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Reassessing SEBI Regulations: Balancing Investor Protection, Market Integrity, and Regulatory Innovation in India's Securities Market

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ABSTRACT

The growth of the securities market in India has had a material impact on the development process of the Indian economy by enabling capital formation, enhancing the financing of corporations, and offering wider investment avenues. While on one hand, it has made considerable contributions towards this objective, the explosive growth of the market has simultaneously opened the floodgates for complex variants of insider trading, fraudulent transactions, corporate failures, and technological vulnerabilities that pose a daunting task for effective regulation. SEBI (Securities and Exchange Board of India), set up under the SEBI Act, 1992, is a cornerstone in confronting these issues with its myriad regulations concerning market functioning, disclosure requirements and investors.

This article critiques the development of the SEBI framework, analyses its efficacy in regulating markets, looks at landmark judicial interventions, and highlights emerging threats due to the new trends in financial instruments.

Thus, although SEBI has established a strong framework for promoting India's capital markets, the emphasis will need to be on flexibility and preparedness to meet new technological challenges and also on the need for prudent enforcement so that the quest for market efficiency does not undermine investor interests.

Keywords: *SEBI, Securities Regulation, Investor Protection, Corporate Governance, Insider Trading, Capital Markets.*

INTRODUCTION

India's capital market has transformed itself from a comparatively administered financial system to one of the world's most bustling markets. Liberalisation, technological advancements, a sharp increase in retail participation and inflow of foreign funds have led to securities trading being a significant contributor to the national economic development. While this development has enhanced access to finance and helped in the rapid growth of corporations, it has simultaneously increased concerns regarding market manipulation, information asymmetry, insider trading, misleading disclosures and complex financial fraud. The central lesson of all this is: no efficient securities market can exist without the support of a strong regulatory regime to keep investor confidence afloat.

One of India's most significant financial reforms is the introduction of the Securities and Exchange Board of India. It was set up in the year 1988 as a merely administrative body, and later became a statutory body by the Securities and Exchange Board of India Act, 1992, with the following triad role to fulfil – investor protection, regulation of the securities market, and development of the securities market. Unlike conventional regulators functioning as purely supervisors, SEBI possesses Legislative, executive, and Quasi-Judicial powers.¹ It has been empowered to make regulations, to investigate, to impose sanctions, and to make binding directions to enforce discipline in the market. This integrated regulatory structure has allowed SEBI to respond better to the changing dynamics of market operations compared to traditional administrative agencies. After liberalisation, the Indian financial markets have become a lot more complex. With the rise of digital trading, algorithmic trading, fintech, AI, and cross-border investing, there have been a host of challenges, such as cyber-related market manipulation, governance issues and ESG-related disclosures. Today, effective securities regulation requires, in addition to the legal framework, tech-knowledge, institutional autonomy and proactive surveillance of markets.

In light of these trends, SEBI has steadily strengthened its regulatory architecture through several specific regulations concerning disclosure obligations, insider trading, takeovers, fraudulent practices in the securities market, compliance with listing requirements, mutual funds, alternative investment funds, and corporate governance. These initiatives try to strike a balance between both - the promotion of market development and the protection of investors

¹ Securities and Exchange Board of India Act, No. 15 of 1992, Acts of Parliament, 1992 (India).

in India's securities market. However, persistent issues with corporate governance, market manipulations, and more complex financial instruments continue to pose significant challenges to the efficacy of the regulatory regime.

In this background, the article attempts to address whether India's progressively evolving regulatory regime under SEBI has been able to strike an optimal balance between market efficiency and investor protection. It analyses the statutory framework in principle, evaluates major regulations and court decisions and finally offers reforms to augment the regulatory effectiveness in the new tech-enabled environment for securities markets.

