

EXECUTIVE SUMMARY

Ministry of Corporate Affairs, Government of India ordered an Investigation in the matter of M/s Goldquest International Private Limited and M/s Questnet Enterprises India Private Limited (herein referred to as GQ & QN respectively) under Section 235 of the Companies Act, 1956, vide Order No. 3/51/2009-CL.II dated 28th July, 2010. By this Order the Ministry appointed Dr Baljit Singh, Sh RK Mishra, Sh AK Verma, Sh Pramod Beri, Sh Anupam Vashishta, Sh Utpal Nath, Sh MO Roy and Sh Sudhir Mehta as "Inspectors" to investigate into the matter.

The Investigation was initiated by gathering information about the Companies from various sources. Visit was paid to the Registered Office of the Companies at No. 7, Rain Tree Place, 9th Floor, McNichols Road, Chetpet, Chennai and the Registered Office was found to be non functional. Records of the Company were collected from the ROC Office, Chennai and efforts were made to trace the whereabouts of the Directors and employees of both the Companies. Chennai Police was also contacted for getting details of the cases lodged against both the Companies. Visits and communication was also done with other State Police Departments to know all the legal action initiated against the Companies either by the Police or by way of complaints against them. Custom Office Chennai was also approached to get details of the actions initiated by them against the Companies. Apart from this a lot of research on the issue of Multi-level Marketing or Pyramid Marketing and legal implications in India was done through the internet and by visiting other offices.



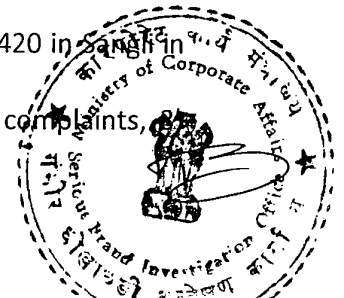
GQ was established in the year 2001 and was registered as a Private Limited Company with ROC Chennai on 21st December, 2001. The Company started the business of selling of numismatic products in the form of specially crafted gold/silver coins which were claimed to be limited edition coins and were imported from Germany. The methodology of selling was of so-called direct sales through personal approach and based on referral system. The Company claimed it did not violate any Indian Law in doing such business. It gave a Compensation Plan to the prospective Independent Representatives, which showed them a business opportunity to earn commissions if the sales of the products are made to more people. The business of the Company picked up after the initial consolidation. Then, on 23.04.2003, one Mr. N. Chandrasekharan lodged a case against the Promoters of the Scheme through Case No. 307/2003 under Section 420 of IPC and 5&6 of The Prize, Chits & Money Circulation Schemes (Banning) Act, 1978 (herein referred to as The Prize Act). The Company in total faced complaints from 172 persons. After this, GQ filed Writ Petition in the Madras High Court who then appointed an Advocate Commissioner to settle the Complaints and report to the Court. Thus, 170 complaints were settled and two remained untraceable. The Court then disposed of the Writ Petition and quashed the FIR. The Central Crime Branch (CCB) filed a Writ Petition before the Bench of Madras High Court against this. The judgment of single judge was set aside by this Bench and CCB was ordered to proceed with Investigation and file the final Report. Now, GQ filed SLP in the Supreme Court of India against this and the Court on 25th August, 2008 granted stay on the operation of Order of Bench of Madras High Court. The plea of illegality of the Scheme run by GQ has thus not been answered till date.

(ii)



During the above litigation the GQ had stated in its affidavit before the Court that it will not indulge in MLM business along with other facts. The business of scheme of pyramidal functioning of Sales and Commission payments was then shifted completely to a newly formed Private Company i.e QN, by the same promoters in March, 2005. QN continues to conduct this business till date and GQ now started supplying products to QN for perpetration of this scheme. In May, 2008 it also faced public outcry in Tamilnadu and Sembium PS Case no. 454/2008 was lodged against this Company and the promoters, under Section 420 of IPC and Sections 4,5&6 of the Prize Act. Ten other cases were also lodged and were clubbed with above case and 32,011 complaints/petitions were also attached with above cases after CB-CID, Chennai took over the case and thus CC No. 3876/2009 was filed in the Court of Chief Metropolitan Magistrate, Egmore, Chennai. The QN Company filed an application before High Court of Madras for compounding all these Cases which allowed the composition. The CB-CID, Chennai preferred an Appeal before the Supreme Court of India against this. The Supreme Court appointed Mr Justice KP Sivasubramaniam as one man Settlement Commissioner to settle the complaints by its Order dated 19th April, 2010. The Court observed, *"Since we have not decided the legal aspect, the question of Law raised shall be left open."* The process is still going on. QN keeps on still doing the business of Pyramidal Scheme claiming that there is no bar on running the Scheme till it is declared illegal.

