Role of SEBI in Regulating Security Market in India

Dr Rinku

Assistant prof in law,

C.R. Institute of Law,

Rohtak.

The first statutory regulatory body that the government of India set up post the reforms of 1991 was the Securities and Exchanges Board of India (SEBI). As a regulator for the securities markets, SEBI was given the powers to create subordinate legislation and to investigate wrong-doing and impose relevant penalties.

In the post-reform period of the last two decades, one of the more important innovations facilitating a more rapid pace of economic development has been the creation of regulators. These are statutory entities that were placed outside of the machinery of the government, but given powers to regulate and supervise a sector[1]. One reason for the government to create such entities was to have expert bodies to regulate sectors where they faced an increasing complexity of economic activities. Here, the regulator would have domain knowledge to deal with such complex issues. A more powerful reason was the arms-length relationship that freed the regulatory entities from the political compulsions of the government. This was especially important in the development of those sectors where there was a dominance of public ownership among them in the sector. In India, there have been several regulators that have been set up, the more prominent of which have been SEBI (securities markets), TRAI (telecom) and CERC (energy)[2]. Of these, SEBI has been seen to be one of the more effective in terms of delivering on a mandate that includes (a) protection of the investor, (b) prudential regulation of securities markets intermediaries and (c) development of the markets[3]. In order to implement the mandate, the legal foundations to create regulators must have broad enabling legislation. The legislation gives the regulator powers to issue regulations for the sector, and to supervise based on them regulation. But most importantly, the regulator must be empowered to conduct investigation, adjudicate and have the authority to impose penalties if wrong-doing is established. Lastly, the credibility of the regulatory process of the regulator is enforced when provision for appeals has been made to

[1]Nyantung, Beny Laura, "Insider Trading Laws and Stock Markets Around the World: An EmpiricalContribution to the Theoretical Law and Economics Debate." Iowa J. Corp. L. , (Vol. 32), 2007, p. 237

[2]Phani, B. V., Reddy, V.N. Nagi, Ramachandran, N. and Bhattacharyya, Asish K., "Insider Ownership, Corporate Governance and Corporate Performance". NSE Research Initiative Proposal No. 89 online avvailable at http://ssm.com/abstract=696462 visited on 12 February 2010 at 4:34 p.m.

[3]The SEBI Act, 1992.

specialized domain knowledge to review regulatory action (which, in the case of the SEBI and securities markets, is the Securities Appellate Tribunals or SAT)[4].

There has been little intervention by Parliament in the regulations implemented by SEBI. While legislation places much of the details of how regulation is operational within SEBIs powers, the government retains the powers to decide the organizational structure, with the powers to appoint the top management at SEBI. Aside of this, SEBI has the freedom to decide how regulation is to be operationalized, which uses the three mechanisms of regulations, circulars and guidelines[5].

The need for transparency is particularly emphasized in the process of enforcement which has proved to be critical in the effectiveness of a regulator. The enforcement process at SEBI includes inspections of intermediaries on a regular basis, investigations on receipt of some information of violation or possible violation, and disciplinary action, which can include a variety of penalties including monetary. Here, it is observed that while the processes at SEBI are some of the most transparent and clear in the market, there are still areas where it can be improved. These include eliminating instances of simultaneous orders, improving consistency of regulatory amendments through circulars, systems for review of the investigative processes, ensuring uniformity of processes followed by adjudicating officers, among others, annual report which is circulated to an internal committee of senior.

The Indian securities market, considered one of the most promising emerging markets, is among the top eight markets of the world. The Stock Exchange, Mumbai, which was established in 1875 as “The Native Share and Stockbrokers Association” (a voluntary non-profit making association), has evolved over the years into its present status as the premier Stock Exchange in the country[6]. At present 23 stock exchanges operate all over India[7]. These stock exchanges provide facilities for trading securities; Securities markets provide a common platform for transfer of funds from the person who has excess funds to those who need them. Securities market is regulated by the Securities& Exchange Board of India (SEBI). Due to recent frauds in the role of SEBI played in security market has came into light which reveals that it has failed to achieve the objective for which it has established. Though SEBI has issued various guidelines and makes law but all has failed. Before discussing the role of SEBI it is necessary to understand the security market.

