



Laws and Policies related to Security Market in India with special reference to function and role of SEBI

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ABSTRACT

Indian security market is the driving force behind India's economic growth with resource mobilization and investment in productive purposes. To the cause of which such dynamic changing market ought to be fair, transparent, and efficient, strong regulation mechanism has to exist. The Securities and Exchange Board of India (SEBI), formed by the SEBI Act, 1992, is the topmost regulator vested with the duty to regulate and oversee the Indian securities market.

This article critically examines the laws and policies related to the securities market, emphasizing SEBI's vital role in safeguarding investor interests, maintaining market integrity, and fostering sustainable growth. The study analyzes the key legislative instruments governing the securities market, including the SEBI Act, the Securities Contracts (Regulation) Act, the Companies Act, and the Depositories Act, among others. It also examines the various functions that are fulfilled by SEBI like the regulatory function, protective function, and developmental function and explains how these lead to a healthy and healthy securities market.

Other than this, the article points out the challenges SEBI has faced while regulating effectively in the context of emerging market trends such as algorithmic trading and fintech innovations. It also places emphasis on significant policy initiatives of the authorities in filling regulatory gaps and generating investor confidence. Through the narration of descriptions of judgments and case studies that are relevant, the article discusses how SEBI has dealt with key regulatory issues and enforced compliance.

Summing up, the research brings forth the gaps which have existed under the regulatory policy and makes recommendations for enhancing SEBI to become more proactive in an increasingly evolving and technology-focused financial environment. Emphasizing international best practice and comparative analyses, the research points out that there needs to be continuous transformation within policies so that the integrity and stability of the Indian market for securities remain intact

KEYWORDS

Securities market, SEBI, regulation, investor protection, insider trading, corporate governance, market integrity, regulatory framework, legal challenges, capital market, stock exchange, market manipulation, investor education.

1. INTRODUCTION

Indian capital market is one of the strongest pillars of support of the country's financial infrastructure that provides a strong foundation for effective mobilization and utilization of capital. It facilitates issue, trading, and investment in different financial instruments such as equities, bonds, derivatives, and other marketable securities. As the market continues to grow and diversify, there is still a need to set up an extensive regulatory framework so that fairness, transparency, and efficiency of trading activity can be maintained. It is in this context that the Securities and Exchange Board of India (SEBI) has emerged as the first regulator, as the defender of investors' rights and market watchdog.¹

The significance of adequately controlled markets for securities cannot be overstated in a growing universe of globalized economies. Complex financial instrument diversification and increased entry by institutional and retail investors have generated fears for the need for further protection by regulation. SEBI, established by the Securities and Exchange Board of India Act, 1992, was a reaction to the need for an effective system of regulation that could handle issues resulting from financial malpractices and manipulative devices. The main activities of SEBI are to protect the interest of the investor, regulate the securities market, and promote its recurring and orderly growth.²

Its development as a regulator is also closely entangled with large financial scams and crises that revealed huge loopholes in the existing regulatory framework. The most glaring among them was the Harshad Mehta Scam of 1992, which revealed huge loopholes in the Indian banking and stock market system. This fraud, which was achieved by the highly advanced spoofing of share prices by the use of bank receipts, not only shook the confidence of the investors but also witnessed the imperative need of sweeping reforms to put a promise to avoiding such malpractices in the future. The Supreme Court judgment in *Harshad S. Mehta v. The State of Maharashtra* was a landmark in Indian financial regulation, marking the way to the establishment of strong supervisory frameworks under the auspices of SEBI.

After-the scam, SEBI was vested with statutory powers of regulation and supervision of market transactions, enforcing compliance and instituting proceedings in case of non-compliance. The SEBI served as a protector in protecting the investors from insider trading, price rigging, and other forms of securities fraud. SEBI has introduced plenty of regulations in recent years to address the various facets of the market, i.e., Insider Trading Regulations, Mutual Funds Regulations, and Listing Obligations and Disclosure Requirements (LODR). Such programmes are intended to promote a culture of equity and transparency and improve best practices of corporate governance.

