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ANALYSIS OF SEBI REGULATIONS

~Sumeghna Paul

ABSTRACT

This research examines the regulatory framework established by the securities and exchange board of India and its role and objective of promoting investor protection, market transparency and orderly development of the Indian securities market. The study adopts a doctrinal method of research relying on the SEBI Act 1992 various key SEBI regulations, judicial decisions and scholarly papers to evaluate the effectiveness of securities regulation in India.

The paper examines the evolution of SEBI starting from its establishment as a non statutory body to a statutory regulatory body backed by the SEBI Act 1992, following the financial discrepancies and irregularities exposed by the Harshad Mehta scam. It further analyzes the major regulations introduced by SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015; the Prohibition of Insider Trading Regulations, 2015; the Issue of Capital and Disclosure Requirements Regulations, 2018; and the Substantial Acquisition of Shares and Takeovers Regulations, 2011. The study also examines landmark judicial decisions that have strengthened SEBI's regulatory and enforcement powers and clarified the scope of investor protection and confidence in the securities market.

This research concludes that SEBI has significantly enhanced Corporate Governance disclosures standards and market integrity but continues to face contemporary challenges due to the emergence of new technology, financial influencers and algorithmic trading etc.,. This highlights the continuing need for adaptive and effective securities regulation to ensure sustained investor confidence and fair market practices.

KEYWORDS

SEBI, securities regulation, investor protection, corporate governance, insider trading

INTRODUCTION

The Indian equity market went through significant transformation over the last three decades. Following the economic reforms of 1991, which led to an influx of foreign investment and change in trade regulations, there was roughly a ten-fold improvement in market liquidity.¹

There was a heightened interest among policy makers² to develop the securities market due to increased impact of capital markets in shaping resource allocation in the country. Thus the efforts towards investing in the securities market regulator and towards attracting foreign portfolio investment, started early in the reform process.

A well functioning securities market performs a very important role while facilitating capital formation and enabling businesses to raise long term capital from the public. However, these markets have faced drawbacks and irregularities through insider trading, fraudulent disclosure of vital information and market manipulation for decades. These result in loss of investor confidence and threaten the integrity of the market itself. Thus it was the need of the hour to strengthen the securities market regulators of the country for the better interest of not only the investors but also for market stability as a whole.

The Securities Exchange Board of India (SEBI) was set up as a regulatory body in 1988, which further gained statutory backing after the SEBI Act, 1992³ following major discrepancies in the financial markets that exposed the weaknesses of the then current regulatory system. The Act empowered SEBI to regulate intermediaries, supervise stock exchanges, protect investors' interests, and promote orderly development of the securities market.

Over time, SEBI introduced a comprehensive body of regulations concerning and governing various aspects of the financial market, like that of corporate disclosures, insider trading,

¹ Ajay Shah & Susan Thomas, Policy Issues in the Indian Securities Market (Indira Gandhi Inst. of Dev. Research, Working Paper No. 119, 2001)

² Ajay Shah & Susan Thomas, Policy Issues in the Indian Securities Market (Indira Gandhi Inst. of Dev. Research, Working Paper No. 119, 2001)

³ The Securities and Exchange Board of India Act, 1992, Preamble.

public offering, mutual funds, etc, which made it the principal regulator of the securities market in India.

Among its most influential regulatory instruments are the SEBI LODR (Listing Obligations and Disclosure Requirements) Regulations, 2015, the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018, and the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011⁴. These regulations collectively seek to ensure transparency, strengthen governance and prevent unfair trading practices among many other objectives. These implementations aim to fulfill SEBI's larger objective of balancing market efficiency along with investor protection, in an ever increasing, complex economic and financial landscape.

But despite the existence of a regulatory framework, several contemporary challenges still exist. The rise of algorithmic trading, finance influencers, fintech platforms and cross border investments and increasingly advanced market abuse techniques has expanded beyond the scope of regulatory oversight. Tackling such irregularities requires stricter measures but the regulators must also ensure that compliance requirements do not impose unnecessary burdens on legitimate business or hinder capital growth in any way. This creates a long standing and complex tension between heightened innovation and maintaining regulatory discipline.

RESEARCH METHODOLOGY

This paper adopts a doctrinal research approach to answer the question of whether SEBI regulations adequately protect investors while maintaining market efficiency.

It involves a systematic examination and analysis of statutory provisions, judicial precedents, legal cases as well as scholarly literature relating to the securities regulation in India. The study seeks to evaluate the effectiveness of the regulatory framework administered by the Securities and Exchange Board of India (SEBI).

⁴ Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015.

The research is descriptive in nature. It first describes the legal framework governing the Indian securities market and subsequently analyses the objective, scope, implementation, and practical effectiveness of major SEBI regulations.