Securities market is an economic institute within which sale and purchase transactions of securities take place between subjects of economy on the base of demand and supply. Also we can say that securities

[4] www.eagletraders.com visited on 20th Nov 2017 at 5:00 P.M.

[5] Amrita S., Nain: Does Insider Trading Regulation Deter Private Information Trading International Evidenced 2007) SSRN working paper available at ssrn.com ; Beny, L., “Do insider trading laws matter"? Some preliminary comparative evidence, American Law and Economics Review 7, 144-83.(2005)

[6] www.google.com visited on 26th Dec 2017 at 2:00 P.M.

[7] On July 9, 2007 SEBI has withdrawn its approval from Saurashtra Stock Exchange, Rajkot due to its passive working. Hence the number of approved stock exchanges are 23. Earlier it were 24.

market is a system of interconnection between all participants (professional and nonprofessional) that provide effective conditions:

- to buy and sell securities,
- to attract new capital by means of issuance new security ,
- to transfer real asset into financial asset,
- to invest money for short or long term periods with the aim of deriving profit.

A security is generally a fungible, negotiable financial instrument representing financial value. Securities can be divided into-

- debt securities (such as banknotes, bonds and debentures),
- equity securities, e.g., common stocks; and,
- Derivative contracts, such as forwards, futures, options and swaps.

The company or other entity issuing the security is called the issuer. A country's regulatory structure determines what qualifies as a security. For example, private investment pools may have some features of securities, but they may not be registered or regulated as such if they meet various restrictions.

Securities may be represented by a certificate, or non-certificated(that is in electronic form).

FUNCTIONS OF SECURITIES MARKET

The common market functions of securities market are-

- Commercial function[8]
- Price determination[9].
- Informative function[10].
- Regulation function[11].
- Transfer of ownership[12].
- Insurance (hedging) of operations though securities market.

[8]to derive profit from operation on this market

[9]Demand and Supply balancing, the continuous process of prices movements guarantees to state correct price for each security .So, the market corrects mispriced securities.

[10]market provides all participants with market information about participants and traded instruments.

[11]securities market creates the rules of trade, contention, regulation, priorities determination.

[12]securities markets transfer existing stocks and bonds from owners who no longer desire to maintain their investments to buyers who wish to increase those specific investments. There is no net change in the number of securities in existence, for there is only a transfer of ownership. The role of securities market is to facilitate this transfer of ownership. This transfer of securities is extremely important, for securities holders know that a secondary market exists in which they may sell their securities holdings. The ease with which securities may be sold and converted into cash increases the willingness of people to hold stocks and bonds and thus increases the ability of firms to issue securities

COMPONENTS OF SECURITY MARKET

The major components of the securities market are listed below:

• Securities-Shares, Bonds, Debentures, Futures, Options, Mutual Fund Units

• Intermediaries-Brokers, Sub brokers, Custodians, Share transfer agents, Merchant Bankers

• Issuers of securities-Companies, Bodies corporate, Government, Financial Institutions, Mutual funds, Banks

• Investors-Individuals, Companies, Mutual funds, Financial Institution Foreign Institutional Investors

• Market Regulators-SEBI, RBI (to some extent), Department of Company Affairs

There is a growing network of financial intermediaries that operate in a highly competitive environment while being governed by a tight set of norms. India has one of the most sophisticated new equity issuance markets. Disclosure requirements and the accounting policies followed by listed companies for producing financial information are comparable to the best regimes in the world.

The Indian securities market is among the safest and the most efficient trading destinations internationally. The Indian corporate governance code is compared to the Sarbanes Oxley Act of the USA. India has one of the fastest growing and well-developed asset management businesses in the world, with state-owned as well as private sector players. That said, the Indian market is often hostage to some scam or the other from time to time. Effective enforcement of compliance is cited as one of the reasons for these unsavoury episodes. The role that SEBI's initiatives have played in bringing about this transformation of the market has not been researched comprehensively so far. Literature that has analysed the efficiency and the design of the Indian securities market has examined the role of certain specific regulatory provisions on the functioning of the securities market. So also the various annual reports of SEBI discuss the regulatory and other institutional developments that took place during the year under review. However, no attempt seems to have been made to take stock of all the various initiatives of SEBI so far and assess its impact on the activity in the securities market.