Despite having its broad-ranging mandate, SEBI continues to face the test of technological advances and globalization. Algorithmic trading, high-frequency trading (HFT), and fintech technologies have introduced fresh risks that call for evolutionary forms of regulatory actions. Besides that, the increasingly strong interconnections of the international financial markets have also presented a challenge in the regulation and

¹ Rajesh Chakrabarti, *The Financial Market Architecture in India: Evolution and Challenges* (SAGE Publications, 2017).

² V. Sundaresan, "Market Manipulation and SEBI's Regulatory Response," (2021) 34(2) *Journal of Financial Regulation* 89.

enforcement of transactions across borders. Meeting such challenges require not only regulatory innovation but cooperation internationally and convergence of standards too.³

The role of SEBI is not just regulation and enforcement but also includes investor education and market development. The regulator has been keen to introduce programs that seek to improve the financial literacy of investors so that they can be improved decision-makers as an investor. SEBI also works with other financial regulators like the Reserve Bank of India (RBI) and the Ministry of Finance so that there can be a comprehensive and cohesive regulatory approach.

2. EVOLUTION OF THE REGULATION OF SECURITIES MARKET IN INDIA

Indian Securities market regulation has been a journey from a unstructured to a holistic regulatory regime within the parameter of SEBI. Three Phases in the evolution could be identified, which are elaborated below: the pre-SEBI period, passing of SEBI, and the amendments and reforms thereafter.

Early Developments: Regulation prior to the establishment of SEBI

The Indian security market prior to the formation of SEBI was regulated by essentially a scattered collection of miscellaneous individual pieces of legislation and directions. An attempt was made by the Securities Contracts (Regulation) Act, 1956 (SCRA), towards regulation with a perspective to prohibit objectionable business in securities as also in stock exchange trade. Legislation had no effective powers for enforcement and did not address new forms of complications given in the security market.

The lack of power for central control, the stock exchanges were largely self-governed and led to wholesale malpractices and market manipulations. Capital Issues (Control) Act, 1947, regulated issue of shares with fixation of new issue price but its control was half-hearted. Due to this, investor confidence also perpetually remained weak because there existed no transparency and accountability of deal in the market.

SEBI Formation (1992): A Response to Financial Malpractices and Frauds

The need for a regulating body was exposed following the infamous Harshad Mehta Scam of 1992, which had revealed glaring failure in the regulatory process. The security fraud and bank receipt scam had proved the need for vast regulation. The Securities and Exchange Board of India Act, 1992, was hence passed to create SEBI as the statutory body that would regulate the securities market.

SEBI was initially established as a non-statutory organization during 1988 but, by the SEBI Act of 1992, was statutorily instituted. It was meant to conduct core activities like protecting the interest of the investor, regulating the securities market, and arranging it in a proper way. To achieve all these, SEBI had been vested with quasi-legislative, quasi-judicial, and quasi-executive powers so that SEBI may provide rules, question, and levy fines.

One of the earliest regulatory measures taken by SEBI was the formulation of the Prohibition of Insider Trading Regulations, 1992, which aimed to curb the misuse of non-public, price-sensitive information. Additionally, SEBI introduced the Disclosure and Investor Protection (DIP) Guidelines to enhance transparency in public offerings.

Amendments and Reforms: Evolution of SEBI's Powers and Functions through Legislative Amendments

³ R. Sridharan and S. Rajagopalan, *Financial Regulation in Emerging Markets* (Oxford University Press, 2020).

SEBI's regulatory power has also been significantly increased in the past by means of successive amendments. Specifically, the Securities Laws (Amendment) Act, 1995, also conferred upon SEBI the power of registering market intermediaries and their activities. Further, the Securities Laws (Amendment) Act, 2014, also increased SEBI's power to conduct search and seizure operations, freeze assets, and initiate recovery proceedings.

SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997, was a good beginning towards regulation of takeovers and mergers in such a manner that investors were properly informed regarding takeovers. Regulations were revised in 2011 to address newer issues more effectively and improve corporate governance.