EVOLUTION OF SEBI

Following independence of India in 1947 India's economic and financial picture was in a grave condition. The reforms that followed were heavily influenced by socialist ideas and Soviet style plan development which consisted of a macroeconomic framework that prioritized state led economic growth . The primary objective of this model was to achieve economic self-reliance and prevent unfair competition from foreign companies.

The vision was put into practice through the implementation of the successive five year plans and the pivotal industry policy resolution of 1956. This was effectively designed as the main catalyst of capital formation. This leads us to investigate how these policies or reforms affected the pre 1992 market and certain errors that led to major economic reforms in the year 1991.

The pre 1992 market was highly restrictive, state directed and focused heavily on The restriction of the private sector development of small scale industry licensing. The private sector in post independence India was a complex web of government mandates which collectively came to be known as the “licence raj”.⁵

THE HARSHAD MEHTA SCAM A TURNING POINT IN INDIA’S SECURITY REGULATIONS

⁶The Harshad Mehta securities scam in 1992 is considered one of the most significant financial frauds that changed the picture of the security in the market in India forever. It is also considered the core reason for the strengthening of security is regulation in India. The

⁵ Government of India, Industrial Policy Resolution, 1956 (Apr. 30, 1956)

⁶ Are, Sai Sree Vyshnavi,

The Rise and Fall of Harshad Mehta: Case Study on Financial Fraud and Post Scam Reforms in India

scandal exposed serious weaknesses in the securities market supervision and the banking system . This ultimately led to the empowerment of the securities exchange Board of India as a statutory body.

Harshad Mehta popularly known as the big bull of the Dalal Street exploited the Ready Forward (RF) deal mechanisms.

What is the “Ready Forward (RF) deal” mechanism?

In the early 1990s, banks were mandated to maintain a very high Statutory Liquidity Ratio (SLR) up to 38.5%⁷ in any form of government securities. Heavy penalties were imposed otherwise, but during that period of time, the government had also initiated the process of liberalisation, privatisation and globalisation. This meant that the competition was cut-throat and the Public Sector Banks (PSUs) had to keep up with the private sector. Due to this very reason, the main objective of PSU banks at that time was a higher rate of investment.

But banks were not allowed to invest in the stock market, and buying securities from the Reserve Bank of India for a temporary period was an expensive deal. Banks thus started to purchase government securities that were required to fulfill the mandate of the 38.5% SLR from banks, other than the RBI as it proved to be relatively cheaper.

This mechanism was termed as the “Ready Forward Deal”.

The buying and selling system was carried out between the lender bank and the borrowing bank through a system of bank receipts, where the entire process of bringing the participating banks together and negotiation was carried out by a broker. One such broker was Harshad Shantilal Mehta.

Mehta exploited this very process, by convincing smaller banks to issue fake bank receipts, which were to be used as collateral to collect or obtain funds from other banks. These funds were then converted in the stock market, thus resulting in artificial increase in the stock

⁷ Gupta A (2023). Scams That Changed India's Capital Market. SunText Rev Arts Social Sci 4(2): 15

prices, specifically of “Associated Cement Company”⁸ whose stock price increased from ₹200 to ₹9000.

The impact of the Harshad Mehta scam was disastrous, with the stock market crashing over 40% , investor confidence was hampered. Several weaknesses of the banking system of India were exposed including poor oversight, lack of internal controls and inefficient risk management.

Several regulatory reforms were made, post Mehta scam, the most important of them being the establishment of SEBI as an apex body with its main objective being regulating the capital and securities market of the country. Greater emphasis was given to transparency and accountability and regulators strengthened the rules governing operations in the stock market.

The establishment of SEBI under the SEBI Act, and its statutory powers:

The exposure of the Harshad Mehta securities scam in 1992 revealed serious deficiencies in India’s existing system of capital market regulation. Although the Securities and Exchange Board of India had been constituted in 1988 as a non-statutory body, it possessed limited authority to regulate stock exchanges, market intermediaries, and unfair trading practices. Recognising the need for an independent and empowered regulator, the Parliament enacted the ⁹Securities and Exchange Board of India Act, 1992, granting SEBI statutory status and establishing it as the principal regulatory authority for the Indian securities market.

The primary objectives of the SEBI Act are threefold: to protect the interests of investors in securities, to promote the development of the securities market, and to regulate its functioning. These objectives form the foundation of SEBI’s regulatory philosophy and guide the formulation of various regulations governing listed companies, intermediaries, collective investment schemes, and market conduct.