SEBI has been given several powers under the SEBI Act toenable it to accomplish the objectives such as protecting the interest of investors in securities by ensuring full disclosure, transparency, regulation of the securities market etc.Securities and Exchange Board of India (SEBI) was formed officially by the Government of India in 1992 with the introduction of SEBI Act 1992 being passed by the Indian Parliament. The headquarter of SEBI is in Mumbai. The Controller of Capital Issues was the regulatory authority before SEBI came into existence; it derived authority from the Capital Issues (Control) Act, 1947.

Initially SEBI was a non-statutory body without any statutory power. However in 1995, the SEBI was given additional statutory power by the Government of India through an amendment to the securities and Exchange Board of India Act 1992. In April, 1998 the SEBI was constituted as the regulator of capital market in India under a resolution of the Government of India There are many intermediaries involved in stock exchange transactions viz. (a) Merchant bankers (b) Underwriters (c) Registrars (d) bankers (e) brokers (f) depositories (g) custodians. These intermediaries have to be registered with SEBI and they shall have to follow the regulations issued by SEBI then and there. Listing Agreement is an important document which is to be executed by the company with the Stock Exchange where its shares are proposed to be listed[13].

SEBI monitors through Stock Exchanges the compliances of various conditions of Listing Agreement by the listed companies, particularly with regard to submission of quarterly, half yearly along with annual financial results under clause 41, submission of shareholding patterns on a quarterly basis under clause 35, quarterly corporate governance reports under clause 49 and prompt as well as timely payment of annual listing fees. Since compliance with the listing conditions are mandatory for the listed companies, it is always desirable that a company secretary of such companies must ensure timely compliances of those conditions, by preparation of checklists and checking them constantly to fulfil the obligations. It may be noted that recently, SEBI reiterated its stand of bringing under its domain all corporate governance norms for listed companies and lays down guidelines related to corporate governance in to securities market. Governance implies a degree of control to be exercised. Governance is merely governing .It is not merely ownership. Even an owner has to learn to govern. Good Governance implies that the institution is run for the optimal benefit of stakeholder in it and in case of securities market it means security market protect the interest of investor by maintaining transparency and accountability.

BASIC OBJECTIVES OF SEBI[14]: -The basic objectives of the board are:

- to protect the interests of investors in securities;
- to promote the development of Securities Market;
- to regulate the securities market

Since its inception SEBI has been working for targeting the securities and is attending to the fulfilment of its objectives with commendable zeal and dexterity. The improvements in the securities markets like capitalization requirements, margining, establishment of clearing corporations etc. reduced the risk of credit and also reduced the market. SEBI has introduced the comprehensive regulatory measures, prescribed registration norms, the eligibility criteria, the code of obligations and the code of conduct for

[13] www.legalserviceindia .com visited on 24th Dec 2018 at 3:00 P.M.

[14] The SEBI Act, 1992.

different intermediaries like, bankers to issue, merchant bankers, brokers and sub-brokers, registrars, portfolio managers, credit rating agencies, underwriters and others. It has framed bye-laws, risk identification and risk management systems for Clearing houses of stock exchanges, surveillance system etc. which has made dealing in securities both safe and transparent to the end investor.

Another significant event is the approval of trading in stock indices (like S&P CNX Nifty & Sensex) in 2000. A market Index is a convenient and effective product because of the following reasons[15]:

- It acts as a barometer for market behaviour;
- It is used to benchmark portfolio performance;
- It is used in derivative instruments like index futures and index options;
- It can be used for passive fund management as in case of Index Funds

APPROACHES OF SEBI[16]-

Two broad approaches of SEBI is to integrate the securities market at the national level, and also to diversify the trading products, so that there is an increase in number of traders including banks, financial institutions, insurance companies, mutual funds, primary dealers etc. to transact through the Exchanges. In this context the introduction of derivatives trading through Indian Stock Exchanges permitted by SEBI in 2000 AD is a real landmark.