SEBI'S REGULATORY FRAMEWORK: FROM MARKET SUPERVISION TO INVESTOR PROTECTION

We can judge a securities regulator by not just the scope of its powers under the law, but more importantly by its ability to preserve investor confidence, thereby sustaining the growth of capital markets. This balance has been sought to be struck in India, with both legislation and detailed regulations coming to be based on current realities and changing trends. Unlike some regulatory agencies that function in the straitjacket of a single statute, SEBI operates through a synergistic and multi-layered legal structure that takes cognisance of the new realities and emerging trends in the financial market. It comprises the SEBI Act, 1992; Securities Contracts (Regulation) Act, 1956 (SCRA); Depositories Act, 1996 and applicable provisions of the Companies Act, 2013 to constitute a complete regulatory edifice with securities.² The SEBI Act, 1992, is at the centre of the framework. Section 11 of the SEBI Act prescribes SEBI's three-fold mandate of investor protection, development of the securities market and regulation of the securities market. Unlike most regulators, which play only a supervisory role, the SEBI in the Indian securities market has legislative, executive and quasi-judicial powers and can issue regulations, carry out inspections and investigations, issue directions to market intermediaries and listed companies, impose monetary penalties, and even debar such entities from accessing the securities market if required. Its immense powers to react promptly to emerging market risks are not in question, though there are several ongoing discussions on procedural fairness and the accountability of regulators.³ Securities Contracts (Regulation)

² Securities and Exchange Board of India Act, No. 15 of 1992, Acts of Parliament, 1992 (India); Securities Contracts (Regulation) Act, No. 42 of 1956, Acts of Parliament, 1956 (India); Depositories Act, No. 22 of 1996, Acts of Parliament, 1996 (India); Companies Act, No. 18 of 2013, Acts of Parliament, 2013 (India).

³ Securities and Exchange Board of India Act, No. 15 of 1992, §§ 11, 11B, 11C, 15-I (India).

Act, 1956: This Act complements the SEBI Act in that it gives a legal standing for operating recognised stock exchanges in India, and all security trades have to be conducted as per the legal framework specified in the Act, which regulates the exchange of Securities. In addition to these developments, SCRA still plays a critical role in providing the legal certainty needed to enable smooth and orderly securities transactions.

Under this Act, the physical ownership has been replaced by electronic securities held in a book entry system. The Dematerialisation of Securities has resulted in a speedy settlement process, reduced risk from fake or lost certificates and has improved efficiency in transactions. The interaction of depositories and Electronic trading platforms has led to much increased transparency and a significant reduction of settlement and operational risk of investors and market participants alike. Corporate Governance in Securities Markets. The concept of Corporate Governance has been an important pillar in the entire edifice of securities regulation. Basic corporate governance standards can be found in the Companies Act 2013. However, to ensure proper compliance with corporate governance norms of the listed companies, the SEBI has issued regulations in the form of the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015. The aforesaid Regulations provide for continuous, timely and transparent disclosure of material events and matters and have improved corporate governance with integrity of management and board, effective risk management, sound financial reporting and internal controls, and compliance with laws and regulations. In the LODR Regulations, SEBI has endeavoured to adopt a preventive instead of a retrospective enforcement, moving from post-facto penalties to proactive measures to combat information asymmetry. Market Abuse Prevention. To prevent such activities that would hinder fair price discovery and exploit investors, SEBI regulations ensure that they are prevented. Insider Trading Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015, deal with Insider Trading. This regulation prohibits trading based on Unpublished price sensitive information (UPSI) and prohibits persons in possession of UPSI from keeping UPSI confidential by taking care to maintain their digital records. SEBI PFUTP Regulations The Securities and Exchange Board of India (Prohibition of Fraudulent and Unfair Trade Practices Relating to Securities Market) Regulations, 2003 ("PFUTP Regulations") prohibit fraudulent, manipulative, deceptive, unfair and misleading conduct and practices such as insider trading, market manipulation, puffery schemes and circular trading, etc. Public fundraising and corporate restructuring, SEBI regulation also takes care of issues related to public fund raising by companies. Moreover, SEBI (Substantial Acquisition of

Shares and Takeovers) Regulations, 2011 govern the acquisition of more than a 15% shareholding in a listed company. In such cases, an open offer must be made to minority shareholders at a fair price, providing them an opportunity to tender their shares in the open offer. SEBI (Issue of Capital and Disclosure Requirements) Regulations set out standards for disclosures in case of a public issue, a rights issue, or a private placement to help investors make an informed investment decision. Conclusion On the whole, one can say that Indian securities market regulation has made gradual progress from punitive enforcement measures to that of preventive governance, where enforcement is the rule and punitive measure only in exceptional cases. Even penalties are not to merely penalize for a past offence, but they are meant to prevent the offender and deter potential offenders from committing similar offences. As capital markets continue to evolve, regulators also must keep pace with the changing trends in order to ensure the effectiveness of regulations.