ANALYSIS OF MAJOR SEBI REGULATIONS

⁸ Clear tax, harshad mehta scam 1992

⁹ Securities and Exchange Board of India Act, 1992, §§ 3, 11 (India).

i) SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015¹⁰

The listing obligations and disclosure requirements regulations 2015 constitute one of the most significant regulatory measures introduced by the securities exchange Board of India to strengthen the financial market and corporate governance among listed companies. Before 2015 disclosure requirements were spread across multiple listing agreements and circulars creating consistency in compliance. The LODR regulations consolidated these obligations into a single comprehensive framework applicable to companies whose securities are listed on recognised stock exchanges.

The primary objective of the regulations was to ensure that investors receive timely accurate and in detail information regarding the financial and operation and position of listed companies that they might choose to invest in. Transparent disclosure reduces lopsidedness between company management and shareholders enabling investors to make informed investment decisions.

One of the defining features of the all LODR Framework is its emphasis on corporate governance and its importance. Listed companies are required to maintain an optimal composition of Executive and Independence directors, constitute nominations for audit committees and stakeholder relationship committees and establish mechanisms for internal financial control. These requirements aim to improve board accountability and minimise conflicts of interest within corporate management.

The regulations also recommend seamless disclosure obligations. Companies must promptly disclose company events like mergers, acquisitions, litigation, changes in key managerial personnel, financial results, and other developments that may influence the market price of securities. Failure to disclose such information may attract sanctions and disciplinary measures could be taken by SEBI.

Despite its strengths, the LODR framework presents practical challenges. Smaller companies listed under SEBI often face higher compliance costs due to extensive reporting requirements, all of this while ensuring the genuine independence of directors remains an

¹⁰ SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, regs. 4, 17–27 (India).

ongoing governance concern. Nevertheless, the regulations have substantially improved transparency and the protection of shareholders.

ii) SEBI (Prohibition of Insider Trading) Regulations, 2015¹¹

Among the other regulations released by SEBI, prohibition for insider trading is one of the most significant. Insider Trading weakens the fundamental principle that every investor should have equal access to material information before trading in securities.

This was recognized as a perilous threat, and thus Prohibition of Insider Trading regulations was introduced in 2015, replacing the earlier 1992 framework which had a broader and more comprehensive set of provisions.

The regulations prohibit investors from trading while in possession of "Unpublished Price Sensitive Information" (UPSI). UPSI refers to information that is not publicly available and is very likely to materially affect the price of securities, including financial results, dividends, mergers, acquisitions, changes in the capital structure and significant managerial decisions.

A prominent feature of the regulations is the stipulation for listed companies to establish internal compliance mechanisms. Every listed entity must appoint a Compliance Officer responsible for monitoring trading activities, maintaining records of designated persons, and enforcing trading window restrictions. During periods when UPSI exists, concerned employees and people connected to them are prohibited from trading in company securities.

The regulations also present the concept of a Code of Conduct and Code of Fair Disclosure, requiring companies to regulate communication of confidential information and ensure uniform circulation of material information to the public.

From a regulatory perspective, these provisions significantly strengthen investor confidence by reducing unfair informational advantages. However, determining whether a person actually possessed UPSI becomes an inevitable evidentiary challenge during legal and enforcement proceedings, making the investigation of insider trading legally complex.

¹¹ SEBI (Prohibition of Insider Trading) Regulations, 2015, regs. 2, 3, 8, 9 (India).

iii) SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018¹²

The Issue of Capital and Disclosure Requirements (ICDR), 2018, governs the process by which companies raise capital from the public. These regulations lay down certain eligibility criteria, disclosure standards, pricing norms, and procedural requirements for initial public offerings (IPOs), rights issues, qualified institutional placements, and preferential allotments.

The philosophy underneath the ICDR framework, is based on full and fair disclosure rather than the government approving of business quality. SEBI does not guarantee or certify that an investment is profitable, instead, it makes sure that the investors receive adequate information regarding the company's financial position, risks, promoters, management and business operations before investing in the securities.

The prospectus plays an important role within the ICDR regime. Companies are legally compelled to disclose material facts accurately, and any omission or misleading statement may result in civil and regulatory liability. Merchant bankers, legal advisors, auditors and auditing committees, and other intermediaries also bear due diligence responsibilities during the issue process.

The regulations have thus enhanced investor protection by improving the transparency during IPOs (initial public offerings). However, critics argue that lengthy disclosure documents can contain highly technical language and jargon, in the process limiting their accessibility for ordinary retail investors despite satisfying legal disclosure requirements.

iv) SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011¹³

Corporate mergers and acquisitions often result in the change of ownership and managerial control. The SAST Regulations, 2011 aim to ensure that each change occurs in a fair and transparent manner while protecting minority shareholders.