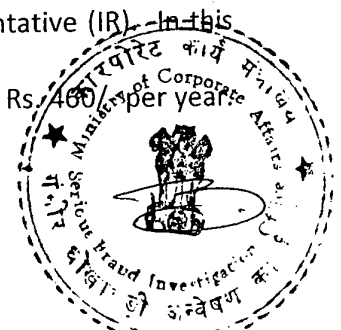
Apart from above, several cases were also lodged in different States under Section 420 of IPC and the Prize Act: 1) FIR No. 128/2008 under Section 420 in Sangli in Maharashtra, 2) Crime No. 190/2008 in Puducherry and 163 similar complaints,



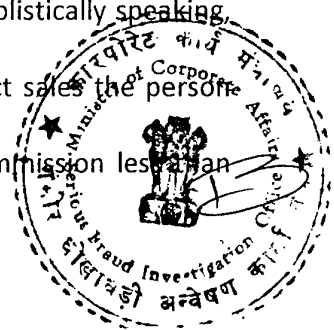
Crime No. 420/2008 in Andheri PS, Mumbai, 4) Crime No. 28/2008 in Bangalore High Grounds PS along with seven other cases in Karnataka and 5) Crime No. 90/2008 in Geesugonda PS of Andhra Pradesh and other cases in different PS were lodged against QN company by different complainants. The methodology of the Company has been to settle the complaints in all above cases and then the Courts passed Orders in all above Cases that as there is no complaint, no action is called for as both the complainant and the accused have settled their dispute and the Courts have also observed that no purpose will be served by continuing with these cases. Thus, the question of illegality of the scheme has never been answered or addressed and GQ-QN keeps on running the illegal scheme.

The complainant of the Case with the Ministry had requested Investigation of the Companies by multiple agencies such as CBI, NIA, IB, RAW, FBI, CIA, CVC, SFIO, SEBI, RBI, etc for illegal international chain of terror criminal act, money laundering by selling of valueless articles illegally imported. Despite efforts by investigation he could not appear for his cooperation. The investigation studied the methodology of the scheme to verify the complainant's claim as other areas of the allegation fall beyond the scope of SFIO.

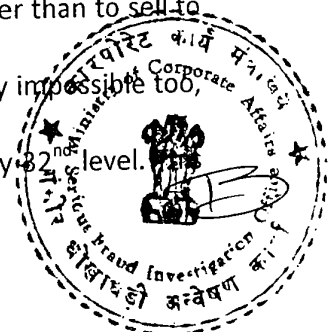
The Pyramidal concept of sale is a complex phenomenon where enrolment of person is done and the minimum price which a person pays for enrolment is through buying of the product and paying the Annual Registration Fees to be eligible for getting commissions and now the customer is called Independent Representative (IR). In this case average product cost has been Rs. 30,000/- and Annual charges Rs. 460/- per year.



Enrollment linked payment of commissions schemes are illegal in India as they violate Section 2(c) of the Prize Act which has been amply judged upon by different Courts of India including the Supreme Court. The key point here, which is exploited by MLM Companies, is that they claim that are selling the product through the mechanism of direct sales and are not doing enrolment; and the commissions are paid for sale of products and not for enrolling members. Thousands of such schemes are rampant across the country as was discovered by Investigation during its work, research and investigation. To prove that a scheme is violating Section 2(c), even though it is claiming that it is not encouraging enrolment, is the point of contention as the Companies, in this case - the GQ-QN, indulged in a lot of deception to circumvent the eye of the Law enforcement agencies and the courts. Hence, Investigation in its charge of violation of the Prize Act has gone to great length with the risk of repetition as minor questions regarding the illegality of the scheme can be easily countered by the Companies through the methodology of deception in their representations/defence, to explain the real nature of these schemes and hoe they violate the Prize Act through deception. In fact, deception is the key to propagate the pyramid schemes as the newly-to be recruited person is to be convinced of buying the opportunity (i.e of earning huge and life changing commissions) rather than of convincing him of buying the product. Here, the business opportunity is sold i.e of earning huge commissions and the seller gains only through payment of commissions to him by sales to his down lines which he makes by enrolling more members on his chain. Simplistically speaking, the key difference in direct sale and pyramidal sale is that in direct sales the person making sales gets maximum commissions and his up lines get commission less than