JUDICIAL INTERPRETATION AND REGULATORY CHALLENGES

Beyond the laws themselves, the consistent application of these laws by courts through interpretation helps reinforce regulatory objectives while at the same time safeguarding rights in securities transactions. Despite the vast investigative, adjudicatory, and enforcement powers available to SEBI under SEBI Act, 1992, the ambit of these powers has time and again come up for examination before the constitutional courts and the SAT, and it has been through judicial interpretation that these powers have been defined to be proportionate, transparent and consistent with the principles of natural justice, between efficient regulation and individual rights into its jurisprudence.⁴ Some of the landmark decisions that have helped define the securities regulation regime in India include:

1. Sahara India Real Estate Corporation Ltd. V. Securities and Exchange Board of India:

This was one of the earliest and most defining cases concerning the definition of a public issue. Sahara had made issues of Optionally Fully Convertible Debentures (OFCDs) to over a million investors, claiming that it was a private placement and outside the regulatory reach of SEBI. The Supreme Court held that when a security is offered to a large section of the public, the nature of the issue, regardless of how it is termed, is a public issue, and SEBI can regulate such issues to protect investors' interests. SEBI was asked to refund thousands of crores raised from investors. This judgment helped consolidate SEBI's powers to investigate even disguised

⁴ Securities and Exchange Board of India Act, No. 15 of 1992, §§ 11, 11B, 11C, 15-I (India).

public issues and solidified the principle that a technical distinction in the terms used should not be used to defeat the protection offered to investors.⁵

2. *N.Narayanan v. Adjudicating Officer, SEBI:*

This case dealt with the extent of responsibility and accountability of company directors regarding truthful and complete financial disclosure. The Supreme Court clarified that corporate governance should not be limited to form over substance, but should involve an effort by directors to ensure transparency and accuracy in their financial disclosures. By upholding SEBI's order, the case further strengthened the liability of directors of listed companies. It is a landmark decision under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.⁶

3. *SEBI v. Rakhi Trading (P) Ltd.:*

This Supreme Court judgment interpreted provisions relating to manipulation in the securities market, specifically by using synchronised trades and artificial creation of a market. The Court held that where trades were executed in a synchronised manner and were made to create a false impression of market activity, this constituted market manipulation even if they conformed to the prescribed exchange mechanisms, as it defeated the purpose of a transparent market. The Court's approach was to consider the substance over form, i.e. To analyze the economic effect and intention of the transaction rather than the literal compliance.⁷

4. *Clariant International Ltd. V.SEBI:*

This case involved the regulation of acquisitions and the need for transparency during takeovers to protect minority shareholders. The Supreme Court held that the disclosure requirements and mandatory open offer for acquisitions are important safeguards to prevent unequal treatment of shareholders. The decision underlined SEBI's objective to foster orderly growth of the securities market by providing a level playing field for investors and ensuring information during major corporate events.⁸

While Indian courts have often sided with investor protection and the regulatory objectives of SEBI, the rapidly evolving capital market environment presents significant regulatory challenges.

⁵ *Sahara India Real Estate Corp. Ltd. v. Sec. & Exch. Bd. of India*, (2013) 1 SCC 1 (India).

⁶ *N. Narayanan v. Adjudicating Officer, SEBI*, (2013) 12 SCC 152 (India).

⁷ *SEBI v. Rakhi Trading (P) Ltd.*, (2018) 13 SCC 753 (India).

⁸ *Clariant Int'l Ltd. v. Sec. & Exch. Bd. of India*, (2004) 8 SCC 524 (India).