Under these regulations, an acquirer crossing the specified shareholding threshold must make a mandatory open offer to the remaining public shareholders. This enables the minority

¹² SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 (India).

¹³ SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, regs. 3–5 (India)

investors to exit the company, during acquisition, at a fair price, when control changes hands. Thus, preventing controlling shareholders from acquiring dominance without extending equal opportunity to public investors. The regulations dictate detailed procedures regarding offer price determination, public announcements of merger or acquisitions, disclosures, and timelines. SEBI thus monitors the compliance, to prevent abusive takeover practices and ensure equal treatment of shareholders.

The SAST framework reflects the broader principle that corporate control should not be transferred secretly or in a manner that is disadvantageous to the minority investors. Although takeover transactions have become more transparent, valuation disputes and procedural delays to generate legal disputes in complex acquisition cases.

SEBI'S ENFORCEMENT AND ADJUDICATORY MECHANISM

An effective regulatory framework depends not merely on how well it is drafted, but also on how well it is implemented and regulated. The SEBI act grants the board ('board' here refers to the Securities Exchange Board of India) extensive investigative, administrative, and quasi-judicial powers to justify and further prevent market abuse and ensure compliance with securities laws.¹⁴

SEBI may initiate investigations whenever it has reasonable grounds to believe that fraudulent or unfair trade practices might have occurred. During such investigations, it may call for the books of accounts, inspect records, examine intermediaries, call for certain individuals and require production of certain necessary documents. These powers enable the regulator to detect insider trading, market manipulation, circular trading, and other forms of securities fraud.

Where violations are established after investigation has been carried out, SEBI may impose monetary penalties, legal sanctions, suspend or cancel registration of intermediaries, restrain entities from accessing the securities market, and issue directions in the interest of investors. In suitable circumstances, parties may choose to engage in settlement proceedings, facilitating the resolution of disputes without an admission of guilt while maintaining regulatory compliance and due payment of settlement sums.

JUDICIAL ANALYSIS: LANDMARK CASES

SAHARA INDIA REAL ESTATE CORPORATE LTD V. SEBI (2012)

¹⁵The Sahara case is one of the most profound decisions in Indian securities law, because it upheld SEBI's authority to regulate public fundraising and protect investors. Sahara had raised thousands of crores through Optionally Fully Convertible Debentures (OFCDs) from millions of investors while arguing that the issue was private rather than public. The Supreme Court rejected this stance and held that the offering was, in substance, a public issue that fell well within SEBI's regulatory jurisdiction.

The court steered Sahara to refund the money collected from the investors with interest and emphasised that companies cannot evade disclosure requirements by merely describing a public issue as a private one. The judgement significantly strengthened SEBI's supervisory and regulatory powers over capital raising and reinforced the principle that investor protection takes priority over technical interpretations of corporate findings.

N.NARAYANAN V. SEBI (2013)¹⁶

Following the Satyam corporate fraud, the Supreme Court considered it the responsibility of the company officials to ensure truthful financial and material disclosures to the investors. The Court observed that transparency and accurate reporting is crucial in maintaining the confidence of investors in the listed companies.

The decision solidified the objectives of SEBI's disclosure and corporate governance framework by recognizing that managerial personnel in senior positions have a legal duty to uphold integrity in financial reporting. It also demonstrated that regulatory accountability extends beyond the company itself to individuals responsible for corporate misconduct.

CONCLUSION

¹⁵ Sahara India Real Estate Corp.Ltd.& Ors vs Securities & Exch.Board Of India & Anr on 31 August, 2012

¹⁶ N. Narayanan v. Adjudicating Officer, Sec. & Exch. Bd. of India, (2013) 12 S.C.C. 152

SEBI in the last three decades evolved as one of the most important economic regulators of the country. From a non-statutory body into a statutory regulator, it has fundamentally transformed India's securities and capital market. The enactment of the SEBI Act, 1992, together with stricter regulations regarding disclosure, insider trading, public issues and takeovers, has created a broad and comprehensive legal framework aimed at protecting the confidence of the investors while promoting fair and efficient markets

The Harshad Mehta scam exposed the consequences of inefficient regulation and became the turning point for institutional reform. Subsequent judicial decisions, particularly Sahara India, and N.Narayanan, have again, further clarified the scope of SEBI's powers and strengthened the principles and policies of transparency, accountability and market integrity.

Although emerging challenges such as increasingly complex financial products, algorithmic trading, finance influencers, etc, continue to test the effectiveness of the regulations put forward by SEBI, its evolving framework showcases a continuing commitment towards the aim of balancing investor protection, upholding investor confidence, along with orderly development of India's capital market.