In recent years, SEBI has responded to newly emerging threats to online trading and algorithmic trading by giving notice to the SEBI (Prohibition of Insider Trading) Regulations, 2015, and SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015. These rules attempt to minimize risk in high-frequency trading and impose stringent disclosure requirements for listed entities.

3. LEGAL FRAMEWORK REGULATING THE SECURITIES MARKET

The regulatory system of India's securities market is wide-ranging and comprises a variety of legislation and regulation operating collectively in the role of transmitting the market discipline, along with investor interest protection. The strongest legislative tools that manage the securities market are as follows:

3.1 The Securities and Exchange Board of India Act, 1992

The SEBI Act, 1992, is the foundation of regulation of the securities market in India. It created SEBI as a statutory body with vast powers to regulate the securities market and safeguard investors. SEBI can frame rules, issue directions, and initiate enforcement action against the offenders.

Section 11 of the Act outlines SEBI's primary functions, including regulating stock exchanges, intermediaries, and protecting the interests of investors.⁴

Section 15 empowers SEBI to impose monetary penalties for violations of its regulations.

3.2 Securities Contracts (Regulation) Act, 1956 (SCRA)

The SCRA, 1956, lays down the regulatory framework of stock exchanges and trading arrangements in securities. It renders recognition of stock exchanges compulsory and lays down terms under which business in securities can be done.

Section 4 grants powers for recognition of stock exchanges and regulation of their functioning.⁵

Section 13 forbids trading without sanction outside a recognized stock exchange.

3.3 Companies Act, 2013

The Companies Act, 2013, regulates the incorporation, conduct, and winding up of companies in India. It insists on rigorous compliance procedures from listed and public companies, such as corporate governance rules and disclosure requirements.

⁴ Securities and Exchange Board of India Act, 1992 (Act No. 15 of 1992), s. 11.

⁵ Securities Contracts (Regulation) Act, 1956 (Act No. 42 of 1956), s. 4.

Section 129 makes it mandatory that financial statements provide a true and fair view of the financial position of the company.

Section 134 mandates that financial statements are approved by the board of directors and are also attached with a comprehensive report.⁶

3.4 Depositories Act, 1996

Depositories Act, 1996, promotes dematerialization and governs depository services. It provides for the transfer and holding of securities electronically to increase the efficiency and transparency of trading in securities.

Section 9 allows the transfer of securities by depository systems.

Section 10 authorizes depositories to keep records of ownership in securities.

4. FUNCTIONS AND ROLE OF SEBI

The Securities and Exchange Board of India (SEBI) is the highest regulator which has been established to protect the interests of the investors and regulate the Indian securities market. Established in 1992 under the SEBI Act, 1992, the main function of SEBI is to develop an investor-friendly environment as well as promoting the orderly development of the securities market. SEBI undertakes an assortment of functions enlisted under regulatory, protective, development, and adjudicatory functions. Such kinds of functions play a very crucial role in ensuring transparency, fairness, and efficiency in the securities market.

Regulatory Functions

Regulatory functions of SEBI involve regulating and monitoring stock exchanges and market intermediaries to the extent that they act in conformity with norms and standards. The regulation of the operation of the intermediaries and exchanges and control of the stock exchanges and supervision for ensuring that trade business is conducted by fair and transparent means is one of its significant responsibilities. SEBI formulates complex guidelines for broker, sub-broker, merchant banker, and portfolio manager and other intermediaries so that no undesirable practice is followed.

Besides, SEBI makes provisions for the regulation and registration of market intermediaries and enacts strict standards to be followed by all such intermediaries before permitting their operation. For instance, the SEBI (Intermediaries) Regulations, 2008 stipulate the procedure for registration, regulation, and discipline of market intermediaries.⁷ Certain regulatory functions by SEBI include the prescribing of rules of corporate disclosure and listing requirements with a view to bringing discipline in the market.

