



## A critically analysis on SEBI's regulation over Indian securities market

Dr. Gyanendra Kumar Sahu

Asst. Professor of P.G. Dept. of Law, Utkal University, Vani Vihar, Bhubaneswar, Odisha, India

### Abstract

Since the empowerment of the Securities and Exchange Board of India (SEBI) through an Act of Parliament in 1992, SEBI has come up with a number of initiatives aimed at regulating and developing the Indian securities market and improving its safety and efficiency. These initiatives have made an impact on nearly every aspect of the market. Some of those initiatives have transformed the market fundamentally. 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.

**Keywords:** charter, exchequer, surveillance

### Introduction

#### Evolution of Joint Stock Companies

There are some branches of Law which cannot be properly understood without their historical background and company law is certainly one of them. The history and development of company law in India is closely linked up with that of England and for that reason it becomes essential to have a brief account of the history of English law for a proper appreciation of Law. Companies formed for the purpose of carrying of business have a long history. Such companies enjoying corporate status to appear in the 16<sup>th</sup> century. one of such companies was the East India Company which started business in this century in 1600 A.D. But the history of modern company law in England began in 1844 when the joint companies Act was passed The Act provided for the first time that a company could be incorporated by registration without obtaining a Royal charter or sanction by a special Act of Parliament. The early history of the accumulation of capital in England is very obscure, especially as most enterprises were either one-man businesses or simple partnerships, where all decisions were informal and hardly ever recorded. This was the state of affairs under the gild system, and the lack of evidence from this quarter increases the importance of the history of the joint-stock companies, which kept records and played a large part in the accumulation of capital even before 1720. <sup>[1]</sup> The concept of the Corporation was well established in the English Law at about the 14th Century. The Concept owes its origin to the Earlier Guild system prevalent at theta point of time. Guilds were built in regard to particular commodity in which they specialized themselves in order to create monopoly. The discoveries of the sixteenth and seventeenth centuries had opened new trade routes all over the world, and the consequent extension of markets offered many profitable openings for capital to be invested in commercial enterprises. Thus the way opened

for the rapid development of capitalist organization that took place in the seventeenth and eighteenth centuries.

It was in the 16th and 17th century when the idea of legal unity coupled with the financial device of joint stock trading bought forth the birth of Business Corporations <sup>[2]</sup>. Company form of Business Organization have originated and developed after the Industrial Revolution <sup>[3]</sup>. In the year 1844 Joint Stock Companies Act <sup>[4]</sup> was Enacted which provided incorporation of companies by way of registration opposed to a Special Act or Charter and further differentiating between private partnerships and joint stock companies. But the concept of limited liability was absent then, it was brought into existence by Limited liability Act, 1855 but was repealed with Joint stock Companies Act of 1856. The concept of having limited liability was preserved and was made compulsory. This was in order to make even small and middle class investors to contribute to the stock of the Corporation to which they were skeptical in the absence of limited liability. Thus it can be concluded that Joint Stock Companies as the name provides are Corporations pooling the fund received from the investor in a common stock benefits of which is divided between the contributors as in accordance of their rights so vested. By the end of Seventeenth Century, share dealings were common and stock broking was a recognized profession abuse of which legislator sought to regulate as early as 1696. It is interesting to note that although the invention of preference shares is generally attributed to Railway boom a century later, certain company's had already experimented with different classes of shares or of a loan stock, the distinction between shares and debentures were not appreciated until much later <sup>[5]</sup>.

#### History of Stock Exchange-The origin

As According to the Oxford dictionary of the business world, the stock market also known as the stock exchange is defined as a place in which stock, shares and other securities are bought and sold, price being controlled by

demand and supply. Stock markets have developed hand in hand with capitalism. Since the 17th century they are constantly growing in importance and complexity. The stock market has therefore been developed with time to open up opportunities to businesses and these individuals, and could be traced far back in history. During the second half of the seventeenth century there existed a considerable volume of securities, both commercial and gilt-edged, and the need to facilitate their transfer was becoming evident. At first, Government securities were predominantly short-term, such as Exchequer Tallies and discounting them with bankers affected liquidation. Similarly, many company stocks were still relatively short term relating to a particular voyage or adventure. When an investor wished to realize his share before the completion of the voyage, this was normally achieved by private negotiation with potential buyers. Towards the end of seventeenth century an organized market existed for the purchase and sale of stocks and shares. Brokers were licensed by the Lord Mayor of the City of London, and carried a silver medal as evidence thereof. These brokers were entitled to trade in any commodity or commodities within the city. After the financial crisis of 1696 the Government attempted to regulate the market and in 1697 passed an "Act" to restrain the number and ill practice and stock Jobbers". This provided that no person was to act as a broker in commodities or stock and shares unless licensed by the City of London, and that the total number of brokers so licensed to be limited to one hundred. Both this Act and Barnard Act of 1733, which made it illegal to buy stock without immediate payment or to sell it without immediate delivery were largely uninformed, and both the number of practicing Stockbrokers and the volume of speculative transactions increased. Up to 1698 the stockbrokers had congregated in the Royal Exchange, which was the center for all commodity transactions in the city.