1. **Technological Disruptions:** The widespread usage of algorithmic trading, artificial intelligence, high-frequency trading and online digital investment platforms has significantly impacted market dynamics in a way that was not envisaged by existing securities laws. As a result, detecting and investigating insider trading through digital, encrypted means, indirect communication, or a manipulative trade by an algorithm has become a complex challenge for SEBI.

2. **Appropriate Intervention vis-à-vis Procedure:** Although SEBI ought to be equipped with sufficient power for prompt and effective intervention against any form of manipulative and fraudulent acts, too much intervention might cause uncertainties to investors and impact valid investment activities. The courts have repeatedly and uniformly held that the exercise of such powers must comply with the principles of natural justice, reasonable procedure, and logical application.

3. **Rise in Retail Investors' participation:** With easy access to trading through numerous online trading apps, retail investors are participating in the market in record numbers. Along with increased participation, we also see an increase in the amount of misinformation, fake advice spread on social media, and unsolicited advice by unregistered advisors and digital influencers. SEBI has been attempting to curtail such issues, but the rapid advancements in technology make regulation a constant uphill task.

EMERGING CHALLENGES, RECOMMENDATIONS, AND CONCLUSION

- **Emerging Challenges in India's Securities Regulatory Framework**

Driven by technological advancement, growing retail investor participation, and international integration of the capital markets, India's securities market is in a state of flux. The market regulator should regulate this ecosystem in a fast-evolving space, as most of the market manipulation nowadays is done using high-tech methods and not old fraud practices.

- One of the primary challenges is the increased reliance on algorithm-based and high-frequency trading (HFT), wherein trades are executed in split seconds. Although beneficial for overall market efficiency, these methods carry with them a higher potential of manipulation by employing stratagems such as spoofing, layering and

quote stuffing. Another area of concern is social media-based financial advice and the unregulated activities of influencers who distribute unsolicited investment advice to millions of retail investors. In the absence of disclosures regarding potential conflicts of interest and risk parameters, recommendations via social media platforms can influence market behaviour in an unhealthy way and result in poor investment decisions; however, recent SEBI regulations in this regard are a positive step forward. Cross-border investment flows are a further area that demands more attention. As foreign portfolio investment has gained prominence in the Indian capital market, it has also become imperative to forge closer ties with foreign securities regulators to exchange information, probe into trans-border securities transactions, and align regulations across jurisdictions to deter cross-border market abuse.

- **Recommendations**

Using artificial intelligence, machine learning and predictive analytics that can provide real-time tracking and detection of fraud and suspicious trading activities. Increased coordination between SEBI, Reserve Bank of India (RBI), Ministry of Corporate Affairs, Stock Exchanges and International regulators will be required to curb cross-border securities fraud. Further enhanced investor education and financial literacy programs that equip retail investors to avoid fraud due to unregistered advisors, false rumours, and speculative trading should be introduced. Similarly, reforms in regulation need to remain just, transparent and proportional to the offence and follow principles of natural justice. We need to put in place a healthy and balanced regulatory system combining regulatory action, technology innovation, and collaborative regulation between authorities, which will help boost investor confidence, enhance the credibility of the market and secure sustained growth.

- **Conclusion**

An intelligent blend of market development and investor protection, SEBI has risen to be one of the most powerful financial regulatory authorities in India, which seeks to protect investor interest whilst facilitating the development of the market. The judiciary has continually given interpretation in favour of SEBI having adequate powers to combat the more complex schemes of market manipulation, and that the powers should have adequate constitutional safeguards.

However, the continuing change in the financial market by use of new technologies such as digital interfaces, machine learning, big data analytics and the continuing integration of global capital into India would require Securities Regulation to be in a more dynamic, proactive and forward-looking posture.

Success for SEBI in the future is not only in terms of having better statutory powers, but more importantly in its capability to embrace technological innovation in conjunction with a policy regime that ensures clear and good governance, timely enforcement, and cooperation from its stakeholders.

A regulatory framework that can anticipate and confront the new emerging risks without impacting the investor's confidence will remain crucial for India's securities market to maintain its integrity, resilience and global competitive positioning. SEBI, with continuous institutional reform, will succeed.