Protective Functions

The protective functions of SEBI are, first and foremost, to safeguard investors against fraud and other unfair practices more common in the securities market. The most essential protecting function is preventing insider dealing and fraud. Insider trading is the misuse of unpublished price-sensitive information to gain unfair profits on trading and is prohibited under the SEBI (Prohibition of Insider Trading) Regulations,

⁶ Companies Act, 2013 (Act No. 18 of 2013), s. 134.

⁷ Securities and Exchange Board of India (Intermediaries) Regulations, 2008, reg. 3.

2015.⁸SEBI closely monitors trading activity and probes such suspicious trading if it is feasible to generate such trades by simulating as insider trading.

Apart from these, SEBI conducts investor awareness campaigns to educate people about the risks associated with different investment products. The schemes enhance the financial literacy of retail investors and enable them to take informed investment decisions. SEBI also has a satisfactory grievance redressal mechanism in the shape of the SCORES (SEBI Complaints Redress System) portal, where grievances may be filed by investors against malpractices on the part of intermediaries or listed companies.⁹SEBI has been able to redress grievances in an effective and transparent manner through this mechanism.

Developmental Functions

Aside from its protective and regulatory role, SEBI also performs a developmental role in the direction of trying to achieve greater transparency and efficiency in the securities market. A large amount of its most significant activity under this umbrella is the promotion of good practice and adequate infrastructure for market operation. SEBI encourages the employment of technology upgrading, such as online trading networks and dematerialization of security, as it attempts to eliminate the risk through physical settlement and trading.

Apart from that, SEBI also promulgates policy guidelines for better market efficiency and transparency, like enforcing algorithmic and high-frequency trading rules to control risk and close manipulative deals. It also advises other regulators as well as market participants with the intention of harmonizing Indian regulations with foreign regulations and motivating investor confidence in the Indian market.

Adjudicatory Powers

As a quasi-judicial authority, SEBI exercises adjudicatory roles to levy fines to enforce compliance and punish wrongdoers. SEBI can afford to undertake inquiry, investigation, and penal proceedings against entities or parties for conducting violations of securities laws. Such jurisdictions belong to listed powers under Section 11B of the SEBI Act of 1992 by giving SEBI the power to issue restraint orders against vexatious transactions and offering protection to shareholders.¹⁰

SEBI may also order prohibition and freeze funds in the case of major offenses. Due to these judicial powers, SEBI makes the securities market fair and criminals accountable, thus the integrity of the market is boosted.

5. IMPORTANT POLICIES IMPOSED BY SEBI

SEBI has imposed various policies and regulations to ensure fair and transparent market operation. These policies include the most critical dimensions of market operation, from insider trading to mutual funds and acquisitions and mergers.

5.1 Insider Trading Rules, 2015

SEBI (Prohibition of Insider Trading) Regulations, 2015, are directed towards prohibiting abuse of unpublished price-sensitive information (UPSI) likely to have an impact on the price of securities. The regulations require standards of disclosure and surveillance mechanisms for detecting suspicious transactions.

⁸ · SEBI (Prohibition of Insider Trading) Regulations, 2015, reg. 4.

⁹ SEBI Complaints Redress System (SCORES), Guidelines 2011.

¹⁰ Securities and Exchange Board of India Act, 1992, s. 11B.

The regulations are directed towards maintaining market integrity by prohibiting insiders from trading in securities based on information to which they might have access.

5.2 Mutual Fund Regulations, 1996

The SEBI (Mutual Funds) Regulations, 1996, were enacted to regulate the establishment and functioning of mutual funds in India. The regulations ensure that mutual funds are fair and transparent in handling investor funds. SEBI wishes to offer protection to investors and facilitate market stability through the confidence on the part of asset management companies (AMCs) in following strict disclosure norms.

5.3 Buyback of Securities Regulations, 2018

The SEBI (Buy-Back of Securities) Regulations, 2018, contain some regulations for buy back of shares by companies. The regulations stipulate that the procedure of buyback shall be fair and transparent so that the minority shareholders are not disadvantaged.¹¹The regulations also make provision for the quantum of shares which can be bought by a company and for its public disclosure.