It is clear that the Stock Exchange developed in order to meet two demands. First, the increased issue of securities of a long-term or permanent nature required a market for the purchase and sale of these securities, so that their holders could liquidate their investments in the short-term. Also the expansion of industry during the nineteenth century necessitated the discovery of new sources of finance. One of the sources of such was the Stock Exchange, which has continued ever since to be an important source of capital for industry.

### **Role of SEBI as a Regulatory Body**

The role of the Regulatory Authority in a Country depends upon the stages of development in the Securities Market in that Country [6]. In the Indian Context where the market is emerging in nature, role of the regulatory body is not only limited to regulation but to create conditions through exercise of function for the development of the market. This will ensure the market development and regulatory measures aiming to create discipline in the market and ensure high degree of fairness and market integrity. Thus we can say that SEBI as the Capital Market Regulator in India has twin objectives i.e. of regulating as well as developing the market [7].

As indicated earlier, a favorably operating capital market requires good rules and laws guiding a prospective market player which is now the duty of Regulatory Authority taking charge of fair market entrance and play. Most countries have treated this as a priority because the development of a country's financial market and institution may contribute substantially to its subsequent economic growth. It's been a decade since the Securities and Exchange Board of India (SEBI) started to put in place the regulatory framework for the capital market and investors have certainly benefited from the availability of more information and a contemporary secondary market structure [8].

### **Regulatory Framework & Investor Protection**

Every law relating to Securities has its objective of investor protection. As we have discussed in the earlier part of the paper that, right form vetting of Prospectus to the all sorts disclosure requirement of the Companies dealing with the public money has a nexus with the protection of interest of investor who form the part of the paid up capital of the Company. Investors make the backbone of the every Corporation by providing the required Finance to the Corporation. Protection of Investor is accomplished through effective regulation and Efficient and biting Securities Law. The Regulatory Framework of Country monitoring the securities dealing in the set market place aims at fair play and of preserving the market integrity which in turn has its objective of protection of Interest of Investor who contribute their hard earned money in the common pool of the Business Corporation. We can take the example of U.S.A. where the Securities Act of 1933 has two basic objectives: require that investors receive financial and other significant information concerning securities being offered for public sale; and Prohibit deceit, misrepresentations, and other fraud in the sale of securities [9].

Further the Preamble of SEBI Act lays down that protection of the interest of investor is its basic and foremost aim which is to be achieved through its functions of regulation. All the Regulatory Measures and actions starting from the vetting of Prospectus till the trading of shares in the market are designed and modified time to time in the Interest of Investor. The Regulator identifies and prohibits certain types of conduct in the markets and provides the Commission with disciplinary powers over regulated entities and persons associated with them.

### **SEBI and Capital Market**

There have been significant reforms in the regulation of the securities market since 1992 in conjunction with overall economic and financial reforms. In 1992, the SEBI Act was enacted giving statutory status as an apex regulatory body.

Over the last few years, SEBI has announced several far-reaching reforms to promote the capital Market and protect investor interests. Reforms in the Secondary market have focused on three main areas: structure and functioning of stock exchanges, automation of trading

and post trade systems, and the introduction of surveillance and monitoring systems<sup>[10]</sup>.

Until the early 1990s, the trading and settlement infrastructure of the Indian capital market was poor. Trading on all stock exchanges was through open outcry, settlement systems were paper-based, and Market intermediaries were largely unregulated. The regulatory structure was fragmented and there was neither comprehensive registration nor an apex body of regulation of the securities market. Stock exchanges were run as "brokers clubs" as their management was largely composed of brokers. There was no prohibition on insider trading, or fraudulent and unfair trade practices since 1992, there has been intensified market reform, resulting in a big improvement in securities trading, especially in the secondary market for equity. The Indian Capital Market has experienced a process of structural Transformation with operations conducted to standards equivalent to those in the Capital Market of the developed countries. It was opened for investment for the Foreign Institutional Investors (FIIs) in 1992 and Indian companies were allowed to raise resources abroad through Global Depository Receipts (GDRs) and Foreign Currency convertible Bonds(FCCBs). The Primary and Secondary segment of the market grew much rapidly, with greater institutionalization and wider participation of individual investors accompanying this growth. However many problems including lack of confidence in the stock investment, institutional overlaps and other governance issues remain as obstacle to the improvement of Indian capital Market Efficiency.