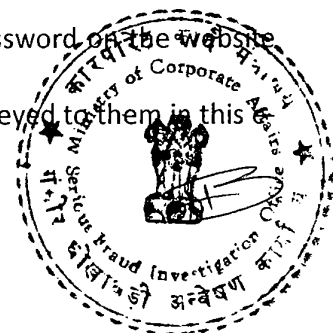
him. While in pyramidal sales the primary seller at first does not get any commission but as the pyramid beneath him grows he gets massive commissions far in excess of primary seller/recruiter. This motivates persons to recruit rather than to sell directly to earn significant commissions, hence the violation. That adding of a product to the pyramid scheme is the latest trend in the evolution of pyramid schemes and that product based pyramid schemes are most virulent, extremely viral and predatory schemes which are rapidly expanding and deluding the most vulnerable among the society, has been widely discussed in the report. The Scheme involves making two members in the down line i.e getting the persons to enrol into the scheme, one on left side and one on right side (called the down lines and person making them members is their up line) and selling two products, thus maximising the chances of earning commissions. One sale is roughly equivalent to one commissioned unit volume (CUV). Three CUVs on either side of the down line makes one person i.e Independent Representative (IR) eligible for first level commissions of Rs. 11,500/-. Every such further six CUVs sales enables additional levels of commissions of Rs. 11,500/-. At the sixth level only e-vouchers are paid and first level commissions start again on next six CUV collections by IR and the cycle is repeated again and again. This commission is paid on weekly basis. As per maximum limits set by the Companies a person can earn maximum of Rs. 6,90,000/- per week as per the compensation plan. This amounts to Rs. 3.69 crores per annum per qualified membership. This is the business opportunity on sale. This is hugely alluring and acts as a strong drive to recruit rather than to sell to non-recruits to earn maximum commissions. But, this is mathematically impossible too, as by this scheme of things all the persons on earth will be covered by 2nd level.



scheme thus, like any other MLM/pyramidal scheme is inherently flawed, unfair, and deceptive and purely cheating apart from being outrightly illegal. Further, the prices of products which are sold are typically overpriced by 5-6 times in the name of uniqueness/fine craftsmanship. This gives the promoters margins, for enabling them to pay, roughly 40% of the sales amount in the form of such heavy up line commissions. The Report has also tried to explain in detail that MLMs are basically pyramidal schemes whenever they pay commissions and there is also provision of making members. The details about the Compensation Plan are discussed in the charge of violation of the Prize Act.

As per the data provided by the MD of the Companies, the GQ-QN sold a total of 2,93,436 products for a price of Rs. 806.15 crores to 2,39,484 individuals. Out of these only about 50,000 people ever received any amount of commissions. Only about 18,000 people were able to get more commissions than Rs. 30,000/- approximately – The initial amount of investment. So even though people were sold the concept and hence the products as a business opportunity, about 2,20,000 people have actually lost money.

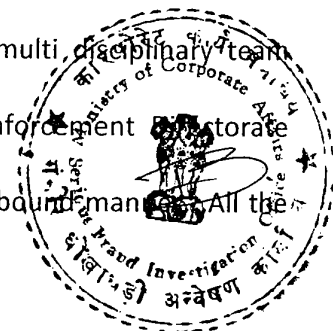
Both the Companies maintained two sets of data for effecting falsification of accounts to siphon out money. The methodology of siphoning out was through payment of false commissions as the Company had full control over the data and all the transactions of Sale, Purchase and Commission payments were done on the website of the Company by the IRs who operated through Login ID and password of the website of the Companies. The amount of commission due was also conveyed to them in this