5.4 Alternative Investment Funds (AIF) Regulations, 2012

AIF Regulations, 2012, have been structured to provide diversified investment channels like private equity funds, venture capital funds, and hedge funds. The regulations facilitate transparent dealing and fair treatment by AIFs. The regulations were useful in institutional investment channeling and providing an alternative investment fund of investment to sophisticated investors.

5.5 Substantial Acquisition of Shares and Takeovers (SAST) Regulations, 2011

The SAST Regulations, 2011, regulate takeovers, mergers, and acquisitions of the Indian capital market. The regulations require acquiring parties to issue a mandatory public issue if their holding exceeds a threshold.

6. CHALLENGES OF IMPLEMENTATION AND LOOPHOLES IN THE REGULATIONS

Despite the sophisticated regulatory framework of SEBI, the Indian securities market is still going through a number of challenges. Insider trading and market manipulation are the most significant among them, wherein sophisticated trade tactics and digitalization make it difficult to detect violations on schedule.

The other major issue of concern is overlap of jurisdiction with other regulators, such as Reserve Bank of India (RBI) and Ministry of Corporate Affairs (MCA). This, in some cases, leads to controversy around regulatory intervention as well as tardiness in enforcement.

Apart from this, the advent of algorithmic trading has also created new challenges as detection of manipulative algorithms requires advanced surveillance systems. Apart from this, the grievance redressal mechanism via SCORES, although effective, is generally slow in redressing investor grievances owing to procedural backlog.

SEBI lags behind in recovery of compensation from fraud and malpractice victims among investors. SEBI can attach assets and penalize but is plagued by pragmatic constraints in enforcement and thus faces a lag in refund.

¹¹ SEBI (Buy-Back of Securities) Regulations, 2018, reg. 4.

7.CONCLUSION AND RECOMMENDATIONS

Conclusion

Securities and Exchange Board of India (SEBI) played an essential part in transforming the Indian capital market into a previously unorganized, sinister mode into an organized, transparent, investor-friendly regime. SEBI was perpetually shaping a suitable regime for regulation from its very origin in the year 1992 with regard to the protection of investors, restraint from malpractices, and inducing smooth development in the securities market. Through its adjudicatory, developmental, protection, and regulation functions, SEBI has achieved the goal of capital market transparency along with growth- and innovation-friendliness.

Despite having been successful so far, a few challenges yet remain to be tackled, and they include confronting cyber-attacks, managing sophisticated cross-border transactions, and keeping an eye on very fast-paced technical advances in schemes of trading. SEBI will also have to work an extra mile in order to make itself more effective by enhancing its surveillance powers and aligning itself with international regulators for effective implementation of norms. Furthermore, as new money instruments and market practices are on the horizon, SEBI will have to be one step ahead in designing new policies for regulating significant threats.

Recommendations

7.1 Enhancing Cyber Security Controls to Fight Cyber Attacks

More cyberattacks are expected as a result of rising cases of algorithmic and high-frequency trading. SEBI will need to deploy advanced cybersecurity controls and monitor end-to-end trading activity using Artificial Intelligence (AI) and Machine Learning (ML) technologies to detect real-time anomalies. Market infrastructure institutions' (MIIs) cyber resilience must safeguard end-to-end trading information and investor information.

7.2 Rising end-to-end cross-border coordination to regulate offshore investment

SEBI must enter into bilateral and multilateral agreements with overseas regulation authorities for cross-border monitoring and enforcement facilities. This alliance will facilitate monitoring of black money transactions by tracking money transactions overseas, verifying tax evasion, and eliminating the risk factor in foreign investments.

7.3 Creating Investor Education Programs to Facilitate Moral Trading

Establishing monetary education classes and campaigns will empower retail investors by educating them regarding investment risks as well as rights. SEBI should implement interactive online modules and mobile applications to make investor education material easily accessible.

By doing so, SEBI can further strengthen its regulatory framework and offer a secure, transparent, and robust Indian market for securities.

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