SEBI appointed the L. C. Gupta Committee in 1998 to recommend the regulatory framework for derivatives trading and suggest bye-laws for Regulation and Control of Trading and Settlement of Derivatives Contracts. The Board of SEBI in its meeting held on May 11, 1998 accepted the recommendations of the committee and approved the phased introduction of derivatives trading in India beginning with Stock Index Futures. The Board also approved the "Suggestive Bye-laws" as recommended by the Dr LC Gupta Committee for Regulation and Control of Trading and Settlement of Derivatives Contracts. SEBI then appointed the J. R. Verma Committee to recommend Risk Containment Measures (RCM) in the Indian Stock Index Futures Market. The report was submitted in November 1998.

However the Securities Contracts (Regulation) Act, 1956 (SCRA) required amendment to include "derivatives" in the definition of securities to enable SEBI to introduce trading in derivatives. The necessary amendment was then carried out by the Government in 1999. The Securities Laws (Amendment) Bill, 1999 was introduced. In December 1999 the new framework was approved. Derivatives have been accorded

[15] https://www.quora.com. Visited on 24th Nov 2018 at 6:00 P.M.
[16] Ibid.

the status of `Securities'. The ban imposed on trading in derivatives in 1969 under a notification issued by the Central Government was revoked. Thereafter SEBI formulated the necessary regulations/bye-laws and intimated the Stock Exchanges in the year 2000. The derivative trading started in India at NSE in 2000 and BSE started trading in the year 2001.

FUNCTIONS & RESPONSIBILITIES

SEBI has to be responsive to the needs of three groups, which constitute the market:

- the issuers of securities
- the investors
- the market intermediaries.

SEBI has three functions rolled into one body: quasi-legislative, quasi-judicial and quasi-executive. It drafts regulations in its legislative capacity, it conducts investigation and enforcement action in its executive function and it passes rulings and orders in its judicial capacity. Though this makes it very powerful, there is an appeals process to create accountability. SEBI has enjoyed success as a regulator by pushing systemic reforms aggressively and successively .SEBI has been active in setting up the regulations as required under law[17].

SEBI has also been instrumental in taking quick and effective steps in light of the global meltdown and the Satyam fiasco, citation needed It had when increased the extent and quantity of disclosures to be made by Indian corporate promoters. More recently, in light of the global meltdown, it liberalized the takeover code to facilitate investments by removing regulatory structures.

POWERS

For the discharge of its functions efficiently, SEBI has been invested with the necessary powers which are:

1. To approve by−laws of stock exchanges.
2. To require the stock exchange to amend their by−laws.
3. Inspect the books of accounts and call for periodical returns from recognized stock exchanges.
4. Inspect the books of accounts of any financial intermediaries.
5. Compel certain companies to list their shares in one or more stock exchanges.
6. Levy fees and other charges on the intermediaries for performing its functions.

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[17] Ibid.

7. Grant licence to any person for the purpose of dealing in certain areas.

8. Delegate powers exercisable by it.

9. Prosecute and judge directly the violation of certain provisions of the companies act.

Various Committee of SEBI-

The following are the committees of SEBI[18]:

1. Technical Advisory Committee
2. Committee for review of structure of market infrastructure institutions
3. Members of the Advisory Committee for the SEBI Investor Protection and Education Fund
4. Takeover Regulations Advisory Committee
5. Primary Market Advisory Committee (PMAC)
6. Secondary Market Advisory Committee (SMAC)
7. Mutual Fund Advisory Committee
8. Corporate Bonds & Securitization Advisory Committee
9. Takeover Panel
10. SEBI Committee on Disclosures and Accounting Standards (SCODA)
11. High Powered Advisory Committee on consent orders and compounding of offences
12. Derivatives Market Review Committee
13. Committee on Infrastructure Funds.

The SEBI is playing active role in regulating security market in India. It has given various powers. It has issued directions and makes rules, bye laws for ensuring smooth functioning of security market. In 2015 it has issued regulation relating to insider trading. Still in many cases SEBI has failed to take timely action due to which investors, employees have to suffer and many frauds have been committed. So it is necessary here not the rules but their proper implementation and timely action and strict penalty to the defaulter or criminal.

[18] Ibid.