#### **Role of SEBI in Primary Market.**

The fundamental objective of the economic reforms undertaken by the government since 1991-92 was to bring rapid and sustained improvement in the quality of life of the people of India. It was with this set of objectives that the government had undertaken economic reforms since 1991-92. One of the important aspects of this reform package was to increase the efficiency of the financial system and securities market so that larger saving could be channeled for productive use reforms in the public sector.

Reforms in the primary market have to be appreciated very well in light of the regulatory framework in regards to market players involved in the work of issue. The regulations guidelines and notifications of SEBI have focused right from vetting of the prospectus to actually reaching the secondary market and have ensured a fair play ensuring the Protection of the interest of the Investor. Reforms in the Primary securities market over a decade or so have been of immense help to the investors. Since the Primary market provides for floating of capital of the Company, measures regarding market intermediaries, their eligibility criteria and simplification and streamlining of issue procedure has been the areas of achievement from the aspect of regulatory framework in India. Disclosure requirement of Company through its prospectus, market players and all those who play a part in the Primary market has been appreciated and strengthened with the growing time and need of the Hour. The focus of these measures was to enhance the level of

investor confidence and inhibit fraud in public offerings. To give effect to these measures, the Guidelines for Disclosure and Investor Protection were amended<sup>[11]</sup>. Further the introduction of Book Building, Regulations of Credit rating agencies, lock in requirements and Enhancing the Disclosure requirement has been the Achievement over a period of more than a decade since SEBI has taken Charge as a Regulator of the Capital Market in India.

#### **Role of SEBI in Secondary market**

A series of re-forms was introduced to improve investor protection, automation of stock trading, integration of national markets, and efficiency of market operations. India has seen a tremendous change in the secondary market for equity. It is ten years since the Securities and Exchange Board of India (SEBI) started to put in place the regulatory framework for the capital market and investors have certainly benefited from the availability of more information and a contemporary secondary market structure.

Reforms in the Secondary market include Encouragement to stock Exchange to act as Self-Regulatory Organisations (SROs) with accountability and responsibility. Further the Reforms have been in areas of Reconstruction of the Governing body of the Stock Exchanges, audit of broker book, market makers, insider trading, code for merger and takeover, grievance redressal by Stock exchange and function of inspection of and monitoring of Stock Exchange. Market has been made Infrastructural sound and modern in terms of transparency and Efficiency in Light of Investor Protection. In this regard continuous interfaces with stock Exchanges were kept in regard to various issues as that of Investor Protection, improvement in intermediary quality and building auto modated market Infrastructure. Introduction of rolling Statements, scrip's, maintenance of Accounting standards, warehousing of shares , market making, setting up of Depositories, stringent disclosure requirement for the Listed Corporate have added to the achievement and Reforms in the Secondary Market.

#### **Conclusion**

The present regulatory regime for the securities markets established under the SEBI Act 1992 has led to improvements in standards of investor protection. At the same time a number of challenges remain and there is a scope for potential further improvements and greater efficiency in the regulatory system. Some of the measures that SEBI proposes to take in this direction are mentioned above. As the changes and reforms brought in by SEBI get bedded in and markets mature, it is expected that Indian securities markets will take up their rightful role in the Indian economy. The Capital market has made tremendous progress in terms of institution building. In a period of three years, we had the elimination of unlimited leverage in stock trading; the onset of anonymous, electronic trading; the rise of a clearing corporation which eliminates counter party risk from the exchanges for which it does clearing, and the onset of depository settlement. These are profound changes in market mechanisms. They have transformed the lives of

investors and of market intermediaries. They have given us an unprecedented level of market liquidity and market efficiency. With the rapid expansion in the primary market, there were concerns raised about the quality of some of the issuers who were able to raise funds from the market in the period after the repeal of the Capital Issues (Control) Act, 1947. In response to these concerns, SEBI had strengthened norms for public issues, raised the standards of disclosure in public issues to enhance the level of investor protection without seeking to control the freedom of eligible issuers to enter the market and freely price their issues. But there still may be some grayer areas in takeover, merger region etc.

SEBI began to put in place regulations a decade ago, starting with its Guidelines for Disclosure and Investor Protection (primary markets) in 1992. A fairly broad-based regulatory framework is now in place, though, going forward, SEBI has to make the market a friendlier place for investors by plugging the gaps in its performance.

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