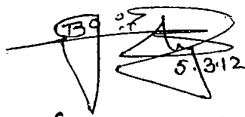
portal but IRs could never ascertain the whole tree in their down lines from the website only. This means promoters could create false pyramids and siphon out money through these payments. To avoid detection by the agencies they would have to falsify their books of accounts which Investigation has proved in the Charge on Falsification of Accounts. The Companies first provided one set of data of Total Sales and Total commissions paid from inception of the Companies to till date. When after extensive Investigation, they were questioned about the unmatched entries – the MD of the Company disowned the data provided earlier by saying that the data has been erroneously sent and provided another set of data of Total Sales and Commissions from inception of the Company to 31st March, 2008. The Investigation did extensive and meticulous data analysis and has brought out clear cut falsification of accounts as both these data referred to as Old Data and New Data respectively, do not match with the figures of the Balance sheet. It seems the Company has been paying the top of the pyramid promoters (TOPPs) by way of showing as the payments of commissions and getting the money from them apart from also making false entries in the payment of commissions. To avoid detection the Company has tried to mislead the Investigations by playing with the data. Thus, the Companies are not only conducting an illegal business contumaciously but are also, keeping and submitting falsified documents to the regulatory agencies. Their business, operations and conduct are thus totally unfair and prejudicial to the public interest. They are also a potential threat to National Security as this scheme as well as all such type of illegal schemes (e.g. Speakasia) are being run by overseas operators and State as well as Central Government employees either directly or through their family members/wives are also members of these




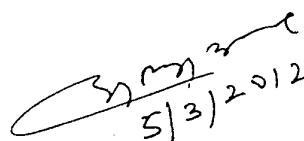
schemes in large numbers and these includes persons from Defense services and Ministries especially. As the promoters keep on running the illegal business of pyramidal scheme in clear violation of the Prize Act – and where the number of victims increase geometrically as the time passes, it is in greater public interest that the management of the Company be taken over by the Government and a stop be put to the deception and cheating of gullible public through running of an outrightly illegal scheme in the garb of direct selling scheme of MLM. Thus, appropriate action under the Companies Act has been recommended in this Charge. These conditions have developed and the Company has been able to perpetrate its illegal scheme for such a long time despite multiple actions by the Law enforcement agencies due to lack of regulatory authority to implement the Prize Act, which is implemented by MHA through State Polices but the ultimate decision it seems is left with the Courts – which takes long time by which the damage is already being done to lakhs of people. Even this issue is not allowed to be addressed by the Courts by the perpetrator Companies as they fight vehemently and also reach to a compromise with the victims. All this while, the point of illegality of the scheme has never been allowed to be addressed. This is more or less the case with all pyramidal schemes in the country. Thus, establishment of a regulatory agency for the Prize Act has been suggested in this Report for deciding beforehand which scheme is legal and which is not – which can be decided by closely looking at the Compensation Plan of any company as discussed in the Report. For the lakhs of companies already running this illegal scheme – a multi disciplinary team preferably under Central Economic Intelligence Bureau or Enforcement Directorate needs to be created to expeditiously suggest actions in a time bound manner. All the

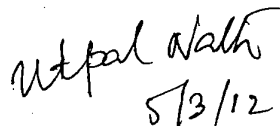



persons who have earned commissions through this scheme have been recommended to be proceeded against for recovery of illegally earned money as per Prevention of Money Laundering Act. This, along with massive awareness campaign about product based pyramid schemes preferably through a dedicated website coupled with publicity through print and electronic media especially in the affected States, can only put to an end to the social, financial, psychological and economic sufferings of the millions of people through all the illegal pyramid schemes running in this country and also mitigate a potential threat to National Security as greed to earn quick money is inherent in these illegal schemes which can be exploited by anyone who is looking for weak links and who has the data of these potentially willing people.

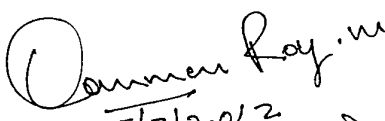

(DR. BALJIT SINGH)

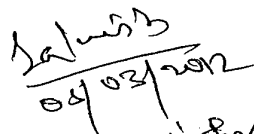

5/3/2012
(ANUPAM VASHISTA)


5/3/2012
(A. K. VERMA)


5/3/12
(UTPAL NATH)


5/3/12
(SUJATA MEHTA)


5/3/2012
(M. O. ROY)


04/03/2012
(R. K. MISHRA)

