out that no such claim is made by the Custodian in his Application. He points out that the 2nd and 3rd Respondents cannot make any such claim in this Application. In my view, Mr. Madon

is right. These cannot be considered in this Application. It is open to the 2nd and 3rd Respondents to make whatever claim they want for additional Units or for loss or damages by way of a separate Application, if they so desire.

22. Mr. Madon next submitted, relying upon para 52 of the Order dated 14th December 1993 in Misc. Application No. 11 of 1993 that the property in these Units stands transferred to the 1st Respondent. He submitted that therefore on the principles laid down in this paragraph the only remedy of the Custodian would be to move under Section 4 of the Special Courts Act to set aside this Contract and to claim recovery of the Units. In my view, the observation made in the said para 52 are being misconstrued. They do not deal with cases of illegal contracts. They deal with cases where there is a valid contract under which a transfer has taken place. In this case, it is an admitted position that there was a Ready-forward transaction. The Court has held that all Ready-forward transactions are illegal transactions. The Court has clearly held, in this very Order that under such illegal transactions, no third party rights are created and that the properties remain properties of the Notified party. In this case, therefore, no rights can be claimed by the 1st

Respondent under an illegal transaction. What Mr. Madon has relied upon is only the forward part of the illegal transaction. Under the circumstances, I see no substance in this contention also.

23. It is submitted by Mr. Madon that even in the event of this Court coming to the conclusion that there is a breach of the Contract, all that the Custodian is entitled to is difference in price between Rs. 14.76430 and the market price of these Units as on 12th May 1992, provided the market price was higher. I am unable to accept this submission. The claim of the Custodian is for the return of Units. This not on the ground that 1st Respondent was bound to return on 12th May 1992 but mainly on the ground that this being a Ready Forward Transaction is illegal and that no rights are created in the Units in favour of Respondent No. 1. By Order dated 14th December 1993, mentioned above (which is binding on Respondent No. 1) this contention has been upheld. Thus the Units which continue to belong to Respondents 2 and 3 must be returned. As held above, the 1st Respondent is bound to return the Units. There is therefore no question of considering any damages in this matter. All that the Court has to do is to call upon the 1st Respondent to return the Units. They would be entitled to receive the sum paid by

them on 13th February 1993 for these Units. However, as held by the Order dated 14th December 1993, since Ready-forward transaction itself is an illegal transaction, the question of restitution to the 1st Respondent would be at the stage of the distribution under Section 11.

24. It must also be mentioned that the Applicants have not challenged the Order dated 14th December 1993 nor sought, so far, to intervene in the Appeals filed in the Supreme Court against that Order. This in spite of the following which is set out in Order dated 14th December 1993 in Misc. Application No. 11 of 1993 :-

> "...Mr. G. E. Vahanvati is appearing for Vijay Bank in Misc. Petition No. 22 of 1993 and for the Standard Chartered Bank in Misc. Application No. 269 of 1993. He however clarified that Misc. Application No. 269 of 1993 is not ready for hearing and, therefore, at this stage he is not making any submissions on behalf of the Standard Chartered Bank. He clarified that he realised that the Judgment in this matter, on the question of law, would also bind the Standard Chartered Bank. "

25. Under these circumstances, the Application is made absolute in terms of prayer (a). The 1st Respondent to return to the Custodian 50 lac Units within a period of 16 weeks from today. No other Orders on this Application.

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Applied on 9/2/2017
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Compared with mrs kamili
Ready on 10/2/2017
Delivered on 10/2/2017

Certified to be a true copy
10/2/17
For OFFICER ON SPECIAL DUTY
Officer of the Special Court
Bombay

10/2/2017

SPECIAL COURT (Trials of Offences Relating to Transactions in Securities) Act, 1992 BOMBAY